

The State of Pakistan's Economy

HALF YEAR
REPORT
of the Board of Directors

2021-22



HALF YEAR REPORT 2021-22

THE STATE OF PAKISTAN'S ECONOMY



STATE BANK OF PAKISTAN

SBP BOARD OF DIRECTORS

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LETTER OF TRANSMITTAL

State Bank of Pakistan
Karachi.
August 12, 2022

Dear Mr. Chairman,

In terms of Section 39(2) of the State Bank of Pakistan Act, 1956, the Half Yearly Report of the Board of Directors of State Bank of Pakistan on the State of Economy for the year 2021-22 is hereby enclosed for submission to the Majlis-e-Shoora (Parliament).

With warm regards,

Yours sincerely,



(Dr. Murtaza Syed)
Acting Governor

Muhammad Sadiq Sanjrani
Chairman
Senate
Islamabad

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Acting Governor

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National Assembly
Islamabad

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Contents

Chapters

1	Overview	1
2	Real Sector	7
2.1	Economic Growth	7
2.2	Agriculture	10
2.3	Large Scale Manufacturing	15
2.4	Services	25
2.5	Labor Market	28
3	Monetary Policy and Inflation	33
3.1	Policy Review	33
3.2	Monetary Aggregates	36
3.3	Credit to Private Sector	41
3.4	Inflation	46
4	Fiscal Policy and Public Debt	53
4.1	Fiscal Trend and Policy Review	53
4.2	Revenues	58
4.3	Federal Expenditures	66
4.4	Provincial Fiscal Operations	70
4.5	Public Debt	74
5	External Sector	85
5.1	External Sector Developments	85
5.2	Current Account	90
5.3	Financial Account	93
5.4	Exchange Rate and Reserves	97
5.5	Trade Account (Customs Record)	98

Special Section: Role of Trade Organizations in Economic Growth and Development: Understanding the Dynamics in Pakistan	115
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Annexure: Data Explanatory Notes	149
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List of Acronyms **153**
Box Items

Box 2.1: Rebasing of National Income Accounts (NIA)	8
Box 2.2: The Expanded Coverage and Impact of Rebased QIM	17
Box 3.1: Inflation and Monetary Policy Response in EMDEs	35
Box 4.1: Tax Exemptions Erode the Tax Base of General Sales Tax (GST) in Pakistan	56
Box 4.2: Track and Trace System - A step towards containing tax evasion in Pakistan	61
Box 5.1: Factors Driving Import Growth in Pakistan & their Impact on Interbank Availability	87
Box S1.1: Examples of Market Supporting and Market Complementing Services by TO	121
Box S1.2: Examples of Umbrella Bodies in Apparel Sector of India and Sri Lanka	139

The analysis and projections presented in this report were prepared on data outturns for the July-December period of FY22 and finalized in April 2022, using data and developments as of then.

1 Overview

Pakistan's economic recovery continued in H1-FY22, with its momentum moderating in the second quarter. Indeed, from a first half perspective, the large scale manufacturing (LSM) exhibited broad-based expansion; exports grew buoyant alongside growth in FBR taxes; and *Kharif* crops recorded higher production (**Table 1.1**). However, amid multi-year high global commodity prices, rising inflation and current account deficit posed a challenge as the year progressed. These pressures necessitated monetary tightening amidst other regulatory measures to moderate demand.

Globally, the H1-FY22 period witnessed a Delta-driven surge in coronavirus cases in Q1, and the beginning of a new wave driven by the Omicron variant towards the end of Q2. However, the ongoing vaccine roll-outs, along with continuation of supportive policies (especially in the advanced economies), helped sustain the global economic recovery. Nonetheless, supply chain disruptions due to container shortages induced by Covid, and post-Covid global economic recovery, contributed to price hikes in internationally traded commodities (**Figure 1.1**).

Within Pakistan, the slide in Covid-19 cases that began at the end of Q1 continued throughout Q2, as the Delta variant-driven wave fell rapidly by the end of H1-FY22. While the Omicron variant emerged by the end of H1-FY22, it did not lead to another wave of Covid cases during the review period (**Figure 1.2**). These improved conditions, alongside the government's

Selected Economic Indicators **Table 1.1**

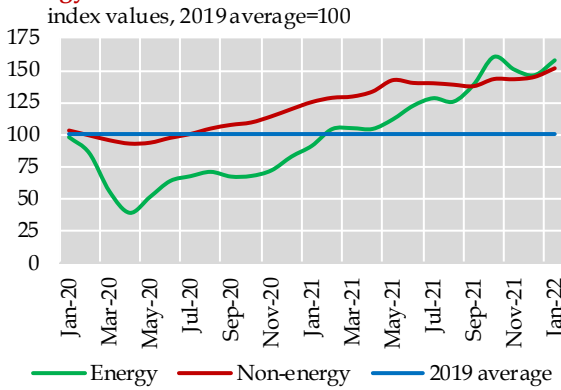
	FY21		FY22		
	Q2	H1	Q1	Q2	H1
<i>Growth rate (percent)</i>					
LSM ^a	5.5	1.5	9.7	5.5	7.5
National CPI ^a	8.4	8.6	8.6	11.0	9.8
Private sector credit ^b	6.2	5.0	3.0	10.1	13.4
Money supply (M2) ^b	4.3	5.6	0.6	3.7	4.3
Exports ^b	0.7	-4.8	34.5	24.3	28.9
Imports ^b	4.4	-0.5	63.5	51.4	57.0
Ex. rate (+app/-dep percent) ^b	3.7	5.1	-7.7	-3.3	-10.7
FBR tax revenue ^c	6.2	5.6	38.3	26.9	32.1
Policy rate (end period) ^b	7.0	7.0	7.25	9.75	9.75
<i>billion US\$</i>					
Remittances ^b	7.1	14.2	8.2	7.6	15.8
FDI in Pakistan ^b	0.4	0.9	0.5	0.6	1.1
FX loans (net) ^b	1.5	1.5	4.8	5.1	9.9
Current account balance ^b	0.4	1.2	-3.5	-5.5	-9.0
Change in SBP reserves ^b	1.3	1.3	2.0	-1.6	0.4
<i>percent of GDP</i>					
Fiscal balance ^c	-1.2	-2.1	-0.7	-1.5	-2.1
Primary balance ^c	0.1	0.6	0.3	-0.2	0.1

Sources: ^a Pakistan Bureau of Statistics; ^b State Bank of Pakistan; ^c Ministry of Finance

vigorous vaccination drive, paved the way for largely uninterrupted economic activities.

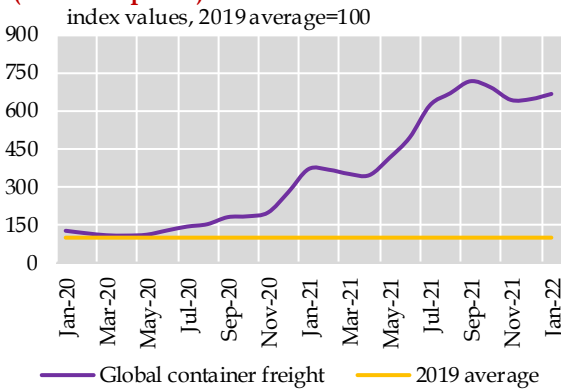
In addition, a combination of policy factors contributed to elevated domestic demand. In particular, expansion in federal and provincial development spending, along with an increase in non-interest current expenditures, supplemented economic growth outcomes. On the monetary side, two major factors facilitated capacity expansion and economic activities: the lagged impact of favourable monetary conditions of FY21 along with SBP's concessionary financing schemes; and an accommodative policy environment at the start of FY22. At the same

Trend in Global Energy & Non-Energy Prices



Source: World Bank Commodity Price

Container Freight Benchmark (WCI Composite)



Source: Bloomberg

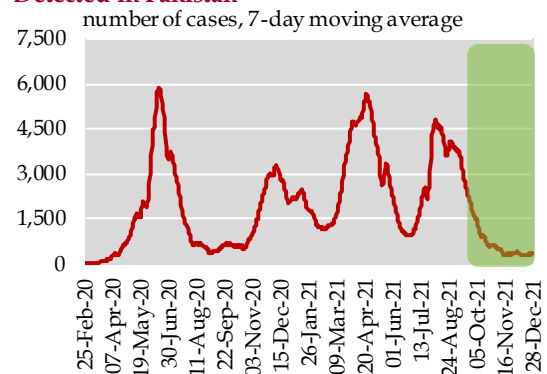
time, the continuation of the Export Finance Scheme (EFS) helped businesses cope with the surge in global commodity prices.

The LSM witnessed a broad-based increase in H1-FY22, although a rise of 9.7 percent in Q1 outweighed relatively moderate growth of 5.5 percent in Q2. In contrast to H1-FY21 when 11 out of 22 LSM sectors posted positive outcomes, 16 sectors recorded output growth in H1-FY22. In addition to SBP's Temporary Economic Refinance Facility (TERF), Long Term Financing Facility (LTFF) and other SBP schemes that helped the textile sector expand its capacity and output, fiscal policy measures also enabled this growth. Tax cuts (on domestic sales and imported inputs) for automobile were among the sector's drivers, whereas the steel sector continued to benefit from the government's construction package and higher development spending. Wearing apparel, a new addition to the LSM index, displayed a strong performance, in line with growing external demand for Pakistan's apparel products.

Growth in the agriculture sector during *Kharif* was primarily driven by record rice and sugarcane production, mainly due to an increase in the area under cultivation. Cotton production also increased over last year; it largely benefited from favourable weather conditions that enabled a sizeable increase in cotton crop yield, which offset the decline in its cultivated area. However, input utilization decreased during the second quarter in the *Rabi* season, with fertilizer usage declining notably due to higher prices.

Trend in Daily Covid-19 Cases Detected in Pakistan

Figure 1.2



Source: World Health Organization

Private sector credit grew nearly fourfold in H1-FY22 on YoY basis. This was mainly on the back of working capital requirements that rose due to increased domestic demand, higher exports, as well as the global commodity price hike and ensuing jump in the Wholesale Price Index (WPI) during H1-FY22. The expansion in economic activities was also visible in the demand for loans for fixed investments and consumer financing. The growth in loans for fixed investments was mainly led by telecom and textile sectors; the former was on account of 4G license issuance and the latter due to TERF and LTFF-led machinery imports and capacity expansions. Despite slower growth in Q2, consumer financing grew 26 percent in H1-FY22. The pace of growth in consumer financing had experienced a policy-induced moderation in Q2, as auto and personal loans posted negative growth following increases in the policy rate and introduction of regulatory measures to curtail demand. However, this was offset by consistent growth in house building loans in both quarters partly due to the SBP's mandatory targets for housing and construction. Soaring global commodity prices, coupled with growing domestic demand, especially for industrial inputs, also resulted in a widening of the current account deficit, despite double-digit growth in workers' remittances to US\$ 15.8 billion in H1-FY22. Exports grew considerably in the first half, notwithstanding some deceleration in the second quarter. Both higher unit prices and export volumes contributed to this growth. While these dynamics were generally visible across both textile and non-textile segments, rising export volumes of value-added textile items played a dominant role in pushing up the sector's exports. As a result, overall exports saw a US\$ 3.4 billion year-on-year

increase in H1-FY22 to US\$ 15.2 billion – their highest ever half-yearly outturn.

Nevertheless, despite slower import momentum in the second quarter, the increase in H1-FY22 imports was nearly four times the increase in exports. In addition to the dominant role of high global commodity prices, import growth was also buoyed by elevated demand for raw materials and capital goods; Covid-19 vaccine procurement; and the continued need to import wheat and sugar to plug domestic supply gaps.

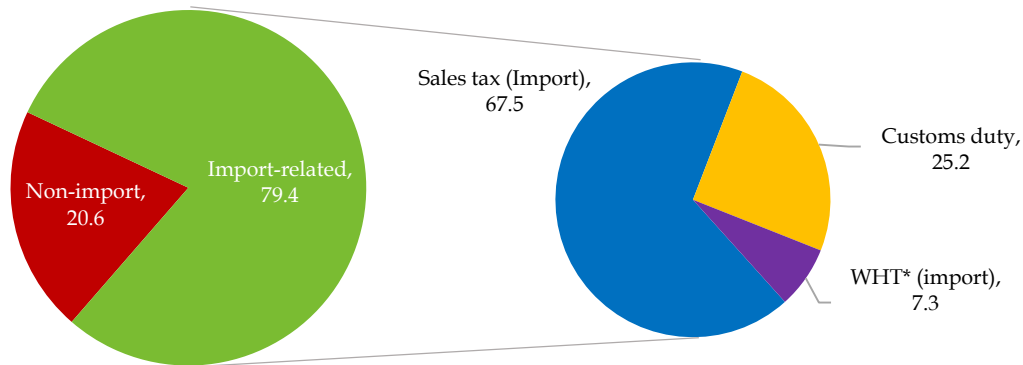
Amid the widening current account deficit, the PKR depreciated 10.7 percent in the interbank market during H1-FY22. However, the SBP's FX reserves remained relatively stable. Complementing the US\$ 1 billion inflow from Eurobond issuance and the additional SDR allocation of US\$ 2.8 billion from the IMF in Q1, bilateral deposits of US\$ 3 billion from Saudi Arabia in Q2 supported the SBP's FX reserves position.

The confluence of costlier imported commodities (such as edible oil and pulses) and some demand-side pressures pushed national CPI inflation (NCPI) into double digits during H1-FY22. Food inflation, the biggest contributor in H1-FY22, was mainly driven by non-perishables, which more than offset the decrease in the prices of perishable food items. In addition, upward adjustments in administered prices of petrol, LPG, and electricity continued to push up input costs. At the same time, core inflation also ticked up, with prices of more than half of non-food non-energy (NFNE) items in the urban and rural baskets posting above-average increases during the second quarter.

In the wake of broad-based inflationary pressures and the widening of the current

Growth Contribution of Import-Related Taxes in Overall FBR Tax Collection* - H1-FY22 (percent)

Figure 1.3



*Import-related taxes include: sales tax (imports), custom duty and Withholding tax (WHT) on imports

Source: Federal Board of Revenue

account deficit, the monetary policy committee (MPC) increased the policy rate by 25 basis points at the end of Q1.

Subsequently, with the balance of risks shifting more quickly than expected away from growth and toward inflation and the current account due to larger and more persistent global price increases, the MPC raised policy rates twice in the second quarter: 150 basis points in November 2021, followed by 100 basis points in December 2021. This normalization of monetary policy settings was aimed at ensuring sustainability in both economic growth and the external account, as well as anchoring inflation expectations.

Apart from the rate hikes, three additional measures were taken to moderate the demand pressures. First, the average cash reserve requirement for banks was increased to tighten the money supply. Second, prudential regulations for consumer financing were tightened by the end of Q1, and its impact became visible in Q2 through a contraction in auto and personal loans. Third, 100 percent cash margins were imposed on

an additional 114 items in September 2021, bringing the total number to 525 items.

On the fiscal side, the overall deficit remained unchanged in H1-FY22 at last year's level of 2.1 percent of GDP. However, the primary balance narrowed to 0.1 percent of GDP in H1-FY22, from 0.6 percent in the same period last year, as the increase in non-interest expenditures more than offset the robust rise in tax revenues.

Non-interest expenditure rebounded sharply in H1-FY22, on the back of increased spending on social protection and subsidies. Federal PSDP rose by almost one-fifth in the first half, although it declined in Q2 due to the government's efforts to contain the fiscal deficit. On the revenue side, FBR taxes grew by 32 percent in H1-FY22, notwithstanding somewhat slower growth in Q2, as economic activities improved and general price levels rose as compared to last year. However, most of this increase stemmed from import-related taxes, on account of the broad-based increase in import volumes, international commodity prices and PKR depreciation (**Figure 1.3**).

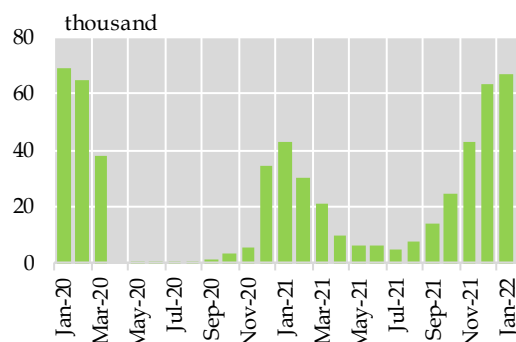
In addition to various structural impediments to sustained economic growth, as consistently highlighted in SBP's quarterly and annual reports, there is a need to increase public-private collaboration in the planning and implementation of different kinds of reforms. To this end, regular public-private dialogue (PPD) plays an important role for economic growth and development, especially as government planning around the world has become participatory, collaborative and market-oriented in nature.

In this regard, a special section in this report underscores the role of Trade Organisations (TOs). With a focus on local TOs, the section highlights their importance in making PPD effective and in providing market-complementing services to their members. It also identifies some gaps that need to be addressed to ensure that local TOs fulfil their intended objective of improving the business environment and contributing towards the country's economic growth and development.

2 Economic Outlook

The economy is expected to grow around the middle of the forecast range of 4-5 percent for FY22, lower than last year's growth of 5.6 percent. This outlook is based on three main factors. First, industrial output across some sectors may exhibit a slowdown, in part due to the lagged impact of monetary tightening and other regulatory measures taken in H1-FY22. In particular, the slowdown may also be visible in sectors affected by consumer financing, such as automobiles and other consumer goods. However, export-oriented sectors are expected to continue benefiting from the SBP's concessionary financing schemes (EFS and LTFF), as the increase in interest rate on EFS, announced in April 2022, is expected to have a lagged impact.

Number of Migrants Going for Work to GCC **Figure 1.4**



Source: Bureau of Emigration and Overseas Employment

Second, uncertainty surrounds the agriculture output. On one hand, estimates for *Kharif* agriculture output are promising, with record production estimated for sugarcane and rice and decent growth expected for cotton. However, on the other hand, downside risks stem from vulnerabilities faced by wheat crop, which was marked by lower input usage in Q2-FY22. Third, the performance of commodity-producing sectors would continue providing the impetus for service sector growth, whereas import growth would also provide support.

On the fiscal side, the rationalization of GST exemptions, including elimination in some cases, bodes well for the fiscal deficit in FY22, which is projected to be slightly lower than last year. However, higher than expected commodity prices, including oil, may increase the government's spending on subsidies, given its decision in March 2022 to freeze fuel and power rates.

NCPI inflation is expected to be slightly exceed the forecast range of 9-11 percent in FY22, as revised upward by the MPC in its decision on April 07, 2022. The government's decision to reduce and freeze administered

prices of fuel and power in March 2022 significantly offsets the risks emanating from the persistent rise in global commodity prices. However, the upside risk stems from a more-than-expected increase in global oil, food and fertilizer prices, owing to the geopolitical tensions between Russia and Ukraine. Both these countries are major suppliers of multiple commodities including oil, gas, wheat, fertilizer, metals and edible oil (sunflower oil).

Workers' remittances are expected to post decent growth in FY22 on the back of rising incomes in oil-exporting GCC countries and the advanced economies. Moreover, the monthly flow of Pakistani workers has reverted to pre-Covid levels as well (**Figure 1.4**).

Exports are projected to continue expanding in FY22, as the cuts in fuel and power rates would help exporters maintain competitiveness in international markets, amid continued support from the SBP's concessionary financing schemes and estimates of record rice output. However, export growth prospects face risks from policy reversal in advanced economies, which may impact consumer spending and thereby slow the pace of their economic growth. Moreover, the impact of the Russia-Ukraine war also poses a downside risk to

demand in the EU, considering that Russia supplies nearly 40 percent of the EU's energy needs.

The sharp increase in global commodity prices will keep import payments at an elevated level in FY22, partly offsetting the expected decline in import volumes on account of lagged impact of monetary tightening on overall economic activity, and other demand-compressing regulatory measures. As a result, the current account deficit is projected to increase to around 4 percent of GDP.

Nonetheless, the external account pressure is expected to remain manageable. Some big-ticket import items, such as Covid-19 vaccines and energy imports (oil and LNG), are mainly imported in kind, which means that they are financed via external sources instead of the interbank FX market. External financing for these purchases is recorded in the financial account. Moreover, the completion of the 6th EFF review in February 2022 unlocked an additional US\$ 1 billion from the Fund, whereas the country also issued a Sukuk for US\$ 1 billion in January 2022. The country is also likely to retain access to multilateral and commercial financing, which would help sustain the SBP's liquid FX reserves.

2 Real Sector

The economy experienced broad-based growth during H1-FY22. In the agriculture sector, the production of important Kharif crops such as cotton, rice, and sugarcane was better than last year; however, indicators of the crop sector in Rabi season point to some reduction in area for wheat. Within industry, the large-scale manufacturing activity was upbeat during H1-FY22 compared to the same period last year, as sectors such as automobiles, wearing apparel, and steel posted robust growth. However, some moderation in LSM growth and high frequency demand indicators such as cement dispatches and POL sales was noted in Q2. The decent overall performance of the commodity-producing sector during H1-FY22 provided the impetus for services sector growth, as reflected in proxy indicators such as import growth and sales of FMCG firms, commercial vehicles, and POL products. The labor market also showed signs of strengthening, as more employees were hired across industries and the business community remained optimistic about employment prospects.

2.1 Economic Growth

The available information on the real sector indicates that the growth momentum gained in FY21 was carried forward into H1-FY22. In agriculture, the crop sector performance was better than last year, with record output expected for rice, sugarcane and maize. In the industrial sector, Large Scale Manufacturing (LSM) activities sustained their positive trajectory, with some slowdown evident in Q2. The performance of the commodity producing sector, along with a rise in imports, had a favorable impact on the services sector. Meanwhile, the SBP's Business Confidence Survey reflected an overall optimism in the labor market, in the wake of increase in the number of industrial workers and growth in wages during the review period.

In the agriculture sector, *Kharif* crops (cotton, rice and sugarcane) were estimated to beat last year's production levels. The growth in rice and sugarcane was primarily driven by an increase in the area under cultivation. Cotton production increased on the back of improvement in yield. Unlike *Kharif* season, the first half of Rabi season was marred by

several issues. On the input front, farmers faced a shortage of irrigation water and elevated input prices of fertilizer, electricity and diesel. Moreover, below normal rainfall during the sowing period further complicated the situation during Q2-FY22. As a result, the cultivation area of wheat (the major crop of *Rabi* season) declined compared to last year.

LSM grew by 7.5 percent during H1-FY22, compared to 1.5 percent in the same period last year. This occurred against the backdrop of elevated demand during the review period, with supportive policies contributing to sectoral growth. Specifically, the automobile sector benefitted from tax relief and accommodative monetary policy for the greater part of the review period, which drove up the demand for automobiles.¹ The textile sector capitalized on concessionary financing schemes (such as TERF and LTFF) to scale up its output. The value-added segment of the textile sector grew notably, as evident from the ramped-up production of the wearing apparel subsector, in response to strong external demand for readymade garments. Meanwhile, the steel sector witnessed positive spillovers from incentives

¹ Specifically, the MPC maintained the policy rate at 7 percent in July 2021, before raising it by 25 basis points (bps) on September 20; 150 bps on November 19; and 100 bps on December 14. Thus, the rate was cumulatively raised by 275 basis points to 9.75 percent during the review period.

given for construction and housing activities, as well as higher PSDP spending during H1-FY22 compared to the same period last year.

Positive growth in agriculture during the *Kharif* season and in LSM had a favorable impact on services sector activities during H1-FY22. The wholesale and retail sector benefited from these developments, coupled with significant rise in imports. Activity in the transport sector also picked up, as evident from commercial vehicle and POL sales. Indicators of finance and insurance and real estate activities also suggested growth in these sectors.

In line with pickup in other sectors of the economy, there were more job opportunities for the labor force during H1-FY22. Proxy indicators such as industrial employment,

SBP Confidence Surveys, and wage rate data indicate positive trends in the labor market. Employment in the industrial sector grew in both Sindh and Punjab during H1-FY22. The increased optimism about the job market was more evident in the industrial sector than the services sector, according to the SBP's Business Confidence Survey. Moreover, relatively better growth in wages of industrial sector employees was recorded compared to the services sector.

In addition to these developments, the Pakistan Bureau of Statistics (PBS) released national accounts data for the past 5 years on the new FY16 base. Based on new estimates the economy grew by 5.6 percent during FY21, compared to a 1.0 percent contraction in the preceding year (**Box 2.1**).

Box 2.1: Rebasing of National Income Accounts (NIA)

The PBS published revised estimates of NIA, which included comprehensive revisions in addition to the regular revisions. While regular revisions are made on an annual basis², the major revisions are carried out at the time of change of base year for the compilation of NIA.³ These comprehensive revisions are necessary to accommodate transition in the underlying economic activity emerging from change in the number of goods produced/services rendered and the number of production units and service providers. Since the last re-basing of NIA estimates on 2005-06, which was introduced in FY13, the level of economic activity has undergone a significant expansion as reflected by an average 0.4 percent increase in real GDP growth during FY17-21.

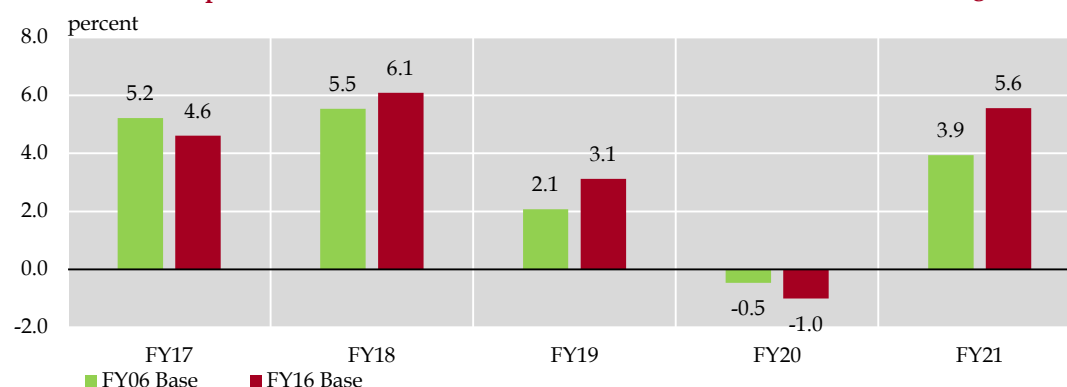
In its latest revision, PBS had changed the base year from FY06 to FY16, resulting in revision of economic growth figures for the past 5 years (**Figure 2.1.1**). For the rebasing exercise and to improve coverage of the economy, PBS conducted various censuses, surveys and studies: Census of Manufacturing Industries, Census of Electricity, Census of Exploration Companies; Rent Survey, Household Integrated Income, and Consumption Survey, Survey on Small & Household Manufacturing Industries and Survey on Other Private Services.

² At the time of collation of NIA which is end-March, data for Q4 (April-June) is estimated. As the data for Q4 becomes available, the PBS revises its NIA dataset to reflect actual economic activity.

³ The Governing Council of PBS issued a policy directive to rebase the NIA after every 10 years in 2013.

Growth Rate Comparison: Old Base vs New Base

Figure 2.1.1



Source: Pakistan Bureau of Statistics

In the agriculture sector, the contribution of plant nurseries, honey bees, cotton ginning, forestry and fishing was re-assessed through studies. For the industrial sector, the coverage of LSM was enhanced and new industries such as water supply, sea salt and hydro IPP were included.⁴ In the services sector, accommodation and food services (hotels and restaurants), information and communication industries and education, human health & social work activities were estimated separately in the rebased accounts.

Sectoral Shares and Real GDP Growth

Table 2.1.1

FY16 Base							
	percent share in real GDP			Growth rate (percent)		Growth Contribution (percent)	
	FY19	FY20	FY21	FY20	FY21	FY20	FY21
Agriculture	22.4	23.5	23.1	3.9	3.5	0.87	0.82
Industry	19.5	18.5	18.9	-5.8	7.8	-1.13	1.44
Services	58.1	57.9	58.0	-1.3	5.7	-0.76	3.30
Real GDP	100	100	100	-1.0	5.6	-1.0	5.6
FY06 Base							
	percent share in real GDP			Growth rate (percent)		Growth Contribution (percent)	
	FY19	FY20	FY21	FY20	FY21	FY20	FY21
Agriculture	18.7	19.4	19.2	3.3	2.8	0.6	0.5
Industry	19.9	19.2	19.1	-3.8	3.6	-0.7	0.7
Services	61.4	61.4	61.7	-0.6	4.4	-0.3	2.7
Real GDP	100	100	100	-0.5	3.9	-0.5	3.9

Source: PBS

⁴ For LSM, PBS used information from 23,712 manufacturing establishments. Previously 112 items with a total weight of 70.3 percent of value added were covered in the QIM index on FY06 base. This has now been revised to include 123 items having a total weight of 78.4 percent in the FY16 rebased QIM. In addition, wearing apparel, towel, furniture and football have been added to the computation of rebased QIM.

As a result of this comprehensive revision, the contribution of the share of agriculture, industry and services in GDP has changed. While the contribution of agriculture and services increased, the share of industry declined in the rebased NIA. **Table 2.1.1** shows this trend after the change in reference period.

The comprehensive revision in NIA as a result of change in base year is a timely development. The inclusion of several new sectors increases the coverage and accuracy of GDP estimates. This also facilitates policy decisions on sector specific issues and analysis of short-term and medium-term dynamics of these sectors. That said, there is still room for further improvement in subsequent base-year revisions. New livestock and small-scale industry censuses would further enhance the accuracy of the NIA.

2.2 Agriculture

After a promising *Kharif* season, the crop sector faced some headwinds in the *Rabi* season. Area under wheat cultivation declined compared to last year's crop in both Sindh and Punjab. The major reasons for the decline in area are: insufficient water availability, high cost of production, and late harvesting of the sugarcane.

On the input side, canal water availability was lower than last year during the sowing period. Moreover, the application of fertilizer also remained lower during the review period. On the other hand, credit disbursements to agriculture increased by 3.9 percent during H1-FY22 compared to last year, mainly due to higher borrowing in the non-farm sector.

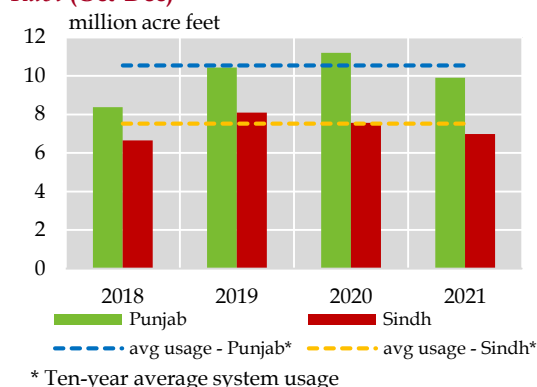
Inputs

Irrigation water shortage was witnessed during the first half of Rabi FY22. The cumulative canal water withdrawals in Punjab and Sindh, which together account for more than 85 percent of the area under wheat, stood at 16.9 million acre feet (MAF), showing a decline of 10 percent compared to the previous year. Moreover, the irrigation water releases in Punjab and Sindh were also

lower than the long-term average (**Figure 2.1**). This could be due to lower rainfall recorded in 2021 compared to last year.⁵

With regard to fertilizer application, the offtake of urea and DAP contracted by 7.7 percent and 14.1 percent respectively in Q2-FY22, compared to the same period last year (**Figure 2.2**). The decline in DAP offtake was primarily due to a significant increase in its price on the back of surge in international prices (**Figure 2.3**). Specifically, the price of 50kg bag of DAP almost doubled to Rs. 7,760 in Q2-FY22, as opposed to Rs. 3,982 recorded in the previous year.

Irrigation Water Releases during Rabi (Oct-Dec) **Figure 2.1**

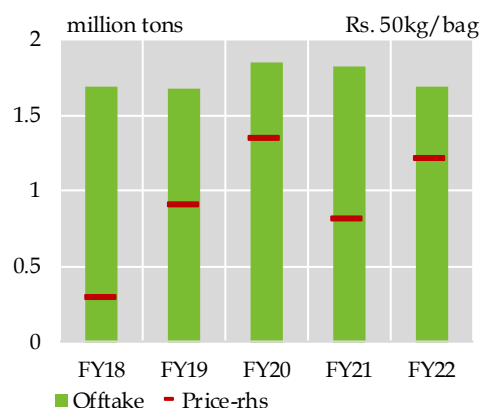


Source: Indus River System Authority

⁵ During 2021, national annual average rainfall was 242.3 mm, 18.6 percent below *average*. (Source: State of Pakistan's Climate in 2021, Pakistan Meteorological Department, Government of Pakistan.)

Urea Offtake and Price during Q2

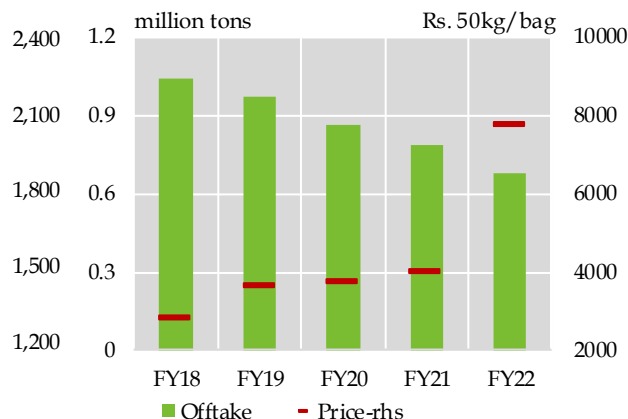
Figure 2.2a



Source: National Fertilizer Development Centre

DAP Offtake and Price during Q2

Figure 2.2b



In case of urea, a host of factors resulted in lower offtake during the review period. The decline in urea production during Q1-FY22 led to lower availability in Q2-FY22.⁶ Specifically, the current *Rabi* season started with the opening inventory of 0.1 MMT as opposed to 0.5 MMT in the last year. Moreover, during Q2-FY22 the total availability of urea was 2.0 MMT against the 3.4 MMT in Q2-FY21.⁷

In addition, due to global supply shortage, international prices of urea jumped significantly in the latter half of 2021 (Figure 2.3). This created substantial price differential between local and

international markets. The differential resulted in hoarding⁸ and smuggling of urea to neighboring countries, which further squeezed supply of urea locally and pushed the secondary market prices upward.^{9,10} Given the short supply, prices in the secondary market increased considerably, making application of urea costlier for growers.

The support to the farmers came through Agriculture Emergency Program. In order to increase the yield of wheat crop, a subsidy of Rs. 250/acre (up to five acre of land) on the use of pesticides/herbicides was provided to the farmers.¹¹ Moreover, one million bags of

⁶ This mainly stemmed from temporary suspension for plant maintenance and the curtailment of gas supply to two small-scale fertilizer plants.

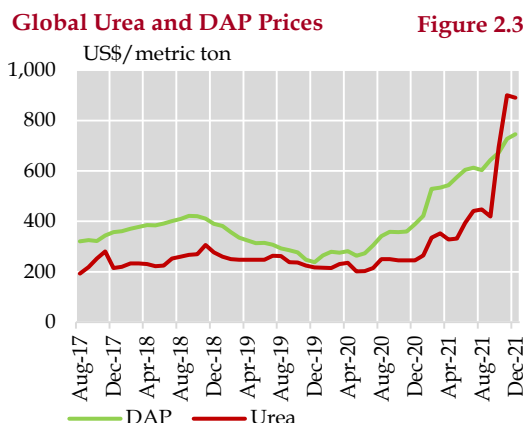
⁷ Source: MNFSR

⁸ Punjab Government to Crackdown on Fertilizers' Hoarders, date Nov 11, 2021, available at: www.punjab.gov.pk/node/4660, accessed on April 20, 2022.

⁹ Source: 'Pakistan Customs, (FBR) foils an attempt of smuggling of urea fertilizers to Afghanistan worth Rs 7.2 million', available at: www.fbr.gov.pk/pakistan-customs-fbr-foils-an-attempt-of-smuggling-of-urea-fertilizers-to-afghanistan-worth-rs-7/173311, accessed on April 20, 2022

¹⁰ According to market sources, the farmers were getting urea at Rs 2,200-2,600 against retention price of 1,725/bag for the manufacturers.

¹¹ In Punjab, the subsidy was distributed through vouchers inside the pesticides/herbicides packs. Registered farmers could avail the subsidy by sending the hidden voucher numbers, along with their



Source: World Bank

approved varieties of wheat seeds were also provided at a subsidy of Rs. 1,200 per bag.¹²

Overall credit disbursements to agriculture grew by 3.9 percent in H1-FY22 (Table 2.1). This was mainly due to higher credit offtake by the non-farm sector, as disbursements to livestock and poultry grew by 9.8 percent and 14.9 percent in H1-FY22 compared to the

same period last year. The increase was mainly attributed to rise in prices of raw materials such as poultry feed (Figure 2.4).¹³

However, credit disbursements to the farm sector contracted by 2.9 percent during H1-FY22 compared to the same period last year, as production-related loans declined by 4.0 percent. Nonetheless, loans for the purchase of tractors grew during the review period, as farmers benefitted from the *Kamyab Jawan Kamyab Kisan Tractor Loan Scheme* launched by the government in January 2021.

Output

Wheat

For *Rabi* FY22, the government set the wheat production target of 28.9 MMT from an area of 9.2 million hectares (Table 2.2). The achievement of this target largely depends on better yield, as the targeted area was set

Agriculture Credit Disbursements

billion Rupees

Table 2.1

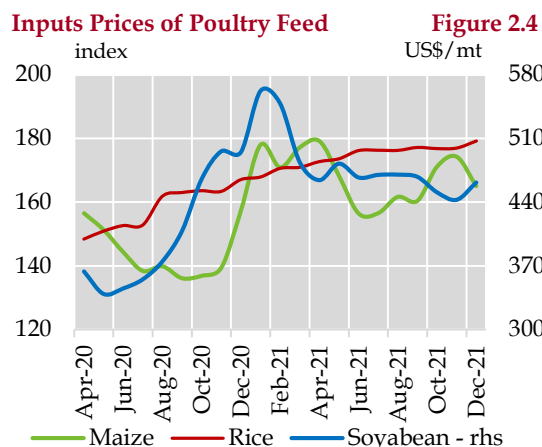
	Q1-FY21	Q1-FY22	Q2-FY21	Q2-FY22	H1-FY21	H1-FY22
Farm sector						
A. Production	113.8	136.3	193.2	158.4	307	294.7
B. Development	5.6	8.1	16.7	16.8	22.3	24.9
Tractor	0.6	1.7	1.0	2.9	1.6	4.6
C. Total farm sector (A+B)	119.4	144.4	209.9	175.2	329.3	319.6
Non-farm sector						
Livestock/dairy	71.2	81.7	89.6	94.9	160.8	176.6
Poultry	49.5	55.3	52.5	61.9	102	117.2
Other	14.4	10.5	10.4	17.1	24.8	27.6
D. Total non-farm sector	135.1	147.5	152.5	173.7	287.6	321.2
Total agri (C+D)	254.5	291.9	362.4	348.9	616.9	640.8

Source: State Bank of Pakistan

CNIC, to a short code and collect the subsidy from the designated branchless banking operators. In this way, the benefit of the subsidy was passed on directly to the growers. (Source: Agriculture Department, Government of Punjab)

¹² Agriculture Department, Government of Punjab.

¹³ In the poultry sector the largest component within direct costs is raw material comprising almost 71 percent of the total manufacturing cost. (source: PACRA)



Source: Pakistan Bureau of Statistics and World Bank

almost similar to last year's achieved level of 9.1 million hectares.

The initial estimates suggest that area sown in Punjab and Sindh was lower than the area cultivation recorded in the previous *Rabi* season (Table 2.3). Specifically, the area under crop in both provinces declined by 2.6 percent compared to last year. One reason for the decrease in the area was the shortage of canal water (Figure 2.1). Moreover, rain-fed areas also witnessed dry spell during the sowing months, making conditions relatively challenging for wheat growers (Figure 2.5).¹⁴

Another factor for low cultivation, particularly in Punjab, could be the lower wheat support price relative to cost. The federal government announced wheat support price of Rs 1,950 per maund (40 kg) for the Rabi FY22.¹⁵ The new price is Rs 150

Wheat Crop **Table 2.2**
area in million hectares, production in million MT

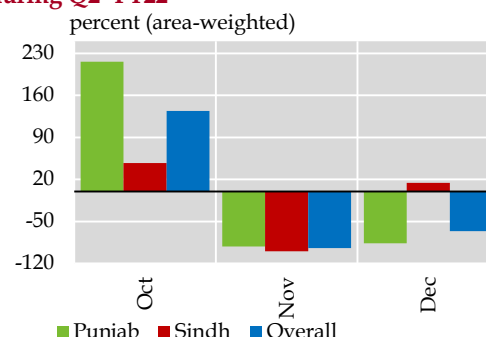
	Area		Production	
	FY21	FY22 ^T	FY21	FY22 ^T
Punjab	6.7	6.6	20.9	21.9
Sindh	1.2	1.2	4.0	4.2
KP	0.8	0.9	1.2	1.5
Baluchistan	0.5	0.6	1.2	1.2
Pakistan	9.18	9.21	27.3	28.9

T: target

Source: FCA, PBS

more than the last year's support price of Rs 1,800; however, farmers raised concerns that the announced price was insufficient to meet rising input prices of fertilizer, electricity, and diesel.¹⁶ Lastly, delay in harvesting of sugarcane in Sindh resulted in less sowing of wheat crop as compared to last year.¹⁷

Departure of Rainfall from Normal* **Figure 2.5**
during Q2 -FY22



* Normal refers to area-weighted rainfall during 1961-2010 (base)

Source: Pakistan Meteorological Department

¹⁴ Monthly Agromet Bulletin, National Agromet Centre, Pakistan Meteorological Department. Vol: 11-2021, November, 2021.

¹⁵ The Government of Sindh, in contrast, announced wheat support price of Rs 2,200 per maund (40 kg) for Rabi FY22.

¹⁶ Grain and Feed update, report number PK2021-0018, Date: January 04, 2022. United States department of Agriculture (USDA)

¹⁷ Source: Crop reporting center, Government of Sindh

Estimates of Area for Wheat Crop in Punjab and Sindh**Table 2.3**

thousand hectares

Punjab				Sindh			
Division	FY21	FY22*	Growth	Division	FY21	FY22*	Growth
Bahawalpur	1,024.6	997.9	-2.6	Sanghar	110.9	112.7	1.6
DG Khan	966.4	947.4	-2.0	Naushehro feroze	107.9	110.4	2.3
Gujranwala	939.3	970.4	3.3	Ghotki	111.8	108.8	-2.7
Faisalabad	785.9	728.4	-7.3	Khairpur	106.7	106.8	0.1
Multan	758.4	737.7	-2.7	Benzirabad	92.5	90.3	-2.4
Sargodha	735.7	714.7	-2.9	Dadu	83.7	79.1	-5.5
Rawalpindi	630.9	603.4	-4.4	Mirpurkhas	64.1	64.5	0.6
Lahore	517.6	520.0	0.5	Shahdadkot	55.9	56.1	0.4
Sahiwal	387.3	339.9	-12.2	Others	565.1	449.7	-20.4
Punjab	6,746.0	6,559.8	-2.8	Sindh	1,202.5	1,178.3	-2.0

*: First estimates

Source: Crop Reporting Services, Government of Punjab and Government of Sindh

Given the decline in cultivation area, achievement of targeted wheat production would mainly depend on the better yields. The use of approved varieties of wheat seeds on area of 10 million acres in Punjab may prove instrumental in achieving the higher yield. In addition, under the National Program for Enhancing Profitability through Productivity Enhancement of Wheat, modern agricultural machinery is being provided on 50 percent subsidy to farmers which may also aid to get higher yield.^{18 19}

Minor Crops

Within minor crops, the FY22 *Rabi* season targets envisioned increase in both area and production for onion, gram and tomatoes. Specifically, for the onion crop production is targeted to grow by 15 percent to 2.4 million tons from an area of 162 thousand hectares during *Rabi* FY22. Likewise, tomatoes production is set to 622 thousand tons for *Rabi* FY22, showing an increase of 5.1 percent against the last year production of 592

Minor Crops (*Rabi*)

Table 2.4

Area in '000 Hectares; production in '000 Tons; growth in percent

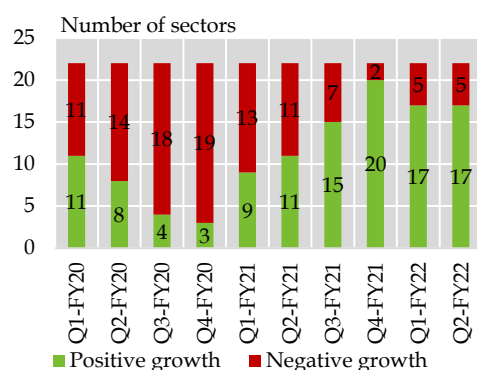
	FY21 Output		FY22 Target		Growth	
	Area	Production	Area	Production	Area	Production
Potatoes	234.4	4,681	226.1	6,029	-3.5	28.8
Onion	153.8	2,099.8	162	2,422	5.3	15.3
Gram	872.7	251.2	989	560	13.3	122.9
Tomatoes	50.2	591.9	52	622	3.6	5.1

Sources: Ministry of National Food Security and Research; FCA and PBS

¹⁸ Source: 'Punjab Government is Taking All Possible Steps to Provide Resources to Farmers for Wheat Cultivation', Press release dated 3-Nov-2021. available at www.punjab.gov.pk/node/4646, accessed on April 15, 2022

¹⁹ According to SUPARCO wheat condition in irrigated areas is generally better for timely sown however late sown areas have shown stressed growth. (Source: PAK-SCMS bulletin, Volume XII, Issue 02, Serial No. 134 1-February 2022)

Positive & Negative Growth Sectors in LSM **Figure 2.6**



Source: PBS

thousand tons. While for potatoes the target is to achieve higher production by enhancing the yield (**Table 2.4**).

For potatoes, the initial estimates of area under cultivation in Punjab indicated significant increase of 35.8 percent from last year.²⁰ The growth in the acreage could be traced back to rise in the international demand for potatoes which is incentivizing growers to dedicate more area to crop and earn better profits.^{21,22} Given that the province accounts for more than 80 percent of potatoes production, the harvest for current year is likely to exceed target, leaving surplus quantity for export.

Meanwhile, the area for gram crop in Punjab observed decline of 6.6 percent compared to last year. The decrease in the gram was more significant in the southern part of Punjab, as farmers in these areas switched to potatoes cultivation.

2.3 Large-Scale Manufacturing²³

Large-scale manufacturing (LSM) grew by 7.5 percent during H1-FY22, compared to 1.5 percent in the same period last year (**Table 2.5**). The pickup was evident across both quarters of H1-FY22 of ongoing fiscal year. Specifically, 17 out of 22 sectors posted positive growth during Q1-FY22 and Q2-FY22, compared to 9 sectors in Q1-FY21 and 11 sectors in Q2-FY21 respectively (**Figure 2.6**). In particular, the automobile sector and wearing apparel sector (a new addition to LSM – **Box 2.2**) made the most notable contributions.

The base effect also accentuated LSM growth during the review period, with growth of 18.8 percent reported for August 2021 compared to a decline of 9.4 percent in August 2020 (**Figure 2.7**).²⁴ As a result, LSM growth during Q1 suggested a significant rebound compared to the same period last year. However, in Q2 growth was moderate in comparison to the first quarter.

²⁰ Source: Crop reporting center, Government of Punjab

²¹ During H1-FY22 the potatoes export (in quantum terms) witnessed growth of 13.4 percent compared to same period last year. Moreover, in FY21 Pakistan exported 395.2 million kg potatoes compared to 364.8 million kg during FY20, showing YoY growth of 8.4 percent. (Source: PBS)

²² Vegetables and Pulses Outlook: November 2021, Economic Research Service, VGS-367, USDA.

²³ The analysis of LSM is based on the provisional QIM data for base year 2015-16 up to January 2022, released by the PBS in March 2022. Previously, for the SBP's First Quarterly Report on the State of Pakistan's Economy, the analysis had been made on the QIM data for base year 2005-06 available at the time.

²⁴ For reference, the August 2020 LSM decline was mainly attributed to factors such as heavy monsoon downpour and subsequent flooding, particularly in the industrial hub of Karachi.

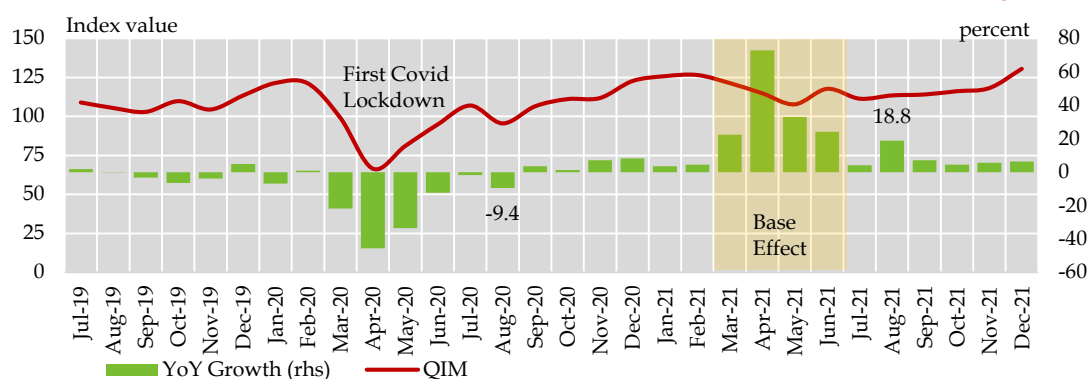
LSM Growth
percent, YoY**Table 2.5**

	wt.	H1		Q1		Q2	
		FY21	FY22	FY21	FY22	FY21	FY22
LSM	78.4	1.5	7.5	-2.6	9.7	5.5	5.5
of which:							
Textile	18.2	4.0	3.4	-1.9	6.5	10.1	0.6
Food	10.7	48.0	1.3	46.8	3.0	48.7	0.3
Coke & Petroleum products	6.7	3.9	0.7	1.5	6.1	6.3	-4.2
Chemicals	6.5	9.4	3.3	5.4	1.5	13.5	4.9
Chemical products	2.5	12.6	16.9	11.8	17.8	13.3	16.2
Fertilizers	3.9	7.6	-4.5	2.2	-7.3	13.6	-1.7
Wearing Apparel	6.1	-40.8	20.5	-44.8	20.3	-36.7	20.6
Pharmaceuticals	5.2	11.1	-5.0	13.1	4.7	9.4	-13.9
Non-Metallic Mineral products	5.0	14.8	1.8	17.7	1.2	12.4	2.3
Beverages	3.8	-4.2	4.5	-2.3	6.0	-6.7	2.3
Iron and Steel products	3.4	-12.1	18.4	-17.6	18.7	-6.5	18.1
Automobiles	3.1	3.4	69.4	-20.5	86.0	36.3	56.0
Tobacco	2.1	14.6	21.6	31.2	16.7	0.9	26.9
Electrical Equipment	2.0	-17.4	-2.6	-15.5	-3.7	-19.7	-1.2
Paper & Board	1.6	-2.7	8.3	-2.2	11.3	-3.2	5.5
Leather products	1.2	-42.4	6.1	-44.5	13.5	-40.5	-0.1

Source: PBS

The positive impetus of LSM was enabled by growth-inducing policies. The automobile sector benefitted from supportive fiscal and monetary policies. These included lower taxes and accommodative monetary policy

environment; the latter being particularly applicable during Q1-FY22. Similarly, the wearing apparel sector availed the concessionary financing schemes of the SBP such as TERF and LTFF, which was reflected

Monthly Quantum Index of Manufacturing (QIM)**Figure 2.7**

Source: Pakistan Bureau of Statistics

in the elevated growth and export of readymade garments. The steel sector's output also rebounded from last year, benefitting from the incentives provided to

the construction sector and higher PSDP spending during H1-FY22 compared to the same period last year.

Box 2.2: The Expanded Coverage and Impact of Rebased QIM

The Quantum Index of LSM (QIM) allows the changes in LSM to be measured on a monthly and cumulative basis. The PBS has recently rebased the QIM using the Census of Manufacturing Industries (CMI), 2015-16. A key objective of the rebasing exercise is that it captures the structural changes that inevitably take place in the manufacturing sector, as new types of industries emerge while others shrink in size and relative importance. Previously, the QIM was being computed from a total of 112 items with cumulative weight of 70.3 percent, derived from CMI 2005-06. After rebasing, the coverage of items has been expanded to 123, while the index weight has increased to 78.4 percent.

Items Included in Rebased QIM

Table 2.2.1

Name of item	Old Weight	New Weight	Change
<i>New Items</i>			
Garments	-	6.08	-
Terry towels & Bath robes	-	0.59	-
Furniture	-	0.51	-
Footballs	-	0.32	-
<i>Adjusted Categories after Addition of New Items (in Bold)</i>			
Wheat & Rice Milling	1.01	3.66	2.65
Sugar, Bakery products and Chocolate & sugar confectionery	3.54	3.43	-0.12
Juices, syrups, & squashes, and preserved milk	0.20	2.21	2.01
Soft drinks and Mineral waters	0.90	1.63	0.73
Corrugated paper/ paperboard containers			
weight has been added to: Paper and Paper products	2.31	1.63	-0.69
Electric Motors (including Insulated wire & cable)	0.71	0.43	-0.28
Pesticides: Weight has been distributed to Fertilizers		n/a	
Parts & accessories for motor vehicles:			
Weight has been distributed to Automobiles		n/a	

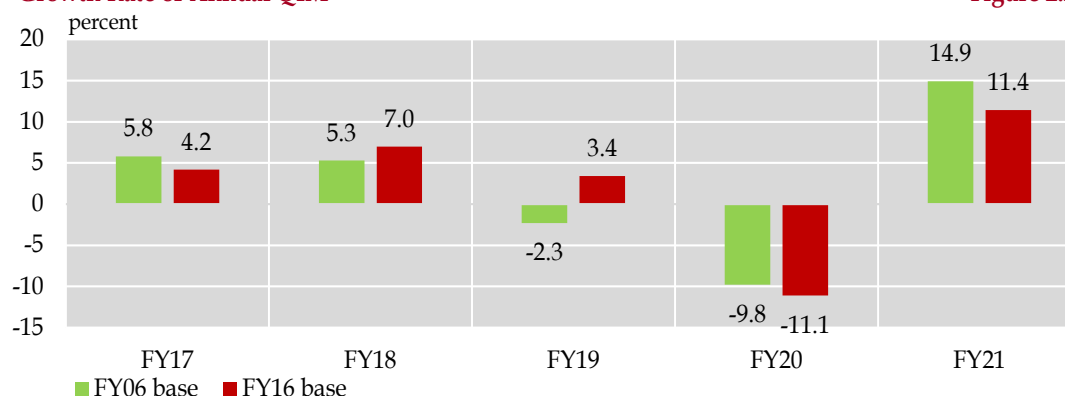
Source: PBS

Among the new items in the QIM, a notable addition is garments within the new category of *wearing apparel*, with a weight of 6.08 percent (Table 2.2.1). The PBS has used the export quantum of wearing apparel/ready-made garments, towels, furniture, and footballs as a proxy for LSM production.²⁵ This would allow the rebased QIM growth to be more representative. For industries like textiles in particular, the LSM growth estimated from 2005-06 base (largely capturing the low-value added segment) had at times been at odds with the growth in textile sector exports, particularly of value added items. The rebased QIM would help address this discrepancy.

²⁵ Other items, whose weight has been added to existing categories, include: bakery products and chocolate and sugar confectionery; rice milling; mineral water; preserved milk; corrugated paper/paperboard containers; pesticides; insulated wire and cable; and parts and accessories for motor vehicles.

Growth Rate of Annual QIM

Figure 2.2.1



Source: PBS

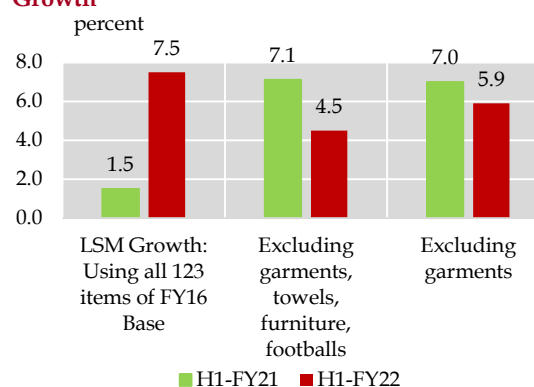
The coverage has also been improved by utilizing a new frame. The previous CMI was conducted using the frame of Labour and Industries departments, which was incomplete for some categories. By contrast, the Business Register of PBS utilized for CMI 2015-16, from which weights were ultimately derived for the QIM, is based on a broader array of administrative sources, such as the Securities and Exchange Commission of Pakistan, (SECP), Federal Board of Revenue (FBR), Employees' Old-Age Benefits Institution (EOBI), Pakistan Stock Exchange (PSX), and provincial labor and industries departments. As a result, the number of manufacturing establishments covered by 2015-16 CMI grew to 42,578, compared to 8,680 such establishments covered in 2005-06 – a nearly five-fold increase. Moreover, a substantial amount of data would now be collected from Balochistan as well as from Islamabad Capital Territory (ICT) based industries to update the QIM, as reflected in the province wise sample design of QIM. The PBS regional office Rawalpindi will collect data from ICT, whereas the Provincial Bureau of Statistics, Balochistan and Regional Office Karachi PBS will collect data from Balochistan.

Using the new base, the growth rate of LSM is higher in two of the past 5 years, namely FY18 and FY19 (Figure 2.2.1). However, the growth during FY21 is relatively lower using the new base. Rather, the rebasing suggests that the decline in LSM during FY20 – triggered by the initial, strict Covid lockdown – was sharper than previously estimated; similarly, the recovery during FY21 was somewhat lower compared to the estimates previously computed with the old QIM base.

Moreover, the impact of rebasing is evident from the performance of LSM during the current review period as well. Excluding the four new categories introduced in the rebased index – namely garments, towels, furniture, and footballs – changes the LSM growth significantly. Specifically, LSM then shows a slowdown, from 7.1 percent growth in H1-FY21 to 4.5 percent growth during H1-FY22 (Figure 2.2.2). In

Impact of New Items on LSM Growth

Figure 2.2.2



Source: PBS

fact, one heavy weight item of garments alone changes the picture significantly, given that it is proxied by the export quantum of readymade garments, which saw a sharp reversal during the two periods.²⁶

Automobile Industry

The automobile sector posted 69.4 percent growth during H1-FY22, compared to 3.4 percent in the same period last year. Tax relief measures for the automobile sector adopted in the FY22 Budget, an accommodative monetary policy maintained for most of Q1-FY22, broader pick-up in economic activities, workers' remittances, and improved farm incomes were among the primary factors driving the sector's growth during H1-FY22. Specifically, regarding tax relief in the Budget, the government reduced the federal excise duty (FED) on vehicles up to 3,000cc by 2.5 percent, cut the general sales tax for vehicles up to 1,000cc to 12.5 percent from 17.0 percent, and also allowed locally manufactured cars of 850cc or less to be exempted from value-added tax (VAT).

Furthermore, the accommodative monetary policy environment contributed to a flow of Rs 45.5 billion in auto loans during H1-FY22, compared to Rs 45.3 billion in the same period last year.²⁷

Within automobiles, car and jeep production responded favorably to the policy support. Specifically, the production of cars and jeeps grew by 72.4 percent during H1-FY22 compared to 5.1 percent growth in the same period last year, with significant expansion in the production of cars during both quarters of the current fiscal year (Table 2.6).

The positive momentum generated by aforementioned factors overshadowed the headwinds created by other policy measures and developments during the review period. Specifically, the SBP introduced restrictions

Automobile Sector Production

Table 2.6

Number of automobiles; YoY growth in percent

					Growth	
	FY21		FY22		FY22	
	Q1	Q2	Q1	Q2	Q1	Q2
All Cars	27,574	34,467	51,752	55,490	87.7	61.0
<800 cc	5,789	10,612	15,792	19,645	172.8	85.1
between 800-1000 cc	5,335	6,702	13,698	9,615	156.8	43.5
>1000cc	16,450	17,153	22,262	26,230	35.3	52.9
Jeeps/SUVs	1,655	2,452	3,653	3,137	120.7	27.9
Light commercial vehicles	3,708	5,090	6,790	7,426	83.1	45.9
Trucks	769	788	1,516	1,271	97.1	61.3
Buses	125	156	116	140	(7.2)	(10.3)
Tractors	11,258	12,129	12,533	14,412	11.3	18.8
Two/three wheelers	449,306	500,444	452,648	486,875	0.7	(2.7)

Source: PAMA

²⁶ In quantum terms, the exports of readymade garments grew by 20.4 percent during H1-FY22, compared to a 40.8 percent decline in the same period last year.

²⁷ Auto financing was more upbeat during Q1-FY22, before monetary tightening and revision of prudential regulations led to a moderation in Q2-FY22. For details, see Chapter 3.

on car financing from September 2021 to curb imports.²⁸ The policy rate was also increased by a cumulative 275 basis points between September to December 2021, raising, inter alia, the cost of auto financing. Moreover, the exchange rate depreciated by 10.7 percent during H1-FY22, while elevated raw material prices and freight charges pushed up manufacturing costs. These developments played a part in the automobile manufacturers' decision to raise prices during the review period, while the global semiconductor chip shortage also contributed to delayed deliveries of some models during H1-FY22.

Nonetheless, automobile demand and production remained robust. This was evident from the surge in imports of completely knocked down (CKD) and semi-knocked down (SKD) automobile kits during the review period (**Figure 2.8**).

Construction-allied Industry

The construction-allied sectors continued to benefit from the government's incentive package, as well as the promotion of the Mera Pakistan Mera Ghar scheme. The SBP augmented these efforts by prescribing mandatory targets for banks for the housing and construction finance in July 2020.²⁹ Resultantly, the flow of house building

finance rose to Rs 40.2 billion during H1-FY22, compared to Rs 6.4 billion in the same period last year. Finally, PSDP spending grew by 40.2 percent during H1-FY22 compared to a decline of 11.8 percent in the corresponding period last year, which tends to contribute to construction activity on large scale infrastructure projects.

Cement

The cement sector's output grew by 1.8 percent during H1-FY22, compared to 14.8 percent in the comparable period last year.

According to APCMA data, total cement dispatches declined by 4.1 percent during H1-FY22, compared to growth of 15.7 percent during H1-FY21. This mainly stemmed from a 32.5 percent decline in the quantum of cement exports during the current period amid elevated freight costs and reduced demand from Afghanistan, compared to a 14.7 percent increase last year.^{30,31} In fact, following positive contributions to overall growth of dispatches in 7 consecutive quarters from H2-FY18 to H2-FY21, the negative contribution of exports in the current fiscal year was the steepest since H1-FY16 (**Figure 2.9**).

On the other hand, local cement dispatches grew by 1.9 percent during H1-FY22,

²⁸ For details, see the SBP's press release titled 'State Bank of Pakistan revises Prudential Regulation for Consumer Financing to moderate import and demand growth', dated September 23, 2021.

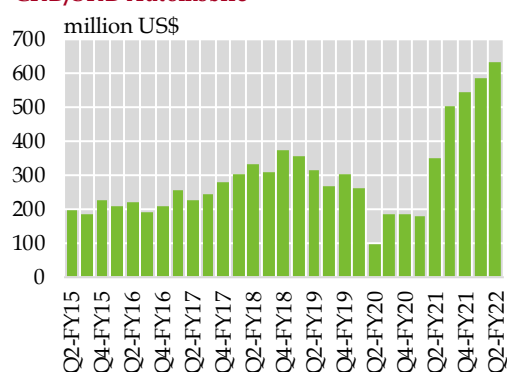
²⁹ For details, see SBP circular: IH&SMEFD Circular No. 10 of 2020 of 15 July 2020 and subsequent circulars on the subject.

³⁰ To put the impact of freight rates on cement exports into perspective, the Baltic Dry Index (BDI) – which tracks the price of transporting dry bulk cargo such as cement on bulk freighters – recorded an increase of 103.8 percent during H1-FY22, compared to a decline of 19.9 percent in the same period last year. This included a peak index value of 5,670 touched on 7th October 2021 – the highest level since September 2008. By extension, the surge in bulk freight rates is mainly attributed to a reopening of economies after the initial Covid-19 shock and lockdowns, which had caused the BDI to crash to 393 in mid-May 2020.

³¹ Specifically, cement exports to Afghanistan declined by 54.1 percent to 543,888 MT during H1-FY22, compared to 1,185,566 MT in the same period last year

Quarterly Imports of CKD/SKD Automobile

Figure 2.8



Source: PBS

compared to 15.9 percent in the same period last year. Within this, local dispatches to the South rebounded from a 13 percent decline during H1-FY21 to 15.2 percent growth in the current period. The rebound was aided by construction activities for development projects, such as the Karachi Transformation

Plan (KTP).^{32 33} By contrast, dispatches to the North witnessed a 0.3 percent decline during the half-yearly review period compared to 20.6 percent growth last year.

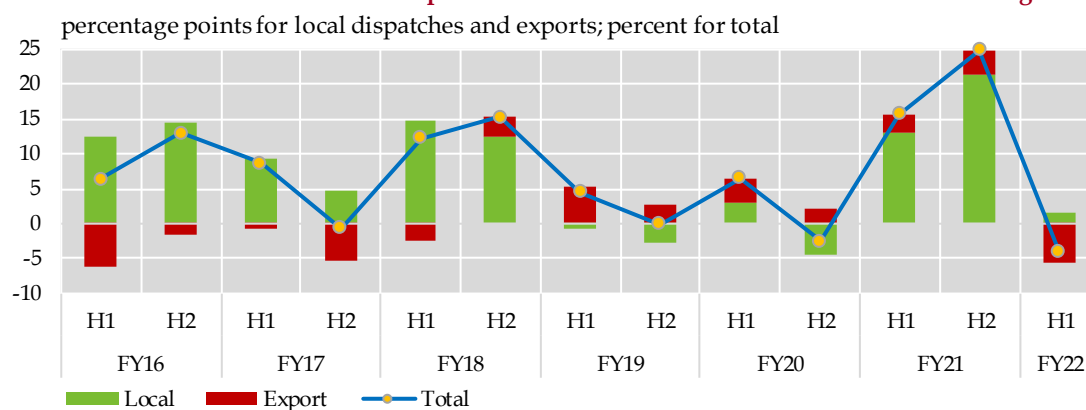
The slowdown in local dispatches was partly attributed to a significant increase in domestic cement prices. Specifically, the price of a 50 kg bag of cement rose by 21.3 percent in urban areas and 25.8 percent in rural areas during H1-FY22, compared to declines of 3.1 percent and 1.8 percent in the same period last year. The rising global prices of inputs such as coal coupled with exchange rate depreciation contributed to the upward pressure on cement prices.

Steel

The steel sector witnessed 18.4 percent growth during H1-FY22, compared to 12.1 percent decline in the same period last year.

Contribution to Growth of Cement Dispatches

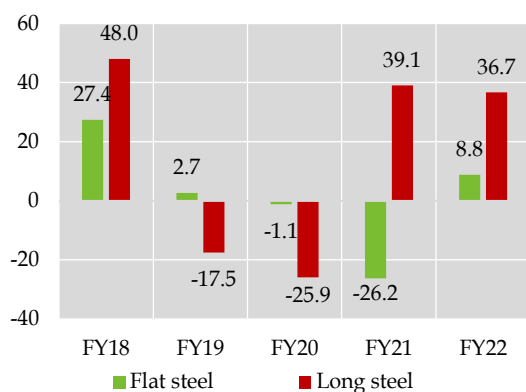
Figure 2.9



Source: APCMA

³² The KTP consists of large scale development projects such as Karachi Circular Railway and Greater Karachi Bulk Water Supply which would be developed over a period of three years, as well as fast-tracked revival of rivers and nullahs and development of roads and expressways scheduled for completion by June 2022. Source: Planning Commission, Annual Plan 2021-22.

³³ Some notable water sector development projects in the South mentioned in the Annual Plan 2021-22 include: Nai Gaj Dam, Sindh; Naulong Dam and Winder Dam, Balochistan; Rainee Canal, Sindh; and projects under the Southern Balochistan Package.

Growth in Steel Sector in H1 **Figure 2.10**

Source: PBS

The increase in steel production is partially a response to demand side factors. The demand for flat steel is attributed to robust growth of sectors such as automobiles (discussed earlier) and domestic appliances. Within appliances, the manufacture of refrigerators, deep freezers, and air conditioners grew by 41.5 percent, 13.8 percent, and 79.6 percent during H1-FY22, compared to 28.3 percent, -8.7 percent, and 32.3 percent last year, respectively. As a result, flat steel registered growth of 8.8 percent during H1-FY22, compared to a decline of 26.2 percent in the same period last year (**Figure 2.10**).

Meanwhile, the demand for long steel is associated with higher PSDP spending and infrastructure development, including dams (as mentioned earlier). Steel manufacturers had positioned themselves to meet the anticipated demand and have continued to undertake capacity expansion.³⁴ Moreover,

anecdotal evidence suggests that the large, graded steel manufacturers have recently been able to capture some market share from smaller firms by, inter alia, branding their graded rebars as superior products. Resultantly, the long steel segment posted 36.7 percent growth during H1-FY22, compared to 39.1 percent expansion in the same period last year.

Fertilizer Industry

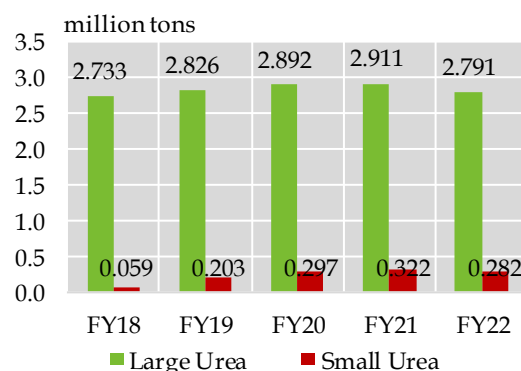
The fertilizer sector registered a decline of 4.5 percent during H1-FY22, compared to an expansion of 7.6 percent in the same period last year.

Urea production declined by 5.0 percent during H1-FY22, compared to a 1.0 percent contraction in the same period last year, according to NFDC data. For large urea producers, this mainly stemmed from temporary suspension for plant maintenance and upgrades; as a result, their production amounted to 2.8 million tons during H1-FY22, compared to 2.9 million tons in the same period last year (**Figure 2.11**). On the other hand, the production of small urea producers was affected by disrupted gas supply, particularly during Q1-FY22. This contributed to a 12.6 percent decline in their output, from 322,158 tons during H1-FY21 to 281,714 tons in the current period.

Meanwhile, production of fertilizers other than urea declined by 2.8 percent during H1-FY22, compared to growth of 54.8 percent in the same period last year.³⁵ Within this sub-

³⁴ Recent developments on capacity expansion include Agha Steels MicroMillDanieli (MiDa) plant and Mughal Steel's BMR of girder-rerolling mill. Source: Company financial reports for six months period ending 31 December 2021.

³⁵ Fertilizers other than urea produced domestically include Diammonium Phosphate (DAP), Calcium Ammonium Nitrate (CAN), Nitro Phosphate (NP), Single Superphosphate (SSP), and NPK fertilizer.

Urea Production by Large & Small Units, H1 **Figure 2.11**

Source: National Fertilizer Development Centre

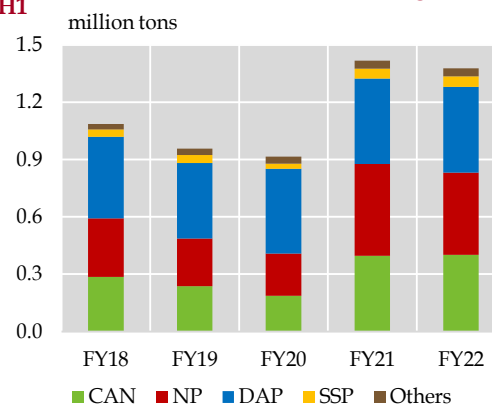
group, there was a marginal decline in production of NP fertilizer during H1-FY22 compared to the same period last year (Figure 2.12).

Wearing Apparel

The production of wearing apparel grew by 20.5 percent during H1-FY22, compared to a decline of -40.8 percent in the same period last year. This sector is a new addition to the LSM coverage, following the rebasing of the QIM.

The notable rebound in wearing apparel production is primarily attributed to strong demand in Pakistan's export destinations (see Chapter 5, discussion on exports of textile sector). Specifically, in value terms, the exports of readymade garments grew by 23.1 percent in H1-FY22, compared to 5.5 percent growth in the same period last year.

The development is also consistent with the expansions underway in the textile sector as the industry looks to achieve its US\$ 21

Fertilizer Production (except urea) H1 **Figure 2.12**

Source: NFDC

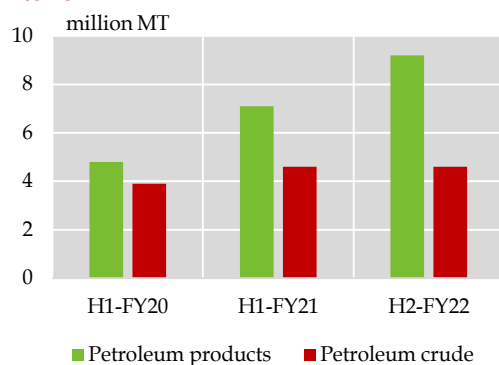
billion export target for FY22. Specifically, the imports of textile machinery amounted to US\$ 436.4 million during H1-FY22, which represented a historic high on half-yearly basis.³⁶ Furthermore, textile firms have also taken benefit of SBP's concessionary financing schemes to undertake fixed investment (see Chapter 3, discussion on credit to private sector).

POL

The POL sector's growth slowed down to 0.7 percent during H1-FY22, compared to expansion of 3.9 percent in the same period last year.

This can mainly be attributed to greater import of refined petroleum products relative to import of crude for domestic refining. Specifically, the import quantum of petroleum products grew by 29 percent to 9.2 million MT during H1-FY22, compared to 7.1 million MT in the same period last year (Figure 2.13). At the same time, quantum imports of petroleum crude declined by 0.7

³⁶ For reference, the last time textile machinery imports crossed the US\$ 400 million mark on half-yearly basis was back in H1-FY06, when they touched US\$ 417.9 million.

Import Quantum of Petroleum Items **Figure 2.13**

Source: PBS

percent during H1-FY22 compared to last year.

The increased import of refined products is linked to capacity issues. A number of oil refineries are still catching up to changing market dynamics and regulatory measures which require them to upgrade their plants and reconfigure production in favor of Euro-V compliant fuels and away from furnace oil.³⁷

Moreover, furnace oil (FO) production was affected by lower demand, particularly from IPPs during Q2-FY22. With IPPs refraining from buying FO from refineries, the latter faced an excess build-up of stocks, and some refineries suspended operations in the face of limited storage capacity.³⁸ As a result,

furnace oil production declined by 14.8 percent during Q2-FY22, compared to growth of 13.9 percent in the same period last year.

Another probable factor is that importing petrol from China has become lucrative for OMCs following its exemption from customs duty under the revised China Pakistan Free Trade Agreement (CPFTA). This would help explain why quantum imports of motor spirit from China recorded a more than five-fold increase, from 0.3 million metric tons (MMT) during H1-FY21 to 1.6 MMT during H1-FY22.^{39, 40}

Food

The food sector grew by 1.3 percent during H1-FY22, compared to 48.0 percent in the same period last year. Growth in the wheat and rice milling sub-sector had driven up overall food sector growth during H1-FY21, owing to an increase in the number of reporting units in the LSM survey (**Figure 2.14**). By contrast, this growth was more subdued during the current review period. Moreover, growth in the sugar subsector – the second largest component of the food sector in terms of weight – declined by 4.0 percent during H1-FY22, compared to 72.1 percent growth in the same period last year. This was mainly attributed to the relatively late start of the sugarcane crushing season

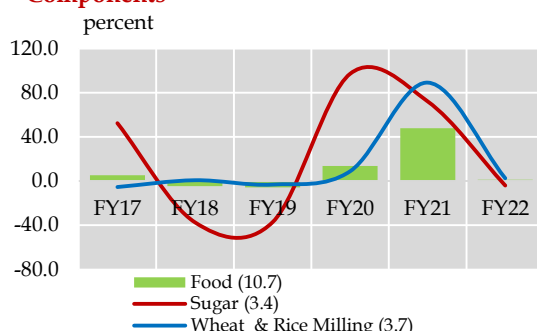
³⁷ For background, see Box 2.1 (Introduction of Ultra-Low-Sulfur-Fuel (ULSF) and its Implications for Domestic Automotive and Petroleum Industries) in the SBP's First Quarterly Report for FY21.

³⁸ For instance, Pakistan Refinery Limited (PRL) was shut down for 16 days in December 2021 due to reduced demand for high sulphur furnace oil since November 2021. Source: Pakistan Refinery Limited Half Yearly Report for December 2021.

³⁹ The share of motor spirit imports from China also increased significantly, from 7 percent during H1-FY21 to 33 percent during H1-FY22.

⁴⁰ The sharp increase prompted the government to initiate a probe in January 2022 into the potential misuse of the CPFTA for petroleum imports, with anecdotal evidence suggesting that some stakeholders might have engaged in questionable transfer pricing or over-invoicing.

Growth of Selected Food Sector Components* Figure 2.14



* The QIM weight of the Food sector and selected subsectors is given in parentheses

Source: PBS

during the review period compared to last year.

2.4 Services

The indicators for the services sector showed expansion in activities during H1-FY22 (Table 2.7). A significant increase in imports coupled with decent growth in the commodity producing sector is indicative of a positive effect on wholesale and retail trade. The transport sector also benefited from the increase in economic activity during the period. Moreover, indicators of banking sector and communication sector point to growth in these industries.

The proxy indicators of the *wholesale and retail trade* segment point to growth in the sector. This was achieved on the back of improvement in the crop sector output during *Kharif* FY22. Record output of cash crops – rice and sugarcane – and increase in cotton production indicates strong growth in crop sector during *Kharif* FY22. In the industrial sector, LSM sector growth remained robust, driven mainly by

automobile, steel and wearing apparel industries. In addition, the flow of private sector credit to the sector rose sharply during the period to Rs 55.4 billion in H1-FY22 compared to Rs 30.2 billion last year. Meanwhile, growth in revenues of FMCG (fast moving consumer goods) firms remained robust during H1-FY22. Sales of FMCG firms rose by 19.9 percent during H1-FY22 compared to 20.3 percent growth last year.⁴¹

The *transport and storage* sector indicators also suggest an uptick in growth. Increase in sales of vehicles, such as trucks and tractors, show that commercial activities picked up during H1-FY22 compared to last year. This was further evidenced by increase in quantum of petroleum sales for road transport, which increased by 11.2 percent during H1-FY22 compared to last year. Similarly, sales of petroleum products to aviation and railways also expanded by 46.4 and 9.4 percent respectively during H1-FY22 compared to last year. The increase in domestic energy sales to aviation industry was more noticeable for private sector airlines, as evident from a 74.9 percent jump during H1-FY22 compared to last year's sales.

Within the *information and communication* sector, demand for cellular services remained robust during H1-FY22. This may be attributed to increased reliance on remote-working under smart lockdowns, online education, and continued rise of e-commerce in the country. Inclusion of Pakistan to the seller list of Amazon, a leading global e-commerce firm, may have also played a positive role in aiding the e-commerce

⁴¹ Based on a sample of 23 FMCG firms in the country.

Services Sector Indicators

Table 2.7

	FY21			FY22		
	Q1	Q2	H1	Q1	Q2	H1
Wholesale and Retail Trade						
Sectoral credit off take*- flow (billion Rs)	17.7	12.5	30.2	21.5	33.9	55.4
Imports (billion US\$) ^a	11.3	13.2	24.5	18.7	22.1	40.8
<i>Growth</i>	0.8	9.8	5.4	65.8	68.0	67.0
LSM (YoY growth)	-2.6	5.5	1.5	9.7	5.6	7.5
Agriculture credit (disbursements – Rs bln)	254.6	362.3	616.9	291.9	348.9	640.8
FMCG sales (YoY growth)	22.7	18.0	20.3	21.0	18.8	19.9
Transport & Storage						
POL sales to transport sector (million MT)	3.7	4.1	7.9	4.4	4.4	8.8
<i>Growth</i>	7.9	10.2	9.1	17.0	6.0	11.2
Commercial vehicle sales (units)	6,618	7,677	14,295	12,330	11,272	23,602
<i>Growth</i>	32.4	18.3	24.4	86.3	46.8	65.1
Teledensity (%)	79.6	82.3	82.3	86.2	87.1	87.1
Broadband users (million)	87.0	93.0	93.0	107.6	109.6*	109.6*
Finance and Insurance Activities**						
Assets (billion Rs)***	23,808	25,124	25,124	28,790	30,058	30,058
Deposits (billion Rs)***	17,543	18,519	18,519	20,516	21,720	21,720
ROA (percent)	1.1	1.0	1.0	0.9	1.0	1.0
ROE (percent)	14.8	13.8	13.8	13.7	14.1	14.1
Profit after tax (billion Rs)	68.7	49.6	118.3	68.7	72.7	141.4
Infection ratio	9.9	9.2	9.2	8.8	7.9	7.9
General Government Services						
Expenses-general govt & defense**** (billion Rs.)	313.4	368.6	682.0	351.2	379.2	730.4

*Data for Nov 2021 **Banking sector only ***Stocks, as of end-December 2021 ****Only federal government

Source: SBP, ^a PBS, OCAC, PAMA, PTA and MoF

industry.^{42,43} The indicators of telecom industry, such as teledensity and number of subscribers, also highlight positive trends in the sector. Further evidence of increased activity in this sector can be seen from ICT exports, which increased to US\$ 1.3 billion during H1-FY22 compared to US\$ 1.0 billion last year (**Figure 2.15**). This was largely on the back of export of software and software consultancy services.

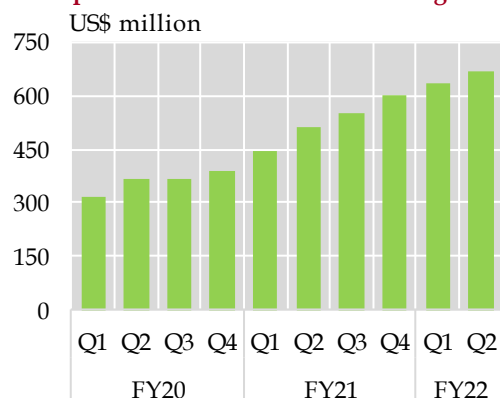
The *finance and insurance* sector performance as proxied by indicators presented in **Table 2.7** suggests growth in the industry. The profit of the financial sector rose by 46.6 percent to Rs 72.7 billion during H1-FY22. The profits rose as a result of lower provisioning/debt write-off expense and increase in non-interest income during the period. In addition, the infection ratio, which had grown previously in the midst of Covid-

⁴² Source: Ministry of Commerce

⁴³ Trade Development Authority of Pakistan (TDAP) and Small and Medium Enterprise Development Authority (SMEDA) started offering training courses to interested individuals and businesses in becoming a seller on Amazon.

ICT Exports

Figure 2.15



Source: State Bank of Pakistan

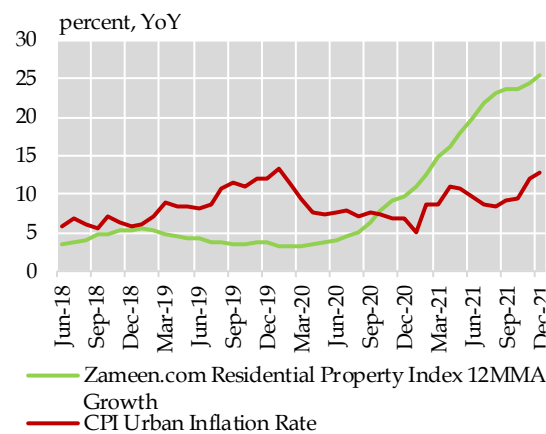
induced monetary stress, continued to decline during H1-FY22.

The price index of residential property from Zameen.com suggests that the activity in *real sector services* picked up considerably during H1-FY22. Average property prices rose on average by 25.4 percent during H1-FY22 as opposed to 7.1 percent last year. This increase in price of residential property was more than the overall inflation during the period (**Figure 2.16**). There were both supply side and demand side factors at play that led to escalation in prices. Increase in prices of building materials – such as cement, steel, aluminum, sanitaryware, etc were, however, partially offset by incentives offered by the government to real estate developers. Depreciation of PKR and increase in the global commodity prices were the major factors behind rise in cost. Prices of construction inputs rose by 11.4 percent YoY in December 2021 compared to 3.7 percent last year.⁴⁴

Increased access to mortgage under the SBP's *Mera Pakistan Mera Ghar* scheme coupled

Growth in Prices of Real Estate

Figure 2.16



Source: Zameen.com

with relatively low mark-up rates also aided in demand for property which in turn also caused prices to rise. It is evident from increase in house building finance which rose to Rs 40.2 billion during H1-FY22, compared to Rs 6.4 billion in the same period last year.

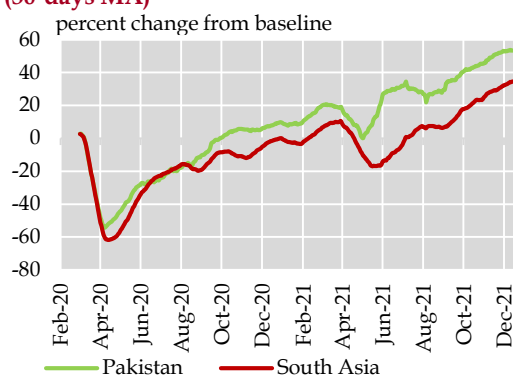
On the demand side, easy access to bank credit, low interest rates (especially during Q1-FY21), spillover of healthy economic growth during FY21 and higher inflow of remittances filtered into domestic demand for real estate. Moreover, real estate consumers view investment in the sector as a store of value and alternative investment in times of high inflation and this phenomenon may also have contributed to increase in demand.

Google community mobility indicators also suggest growth in the services sector during H1-FY22 compared to last year. Visits to grocery-and pharmacy-stores, retail-and-recreation, transit-stations, and workplaces increased. The performance of Pakistan was

⁴⁴ Source: PBS

Google Mobility Changes in Pakistan vis-a-vis South Asia (30-days MA)

Figure 2.17



Source: Covid-19 Community Mobility Report

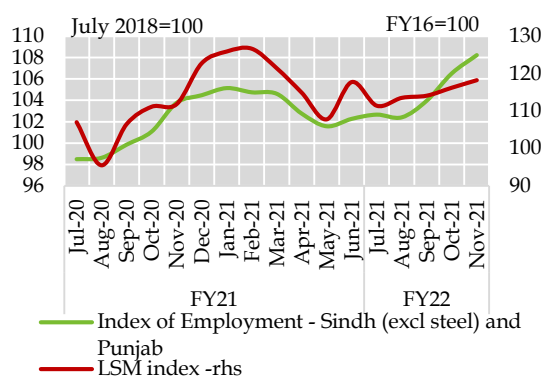
relatively better than South Asia's regional average, and this may have also helped generate activity in the services segment (Figure 2.17).

2.5 Labor Market

Indicators of the labor market in Pakistan point to growth during H1-FY22. This upward trend was gauged on the basis of industrial employment data, SBP surveys, and PBS wage/fees data. The industrial sector hired more workers in both Punjab and Sindh as output expanded. Meanwhile, SBP Business Confidence Survey (BCS) highlighted relative improvement in sentiments towards employment creation during H1-FY22; however, deterioration in perceptions about job growth was witnessed in SBP Consumer Confidence Survey (CCS) during the period. The wages of construction sector laborers and fees charged by various professionals in the services sector point to growth, albeit the growth in wages and fees charged was varied.

Combined Punjab and Sindh Industrial Employment and

Figure 2.18



Source: Bureau of Statistics, Punjab, Bureau of Statistics Sindh and PBS

Industrial Employment

As measured by the index of industrial employment for the provinces of Punjab and Sindh, employment rose by 4.3 percent during Jul-Nov FY22 compared to 2.6 percent last year (Figure 2.18). Sindh accounted for significantly more hiring during the period with pharmaceutical sector contributing with major share towards the overall growth. Cotton textile industry was another noteworthy contributor to job growth, with both the regions hiring more workers.

Punjab

Overall, industrial sector hired more workers in Punjab during H1-FY22 compared to last year (Table 2.8). Employment in the sector, as gauged through *Monthly Survey of Industrial Production & Employment*, increased by 1.6 percent during the Jul-Nov period compared to 1.5 percent last year.

This growth was predominantly driven by export-oriented industries.

Demand for workers in the textile and wheat milling industry remained robust during the period, albeit at a slower pace. On the other

hand, job creation in leather footwear and cement rebounded sharply in H1-FY22. Meanwhile, though sugarcane crop output is likely to be better than last year, the upstream sugar mills hired less workers during H1-FY22.

Increase in workers in the textile industry reflects the expansion in output of the sector that grew by 4.3 percent during Jul-Nov FY22 compared to 2.8 percent growth last year. Moreover, increase in exports of wearing apparel and in its production also had a positive impact on the downstream textile and ginning sectors, which may also have contributed to increase in job openings in the sector.

Employment in the leather industry rebounded sharply during Jul-Nov FY22. The jump was notable in the footwear sub-category as average number of employees registered an increase of 2,044 compared to a decrease of 1,550 workers last year. This coincides with increase in footwear production which expanded by 19.4 percent during Jul-Nov FY22 compared to a decline of 43.5 percent last year.

The decrease in employment in sugar industry in the province can be attributed to late start of crushing season in FY22. This led to less seasonal workers being hired by the mills. This was in contrast to last season when the Punjab government's drive to urge sugar mills to start crushing earlier may have contributed to job creation during the period.

Sindh

Latest data on industrial employment in Sindh shows that the firms hired 11.9 percent more workers during Jul-Nov FY22 compared to 0.6 percent layoffs last year. The

Average Number of Industrial Workers Hired/Fired during Jul-Nov

Table 2.8

	FY21	FY22
Punjab	4,290	4,423
Cotton textiles	2,150	1,434
Wheat milling	1,282	1,265
Sugar	5,267	-900
Leather footwear	-1,550	2,044
Cement	-607	447
Pharmaceutical	264	19
Automobile	1	5
Sindh*	-955	13,152
Cotton textiles	-1,326	3,797
Sugar	-1,621	3,732
Leather tanning	728	92
Cement	448	-2,493
Pharmaceutical	411	9,791
Automobile	796	-4,054

*Excluding the steel industry

Source: Bureau of Statistics, Punjab and Bureau of Statistics, Sindh

impetus to growth came largely from the pharmaceutical sector that hired more staff to meet both the domestic and foreign demand for its products (Table 2.8).

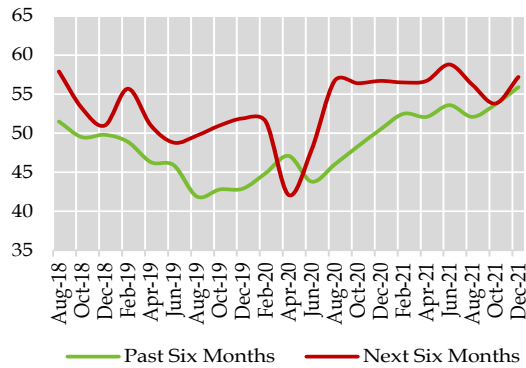
Similar to Punjab, the textile sector also played a part in employment growth during Jul-Nov FY22 period. Meanwhile, the automobile and cement industry lost more workers during the Jul-Nov FY22 period. In the former case, two factors may be at play: lower localization of parts, and shortage of semiconductor chips. In the case of cement, a decrease in foreign demand, owing partly to an increase in freight costs, hampered growth of the cement producers in the south, which led to layoffs in the province.

SBP Confidence Surveys

The results of the SBP-BCS conducted in January 2022 point to optimism in the past and future perceptions, whereas the outcome

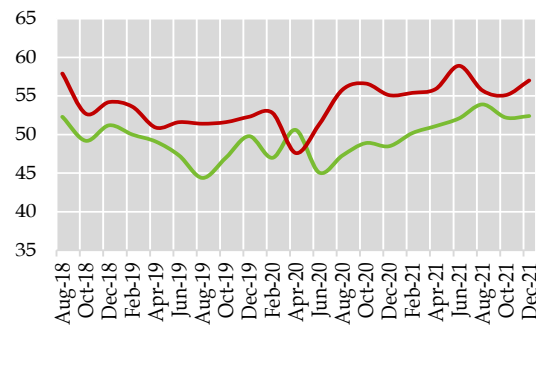
BCS Employment Index for Industrial Sector

Figure 2.19a



BCS Employment Index for Service Sector

Figure 2.19b



Source: State Bank of Pakistan

of the SBP-CCS highlighted deteriorating expectations about the domestic labor market.⁴⁵ After witnessing deterioration in the August 2021 and October 2021 rounds of the bimonthly BCS when the country was going through its 4th Covid wave, future expectations about the domestic labor market improved markedly in the subsequent December 2021 cycle (**Figures 2.19a & b**). Meanwhile, perceptions about the past 6 months worsened only in August 2021, whereas in the following rounds the businesses were optimistic about employment creation.

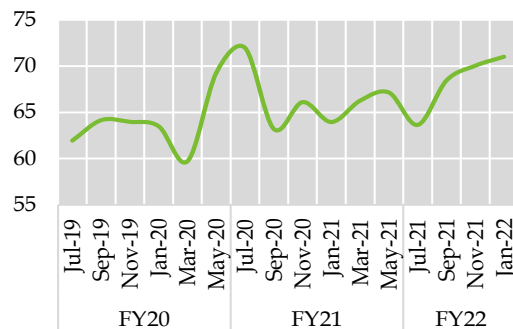
In terms of sectoral analysis of the SBP-BCS, businesses in the manufacturing sector were more optimistic about employment growth than the services sector. Perceptions about the job market remained broadly optimistic in H1-FY22 rounds of the BCS for the industrial sector. However, the services sector showed mixed trend, as perceptions about employment remained rather dull as gauged by past 6-month diffusion index

while the businesses were more optimistic about job openings in the next 6 months.

On the other hand, the result of the CCS, capturing the responses of consumers, about the prospects about job market were not favorable (**Figure 2.20**). Consumers were not optimistic about employment creation in the

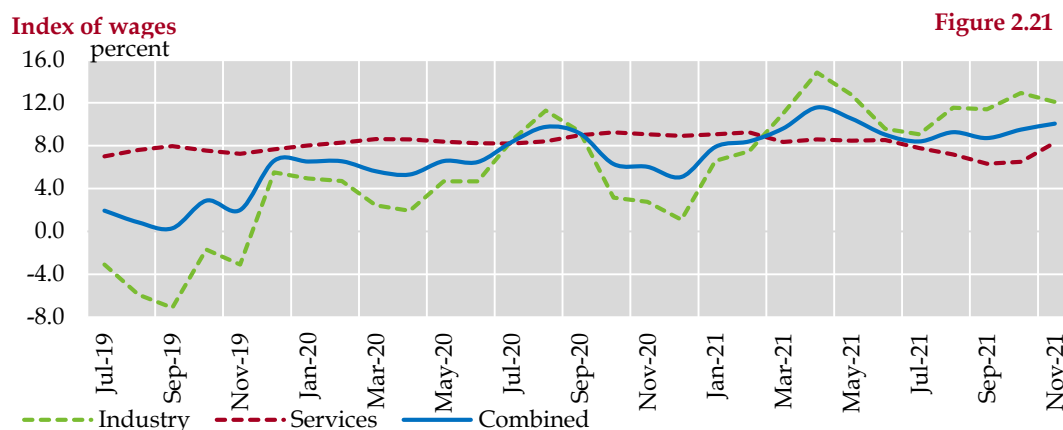
Future Unemployment Index (Next Six Months) - SBP CCS

Figure 2.20



Source: SBP

⁴⁵ The survey results of BCS and CCS are presented in Diffusion Index (DI) format, which varies between 0 and 100. The DI can be interpreted as follows: DI < 50 indicates that positive views regarding credit/availability of funds/ borrowing cost are less than the negative views; DI = 50 shows that positive views are equal to negative views; and DI > 50 indicates that positive views are more than negative views.



Source: Pakistan Bureau of Statistics, Bureau of Statistics -Punjab

country as future unemployment index continued to climb.⁴⁶

Wages

As estimated by index, domestic wages showed an increasing trend during Jul-Nov FY22.⁴⁷ On average, the overall remuneration rose by 9.2 percent during the Jul-Nov FY22 period compared to 7.9 percent growth last year (**Figure 2.21**). That said, salaries in the

industrial sector rose more than in services. Whereas the growth in wages is apparently impressive, analysis of real wage shows that the purchasing power of the domestic workforce had declined slightly over the past 4 years.

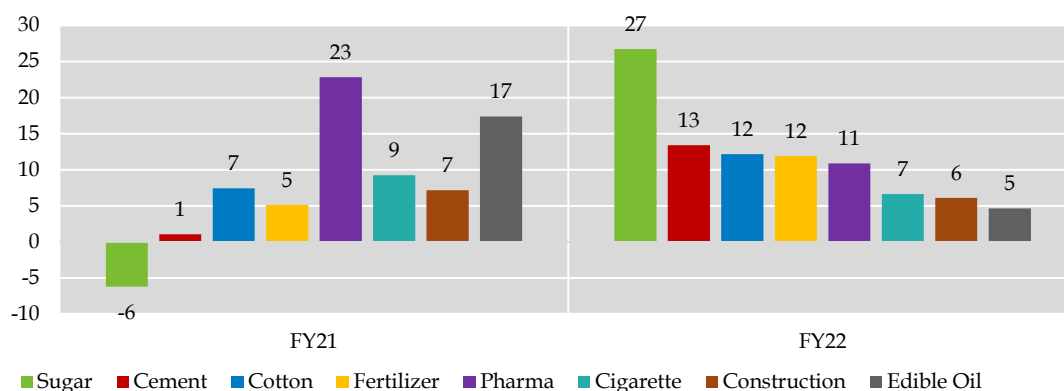
Wages in the industrial sector increased by 11.4 percent during Jul-Nov FY22 compared to 7.0 percent last year. Analysis of industries covered shows that impetus to growth came

⁴⁶ The deviation between consumer and business expectations about economic conditions is not a new phenomenon and may be key to macroeconomic dynamics, according to Mankiw *et al* (2003). Despite sharing the same available set of information, expectations across economic agents varies; the amount of disagreement can be large and varies over time, and some people form expectations based on outdated information. (Source: N.G. Mankiw, R. Reis and Justin Wolfers (2003). *Disagreement about inflation expectations*. NBER Chapters. NBER Macroeconomics Annual 2003, Volume 18, pages 209-270. Massachusetts, NBER.)

⁴⁷ For monthly analysis of wages in Pakistan, an indicative nominal wage rate index is calculated based on available data on wages in the industrial and services sector. For the industrial sector, data on wages in some LSM sectors was available for Punjab (Cotton, Edible Oil, Cement, Fertilizer, Pharma, Sugar and Cigarette) from Monthly Survey of Industrial Production and Employment in the Punjab, a Bureau of Statistics publication. For the construction sector (part of industrial sector) and services sector wages (Tailoring, doctor clinic fee, dental services, hospitals services, mechanical services, household servant, cleaning and laundering, garbage collection, personal grooming services), monthly price survey data released by PBS was used. The wages of these 17 sub-groups were used to form a wage index using FY16 as the base year, which is the same for CPI. For the general price level, CPI is the most comprehensive index available on a monthly frequency.

Growth in Wages of Industrial Sector

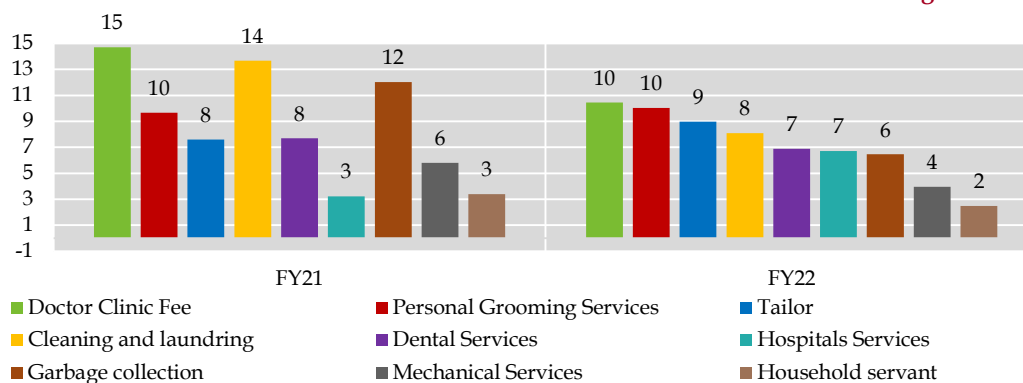
Figure 2.22



Source: Pakistan Bureau of Statistics, Bureau of Statistics -Punjab

Growth in Wages of Services Sector

Figure 2.23



Source: Pakistan Bureau of Statistics

from sugar, cotton, pharmaceutical and cement industries, whereas growth in the edible oil, fertilizer, construction and cigarette industries was rather subdued (Figure 2.22).

Available wage rate data for various occupations in the services sectors suggests that growth remained lackluster during Jul-

Nov FY22. The index of services sector remuneration rose by 7.2 percent during the period compared to 8.8 percent growth last year. Fees charged by doctors, personal grooming services and tailors were higher than those charged by mechanics and household servants (Figure 2.23).

3 Monetary Policy and Inflation

On account of rising inflation and current account deficits during most of the H1-FY22 fueled by the sharp rise in global commodity prices, SBP raised the policy rate cumulatively by 275 basis points to 9.75 percent. To contain the monetary expansion, SBP also took targeted measures by increasing the cash reserve requirements for commercial banks by 100 bps, further tightening the regulatory regime for consumer financing and imposing cash margin requirements on import of additional 114 items. Growth in money supply, though at an elevated level, slightly moderated in the H1-FY22, owing to a decline in the NFA of the banking system. Credit to private sector, however, registered a strong off-take during the period. This was mainly because of high commodity prices that increased the borrowing needs of some business sectors such as textile, iron and steel. In addition, uptick in production and trading activity and SBP's concessionary financing schemes (LTFF and TERF) also drove the demand for credit. National CPI inflation, in the meantime, followed an upward trajectory in the H1-FY22, with both urban and rural baskets accelerating the national CPI in the Q2-FY22. While the food group, non-perishable food items in particular, remained the main contributor, the steep rise in energy prices along with increased core inflation also intensified the inflationary pressures during Q2-FY22.

3.1 Policy Review

Global commodity prices super-cycle characterized by post-pandemic rise in demand, particularly the increase in petroleum prices, impacted domestic inflation out-turns and worsened current account deficit in H1-FY22. These increasing pressures, therefore, warranted vigilant policy actions.

With respect to the balance of payments, persistently high international commodity prices together with increased domestic economic activity continued to widen the current account deficit. On the other hand, headline inflation rose to 9.8 percent in H1-FY22 compared to 8.6 percent in year-ago period largely stemming from the strengthening of inflationary pressures in Q2-FY22 both in terms of magnitude and in terms of dispersion. Number of items with double digit started increasing Q1-FY22 onwards (Figure 3.1).

In particular, disaggregated analysis suggests that inflation not only was higher on a YoY basis during Q2-FY22, but MoM outturns also remained high on a sequential basis,

indicating significantly rising inflation momentum. Three factors largely explained the surge in inflation. First, in response to rising global commodity prices, administered prices (of petrol, electricity and LPG) were adjusted upwards; not only did this inflate the energy component of the CPI, but it also escalated transport services expenses. The rise in electricity tariffs also reflected upward adjustments under the government's circular debt management plan. In addition, rising global commodity prices also built inflationary pressures in imported edible items (such as edible oils, pulses etc.) as well

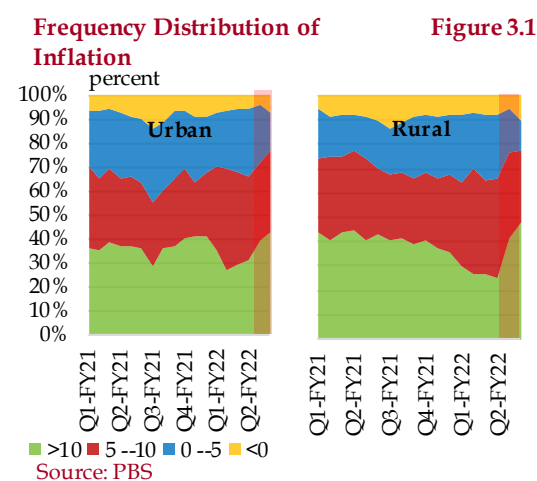


Figure 3.1

as industrial inputs (such as metals, cotton, paper etc.). Second, core inflation, which had previously remained within the range of 6 to 7 percent, began to rise, reflecting domestic demand pressures. Finally, house rents posted a significant YoY increase during Q2-FY22 due to base effect, which increased H1-FY22 house rent to 6.3 percent. With the given broad-based inflationary pressures, the inflation forecast range for FY22 was also revised upward from 7-9 percent to 9-11 percent.

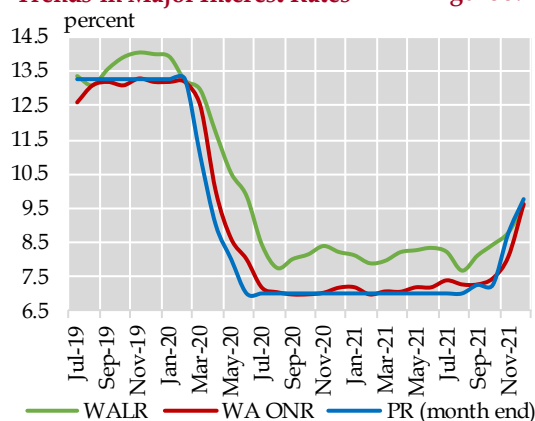
In the same vein, another important concern from the monetary policy perspective was the deterioration in the current account deficit despite strong exports and workers' remittances. The current account deficit numbers had been larger than expectations in October 2021 and November 2021, stemming mainly due to the sharp rise in global commodity prices together with increased domestic demand.

Meanwhile, domestic economy activity continued its momentum in the Q1-FY22. High-frequency demand indicators, including electricity generation, cement dispatches, sales of FMCGs and petroleum products registered positive growth.¹ Similarly, large-scale manufacturing (LSM) continued to gain further traction, reflective of the ongoing positive momentum in the economic activity.² However, with the ongoing economic activity, real money supply growth remained at an elevated level, although slightly less than last year and decelerating sharply in Q2.

Taking stock of these developments, in particular the faster than expected shift in risks away from growth toward inflation and the current account, the Monetary Policy Committee (MPC) increased the policy rate by cumulative 275 bps in H1-FY22.

Following the beginning of the tightening cycle in September 2021 with rate increase of 25 basis points, the policy rate was increased further by 150 bps in November 2021 and by 100 bps in December 2021 (**Figure 3.3**). The MPC was of the view that this would achieve sustainable economic growth, by countering inflationary pressures and ensuring sustainability of the current account. Importantly, Pakistan was not an exception as major central banks also tightened monetary policy during the second half of 2021 to keep the inflation expectations anchored (**Box 3.1**). However, Pakistan was among the countries that proactively opted to normalize the Monetary Policy to contain inflation and anchor expectations. In addition, in November's meeting, it was

Trends in Major Interest Rates **Figure 3.2**



Source: State Bank of Pakistan

¹ The cumulative sales of 23 listed FMCG companies grew by 19.9 percent in H1-FY22 compared to 20.3 percent same period a year ago. POL sales registered an increase of 12.1 percent during H1-FY22 over and above 11.0 percent growth last year, whereas cement sales maintained last year's multiyear high level of domestic dispatches of around 24.1 million tons during H1-FY22.

² LSM rose by 7.4 percent in H1-FY22 compared to 1.5 percent same period last year.

decided to increase the frequency of monetary policy reviews from six to eight times a year in continuation of efforts to make the process of monetary policy formulation more predictable and transparent in line with international best practices.

In addition to changes in the policy rate, some other specific measures were also taken to counter emerging demand pressures. First, the average Cash Reserve Requirement (CRR), to be maintained during a period of two weeks by scheduled banks, was increased from 5 percent to 6 percent and minimum CRR to be maintained each day from 3 percent to 4 percent. Second, Prudential Regulations (PRs) for consumer financing were tightened. Third, 100 percent cash margin requirement was imposed on the import of additional 114 items, leading to

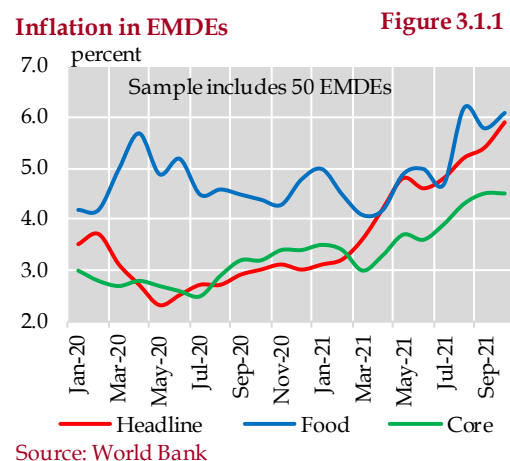
slower import growth and thus supporting the balance of payments position.³

Thus, with the increase in the policy rate during H1-FY22, weighted average overnight rates as well as weighted average lending rates registered an increase of almost the same magnitude; however, the impact was more pronounced in Q2-FY22. Consequently, in response to both policy rate and revised PRs, consumer financing registered 16.2 percent decline in Q2-FY22 compared to Q1-FY22 particularly on account of auto, personal and consumer durable groups. However, overall credit to the private sector registered strong off-take during the quarter primarily because of a rise in working capital demand stemming from higher commodity prices. In addition to cost pressures, uptick in activity in some sectors such as textiles also raised working capital requirements.

Box 3.1: Inflation and Monetary Policy Response in EMDEs

Inflationary pressures across the globe have strengthened at a faster than expected pace during the past few months. Emerging market and developing economies (EMDEs) have observed broad-based increases in inflation since mid-2020, however, the rise has been steeper since July 2021 (Figure 3.1.1). Generally, rising inflation is attributed to pandemic-related supply-demand gaps and higher commodity prices and pick-up in demand compared to last year.⁴ In some economies, exchange rate depreciation also led to higher prices of imported products.

Increase in inflation has been broad based across countries as well as components. For instance, around four fifths of EMDEs – mainly in Europe and



³ The changes in the PRs effectively prohibit financing for imported vehicles. They also tightened regulatory requirements for financing domestically manufactured/ assembled vehicles of more than 1000 cc engine capacity and other Consumer Finance facilities like personal loans and credit cards.

⁴ "World Economic Outlook", October 2021, International Monetary Fund.

Central Asia (ECA), Latin America and the Caribbean (LAC), and Sub-Saharan Africa (SSA) registered higher inflation in 2021. In terms of components, a rise in inflation was registered across food, energy and core groups (**Figure 3.1.1**). In particular, around one third of EMDEs observed double-digit food inflation in 2021.⁵

In order to address inflationary pressures and ensure that inflation expectations remain anchored, multiple EMDEs have tightened monetary policies in recent months (**Figure 3.1.2**) after a substantial amount of fiscal support and monetary stimulus provided to combat pandemic-related challenges.

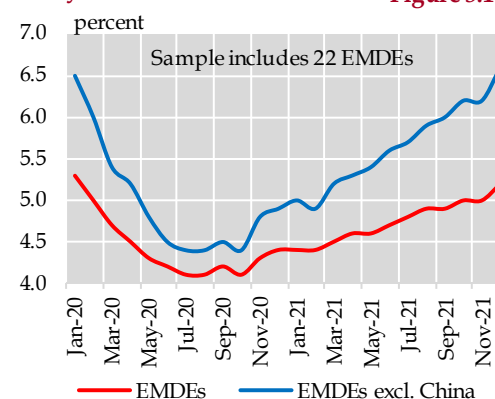
3.2 Monetary Aggregates

The broad money growth slowed to 4.3 percent during H1-FY22 compared to 5.6 percent during the same period last year. The entire growth in the money supply came on the back of the expansion in the net domestic assets of the banking system that posted an increase of Rs 1,274.9 billion during H1-FY22 compared to an expansion of Rs 584.0 billion in the same period last year. Meanwhile, part of this impact was offset by a Rs 227.5 billion contraction in the Net Foreign Assets (NFA) in comparison to an increase of Rs 578.8 billion during H1-FY21 (**Table 3.1**).

Within NDA, the bulk of the increase came from the private credit off-take that clocked in at Rs 1,043.1 billion during H1-FY22 compared to an increase of Rs 343.5 billion in the corresponding period last year. This was mainly driven by high input prices and elevated levels of domestic economic activities. Other factors that contributed towards expansion of the NDA include higher credit offtake by PSEs compared to the same period last year and lower retirements by the commodity procurement agencies. Cumulatively all of these factors

Policy Rate in EMDEs

Figure 3.1.2



Source: World Bank

more than offset the impact of deceleration in the government budgetary borrowings from the banking system which fell to Rs 246.8 billion in H1-FY22 compared to 437.3 billion in H1-FY21.

Meanwhile, NFA of the banking system posted a contraction in the two consecutive quarters of FY22. Cumulatively, during the H1-FY22 the NFA fell by Rs 227.5 billion compared to an expansion of Rs 578.8 billion in the same period last year. This contraction was mainly on account of SBP's NFA that fell by Rs 219.6 billion during H1-FY22 against an increase of Rs 345.5 billion in H1-FY21. This reflects the impact of the deterioration in the current account balance owing to the widening trade deficit. Likewise, the NFA of commercial banks also fell slightly by Rs 8.0 billion compared to an increase of Rs 233.3 billion in the corresponding period last year.

On the liability side, currency in circulation increased by Rs 69.7 billion in H1-FY22 compared to an increase of Rs 64.5 billion in H1-FY21, while the commercial bank

⁵ "Global Economic Prospects", January 2022, World Bank.

Monetary Aggregates^P**Table 3.1**

flow in billion Rupees

	FY21			FY22		
	Q1	Q2	H1	Q1	Q2	H1
M2 (A+B)	260.5	902.3	1,162.7	149.5	897.9	1,047.3
A. NFA	307.3	271.5	578.8	-32.8	-194.7	-227.5
B. NDA	-46.8	630.8	584.0	182.3	1,092.6	1,274.9
Budgetary borrowing*	285.2	152.1	437.3	76.7	170.0	246.8
SBP	-281.9	-304.0	-585.9	-212.7	185.1	-27.6
Scheduled banks	567.1	456.0	1,023.2	289.5	-15.1	274.4
Commodity operations	-59.9	-19.4	-79.3	9.5	-24.1	-14.6
Private sector credit	-76.6	420.1	343.5	226.4	816.7	1,043.1
PSEs	-11.9	-17.4	-29.3	11.6	55.5	67.1
Other items net	-184.7	91.7	-92.9	-141.5	70.8	-70.7
Reserve money	-149.0	160.8	11.7	-195.9	236.7	40.8
Currency in circulation	-40.4	104.9	64.5	111.6	-41.9	69.7
Deposits	289.3	792.5	1,081.8	35.6	924.0	959.6

P: provisional

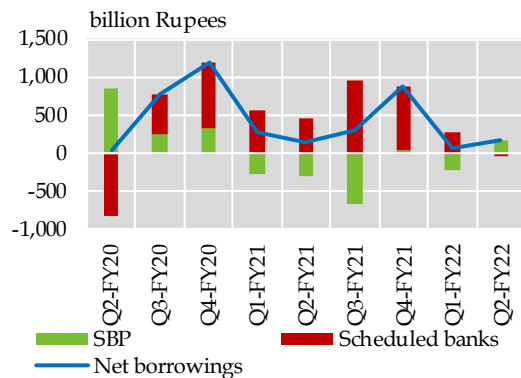
Source: State Bank of Pakistan

deposits increased by Rs 959.9 billion during H1-FY22 compared to an increase of Rs 1,081.8 billion in the same period last year. This brought the currency to deposit ratio down to 38.2 percent – the lowest level since December 2018. This uptick in the deposit mobilization can be attributed to a cumulative 275 bps increase in the policy rate during H1-FY22 and removal of the withholding tax on the banking transactions for persons not appearing in the active taxpayers' list as well with effect from July 1 2021. This was also reflected in the composition of customer deposits. Remunerative deposits of customers increased by Rs 861.6 billion during H1-FY22 compared to Rs 603.4 billion in the same period last year. Meanwhile, with an increased opportunity cost of holding cash in non-remunerative accounts, the customers' non-remunerative deposits increased by Rs 222.2 billion in H1-FY22 compared to Rs 333.0 billion last year.

Government borrowings

The budgetary borrowings from the banking system fell to Rs 247.0 billion during H1-FY22 compared to Rs 437.3 billion in the same period last year. On quarterly basis, the slowdown in budgetary support from the banking system mainly came on the back of significantly lower borrowings during Q1-FY22; in the subsequent quarter however, it inched up slightly compared to the same period last year (**Figure 3.3**). During the quarter, the government borrowed Rs 185.1 billion from the central bank while it made retirements amounting to Rs 15.1 billion to the scheduled banks. The borrowings from the central bank rose mainly on the back of on-lending to the government against the IMF SDR allocation.⁶ Besides this, the government deposits held by the central bank also fell during Q2-FY22, which also inched up the overall borrowings from SBP.

⁶ The SBP issued a loan to the government of Pakistan amounting to Rs 474.9 billion in Q2-FY22.

Government Borrowings from the Banking System**Figure 3.3**

Source: State Bank of Pakistan

Primary Auctions

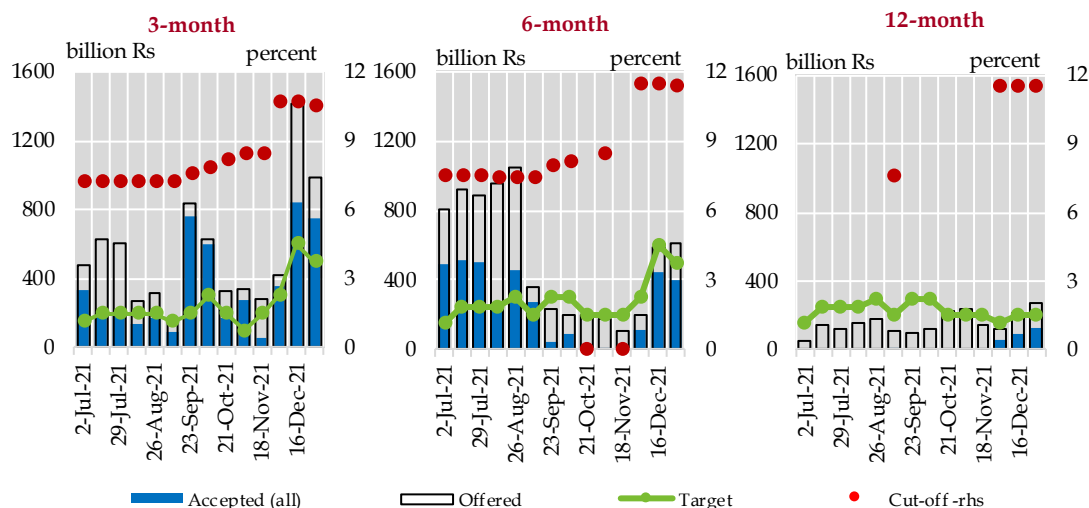
Since the start of the fiscal year, the market's interest in shorter duration instruments remained intact. This was primarily driven by the expectations of the interest rate path. Prior to the reversal of the interest rate cycle, the government did not increase the cut-off rates in the primary market to keep the yields low, at the cost of slightly missing the cumulative targets of T-bills and fixed

coupon PIBs. In September 2021, after the first rate hike of the fiscal year, the market's expectations of further rate increase became stronger.

In this backdrop, the government assigned higher targets to floating rate PIBs on net of maturity basis compared to fixed rate bonds, as floaters provide variable return and have medium to long-term maturities. Around 42 percent of the targets on net of maturity basis were assigned to floating rate PIBs, followed by around 26 percent to Ijarah Sukuk.

In case of T-bills, the market remained keen on investing in 3M papers. The offered to target ratio for 3M T-bills stood at 2.0 times compared to 0.9 times for both 6M and 12M bills. The government, while striking a balance between increasing cut-off rates and maintaining the maturity profile, made the highest acceptances (net of maturity) for 3M bills relative to the other zero-coupon bonds (Figure 3.4).

In the secondary market, the short-term yields rose faster than the long-term yields,

Auction Summary of T-bills during H1-FY22**Figure 3.4**

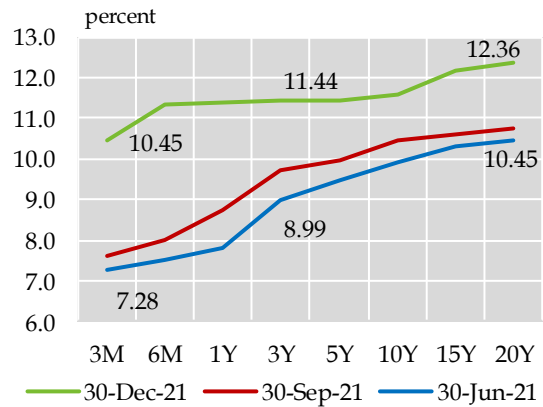
Source: State Bank of Pakistan

highlighting increased expectations of interest rate hikes in the near term. In response to a 250 bps hike in the policy rate during Q2-FY22, 3-month yields rose by 276 bps, while for 6M they picked up by 331 bps. In contrast, on the longer end of the curve, the increase in yields for 3-year, 5-year and 10-year bonds was 170 bps, 151 bps and 117 bps, respectively (**Figure 3.5**).

With the flattening of the yield curve, the government also made close-to-target acceptances of fixed rate PIBs. Though the rates currently stand at a high level which will increase the government's borrowing cost, this will also help the government in maintaining the maturity profile and diversify its outstanding stock of sovereign bonds. For 5-year bonds, the acceptances remained more than twice the targets. Cumulatively, the government made

Secondary Market Yields

Figure 3.5



Source: Financial Market Association of Pakistan

acceptances amounting to Rs 287.6 billion of fixed coupon PIBs against the target of Rs 300.0 billion.

For floaters, the rising interest rate scenario made investment more favorable.

Auction Summary

Table 3.2

billion Rupees

	Target	Maturity	Offered*	Accepted
Treasury bills	5,950.0	5,702.8	7,821.3	4,375.4
3-month	2,200.0	2,148.1	4,400.4	3,059.8
6-month	2,300.0	3,467.1	2,088.9	1,042.3
12-month	1,450.0	87.6	1,332.1	273.3
Pakistan Investment Bonds				
<i>Fixed Rate</i>	300.0	54.8	990.1	287.6
3-year	90.0		281.6	64.9
5-year	75.0	54.8	366.9	167.0
10-year	60.0		331.4	55.7
15-year	45.0		5.2	0.0
20-year	15.0		5.0	0.0
30-year	15.0		0.0	0.0
<i>Floating Rate</i>	650.0	-	1,004.5	606.2
2Y-Qtrly	175.0		575.2	459.9
3Y-Qtrly	175.0		281.5	146.3
5Y-Semi annual	175.0		104.6	0.0
10Y-Semi annual	125.0		43.2	0.0
Ijarah Sukuk	400.0	-	794.6	587.9
GIS-VRR	300.0		586.4	507.2
GIS-FRR	100.0		208.1	80.7

*competitive bids only

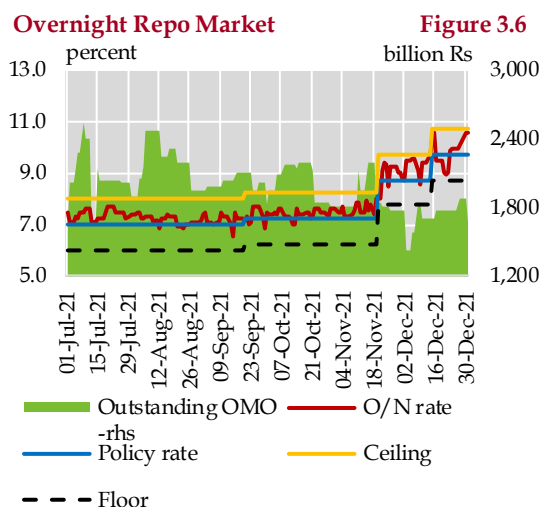
Source: State Bank of Pakistan

The 2-year quarterly coupon floater stood out as the most favored variable rate bond. The acceptances were in excess of the pre-auction target. This is because a 2-year floating rate PIB carries a duration risk of only 14 days, making it the lowest duration bond available in the primary market.⁷

Besides that, the government also resumed the auction of Sukuk which remained suspended since Jan 2021. Like the trend observed in conventional instruments, the market's interest remained skewed towards Variable Rental Rate Sukuk (GIS-VRR). The government made a cumulative issuance of Rs 507.2 billion of GIS-VRR compared to a target of Rs 300.0 billion for Q2-FY22. In comparison, the acceptances for fixed rental rate Sukuk stood at Rs 80.7 billion against the target of Rs 100.0 billion (Table 3.2).

Interbank liquidity

The money market showed signs of liquidity pressures throughout Q1-FY22 that continued to persist until October 2021.⁸ From November 2021 onwards, as the deposit mobilization gained momentum and the government borrowings from commercial banks remained muted, the market's reliance on OMO injections started to ease out. High private credit offtake and increase in the cash reserve requirement, on the other hand, partly offset these liquidity inflows in the system. On quarterly basis, the average outstanding OMO injections fell to Rs 1,875.0 billion in Q2-FY22 compared to Rs 2,092.4 billion in the preceding quarter (Figure 3.6).



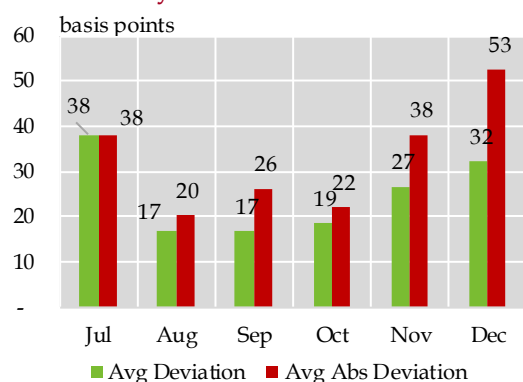
Source: State Bank of Pakistan

As far as the volatility is concerned, the overnight money market remained more volatile during Q2-FY22. The average absolute deviation of overnight rates from the policy rate increased to 38 bps during Q2-FY22 compared to 28 bps in the preceding quarter (Figure 3.7). Importantly, in November 2021 the SBP also increased the Cash Reserve Requirement (CRR) with an objective to contain the expansion of money supply. Consequently, this partly had an offsetting impact on the liquidity inflows coming into the banking system in the form of deposits and net retirements from the government. That said, in the long-term this will provide an incentive for banks to mobilize longer tenor deposits.⁹ Additionally, the overnight market remained more volatile during the quarter on the back of two rate hike decisions by the MPC. In

⁷ The coupon for 2-year floating rate PIB is paid quarterly; however, it resets on fortnightly basis making its duration even lower than that of a 3-month T-bill, which has a maturity of 84 days.

⁸ For details refer to Chapter 3 of SBP's First Quarterly Report on the State of Pakistan's Economy for FY22.

⁹ CRR is applicable on demand and time liabilities of banks with tenor of less than a year.

Deviation of Overnight Rates from the Policy Rate**Figure 3.7**

Source: State Bank of Pakistan

order to ease out heightened volatility and to further enhance the forward guidance given in December 2021's policy, three 63-day OMO injections took place in the month of December following the MPC announcement.

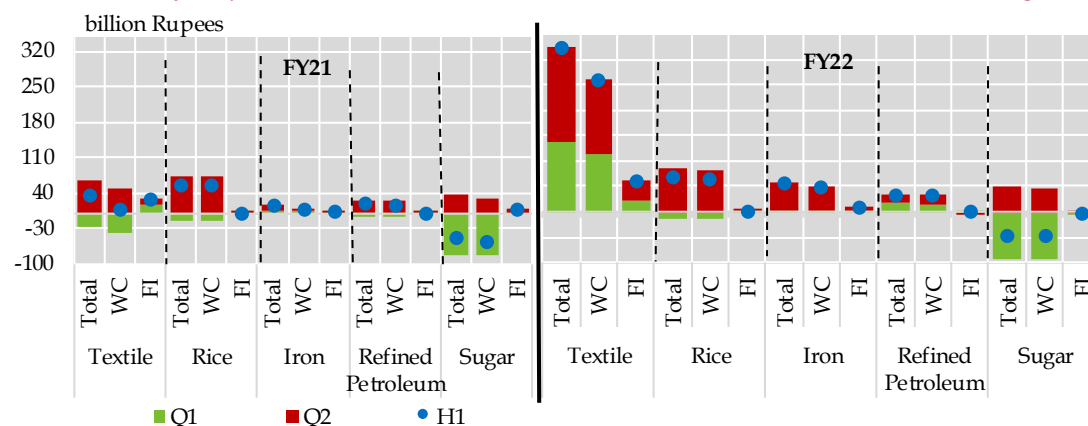
3.3 Credit to Private Sector

The H1-FY22 can be seen as a transition from the last year's favorable environment to relatively tighter monetary conditions for private sector businesses this year, mainly

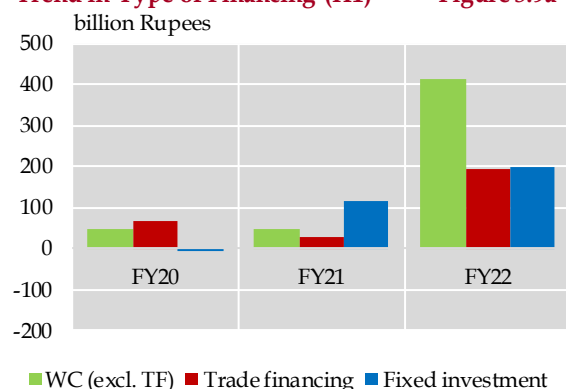
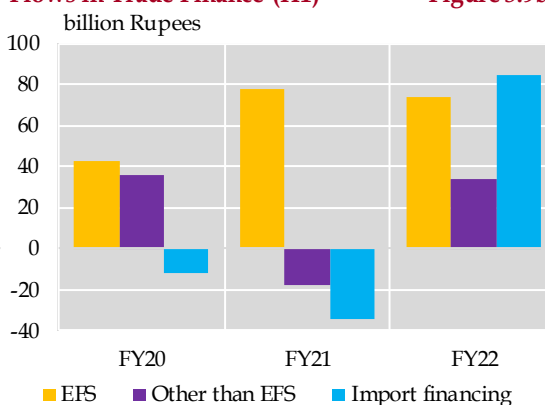
due to two factors. First, the policy environment was less accommodative, with the policy rate up by 275 basis points from 7.0 percent in end-June 2021 to 9.75 percent in end-December 2021 (**Figure 3.2**). Second, there was a persistent increase in the global commodity prices, which increased the input cost for private sector businesses. Despite these factors, the expansion in economic activities continued during the review period, as the policy reversal is expected to have a lagged impact on the overall economic activity.

With a sharp increase in credit offtake during Q2-FY22, loans to private businesses almost quadrupled in the H1-FY22 over the same period last year. The increase mainly came from working capital loans, concentrated in the Q2-FY22 (**Figure 3.8**).

The higher credit offtake can be attributed to: (i) higher input prices (especially of cotton, and basic metals) which increased the borrowing needs of textile and iron and steel; (ii) improved production in sectors such as iron and steel, and paper and paper products; and (iii) vibrancy in trading

Loan Offtake by Major Sectors (flow)**Figure 3.8**

Source: State Bank of Pakistan

Trend in Type of Financing (H1)**Figure 3.9a****Flows in Trade Finance (H1)****Figure 3.9b**

Source: State Bank of Pakistan

activity also contributed to the higher demand for loans, as reflected by a broad-based expansion in trade financing (both import financing and export financing) during the review period (**Figure 3.9**). The overall improved demand for loans is in line with 27.2 percent higher loan applications received during H1-FY22, over last year.

Working Capital Loans

Working capital loans rose by Rs 607.7 billion in H1-FY22, compared to Rs 73.7 billion in the same period last year (**Table 3.3**). Higher demand for short-term loans by businesses is attributed to some sector-specific developments.

The textile sector dominated the overall borrowing with an offtake of Rs 260.1 billion during H1 FY22, compared to only Rs 8.4 billion in the same period last year. Two main factors explain this increase. First, higher cotton prices raised the borrowing needs of textile businesses. This is consistent

with the 56.8 percent YoY jump in the domestic cotton prices during H1-FY22.¹⁰ Second, textile businesses also availed short-term financing to scale up their exports, as reflected by higher quantum exports of major textile products during H1-FY22 (**Chapter 5**).

Likewise, higher prices of base metals in the international market resulted in a five-fold increase in borrowings by the basic iron and steel sector.¹¹ The overall working capital borrowing of iron and steel firms increased by Rs 49.6 billion during H1-FY22, compared to an increase of Rs 9.5 billion during the same period last year. Apart from managing the input price pressure, the sector's borrowing attributes 18.4 percent growth in the production of iron and steel products during H1-FY22, compared to a marginal increase of 1.2 percent last year. This is in line with buoyant construction activity in the country during H1-FY22, reflected in 40.2 percent growth in PSDP spending during H1-FY22, compared to a decline of 11.8 percent last year.

¹⁰ Source: Emerging Textiles.

¹¹ During H1-FY22, the prices of base metals rose by around 30 percent in the international market. (Source: IMF)

Loans to Private Sector Businesses (H1)

Table 3.3

(Flow in billion Rupees)	Total Loans*		Working Capital**		Fixed Investment	
	FY21	FY22	FY21	FY22	FY21	FY22
Private Sector Businesses	219.5	860.2	73.7	607.7	115.7	199.8
Manufacturing	83.7	670.9	10.3	527.4	72.2	136.3
Textile	35.4	326.5	8.4	260.1	26.5	63.3
Rice Processing	57.2	70.5	55.8	67.4	1.3	2.9
Basic iron and steel	15.3	57.8	9.5	49.6	5.8	8.2
Refined petroleum	18.9	35.9	17.7	34.4	1.3	1.5
Paper & paper products	-1.8	24.8	-5.5	17.6	3.7	7.2
Vegetable and animal oils and fats	-10.3	17.4	-13.7	15.4	3.4	1.7
Cement, lime and plaster	-0.6	11.6	-4.1	10.0	3.5	1.6
Motor vehicles	-17.4	13.5	-19.6	6.9	2.2	6.6
Fertilizers	27.7	5.9	24.5	-5.6	3.2	11.5
Sugar	-46.0	-45.9	-54.0	-45.3	8.1	-0.6
Telecommunications	5.1	20.8	10.0	-13.2	-4.9	34.0
Power gen., trans., and dist.	40.4	27.4	-4.7	7.6	45.2	19.9
Agriculture, forestry and fishing	11.5	30.6	13.7	23.9	-2.2	5.6
Transportation and storage	0.2	11.4	-0.3	8.6	0.5	2.2
Wholesale and retail trade	25.2	49.3	19.0	46.9	5.8	1.2
Mining and quarrying	-3.4	-0.9	-7.3	-2.0	3.9	1.2
Real estate activities	-4.6	3.8	-1.5	1.0	-6.0	-0.5
Construction	15.7	31.1	3.7	0.3	-9.1	-3.6

*Total loans in H1-FY21 and H1-FY22 include construction financing of Rs 30.1 billion and Rs 52.7 billion, as the data on credit/loans has been revised since June 2020 due to inter-sectoral adjustment in private sector business (see IH&SMEFD Circular Letter No. 28 of 2020); ** working capital includes trade financing

Source: State Bank of Pakistan

Borrowings by the refined petroleum sector almost doubled to Rs 34.4 billion in H1-FY22, compared to an offtake of Rs 17.7 billion in the same period last year. The increase primarily came from Q1-FY22, as major oil refineries availed bank financing to meet the rising fuel demand, which is consistent with 17.9 percent YoY growth in POL sales during the Q1-FY22.

The paper and paper products sector borrowed Rs 17.6 billion during H1-FY22, compared to a net retirement of Rs 5.5 billion last year. The higher borrowings came on the back of 8.3 percent YoY growth in the production of paper products during H1-FY22.

In addition to the refined petroleum and paper, vegetable and animal oils and fats

sector also increased its short-term borrowings. The sector borrowed Rs 15.4 billion during H1-FY22, compared to a net retirement of Rs 13.7 billion during the same period last year. The entire increase was concentrated in the Q1-FY22, when higher edible oil prices in the international market drove up the working capital needs of these firms.

Rice processing firms borrowed Rs 67.4 billion during H1-FY22, compared to an offtake of Rs 55.8 billion last year. After the usual seasonal loan retirement in Q1-FY22, the sector availed higher loans in the subsequent quarter, to scale-up its exports. This is supported by 11.7 percent YoY growth in quantum exports of rice during Q2-FY22. On the other hand, after posting significantly higher loan retirements by the

sugar sector during Q1-FY22, it increased the offtake in Q2-FY22 over last year, owing to higher sugarcane prices and the start of crushing season (**Figure 3.8**).¹² On a cumulative basis, sugar sector retired Rs 45.3 billion during H1-FY22, compared to a net retirement of Rs 54.0 billion last year.

Among non-manufacturing sector, wholesale and retail trade availed short-term loans of Rs 46.9 billion during H1-FY22, compared to an offtake of Rs 19.0 billion last year. This reflects borrowings by major oil marketing companies (OMCs) to finance the import of petroleum products. This is supported by 29 percent YoY growth in quantum imports of petroleum products during H1-FY22. Notably, some of the major OMCs benefitted from the exemption of customs duty on imports of petroleum products from China under the China-Pakistan Free Trade Agreement.¹³ Consequently, Pakistan's share of petrol (motor spirit) imports from China

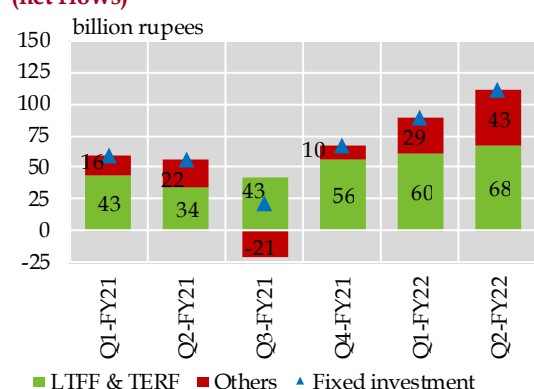
jumped from 7 percent during H1-FY21 to around 33 percent during H1-FY22.¹⁴

Fixed Investment Loans

The borrowings under fixed investment loans were Rs 199.8 billion in H1-FY22, compared to an offtake of Rs 115.7 billion last year. Private sector businesses availed SBP's concessionary financing schemes (LTFF and TERF) for machinery imports and capacity expansion. This is supported by higher disbursements under LTFF and TERF during Q2-FY22 (**Figure 3.10**). It is pertinent to mention that out of the total approved amount of Rs 436 billion under TERF, Rs 269 billion (around 62 percent) were disbursed by end-December 2021.

Within the manufacturing sector, textile businesses dominated by borrowing Rs 63.4 billion during H1-FY22, compared to an offtake of Rs 26.5 billion last year. Benefitting from LTFF and TERF, the textile sector borrowed long-term loans to import textile machinery, which corresponds to 89.0 percent YoY growth in the import of textile machinery during H1-FY22.¹⁵ In addition, the anecdotal evidence suggests that some textile firms having spinning segment availed long-term financing for adding finishing units in order to enhance their production capacity. Besides textile, fertilizer was the second biggest user of fixed investment loans in the manufacturing sector, as it increased its borrowings by Rs 11.5 billion during H1-FY22, compared to Rs 3.2 billion last year. Most of the increase was concentrated in Q1-FY22, as a major listed fertilizer firm resorted

Fixed Investment Loans (net flows) **Figure 3.10**



Source: State Bank of Pakistan

¹² Sugarcane prices jumped by 19.8 percent YoY during Q2-FY22 (Source: Pakistan Bureau of Statistics).

¹³ Source: FBR SRO 1640(I)/2019, dated December 31, 2019.

¹⁴ Source: PBS

¹⁵ Source: PBS

to bank financing for the acquisition of majority shares in a renewable energy business.¹⁶

Among non-manufacturing entities, the telecommunications sector availed higher fixed investment loans. The sector borrowed Rs 34.0 billion during H1-FY22, compared to a net retirement of Rs 4.9 billion last year. The increase represents syndicate financing facility availed by a major cellular firm during the Q1-FY22 to finance the acquisition of a 4G license.¹⁷ Meanwhile, power sector also availed bank financing, albeit lower than last year. The sector borrowed Rs 19.9 billion during H1-FY22, compared to an offtake of 45.2 billion last year. Bulk of the increase came in the Q1-FY22, as a major utility company borrowed in order to partially settle the parent company's loan owing to change of ownership.

Consumer Financing

Table 3.4

flow in billion Rupees

	Q1		Q2		H1	
	FY21	FY22	FY21	FY22	FY21	FY22
Total loans	38.1	58.5	46.6	49.0	84.7	107.5
Auto loans	21.3	30.1	24.0	15.5	45.3	45.5
House building	0.9	14.9	5.5	25.3	6.4	40.2
Credit cards	6.1	3.8	2.3	6.3	8.4	10.1
Personal loans	12.5	7.4	13.8	2.6	26.3	9.9
Consumers durable	-2.6	2.3	0.9	-0.6	-1.7	1.7

Source: State Bank of Pakistan

Consumer Financing

Unlike the favorable conditions for consumer financing during last year, H1-FY22 witnessed some macro-prudential measures aimed at moderating the demand growth in the economy to support the country's balance of payments.¹⁸ The impact of these regulatory measures was visible on consumer financing, as the total loans to consumers moderated in the Q2-FY22. Consumer financing increased by Rs 49.0 billion during Q2-FY22, slightly higher than the same period last year. More importantly, the financing under the transportation segment slowed down to Rs 15.5 billion during Q2-FY22 from Rs 24.0 billion a year earlier.

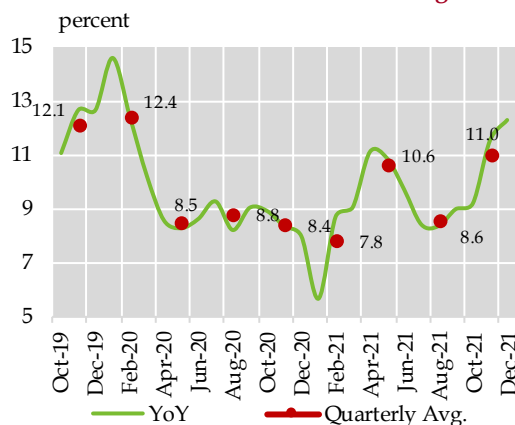
On a cumulative basis, consumer financing reported a flow of Rs 107.5 billion in H1-FY21 as compared to Rs 84.7 billion a year earlier (**Table 3.4**). Apart from auto loans, the increase is attributed to house building loans during the review period.

A significant increase in house building loans offset the slowdown in auto loans during H1-FY22. The house building segment borrowed Rs 40.2 billion during H1-FY22, compared to an increase of Rs 6.4 billion last year. This is reflected by an increase in the outstanding stock of housing and construction finance by Rs 175 billion in December 2021, over last year. The increase was on the back of mandatory targets set by SBP for banks to

¹⁶ Source: Pakistan Stock Exchange, available at: www.psx.com.pk/psx/files-attachment/?file=168789.pdf

¹⁷ Source: Pakistan Telecommunication Authority, press release, dated September 15, 2021

¹⁸ As per revised regulations, the maximum tenure of the auto finance facility was reduced from seven years to five years. In addition, the overall auto financing limits availed by one person from all banks/DFIs, in aggregate, will not exceed Rs 3 million at any point in time; and the minimum down payment for auto financing was increased from 15 percent to 30 percent. (Source: SBP press release, dated September 23, 2021).

National CPI**Figure 3.11**

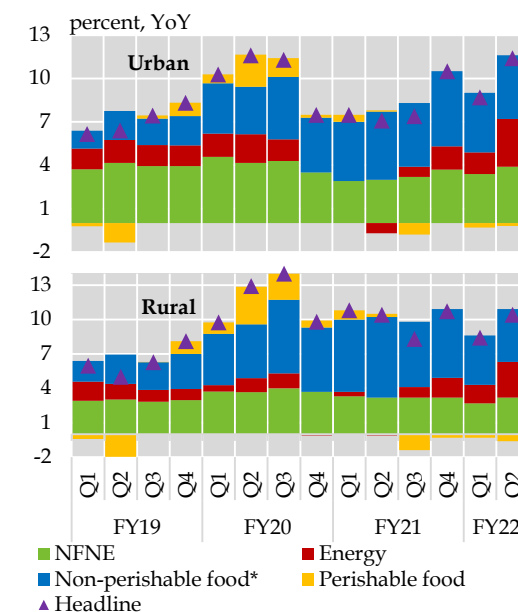
Source: Pakistan Bureau of Statistics

increase their housing and construction loans to 5 percent of their overall private sector credit portfolio by December 31, 2021.¹⁹

3.4 Inflation

Inflationary pressures continued to strengthen throughout the H1-FY22 on account of persistently rising global prices of energy, food and metal group along with elevated domestic demand and weakening of domestic currency. In particular, National CPI (NCPI) inflation stood at 11.0 percent in Q2-FY22 compared to 8.4 percent during the same period last year and 8.6 percent in the preceding quarter (**Figure 3.11**).

While the food group remained the main contributor, the steep rise in energy prices along with increased core inflation also contributed to inflationary pressures during H1-FY22. (**Figure 3.12**). In terms of

Composition of CPI Inflation**Figure 3.12**

*Inclusive of alcohol beverages and readymade food

Source: Pakistan Bureau of Statistics

dispersion, particularly for Q2-FY22, the inflation increase was registered in around half of the sub-indices both in urban and rural areas.²⁰

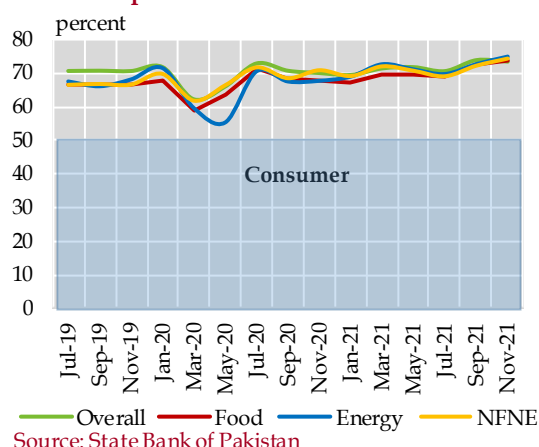
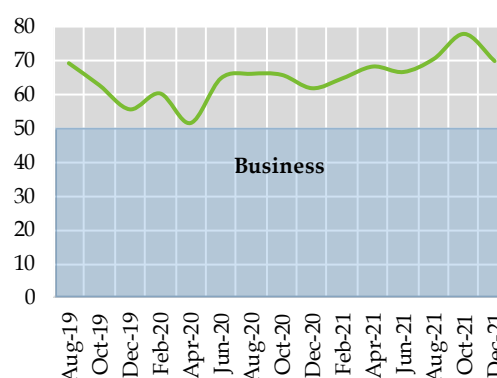
Inflation expectations drifted up

Taken together, the evidence from SBP-IBA Consumer Confidence Survey (CCS) and Business Confidence Survey (BCS)²¹ indicates that inflation expectations drifted up during H1-FY22. In particular, the results of survey conducted in Q2-FY22 depicted that the consumer inflation expectation index remained elevated almost up to the mark of the previous iteration and the business inflation expectations index increased

¹⁹ For details, see SBP circular: IH&SMEFD Circular No. 10 of 2020 of 15 July 2020 and subsequent circulars on the subject.

²⁰ 49 out of 94 items (with about 52 percent share in urban CPI) and 43 out of 89 items (with about 48 percent share in rural CPI) posted higher inflation during Q2-FY22.

²¹ CCS was conducted in July 2021, September 2021 and November 2021, whereas BCS was conducted in October 2021 and December 2021.

Inflation Expectations**Figure 3.13**

significantly. Elevated consumer inflation expectation index was observed on account of rise in all three categories (food, energy and NFNE); however, rising energy and NFNE prices played a major role in the overall increase in inflation expectations. However, in December 2021, inflation expectations of businesses declined compared to the earlier survey results (Figure 3.13).

Food continued to remain the dominant contributor to overall inflation

Food group remained the major contributor to overall inflation in H1-FY22. Particularly, during Q2-FY22, it registered 11.0 percent and 8.3 percent inflation in urban and rural areas respectively during Q2-FY22, compared to 13.2 percent and 15.7 percent increase in the same period last year. Though the pace of food inflation declined on a YoY basis, it accelerated over Q1-FY22. Rising global food prices and supply-demand gaps in some commodities continued to put upward pressures on food prices. (Table 3.5).

Rising global commodity prices amid supply disruptions and production prospects

Elevated global food prices remained one of the major reasons behind double-digit inflation in the food group. Around 1.3 percentage point was contributed by imported contents in the food group (cooking oil, tea, pulses) to total inflation of urban areas in Q2-FY22. For instance, the highest direct impact of increasing international commodity prices to food inflation came from edible oils. Palm oil and soybean prices have been on a steep rising trajectory since June 2020 due to growing demand for biodiesel and unsupportive weather patterns in major crop growing areas. Throughout H1-FY22, price pressures reflect concerns over reduction in exports from Indonesia, the world's top palm oil exporter, along with subdued production in major palm oil producing countries.²²

Similarly, prices of tea, which has 2.3 percent share in urban food basket, also remained elevated during the Q2-FY22 owing to an increase in the unit value of imports.

²² FAO Food Price Index-January 2022

Average CPI Inflation and Contribution

Table 3.5

percent

Urban													Rural				
Items	Wt.*	H1		Q2			Wt.*	H1		Q2							
		FY21	FY22	FY21	FY22	Cont.*		FY21	FY22	FY21	FY22	Cont.*					
Headline		7.3	10.1	7.1	11.4			10.6	9.4	10.4	10.4						
Food & non-alcoholic beverage	30.4	14.0	10.7	13.9	11.1	3.6	40.9	16.2	8.4	16.2	8.2	3.6					
Wheat	0.6	37.7	7.4	37.1	9.7	0.1	3.5	38.7	5.0	38.5	5.5	0.2					
Wheat flour	3.0	18.8	15.8	17.0	17.0	0.5	3.4	23.1	14.3	21.5	15.9	0.5					
Cooking Oil	1.1	11.9	42.9	10.7	51.0	0.6	0.6	15.0	46.3	15.0	52.9	0.3					
Vegetable ghee	1.0	17.0	44.5	16.0	52.6	0.6	2.38	18.9	43.6	17.7	50.7	1.4					
Fresh Fruits	1.4	-1.2	9.4	-5.0	22.4	0.2	1.5	-2.6	7.1	-5.4	16.5	0.2					
Pulse masoor	0.2	18.9	16.6	16.8	24.5	0.0	0.2	26.9	14.4	25.5	20.3	0.0					
Gram whole	0.1	3.7	11.3	2.6	15.8	0.0	0.1	-1.2	16.8	-2.2	21.8	0.0					
Non-perishable food	26.0	15.2	14.0	16.1	14.7	3.9	35.1	17.2	11.4	18.4	11.9	4.3					
Perishable food items	4.5	8.1	-6.1	4.3	-6.4	-0.4	5.8	10.2	-7.2	6.4	-9.8	-0.7					
Tea	0.8	3.4	4.7	0.3	8.3	0.1	1.3	4.0	4.0	1.1	7.4	0.1					
Alcoholic beverage, Tobacco.	0.9	5.9	2.5	6.5	2.0	0.0	1.3	5.6	1.7	5.4	1.7	0.0					
Clothing and footwear	8.0	8.5	10.4	8.6	10.6	0.8	9.5	10.5	8.9	10.2	9.5	0.9					
Housing, Electricity, Gas	27.0	3.6	10.8	2.5	13.3	3.5	18.5	5.3	13.8	4.0	16.9	2.8					
Furniture & household equipment	4.1	6.3	9.8	6.4	10.1	0.4	4.1	9.9	10.6	9.9	11.3	0.4					
Health	2.3	6.9	9.2	7.3	9.3	0.2	3.5	8.8	7.8	8.4	8.0	0.3					
Transport	6.1	-3.3	15.9	-3.2	21.9	1.3	5.6	-2.7	13.7	-2.6	19.4	1.0					
Communication	2.4	0.4	3.6	0.5	3.5	0.1	2.0	0.3	0.9	0.4	0.9	0.0					
Recreation and culture	1.7	3.0	6.7	3.1	7.7	0.1	1.4	5.7	7.5	6.1	7.4	0.1					
Education	4.9	1.0	2.2	1.1	2.2	0.1	2.1	1.6	3.8	2.1	3.3	0.1					
Restaurants and hotels	7.4	8.5	9.8	9.4	11.1	0.8	6.2	8.8	8.3	9.3	9.8	0.6					
Misc. goods & services	4.8	10.7	8.9	10.3	10.0	0.5	5.0	14.3	8.3	14.1	9.4	0.5					
NFNE	53.7	5.5	7.0	5.6	7.5	3.9	42.6	7.7	7.2	7.6	7.9	3.2					

*wt. = weight and Cont. = Contribution for Q2

Source: Pakistan Bureau of Statistics

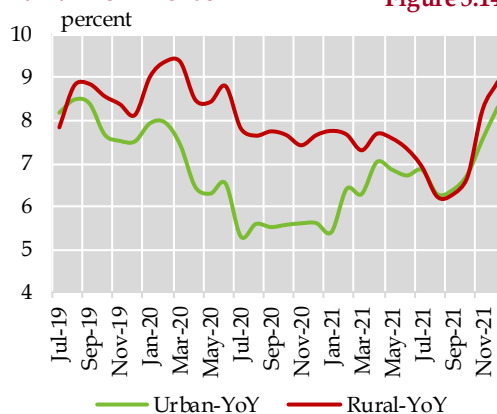
Globally, prices are under pressure on the back of improved demand and a government backed reserve price initiated by Kenya to safeguard small farmers (Table 3.5).

Supply-demand gaps and indirect cost

Pressures on prices of some food items emanated from supply disruptions on imported food items during H1-FY22. For instance, during Q2-FY22, inflation in few pulses remained high. Particularly, pulse masoor and gram whole registered double-digit inflation. Shortfall in domestic

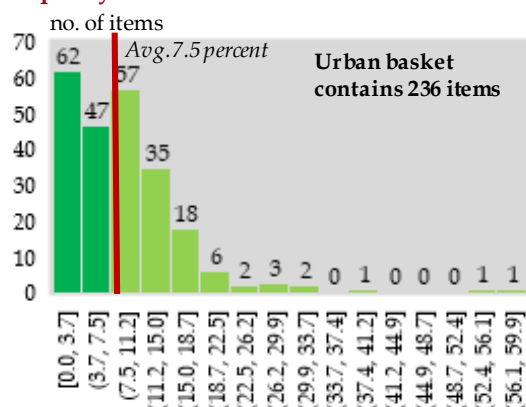
NFNE-YoY Trends

Figure 3.14



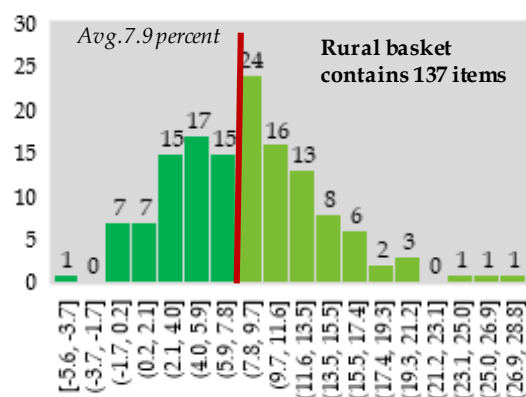
Source: Pakistan Bureau of Statistics

Frequency Distribution NFNE Items



Source: Pakistan Bureau of Statistics

Figure 3.15



production of various pulses and increase in unit values of imported pulses caused inflationary pressures in this food group.

Though overall perishable food group registered deflation during H1-FY22, a trend persisting since Q3-FY21 on account of sufficient domestic supplies and adequate imports, inflation in fresh fruits and vegetables remained high compared to the same period last year. Relatively lower imports of some fruits created supply-demand gaps in the market, causing high inflation in this group.

Double-digit inflation in ready-made food group was observed during H1-FY22 on account of indirect rise in the prices of inputs, such as wheat, edible oil, chicken and transportation cost.

Although wheat inflation remained limited during H1-FY22 both on MoM basis and YoY basis amid relatively better availability of the produce (good crop and imports), inflation in wheat flour remained elevated on a YoY

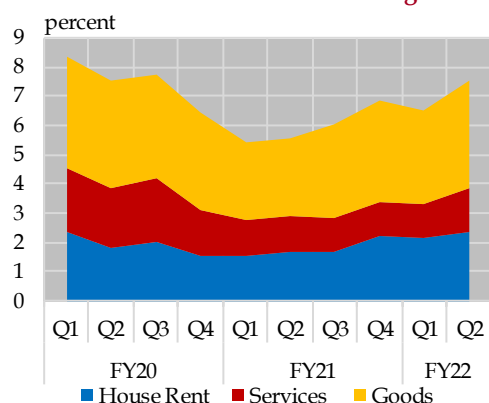
basis amid the increase in wheat issue price by procuring agencies to flour mills.²³

NFNE inflation started intensifying

The inflationary pressures in the non-food-non-energy (NFNE) group increased in H1-FY22. In particular, NFNE inflation intensified in Q2 compared to both Q1-FY22 as well as the same quarter last year for both urban and rural areas (Figure 3.14). In terms of dispersion, more than half of the sub-indices registered higher inflation compared to the same period last year in Q2-FY22.²⁴ Item-wise commodity basket of urban and rural areas reveals that more than half of the items posted above average NFNE inflation during the quarter (Figure 3.15). Acceleration in NFNE inflation reflected increased domestic demand in the economy. In addition, aggravating cost-push pressures on account of increasing international commodity prices and revision in some service charges in Budget FY2021-22 also contributed to rising NFNE inflation.

²³ Minimum release price was raised from Rs 1,475 to Rs 1,950, in an attempt to withdraw subsidies.

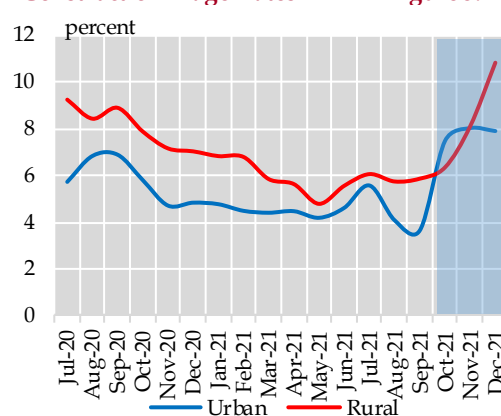
²⁴ Around 62 percent and 55 percent of the sub-indices registered higher inflation in urban and rural areas respectively.

NFNE Inflation-Contribution **Figure 3.16**

Source: Pakistan Bureau of Statistics

Within the urban as well as rural NFNE, both the services and goods indices accelerated in H1-FY22; however, the impact and contribution of the latter remained more pronounced (**Figure 3.16**). House rent also registered significant rise in inflation. Across goods, particularly in Q2-FY22, significant price rise was observed in clothing and footwear, plastic products, household equipment and textbooks during Q2-FY22 over last year amid rising cost of imported inputs as well as improved demand.²⁵ Similarly, rise in iron bar prices, in particular, pushed-up the overall construction input index reflecting both rising demand and global prices.²⁶

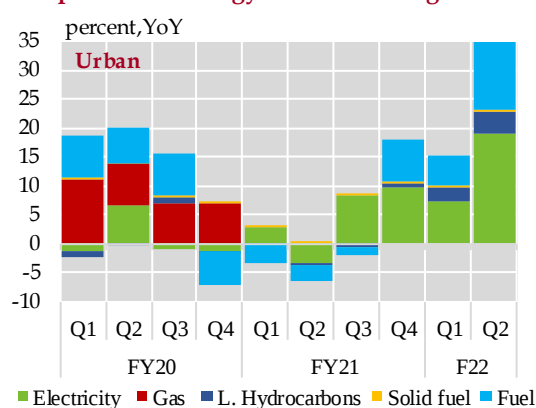
Motor vehicles group, which posted significant deceleration in inflation in Q1-FY22 after reduction in FED by the government in budget FY22, registered significant rise in the inflation during Q2-FY22. This reflects upward price revisions by

Construction Wage Rates **Figure 3.17**

Source: Pakistan Bureau of Statistics

auto manufacturers over passing on the impact of duties on some variants.

In the services group, some of the rise in inflation reflects base effect, as prices are higher compared to the low levels that prevailed last year amid Covid-related relief provided by the government in the FY21 budget.²⁷ Also, wage pressures remained

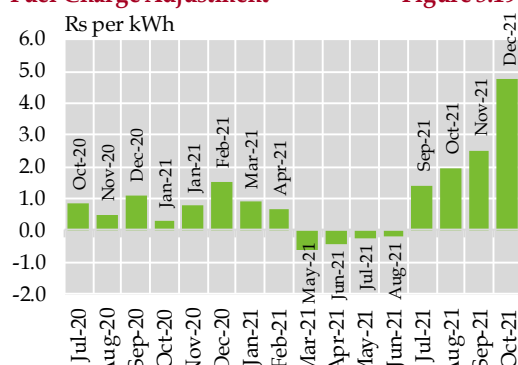
Composition of Energy Inflation **Figure 3.18**

Source: Pakistan Bureau of Statistics

²⁵ International cotton, plastic and paper prices are on rising trajectory amid disruption in the global supply chains.

²⁶ IMF index of base metals rose by 15.5 percent in Q2-FY22 compared to last year.

²⁷ For instance, tax on motor vehicles and charges of postal services were raised in FY22 budget.

Fuel Charge Adjustment**Figure 3.19**

Note: x-axis indicate months for which fuel charge adjustment was charged

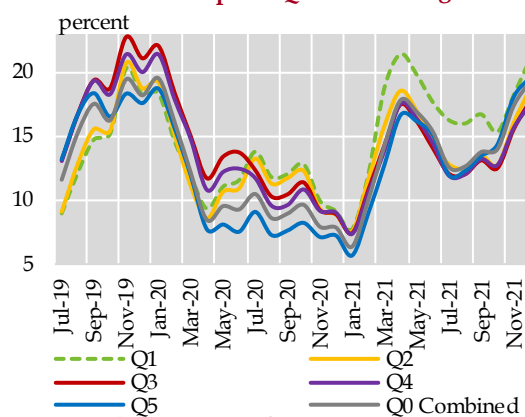
Source: National Electric Power Regulatory Authority

elevated during Q2-FY22 on YoY basis owing to lower base effect as well as rising construction activities and may be construed as the impact of overall inflationary pressures in the economy, which have affected real incomes of the low-income group the most (Figure 3.17).

Energy inflation continued to surge

A sharp increase in administered prices of motor fuel, electricity and LPG remained instrumental in strengthening inflationary pressures in the economy during H1-FY22 (Figure 3.18). These adjustments reflect measures taken under the circular debt management plan and rising international fuel prices.

The largest direct impact came from adjustments in electricity tariffs, as this alone contributed 1.2 percentage points to the headline inflation during H1-FY22 and 1.8 percentage points in Q2-FY22, particularly. Significant upward revision in Fuel Cost Adjustment (FCA) contributed to major rise in inflation in this group (Figure 3.19).

Inflation-Consumption Quintile**Figure 3.20**

Source: Pakistan Bureau of Statistics

In the case of motor fuels, the trend in global oil prices and frequent revisions in the sales tax and PDL structure during the H1-FY22 determined the direction and magnitude of changes in domestic petrol and high-speed diesel (HSD) prices. In overall terms, the motor fuel index posted more than 25 percent inflation during H1-FY22 both in urban and rural areas, contributing around 0.8 percentage points to the overall inflation.

Consumers of the lowest consumption basket were hit-hard

The incidence of increasing inflationary pressures on low-consumption group (with consumption up to Rs 17,732) remained quite elevated throughout H1-FY22, the impact was more pronounced during Q2-FY22 as compared to other consumption quintiles (Figure 3.20). Since the consumption basket consists of the Sensitive Price Index (SPI),²⁸ a broad-based rise in food prices, electricity tariffs, and fuel charges has affected this group severely as compared to other groups.

²⁸ Sensitive Price Index includes 51 essential items.

4 Fiscal Policy & Public Debt

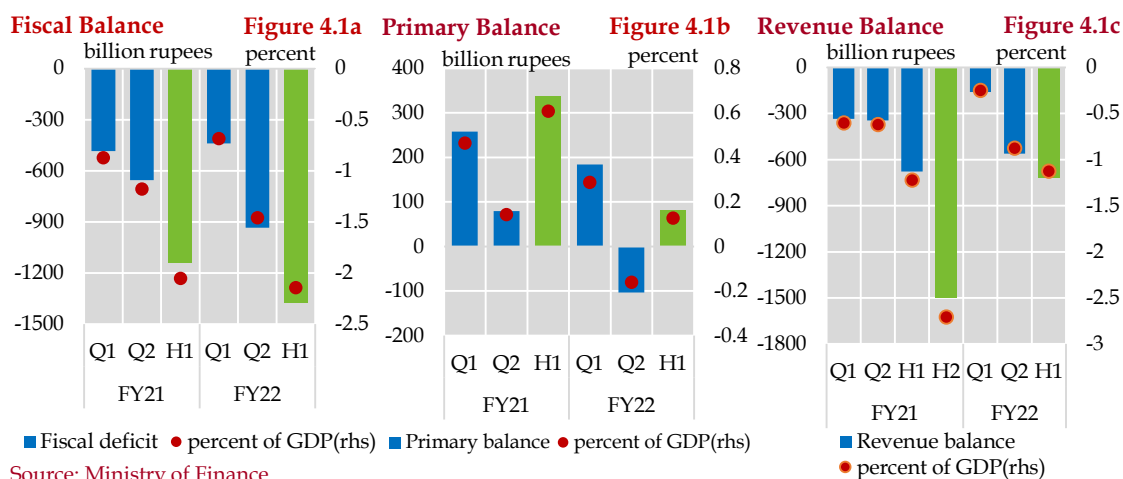
Fiscal indicators slightly deteriorated during H1-FY22 compared to the same period last year, as the primary surplus edged down. A sharp rebound in non-interest expenditures outweighed an otherwise decent increase in revenues. Provinces continued with their fiscal consolidation efforts and delivered a combined surplus of 0.8 percent of GDP in H1-FY22, which helped in containing the overall fiscal deficit. Quarterly analysis shows that deterioration in fiscal indicators was concentrated in Q2-FY22. The fiscal deficit more than doubled while the primary balance recorded a deficit in Q2-FY22. This was despite a sizeable increase in tax collection that neutralized the impact of a decline in non-tax revenues. Specifically, FBR taxes posted a notable import-led increase during the H1-FY22. Social protection grants and subsidies to power sector led to a sharp rise in current spending. Interest payments on debt also increased during Q2-FY22 due to a persistent rise in the outstanding debt stock and increasing interest rates. The accumulation of public debt gained pace during H1-FY22. Revaluation losses due to the depreciation of PKR against the US Dollar contributed almost 60 percent of the increase in public debt. The maturity profile of domestic debt lengthened with an increase in the stock of variable rate long-term instruments. This, however, increased the debt-servicing burden amid increasing interest rates. External debt servicing increased in H1-FY22 amid a scheduled repayment of US\$ 1 billion Sukuk in Q2-FY22.

4.1 Fiscal Trends and Policy Review

The fiscal deficit remained unchanged at 2.1 percent of GDP in H1-FY22 – the level seen in the same period last year (Figure 4.1 a and Table 4.1). However, a sharp rebound in non-interest spending outpaced a strong increase in tax collection, narrowing the surplus in the primary balance to 0.1 percent of GDP in H1-FY22, from 0.6 percent in the same period last year (Figure 4.1b). Provinces met the commitment of fiscal consolidation and posted a combined surplus

of 0.8 percent of GDP in H1-FY22, which was higher than last year.

Most of the expansion in expenditures came in Q2-FY22, with increased current spending on social protection grants and subsidies followed by interest payments. Around one-half of the entire increase in current spending during Q2-FY22 stemmed from social protection grants, where Covid vaccine procurement under the Economic Stimulus Package (ESP) and BISP were the key focus areas.



Consolidated Fiscal Indicators**Table 4.1**

billion Rupees, growth in percent

	Q1		Q2		H1		Growth					
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
1. Total Revenue (a+b)	1,478.7	1,808.5	1,872.4	2,147.5	3,351.2	3,956.0	-0.7	22.3	7.4	14.7	3.7	18.0
(a) Tax Revenue	1,122.4	1,532.8	1,333.5	1,658.3	2,455.9	3,191.0	-1.8	36.6	7.6	24.4	6.4	29.9
Of which: FBR taxes	1,010.6	1,398.0	1,199.4	1,521.8	2,210.0	2,919.8	4.8	38.3	6.2	26.9	5.6	32.1
(b) Non-Tax	356.3	275.7	538.9	489.2	895.3	764.9	-15.2	-22.6	6.9	-9.2	-3.1	-14.6
2. Total Expenditure (a+b+c)	1,963.1	2,247.0	2,526.0	3,081.0	4,489.1	5,328.0	10.6	14.5	3.0	22.0	6.2	18.7
(a) Current Expenditure	1,812.6	1,968.2	2,216.8	2,707.5	4,029.3	4,675.7	14.6	8.6	3.6	22.1	8.3	16.0
Of which : Mark-up Payments	742.1	622.7	733.1	830.2	1,475.2	1,452.9	29.8	-16.1	3.3	13.2	15.1	-1.5
Defence	224.5	261.7	262.1	258.8	486.6	520.5	-7.5	16.6	-8.6	-1.3	-8.1	7.0
Non-markup expenditure	1,070.5	1,345.4	1,483.7	1,877.3	2,554.2	3,222.8	5.9	25.7	3.8	26.5	4.7	26.2
(b) Development Expenditure & net lending	215.2	264.7	242.6	306.8	457.9	571.5	46.2	23.0	-25.6	26.4	-3.3	24.8
(c) Statistical Discrepancy	-64.7	14.2	66.6	66.5	1.9	80.6	n-a	n-a	n-a	-0.2	-94.1	
3. Overall budget balance	-484.3	-438.5	-653.6	-933.3	-1,137.9	-1,371.8	69.3	-9.5	-7.8	42.8	14.4	20.6
percent of GDP	-0.9	-0.7	-1.2	-1.5	-2.1	-2.1						
4. Primary balance	257.7	184.2	79.5	-103.2	337.2	81.1	-9.8	-28.5	n.a	n.a	17.7	-76.0
percent of GDP	0.5	0.3	0.1	-0.2	0.6	0.1						
5. Revenue balance	-333.9	-159.7	-344.3	-560.0	-678.2	-719.7	n-a	-52.2	-13.1	62.6	38.6	6.1
percent of GDP	-0.6	-0.2	-0.6	-0.9	-1.2	-1.1						
6. Financing (a+b)	484.3	438.5	653.6	933.3	1,137.9	1,371.8	69.3	-9.5	-7.8	42.8	14.4	20.6
(a) External (Net)	161.4	466.1	293.1	559.5	454.4	1,025.6	-3.1	n-a	-15.6	90.9	-11.5	n-a
(b) Domestic (Net)	323.0	-27.6	360.5	373.8	683.5	346.2	n-a	n-a	-0.3	3.7	42.1	-49.4

Source: Ministry of Finance

Similarly, a large volume of power sector subsidies necessitated by the partial payment of arrears to IPPs under the Circular Debt Management Plan (CDMP) further inflated current spending during Q2-FY22. Interest payments also showed a sizeable increase during Q2-FY22, which mainly reflects the impact of the increasing share of floating rate domestic debt in an increasing interest rate environment. However, to contain the overall level of fiscal deficit, the authorities curtailed the pace of development spending during Q2-FY22.

On the revenue side, a notable increase in FBR tax collection shored up overall receipts during H1-FY22. Whereas non-tax revenues saw a sizeable reduction because of lower collection from petroleum development levy (PDL). Around three-quarters of the increase in tax collection came from import related taxes that reflected the impact of increase in international commodity prices, higher import volumes and PKR depreciation. In addition, expansion in economic activity, a general increase in price level and continued tax administration reforms also supported tax collection. However, the decline in domestic sales tax collection, amid a

reduction in GST rates on petroleum products, slightly trimmed the pace of tax collection during Q2-FY22. To protect the domestic consumers from the impact of rising international oil prices, the government substantially reduced GST rates on petroleum products during Q2-FY22.

Although a large import-led increase in taxes aided in containing the fiscal imbalance, a long-term improvement in tax revenues hinges on broadening the tax base. The lacunas in tax rules and procedures engender low tax compliance, inhibiting the extension in the tax base (**Box 4.1**). The efforts to improve the tax to GDP ratio are already underway. A greater focus on rationalization of tax exemptions, simplification of tax procedures, and increasing degree of formality will be instrumental for achieving sustainable improvement in tax collection.

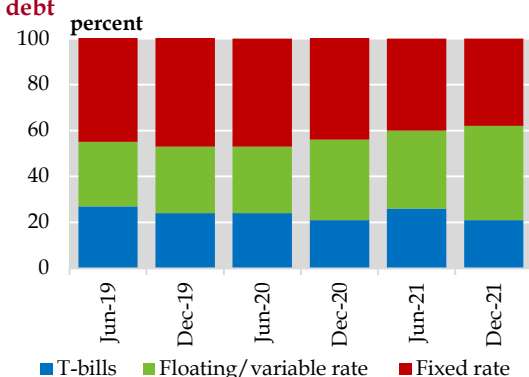
In overall terms, the pickup in current spending overshadowed the expansion in revenues, leading to deterioration in fiscal indicators during Q2-FY22. The fiscal deficit more than doubled to 1.5 percent of GDP in Q2-FY22, from 0.7 percent in Q1-FY22 and 1.2 percent of GDP in the same period last

year. Similarly, the surplus in the primary balance in Q1-FY22 turned into a deficit, whereas the revenue deficit also widened in Q2-FY22 (**Figure 4.1c**).

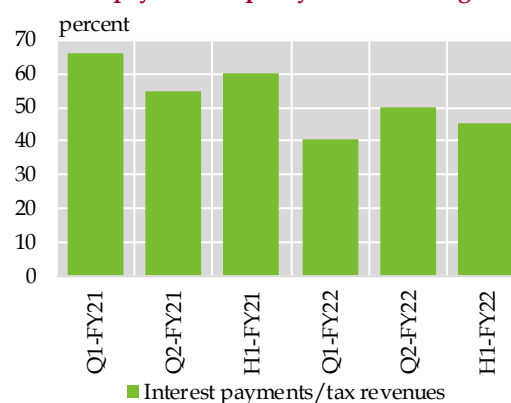
With the increased availability of external inflows, the financing requirements of the deficit were mostly met through external resources. Large revaluation losses and deficit financing needs contributed to a sizeable increase in public debt during H1-FY22. In terms of composition, most of the increase in debt was sourced through long-term instruments. However, with the introduction of long-term domestic debt securities carrying floating rates, the composition of domestic debt has shifted towards variable rate instruments replacing the stock of Market Treasury Bills (MTBs) and fixed rate debt (**Figure 4.2**). While this has improved the overall maturity profile of public debt, the interest-rate risk has intensified as most of the funds are contracted on variable/floating rates in an interest rate rising environment.

Keeping a balance between lengthening of maturity profile and repricing risks is important to ensure debt sustainability.

Increasing Share of Floating/Variable Rate Domestic debt **Figure 4.2**



Debt Repayment Capacity **Figure 4.3**



Already, with the increasing share of variable-rate paper, the debt servicing capacity of the country as measured by interest payments-to-tax revenues started to deteriorate in Q2-FY22 (Figure 4.3). Furthermore, there is a need to diversify the

financing options to keep a check on the cost of borrowing. This can be achieved by reforms to deepen the debt market by focusing on non-bank financing resources, e.g., pension funds, corporations, etc.

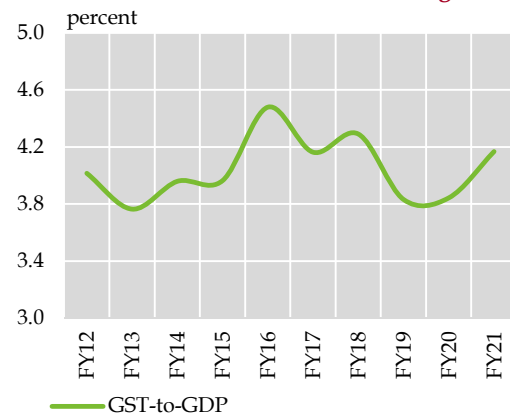
Box 4.1: Tax Exemptions Erode the Tax Base of General Sales Tax (GST) in Pakistan

Pakistan has a large dependence on GST for mobilizing tax revenues like other developing economies. The country's GST revenues slightly increased from 4.0 percent of GDP in FY12 to 4.2 percent in FY21, which was accompanied by an increase in the tax rates from 16 percent to 17 percent (Figure 4.1.1).¹ In overall terms, the share of GST collection in total taxes almost remained unchanged at 41 percent during this period. An international comparison suggests that while the GST rate in Pakistan is close to the median of the peer countries, tax collection is lower by international standards (Figure 4.1.2). This lackluster performance is driven by a range of issues, including extensive tax exemptions, weak tax administration and low tax compliance. These factors have impaired the efficiency of the country's GST regime by corroding the tax base. In this background, this box estimates the efficiency of GST in Pakistan to evaluate the impact of these structural bottlenecks on tax collection.

The efficiency of GST is the ratio of actual GST revenues mobilized in a year with the potential revenues that could be collected if the tax was perfectly enforced at the standard rate, on all consumption, in the absence of exemptions. This notion is referred to as C-efficiency in the literature and is measured as follows: $E^c = \frac{V}{\tau_s C}$

where V is VAT revenues, τ_s is the standard tax rate, C is consumption and E^c shows C-efficiency. C-efficiency is the ratio of actual VAT revenues with the product of standard tax rate and consumption [Ebrill et al (2001), Keen (2013)].^{2,3} A value of 100 indicates the best possible case, where all consumption is taxed at a uniform rate. A lower value of E^c indicates departure from a standard tax rate on consumption, tax avoidance, exemptions and other administrative issues. Likewise, a value greater than 100 indicates double taxation arising from levies on both intermediate and final consumption and the inclusion of investment in the VAT base. Thus, revenue mobilization in countries having similar tax rates may differ because of variations in the efficiency of the tax system.

Performance of GST in Pakistan Figure 4.1.1



Source: Federal Board of Revenue

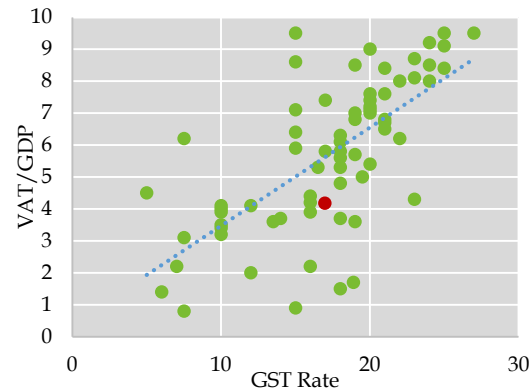
¹ During the economic slowdown of FY19 and the Covid-led contraction of FY20, GST collection fell to 3.8 percent of GDP.

² The data for consumption is obtained from National Income Accounts.

³ Ebrill, L. P., Keen, M., and Perry, V. J. (2001). Understanding the Revenue Performance of VATs. In The Modern VAT. International Monetary Fund; M. Keen (2013). The anatomy of the VAT. Working Paper/13/111. Fiscal Affairs Department. Washington D.C.: IMF;

A large strand of literature has used the concept of C-efficiency to evaluate the performance of value-added taxes (VAT). For instance, Wahid, (2010) estimated average C-efficiency of GST in Pakistan during FY00-10 to be at 28 percent and identified that multiple tax rates and a high volume of tax exemptions lead to low tax efficiency in Pakistan.⁴ Similarly, Cevic (2016) estimated that C-efficiency of GST in Pakistan increased from 0.11 in 1990 to 0.23 in 2015 and highlighted that a low C-efficiency of GST in Pakistan reflects a significant use of tax exemptions.⁵ Ueda (2017) analyzed the key drivers of C-efficiency of VAT revenues in advanced economies and identified that variations in C-efficiency correlates with output gap.⁶ The literature suggests that the impact of GST taxes on economic growth depends on tax design. An increase in GST revenues through an improvement in C-efficiency is considered to be growth enhancing compared to general increase in tax rates [Ormaechea, et al (2019)].⁷ C-efficiency is a commonly used indicator for measuring revenue performance across countries. OECD publishes the VAT efficiency ratio in the annual publication on 'Consumption Tax Trends' OECD (2020).⁸

An International Comparison of GST Rates **Figure 4.1.2**



Sources: OECD Revenue Statistics & Trading Economics

Based on the formula, the C - efficiency of Pakistan's GST revenues oscillated between the range of 24 to 29 percent during FY12-21, showing little variation. For FY21, the ratio stood at 26 percent with a marginal improvement in FY19 and FY20 (**Figure 4.1.3 a, b and c**). This indicates that a one point GST was associated with 0.26 percentage points increase in the GST-to-GDP ratio in FY21. This implies that during FY21, 74 percent of the potential GST revenue was not collected because of inefficiencies of the tax system such as tax exemptions, low compliance, and issues in tax administration. An international comparison shows that while the C - efficiency of GST in Pakistan is better than the worst performing African countries, it is one of the lowest in Asia, and is also below the least efficient VAT systems in the EU and OECD countries (**Figure 4.1.4**)⁹.

⁴ U. Wahid (2010). Economic Analysis of the Reformed General Sales Tax/VAT in Pakistan. Volume 10 No.1. FBR Quarterly Review. Strategic Planning and Research & Statistics Wing. Islamabad: Federal Board of Revenue. Federal Board of Revenue.

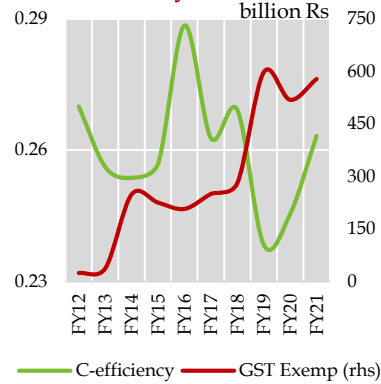
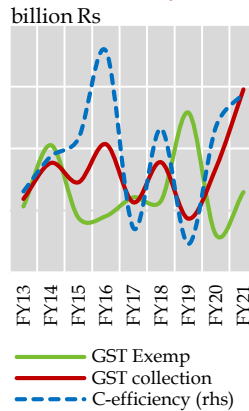
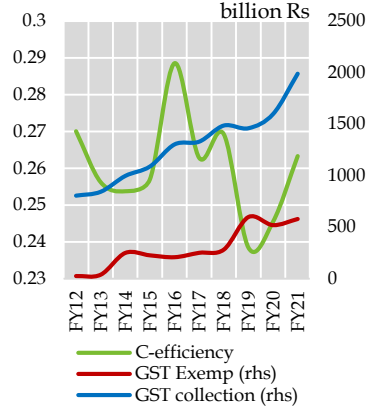
⁵ M. S. Cevic (2016). Unlocking Pakistan's revenue potential. Working Paper/16/182. Fiscal Affairs Department. Washington D.C.: IMF;

⁶ M. J. Ueda (2017). The evolution of potential VAT revenues and C-efficiency in advanced economies. Working Paper/17/158. Fiscal Affairs Department. Washington D.C.: IMF;

⁷ Ormaechea, M. S. A., & Morozumi, A. (2019). The value added tax and growth: Design matters. Working Paper/19/96. Institute for Capacity Development. Washington D.C.

⁸ OECD (2020), Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues, OECD Publishing, Paris, <https://doi.org/10.1787/152def2d-en>.

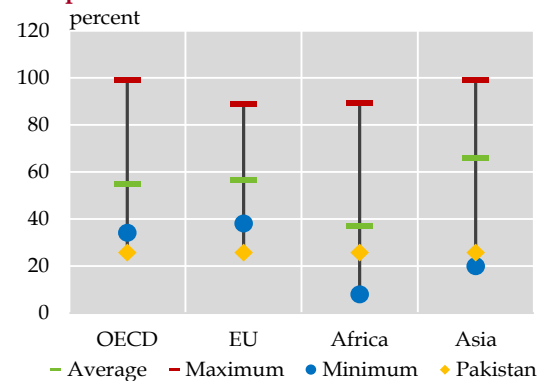
⁹ OECD Revenue Statistics, 2020, available at: www.stats.oecd.org/Index.aspx?DataSetCode=RS_GBL, accessed on January 15, 2022.

GST Exemptions & Tax Efficiency**Figure 4.1.3a****Trend in GST Follows C-efficiency****Figure 4.1.3b****Key Drivers of GST Collections****Figure 4.1.3c**

Source: FBR, SBP estimates

The trend of the GST revenues and its key drivers shows that C- efficiency had a large bearing on GST collection during FY12-21. This implies that GST collection can be enhanced by improving the C- efficiency of tax system without introducing a general increase in tax rates. A long-term comparison shows that a significant increase in GST exemptions during FY12-21 hampered the C- efficiency of GST during this period. For instance, five export-oriented sectors (textile, leather, carpets, sports goods and surgical goods) had been enjoying zero-rating since FY12. In FY19, the revenue impact of these exemptions stood at Rs 86.7 billion. To improve the revenue generation, these exemptions were withdrawn in FY20, which led to Rs 73 billion reduction in tax exemptions during FY20.

These exemptions reduced the taxable consumption and narrowed the tax base for GST; hence, the years with increase in exemptions are marked by a decline in c-efficiency. Moreover, in Pakistan, efforts to improve tax administration and broaden the tax base are already underway. A sustained focus on rationalization of tax exemptions, expanding the tax base and improved tax administration would be instrumental in ensuring a long-term increase in tax revenues.

C-Efficiency of VAT - Country Comparison**Figure 4.1.4**

Source: OECD Revenue Statistics & Trading Economics

4.2 Revenues

Revenue collection posted a notable increase of 18 percent in H1-FY22, compared to 3.7 percent last year. The entire increase came from tax revenues, which offset the 14.6 percent decline in non-tax revenue (NTRs) during this period (**Table 4.2**). In terms of

quarterly performance, the growth in tax receipts marked a slight slowdown in Q2-FY22, compared to Q1-FY22. On the other hand, NTR receipts somewhat improved during Q2-FY22.

The slowdown in tax receipts during the Q2-FY22 mainly emanated from decline in

Consolidated Revenue Collection**Table 4.2**

billion Rupees, growth in percent

	Collection						Growth					
	Q1		Q2		H1		Q1		Q2		H1	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
Total Revenue (1+2)	1478.7	1808.5	1872.4	2147.5	3351.2	3956.0	-0.7	22.3	7.4	14.7	3.7	18.0
1. Tax Revenue (a+b)	1122.4	1532.8	1333.5	1658.3	2455.9	3191.0	5.0	36.6	7.6	24.4	6.4	29.9
(a) Federal	1010.6	1398.0	1199.4	1521.8	2210.0	2919.8	4.8	38.3	6.2	26.9	5.6	32.1
(b) Provincial	111.8	134.8	134.1	136.4	245.9	271.2	7.0	20.6	22.0	1.8	14.7	10.3
2. Non Tax Revenue	356.3	275.7	538.9	489.2	895.3	764.9	-15.2	-22.6	6.9	-9.2	-3.1	-14.6

Source: Ministry of Finance

domestic sales tax collection. Specifically, the GST collection on POL products showed a decline because of both a reduction in GST rate as well as a slowdown in POL sales. On other hand, the pace of contraction in NTRs slightly reduced in Q2-FY22 with an increase in PDL rates on POL products.

FBR Collections

During H1-FY22, FBR tax collection posted a 32.5 percent expansion, against a 5.3 percent increase in the same period last year (Table 4.3). This was despite a decline in GST collection on the domestic stage during Q2-FY22. Import related taxes – GST and custom duty – had a major share in this increase (Table 4.4). In addition, improvement in

economic activity relative to last year and continued tax administration efforts further augmented this increase. These factors helped FBR surpass the half-yearly collection target by Rs 285 billion. Tax collection during H1-FY22 stood at 50 percent of the annual budgeted target, which exceeded the level seen in the past few years – FY20 being an exception, when the target was revised down twice amid outbreak of Covid-19 (Figures 4.4 and 4.5).

Tax administration efforts

Tax authorities stepped up tax administration reforms during H1-FY22 with an aim to improve administrative efficiency,

FBR Tax Collection**Table 4.3**

billion Rs, growth in percent

	Collection						Growth					
	Q1		Q2		H1		Q1		Q2		H1	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
FBR Taxes (a+b)	1,010.2	1,396.4	1,193.8	1,523.4	2,204.0	2,919.9	4.8	38.2	5.7	27.6	5.3	32.5
(a) Direct Taxes	362.7	481.4	463.5	539.9	826.2	1,021.4	2.0	32.7	8.1	16.5	5.3	23.6
(b) Indirect Taxes	647.6	915.0	730.3	983.5	1,377.8	1,898.5	6.4	41.3	4.3	34.7	5.3	37.8
Import related	390.1	644.2	452.7	725.3	842.8	1,369.5	3.7	65.1	13.5	60.2	8.8	62.5
Customs Duties	154.2	218.8	179.9	258.4	334.1	477.2	-0.9	41.9	4.3	43.6	1.8	42.8
Sales Tax	434.9	625.3	481.9	649.7	916.8	1,275.0	7.7	43.8	6.0	34.8	6.8	39.1
Imports	235.9	425.4	272.7	466.9	508.6	892.3	7.0	80.4	20.5	71.2	13.8	75.4
Domestic	199.0	199.9	209.1	183.8	408.1	383.7	8.1	0.4	-7.8	-12.1	-0.7	-6.0
Federal Excise	58.4	70.9	68.5	75.4	126.9	146.3	18.8	21.4	-6.2	10.1	3.8	15.3

Source: Federal Board of Revenue

Import Related Taxes during H1 **Table 4.4**
billion Rs, growth in percent

	FY21	FY22	Growth	
			FY21	FY22
Import related taxes	937.3	1,505.1	21.0	60.6
Sales tax (imports)	508.6	892.3	13.8	75.4
Customs duty	334.1	477.2	3.0	42.8
WHT (imports)	90.8	132.4	-14.2	45.8

Source: Federal Board of Revenue

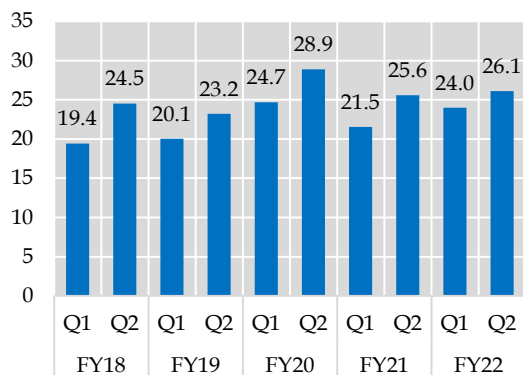
limit tax evasion and ensure ease of doing business.

Some of the important measures include: (i) Introduction of Track and Trace system (TTS) for tobacco and sugar sectors to facilitate documentation of the economy and address tax evasion in these sectors (**Box 4.2**);¹⁰ (ii) Initiating integration of large retailers on POS system. FBR introduced POS invoicing system in FY21 by integrating tier 1 retailers. To improve documentation and expand tax base, this system is now extended to large retailers. A total of 1572 retailers were integrated in this system with installation of 14,160 POS machines during FY21.¹¹ In

continuation of these efforts, FBR has targeted to integrate the largest 500 retailers in this system in FY22; and (iii) Introduction of a single sales tax portal in collaboration with the provincial revenue authorities. This step will reduce the cost of doing business by containing the time and expense of tax compliance. For instance, this portal will allow taxpayers to file single monthly sales tax returns instead of six returns on provincial revenue portals, previously; (iv) FBR has introduced Pakistan Single Window (PSW) in order to reduce clearance times for legitimate trade; (v) the mechanism of e-hearing has been formulated to provide contact-less tax administration resulting in reduced compliance time.

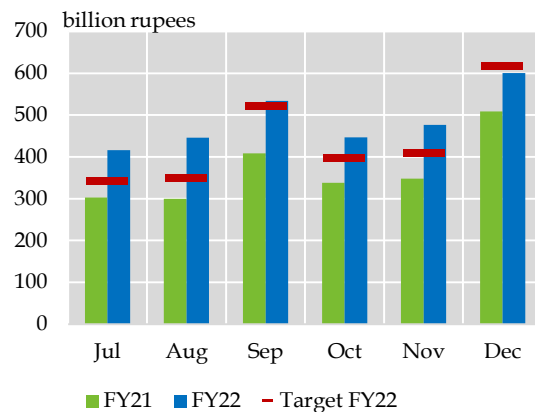
In addition, the authorities continued compliance with the Financial Action Task Force (FATF) action plans regarding anti-money laundering/countering the financing of terrorism (AML/CFT) for Designated Non-Financial Business and Professions (DNFBPs). In this backdrop,

Revenue Collection as Percent of Target **Figure 4.4**



Source: Ministry of Finance

Tax collection Against Target **Figure 4.5**



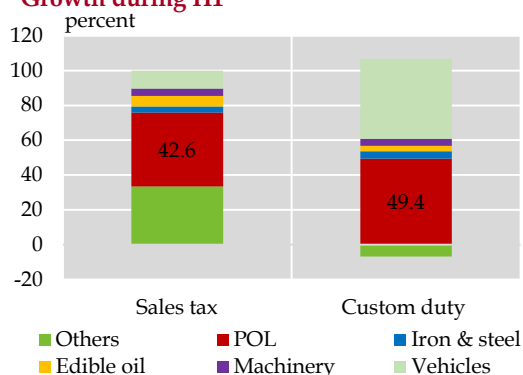
Source: Federal Board of Revenue

¹⁰ TTS on tobacco and sugar was introduced October and November 2021 respectively.

¹¹ FBR Biannual Review July-December 2021-22 (Vol. 21, No. 1) - A Review of Resource Mobilization Efforts of Federal Board of Revenue

Major Revenue Spinners in Indirect Taxes - Share in Growth during H1

Figure 4.6



the FATF plenary had approved two actions specific to Designated Non-Financial Business and Professions in June 2021, which are being regulated by the FBR. Since then, the FBR has launched an online portal and a mobile app to facilitate the DNFBPs in implementing AML/CFT regulations, including generating Suspicious Transaction Reports. Meanwhile, the FBR has carried out number of inspections of DNFBPs to minimize tax evasion and imposed fines on non-compliance.¹²

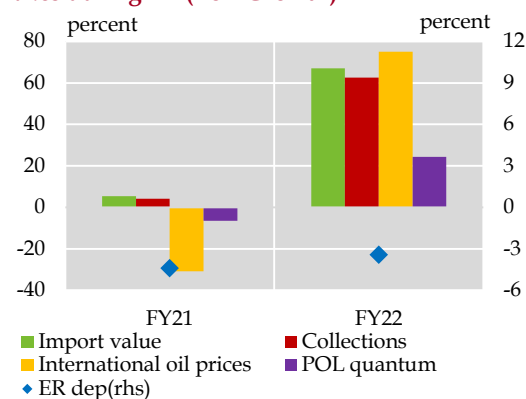
Indirect taxes displayed a strong performance

Collections from indirect taxes grew strongly during H1-FY22. The entire increase came from import related taxes, whereas domestic sales tax collection tapered off during this period.

Specifically, around one-half of the surge in these taxes came from POL products alone during H1-FY22 (**Figure 4.6**). This increase shows the combined impact of rising import volumes, surge in international oil prices as well as PKR depreciation (**Figure 4.7**).

Drivers of Increase in Import Related Taxes during H1 (YoY Growth)

Figure 4.7



Box 4.2: Track and Trace System - A step towards containing tax evasion in Pakistan

FBR implemented Track and Trace System (TTS) on tobacco and sugar sectors during Q2-FY22, with an aim to improve tax collection. TTS ensures electronic monitoring of goods through the entire supply chain from production/imports to retailers to curb tax evasion and illegal production/supply of goods. It is implemented by means of Unique Identification Marking (UIM) or tax stamps that carry digital features to ensure electronic traceability of goods. These stamps are applied to each batch of the goods produced and supplied to the market and help in differentiating between the registered and unregistered supplies. This system aids tax authorities to check supply of smuggled, counterfeit and unregistered products.

¹². Source: FBR Press Release dated October 21, 2021, available at <https://www.fbr.gov.pk/pr/fbr-completes-fatf-actions-on-dnfbps-ahead-of/163201>, accessed on January 15, 2022.

Furthermore, TTS provides a near real time data of production volumes at a centralized point to the tax collection authority.

Various forms of monitoring systems to check tobacco trade have existed for more than a decade, globally. As of now, track and trace system is being used in over 80 countries worldwide.¹³ However, Protocol to Eliminate Illicit Trade in Tobacco Products (ITP) from the WHO Framework Convention on Tobacco Control (FCTC) came into force in 2018.¹⁴ The ITP requires all parties to introduce track and trace system to monitor tobacco trade.

The absence of a reliable system to monitor and collect information about production/sales activities has remained a significant impediment in the tax collection efforts of FBR. Particularly, a sizeable amount of revenues from indirect taxes at domestic stage (GST and FED) is lost each year because of under-reporting of production and sales of various goods. For instance, according to FBR estimate, Rs 70 billion tax evasion takes place each year in tobacco sector alone.^{15,16} To tap these potential revenues, FBR was in the process of introducing TTS since the past few years. However, the system could not be introduced because of various challenges such as lack of expertise and legal issues.¹⁷ During Q2-FY22, the authorities successfully implemented this monitoring system on tobacco and sugar sectors, with an aim to extend coverage to fertilizer, cement and beverages in the near future.

FBR specified the rules for TTS in 2019, in an earlier attempt to introduce the system.¹⁸ According to these rules, the TTS service provider is responsible for ensuring installation of the stamping machines at all the production facilities and import stations of the specified sectors. These machines have to be integrated with the centralized system (centralized control room) at FBR, for recording the production volumes in real time. Every manufactured package (including a tin, container or bottle, of the specified goods) is required to be stamped before dispatch from the production premises. The tax stamp could be a banderole, sticker, label, barcode, etc. While at the manufacturer end, all the production facilities have to be made available for installation of the system, routine operations and inspection of the system. Also, the manufacturer is responsible for providing the requisite quantity of tax stamps/stickers.

FBR established an enforcement and monitoring wing named Inland Revenue Enforcement Network (IREN) in February 2019 to ensure the smooth functioning of TTS with the aim to curb tax evasion in these specific sectors. The IREN mobile squads check the supplying vehicles and storage places to make sure

¹³ Source: FBR News Letter, ReveNews, issue month – November 2021, available at:

<https://download1.fbr.gov.pk/Docs/2022161614145437ReveNewsIssueNovember2021Eng.pdf>

¹⁴ World Health Organization, available at: https://www.who.int/fctc/protocol/illicit_trade/protocol-publication/en/, <https://www.who.int/fctc/mediacentre/news/2018/protocol-officially-entering-into-force/en/>, accessed on January 15, 2022.

¹⁵ FBR News Letter, ReveNews, issue month – November 2021

<https://download1.fbr.gov.pk/Docs/2022161614145437ReveNewsIssueNovember2021Eng.pdf>

¹⁶ The indirect tax revenues (at domestic stage) from tobacco sector stood at Rs 135.3 billion during FY21.

¹⁷ TTS was initially introduced in 2019, however, the system could not be implemented because of litigation issues

<https://download1.fbr.gov.pk/SROs/2019226162246842SRO250of2019SalesTaxRules2006.pdf>,

<https://www.fbr.gov.pk/fbr-clarifies-the-delay-in-the-implementation-of-track--trace-system/132239>, accessed on January 15, 2022.

¹⁸ S.R.O. 250(I)/2019 dated 26th February, 2019

that the products are stamped; the products without tax stamps are confiscated. For instance, IREN has detected a sizeable amount of tax evasion in tobacco and sugar sectors during Jul- November 2021¹⁹.

Import Related Taxes in Indirect Taxes during H1

Table 4.5

billion rupees, growth in percent

	FY21	FY22	Growth	
			FY21	FY22
Sales tax (A)	508.6	892.3	9.7	75.4
POL	109.8	273.2	-14.0	148.9
Iron and Steel	59.4	72.1	10.7	21.4
Edible oil	31.1	55.0	28.1	76.8
Machinery	33.3	49.3	4.6	48.2
Vehicles	28.2	67.6	21.6	140.1
Custom duty (B)	334.1	477.2	3.0	42.8
POL	40.3	110.9	-11.1	175.1
Vehicles	36.9	102.6	20.7	177.9
Iron and Steel	27.3	33.4	20.0	22.5
Machinery	17.7	23.6	7.7	33.4
Edible Oil	15.9	20.3	3.6	27.5
Total (A+B)	842.8	1,369.5	4.1	62.5

Source Federal Board of Revenue

Similarly, the rising automobiles' demand in the domestic market and the ensuing increase in import of CKD and CBU vehicles also bolstered import related taxes during the entire H1-FY22 (Table 4.5). Further impetus in tax collection came from food imports, which was mainly price-led; higher prices of food items in global markets boosted import values and helped increase collection this year.

Reduced GST rates on POL dragged domestic tax collection

Domestic sales tax collection dropped by 6.2 percent in H1-FY22 compared to a 3.2 percent expansion last year (Table 4.6). This decline was skewed toward Q2-FY22 when the GST rate on petrol was brought down to zero in December 2021 (Figure 4.8). In

Domestic Taxes during H1

Table 4.6

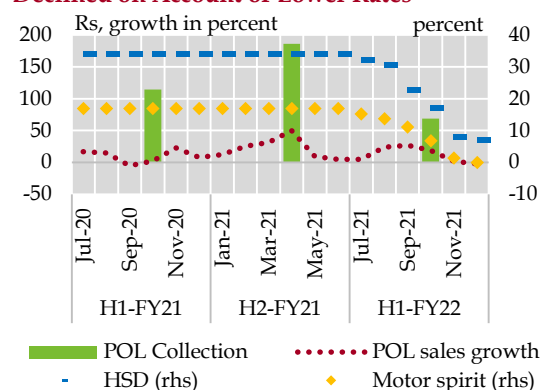
billion rupees, growth in percent

	FY21	FY22	Growth	
			FY21	FY22
Sales tax (A)	408.1	382.7	-0.6	-6.2
POL	114.6	68.9	-16.1	-39.8
Electricity	77.0	78.7	37.0	2.3
Cement	27.3	31.0	147.0	13.6
Sugar	14.2	17.8	-14.1	25.9
Cigarettes	11.2	14.0	23.9	25.0
Vehicles	4.8	2.4	27.8	-50.0
FED	126.9	146.3	1.5	15.3
Cigarettes	44.7	52.7	26.1	18.1
Cement	37.5	35.1	5.8	-6.5
Vehicles	1.9	9.4	n-a	408.3
Total (A+B)	535.1	529.0	-0.1	-1.1

Source: Federal Board of Revenue

addition, weakening sales of POL products during Q2-FY22 further dented collection in the second quarter. (Table 4.7). Notably, the contraction in the GST on POL at the domestic stage alone offset the expansion in

GST (Domestic) Collections Declined on Account of Lower Rates **Figure 4.8**



Source: FBR and OCAC

¹⁹ Rs. 178 million worth of illegal cigarettes were confiscated during Jul-Nov FY22. Similarly, in case of sugar, 172 bags of unstamped sugar were seized by IREN in November 2021.

Economic Growth Indicators**Table 4.7**

percent

	LSM		Auto Sales		POL Sales		Electricity		Steel		FMCG	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
Q1	-2.6	9.7	9.9	57.3	10.5	17.9	1.3	7.9	26.0	29.3	23.0	23.1
Q2	5.5	5.6	43.7	46.2	11.5	6.3	4.2	11.7	53.2	43.2	17.8	22.3

Sources: PBS, PAMA, OCAC and SBP

collection from electricity, sugar, electronics and cigarettes. However, the scale of economic activity as well as general price level remained higher compared to last year that provided some support to GST collection. Furthermore, the implementation of Track and Trace System to curb the revenue loss aided collections from sugar and cigarettes at domestic stage in H1-FY22.

In the case of FED, the collections rose to Rs 146.3 billion in H1-FY22 compared to 126.9 billion last year. Cigarettes, being the major contributor, helped increase the overall FED collections, followed by vehicles. Furthermore, the continued momentum of the sales of vehicles in H1-FY22 also boosted these collections.

Higher collection from WHT and voluntary payments improved direct tax collection

The continued administrative efforts and income tax reforms shored up direct tax collection during H1-FY22. Around one-quarter of the overall surge in FBR taxes came from direct taxes in this period. The main contribution to this growth came from

withholding taxes (WHT) followed by voluntary payments.

Quarterly analysis reveals some slowdown in the pace of direct tax collection in Q2-FY22 compared to Q1-FY22. This partly reflects the impact of concentration of filing of income tax returns during Q1-FY22 as the last date for the filing of income tax returns fell due on 15th October this year. In overall terms, taxpayers filed 2.6 million returns by the last date, with a tax payment of Rs 48.6 billion. Out of this, 1.86 million returns were filed in Q1-FY22 with a tax payment of Rs 39 billion compared to Rs 6.9 billion in corresponding period last year.²⁰

In overall terms, voluntary payments grew by 21.5 percent in H1-FY22, compared to 3.4 percent in H1-FY21 (**Table 4.8**). Collections on demand posted a sharp decline in H1-FY22 against the same period last year. This decline is attributed to an increased recovery period for the amount claimed in demand notices. This relaxation aimed at providing a conducive environment to the businesses.²¹ Meanwhile, the recent Corporate Income Tax (CIT) reforms also led to an increase in direct

²⁰ The filing of income tax returns still continues with total number of returns at 3 million and tax payment of Rs 69.8 billion by end January 2022, against 3.3 million returns filed in FY21 with payment of 52.7 billion.

²¹ During Q2-FY22, the recovery date of the taxable amount claimed in demand notices was extended beyond 90 days, compared to maximum 30 days in Q1-FY22.

taxes (net of refunds). This can be seen from a 90.3 percent decline in the amount of refunds during H1-FY22 compared to same period last year.²²

Within WHT, most of the expansion in tax collection stemmed from imports, followed by salaries and contracts. WHT from imports contributed the most (7.3 percentage points) in overall withholding taxes, followed by salaries and contracts (Figure 4.9). As discussed earlier, the higher rupee value of imports propped up WHT collection. The rise in contracts mirror the expansion in construction activity in private as well as public sector. Similarly, the increase in the salaries of government employees as announced in the FY22 budget strengthened WHT collection from salaries. On the other hand, collection from telephone and cash withdrawal declined following the reduction of 5 percent WHT rate on telephone and removal of 0.6 percent tax on cash withdrawals for non-filers as announced in the budget.

Non-tax Revenues

Non-tax revenues (NTRs) posted a decline of 14.6 percent in H1-FY22 compared to a 3.1 percent decline last year (Table 4.9).

This decline was explained mainly by the decrease in collections from Petroleum Development Levy (PDL) and mark-up payments, which more than offset the increase in other NTR components. Consequently, only a third of the budget estimate was collected during H1-FY22 compared to 55 percent last year.

Direct Taxes during H1

billion rupees, percent

Table 4.8

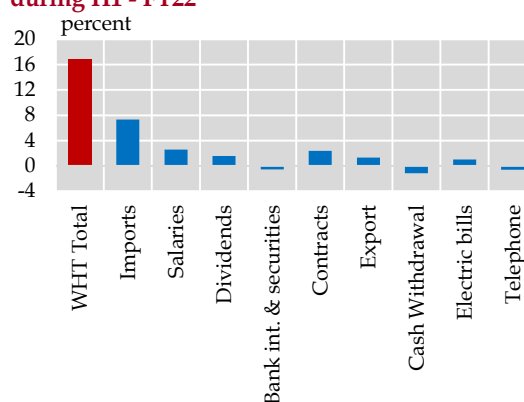
	FY21	FY22	Growth	
			FY21	FY22
Collection on demand	38.5	20.3	95.3	-47.3
Voluntary payment	256.7	312.0	3.4	21.5
Returns	45.1	66.7	n-a	47.8
Withholding Taxes	569.3	665.1	4.6	16.8
Imports	90.8	132.4	-14.2	45.8
Salaries	69.8	84.5	21.4	21.0
Dividends	30.1	39.1	-1.1	30.1
Bank interest & securities	67.6	64.5	19.3	-4.6
Contracts	120.3	133.8	6.7	11.2
Export	20.2	27.8	1.7	37.5
Cash withdrawal	6.9	0.3	-19.5	-96.3
Electricity bills	25.9	31.8	4.1	22.9
Telephone	30.8	27.4	13.8	-11.0
Other WHT	190.6	210.8	5.1	10.6
Total direct taxes	829.2	1,021.4	5.6	23.2

Source: Federal Board of Revenue

The decline in NTRs was observed in both the quarters of FY22. However, the pace of this deterioration was lower in Q2-FY22 compared to Q1-FY22. This decline was mainly attributed to lower collections from PDL due to a downward adjustment in PDL rates compared to last year. The authorities

Growth Contribution in WHT during H1 - FY22

Figure 4.9



Source: Federal Board of Revenue

²² Before CIT, the income tax exemptions were claimed in the form of refunds.

Non-tax Revenues (consolidated)**Table 4.9**

billion Rs, growth in percent

	Q1		Q2		H1		Growth		
	FY21	FY22	FY21	FY22	FY21	FY22	Q1	Q2	H1
SBP profits	105.0	109.0	267.5	271.0	372.5	380.0	3.8	1.3	2.0
PTA profits	8.2	30.1	10.5	8.8	18.6	38.9	269.2	-16.1	108.9
Mark-up (PSEs & others)	25.7	19.5	18.3	13.1	44.0	32.6	-24.1	-28.4	-25.9
Royalties on gas & oil	14.6	21.7	20.5	17.3	35.1	39.1	48.5	-15.5	11.2
Dividends	1.5	1.9	10.4	24.1	11.9	26.0	27.3	132.0	118.8
Passport & other fees	3.0	6.1	4.0	4.3	7.0	10.4	106.7	6.8	49.2
Defence	2.9	2.8	3.7	4.9	6.5	7.7	-1.3	34.3	18.6
Petroleum levy	136.4	13.3	139.0	56.7	275.3	70.0	-90.2	-59.2	-74.6
GIDC	5.0	6.5	4.6	4.6	9.5	11.2	30.8	2.1	17.1
Total	356.3	275.7	538.9	489.2	895.3	764.9	-22.6	-9.2	-14.6

Source: Ministry of Finance

had lowered PDL rates during Q1-FY22 to protect consumers from the impact of rising international oil prices. Subsequently, the government managed to collect only 11.5 percent of the budgeted target. However, this relief measure had a large revenue impact; hence, the rates were adjusted up from September 2021 (**Figure 4.10**). Another segment that contributed to the contraction in NTRs was mark-up receipts. These collections dropped on account of a 190 basis points reduction in the mark-up rate charged on development loans to PSEs and provinces.²³

In contrast, the SBP profits remained almost at the last year's level during H1-FY22. The interest earnings from open market operations (OMO) in Q1-FY22 partly offset the impact of net retirement of the government debt stock with SBP. However, in Q2-FY22, the transfer of SBP profits increased as the SBP paid Rs 167 from balance surplus of last fiscal year to the

government. It may be recalled that a similar payment was transferred to the government in the same period last year. Moreover, the receipts from dividends also increased in both the quarters of FY22. This rise could be traced to the higher profits of OGDCL and PPL during H1-FY22.²⁴ The receipts from these two institutions contribute the most (80 percent) of the total dividend income.

4.3 Federal Expenditures²⁵

Federal expenditures rose by 20.4 percent during H1-FY22 as compared to 5.0 percent in the corresponding period last year. This was a broad based increase (**Table 4.10**), with a prominent contribution by non-interest spending (**Figure 4.11**). The quarterly analysis reveals some variations in spending pattern between the two quarters. While the current expenditures edged up strongly during Q2-FY22 (**Figure 4.12**), federal development spending lost steam during Q2-FY22.

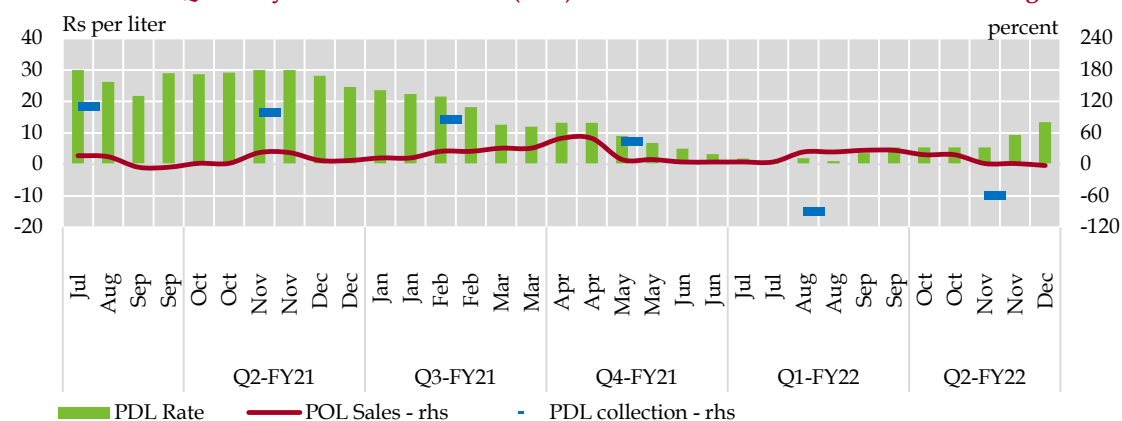
²³ https://www.finance.gov.pk/circulars/circular_11102021.pdf, accessed on January 15, 2022.

²⁴ The earning per share of OGDCL and PPL increased by 63.3 percent and 20.9 percent respectively during Jul-Dec FY22. Also, the dividends disbursed by OGDCL rose by 4.2 percent to 16.1 billion from 15.5 billion last year during this period. (sources: Half Yearly Reports December 2021).

²⁵ The discussion in this section is based on expenditures excluding statistical discrepancy.

PDL Rates and Quarterly Collections Growth (YoY)

Figure 4.10



Source: Ministry of Finance

Federal Current Expenditures

Federal current expenditures surged by 19.4 percent during H1-FY22, which is more than twice the growth seen in the same period last year. Most of this increase came in Q2, which was mainly led by expansion in spending on Covid vaccine and grants for social protection followed by subsidies and interest payments (Figure 4.12).

Spending on vaccine procurement and social protection remained robust

The disbursement of grants more than doubled to Rs 548.9 billion in H1-FY22 from Rs 265.2 billion in the same period last year, with most of the expenditures undertaken in Q2-FY22. The major focus areas were spending under Economic Stimulus Package (ESP) and Benazir Income Support Program (BISP). The main thrust of ESP was on

supporting Covid related vaccination procurement. In this regard, nearly one-third amount in grants was allocated to National Disaster Management Fund for Covid-19 under ESP. Resultantly, the total number of doses administered reached around 142.7 million up till December 2021, with almost 67.8 million individuals fully and 89.1 million partially vaccinated.

The surge in BISP spending is explained by both an increase in the budget allocation for this program as well as an extension in coverage of beneficiaries. The FY22 Budget earmarked Rs 250 billion for BISP spending, with Rs 50 billion increase against last year. Furthermore, the authorities completed the updation of National Socio Economic Registry (NSER) in October 2021 that increased the coverage of households to around 33 million in 2021.^{26 27} As a result, the spending on social protection especially for

²⁶ International Monetary Fund (2022). 2021 Article IV Consultation, Sixth Review Under the Extended Arrangement Under the Extended Fund Facility, And Requests For Waivers Of Applicability And Non-observance of Performance Criteria And Rephasing Of Access – Press Release; Staff Report; and Statement by The Executive Director for Pakistan. Country Report No. 22/27. Washington D.C.: IMF.

²⁷ The last NSER was conducted in 2010-11 that identified 27 million beneficiaries. The government had started to add new beneficiaries on the basis of ongoing updation of NSER since Q3-FY21.

State of Federal Expenditures**Table 4.10**

billion Rs, growth in percent

	H1-FY21	H1-FY22	YoY growth		FY22		YoY Growth	
			H1-FY21	H1-FY22	Q1	Q2	Q1	Q2
Total expenditures* (a+b)	3077.2	3705.7	5.0	20.4	1540.1	2165.5	9.9	29.3
(a) Current expenditure	2807.2	3351.3	6.5	19.4	1360.6	1990.7	7.0	29.6
Mark-up payments	1475.2	1452.9	15.1	-1.5	622.7	830.2	-16.1	13.2
Domestic	1357.0	1312.5	21.1	-3.3	571.1	741.4	-16.6	10.3
Foreign	118.2	140.4	-26.4	18.7	51.6	88.8	-9.7	45.4
Defence affairs and services	486.6	520.5	-8.1	7.0	261.7	258.8	16.6	-1.3
Pension	210.5	251.7	-3.8	19.6	110.7	141.0	27.7	13.9
Running of civil govt.	195.4	209.9	-11.1	7.4	89.5	120.5	0.6	13.1
Subsidies	129.0	313.4	23.8	143.0	73.9	239.5	n.a	89.9
Grants to provinces and others	310.6	603.0	10.3	94.1	202.1	400.9	59.9	117.6
Grants to provinces	45.3	54.1	8.0	19.4	32.6	21.5	80.6	-21.2
Grants to others	265.2	548.9	10.7	106.9	169.5	379.4	56.4	141.8
(b) Development expenditure and net lending	270.0	354.3	-8.5	31.2	179.5	174.8	37.6	25.2
Total development expenditure	243.1	288.3	-14.4	18.6	143.8	144.5	66.4	-7.8
PSDP	232.1	288.3	-15.9	24.2	143.8	144.5	74.3	-3.4
o/w Development grants to provinces	56.6	88.7	46.8	56.5	35.5	53.2	201.5	18.5
Other development expenditure	11.0		35.4	-100.0	0.0	0.0	n.a	n.a
Net lending	26.9	66.0	144.2	145.3	35.7	30.3	-18.9	-277.5
Provinces	-16.8	59.9	-724.6	-456.3	33.1	26.8	-591.5	-365.9
Others	43.7	6.1	424.9	-86.1	2.6	3.5	-94.9	-150.2

* Excluding statistical discrepancy

Source: Ministry of Finance

BISP increased significantly during this period

The expenditure under the Prime Minister's Kamyab Jawan Youth Entrepreneurship Scheme (PMKJ-YES) also picked up with a disbursement of Rs 27.4 million till November 2021.²⁸ Furthermore, a food subsidy program was also initiated in November 2021 that aimed at protecting low-income households from the impact of rising food inflation. Under this initiative, 9.6 million families and over 10,000 retail (Kiryana) stores were registered until mid-December 2021.²⁹

Power subsidies rose substantially

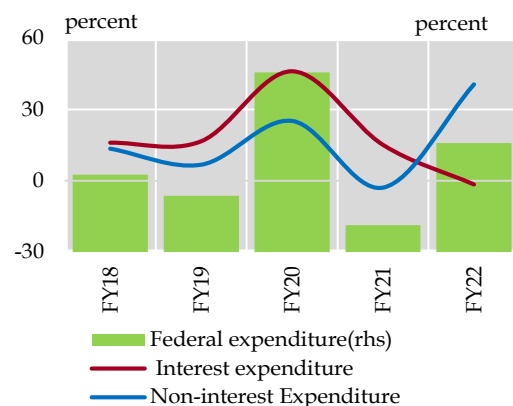
The expenditures on subsidies showed a significant increase during the entire first half. This expansion mainly emanated from power subsidies. The increase was in line with the FY22 Budget estimates that envisaged payment of Rs 266 billion to settle arrears of IPPs/PHPL under the CDMP.

Interest payments moved down slightly during H1-FY22

After rising sharply during FY21, interest payments posted a marginal decline in H1-FY22 because of lower payments on domestic

²⁸ Finance Division (2021). Monthly Economic Update for January 2022. Islamabad: Finance Division

²⁹ Finance Division (2021). Monthly Economic Update for December 2021. Islamabad: Finance Division

Growth in Federal Spending (H1) Figure 4.11

Source: Ministry of Finance

debt. However, these payments grew significantly during Q2-FY22.

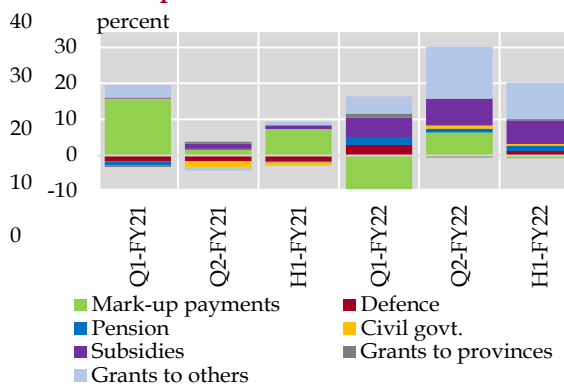
This increase came from an expansion in the government outstanding debt stock amid an increasing interest rate environment during H1-FY22. Moreover, the mark up payments on the foreign debt rose considerably due to the depreciation of PKR against the US dollar.

Pension Spending rose significantly during H1-FY22

Pension expenditures soared by 19.6 percent during H1-FY22 as compared to a decline in H1-FY21. This expansion was underpinned by an increase in pensions of government employees announced in the budget.³⁰

Federal Development Expenditures

Federal PSDP increased by 24.2 percent in H1-FY22 in contrast to a decline of 15.9 percent in H1-FY21. This improvement was

Growth Contribution in Federal Current Expenditures Figure 4.12

Source: Ministry of Finance

in line with the budgetary development priorities of the government that aimed at providing further impetus to economic activity. The development preferences were largely focused on the power sector, regional development, and road infrastructure.

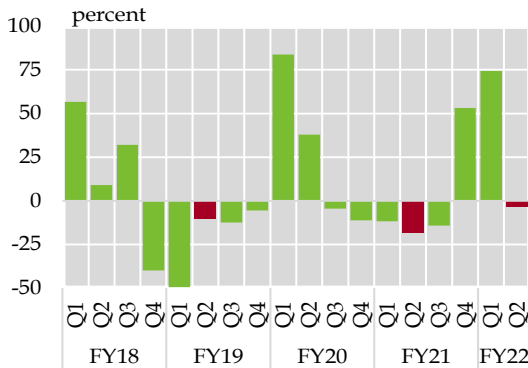
However, the federal PSDP spending dropped by 3.4 percent in Q2-FY22, compared to an 18.1 percent decline in the corresponding period last year. A five-year comparison shows that the pattern of quarterly growth in development spending remains volatile during a year (**Figure 4.13**). The government's efforts to contain fiscal figure deficit by slashing spending as well as factors specific to the independent ministries implementing respective PSDP projects are some of the major factors that influence the pace of development spending.³¹

The actual federal PSDP spending during H1-FY22 stood at 32.0 percent of the total annual development outlay announced in

³⁰ Circular No. 4(1)- Reg.6/2021-486, dated July 8, 2021, Regulations Wing, Finance Division.

Circular No. F.4 (3) R-4/2011 - Revision, dated July 26, 2021, Regulations Wing, Finance Division.

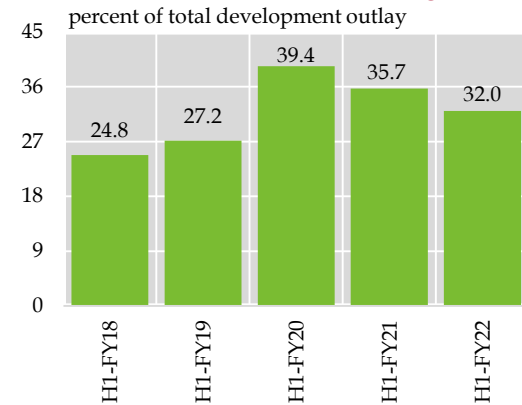
³¹ For reference, see Box 4.3 of the SBP Annual Report FY21 on the State of Pakistan's Economy.

**Federal PSDP Spending
(YoY growth)****Figure 4.13**

Source: Planning Commission

the FY22 budget, which was lower than the last two years (**Figure 4.14**). Furthermore, the actual federal PSDP expenditure was also lower than the benchmark defined in the federal PSDP release strategy.³²

Although the actual spending of federal PSDP declined during Q2-FY22, in overall terms, three areas showed robust spending as seen from PSDP authorization during the second quarter. First, the road infrastructure projects. According to the federal PSDP of 2022, the important projects were Sialkot (Sambrial) – Kharian Motorway (69 km); Improvement, upgradation and widening of Jaglot - Skardu road (S-1, 167 km); dualization & rehabilitation of Karachi - Quetta - Chaman Road (N-25) (460 km); and Hyderabad – Sukkur Motorway (M6). The second priority of federal PSDP during Q2-FY22 was power sector which included Coal Fired Power Project Jamshoro in coordination with Asian Development Bank (ADB), improvement of transmission lines

Federal PSDP Spending**Figure 4.14**

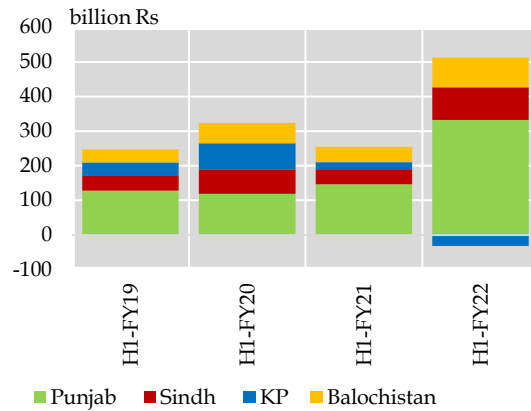
Source: Planning Commission

and grid stations of distribution companies in Sukkur and Hyderabad. The third dominant area of federal PSDP authorization was regional development of Kashmir and Gilgit Baltistan that mainly constitutes the block allocation including multiple development projects for these areas. Here it is important to mention that the federal PSDP allocation for AJK and Gilgit Baltistan was around Rs 70.0 billion for FY22, around two-thirds of which is allocated to the block allocation.

4.4 Provincial Fiscal Operations

The consolidated provincial surplus stood at Rs 480.8 billion during H1-FY22, amounting to 0.8 percent of GDP, which was around 84.0 percent of the annual target for FY22. All provinces contributed to the surplus except for KP, which posted a deficit of Rs 32.0 billion (**Figure 4.15**). A Rs 577.5 billion increase in total provincial revenues offset the Rs 351.9 billion expansion in provincial

³² According to the PSDP release strategy, 20 percent of the federal PSDP spending should be spent in the first quarter; 30 percent in the second and third quarters; and 20 percent in the last quarter of every fiscal year. Source: Revised Release Strategy for Funds Allocated for the Public Sector Development Programme (PSDP) 2019-20, Budget Wing, Finance Division.

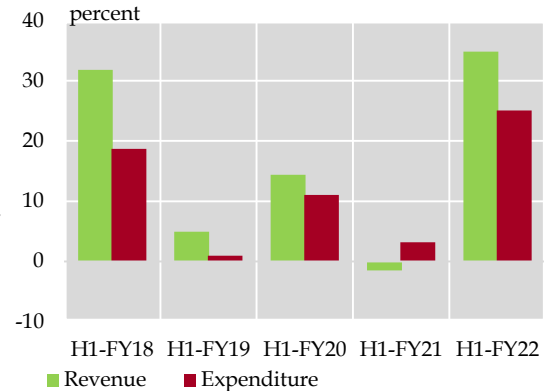
Provincial Surplus during H1**Figure 4.15**

Source: Ministry of Finance

expenditures, driving the overall increase in the surplus (Figure 4.16).

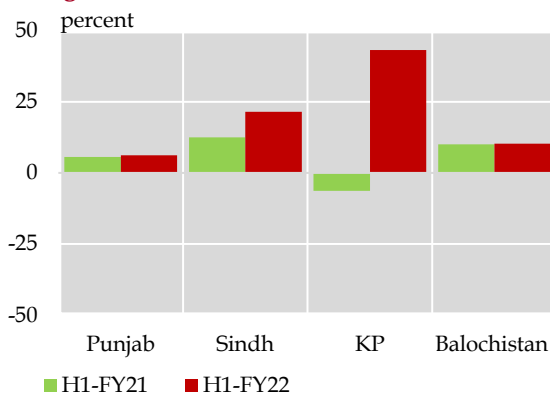
Provincial Revenues

A notable expansion in federal transfers to provinces from the divisible pool resulted in higher provincial revenues. In addition, better revenue collection from provinces' own sources (Figure 4.17a) and higher federal grants to provinces further lifted the growth in provincial revenues.

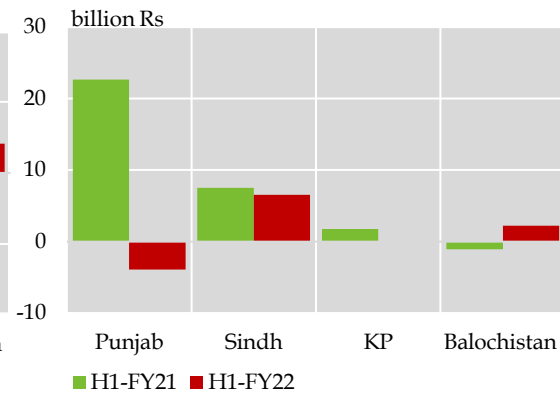
Growth in Provincial Revenue and Expenditure**Figure 4.16**

Source: Ministry of Finance

Provincial own revenue grew by 15.6 percent during H1-FY22, against 6.8 percent increase in H1-FY21 (Table 4.11). The increase in own receipts emerged from both tax and non-tax revenues. Within tax revenues, stamp duties followed by sales tax on services were the major drivers of growth. Particularly, an upsurge in stamp duties had a twenty-five percent share in the overall increase in provincial tax receipts during H1-FY22. Most of the increase came from Punjab, followed by Sindh. The expansion in construction activity in the private sector mainly explains

Provincial Own Revenue - YoY growth**Figure 4.17a**

Source: Ministry of Finance

YoY Change in GSTS Collection - Province-wise**Figure 4.17b**

Source: Ministry of Finance

Provincial Fiscal Operations**Table 4.11**

billion Rs, growth in percent

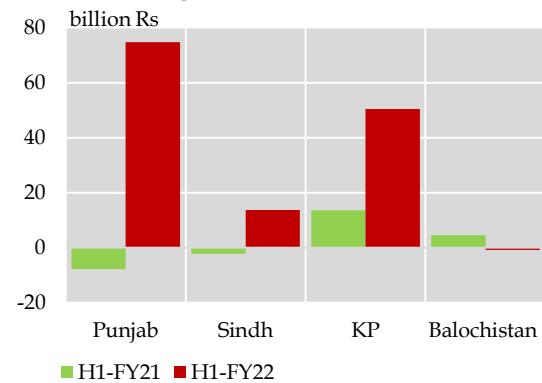
	H1-FY21	H1-FY22	YoY growth		Q1-FY22	Q2-FY22	YoY growth	
			H1-FY21	H1-FY22			Q1-FY22	Q2-FY22
A. Total revenue (a+b+c)	1,658.3	2,235.8	-1.5	34.8	1,077.8	1,158.0	63.6	15.9
a. Provincial share in fed. revenue	1,280.1	1,694.3	-3.5	32.4	807.5	886.8	60.2	14.3
b. Fed loans and transfers	85.2	202.7	2.3	138.0	101.2	101.5	338.1	63.5
c. Provincial own revenue	293.1	338.8	6.8	15.6	169.0	169.8	28.3	5.3
Taxes	245.9	271.2	14.7	10.3	134.8	136.4	20.6	1.8
Non-taxes	47.2	67.6	-21.2	43.1	34.2	33.4	71.0	22.7
B. Total expenditures (a+b+c)	1,403.2	1,755.0	3.2	25.1	800.9	954.2	30.3	21.0
a. Current	1,281.0	1,396.2	12.3	9.0	648.0	748.3	14.5	4.6
b. Development	227.7	365.8	3.8	60.7	153.8	212.0	71.2	53.8
c. Statistical discrepancy	-105.5	-6.9	-	-93.4	-0.9	-6.0	-	-94.3
Overall balance (A-B)	255.1	480.8	-21.2	88.4	276.9	203.8	524.0	-3.3

Source: Ministry of Finance

this increase. The rates of stamp duties remained unchanged in Punjab, whereas Sindh announced a reduction in stamp duty rates during FY22.

The pace of collection from general sales tax on services (GSTS) moderated during H1-FY22, compared to the same period last year. Specifically, the GSTS receipts from Punjab and KP marked a y/y decline during H1-FY22 (**Figure 4.17b**), which pulled down the overall growth in the first half. The primary reason of this decline is a higher base in the same period last year when GSTS in these provinces was adjusted for cross input tax adjustment.³³ However, in the case of Sindh, GSTS collection spurred on the back of higher collections from port and shipping services, followed by telecom and financial services.

The uptick in receipts from non-tax revenues stemmed from hydroelectricity profits – primarily from KP – and receipts on civil

Provincial Development Spending- Absolute Change (YoY) **Figure 4.18**

Source: Ministry of Finance

administration such as revenues from law and order and social services.

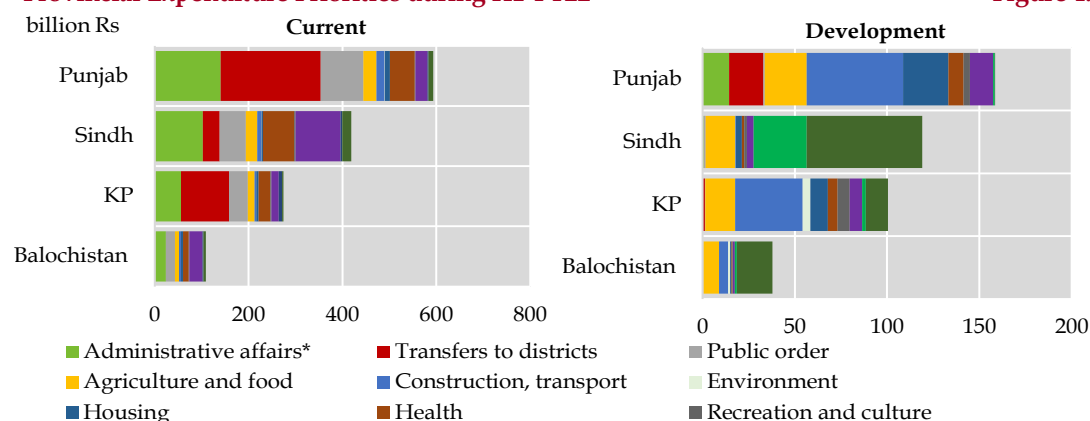
Provincial Expenditures

The total provincial expenditures rose by 25.1 percent in H1-FY22, against a 3.2 percent increase during H1-FY21. The increase was

³³ For reference: State Bank of Pakistan (2021). Chapter 4. Second Quarterly Report on the *State of Pakistan's Economy*. Karachi: SBP.

Provincial Expenditure Priorities during H1-FY22

Figure 4.19



Source: Ministry of Finance

observed across current and development expenditures. However, the pace of development expenditures was much higher than the provincial current spending (Table 4.11).

The increase in current expenditures was contributed by salaries and pensions of government employees. Punjab announced an increase of 10 percent in the salaries and pensions and a 25 percent special allowance for the financially distressed employees in the budget for FY22.³⁴ Likewise, Sindh and KP also announced a 20.0 percent increase in salaries for FY22. This was reflected in higher spending on financial and fiscal affairs of these provinces, specifically for Punjab and Sindh during H1-FY21. In addition, spending on health, education, public order, and district development rose across the provinces to improve service delivery. Some major areas of focus were improvement in hospital services and the continuation of educational projects. Specifically, the volume of current spending on education was the

highest in Sindh compared to other provinces in H1-FY22. Similarly, Punjab introduced the 'District Development Package' worth Rs 360 billion in FY22.³⁵ In this regard, a large sum was transferred to districts during H1-FY22 to expedite the projects.

Moreover, there was some variation in the scale of development spending between the two quarters. While in Q2-FY22, Punjab marked a large increase in development spending, followed by Sindh, whereas KP was the major contributor in provincial development spending in Q1-FY22. In overall terms, Punjab and KP recorded significant increase in development spending during H1-FY22 (Figure 4.18). The development priorities in Punjab mainly addressed agriculture, transport and infrastructure projects. The province of Sindh also focused on agriculture projects along with expenditure on social protection. In KP, allocation to construction and transport

³⁴ Punjab Budget Highlights for FY22. Government of Punjab.

³⁵ Source: Government of the Punjab. Highlights of the Budget 2021-22. Lahore: Punjab government.

dominated the development expenditures during H1-FY22 (**Figure 4.19**).³⁶

4.5 Public Debt

The stock of outstanding public debt reached Rs 42.7 trillion as of the end December 2021 – reflecting an addition of Rs 2.9 trillion during H1 FY22 compared to a Rs 1.1 trillion increase during the same period of last year. This expansion primarily came from the depreciation of PKR against US dollar during H1-FY22 that inflated the rupee value of external debt by Rs 1.7 trillion. In addition, an increase in the government financing requirements further augmented public debt stock in H1-FY22.³⁷ In terms of composition, external debt constituted a little more than three-quarters of the increase in public debt.

The pace of public debt accumulation slightly eased in Q2

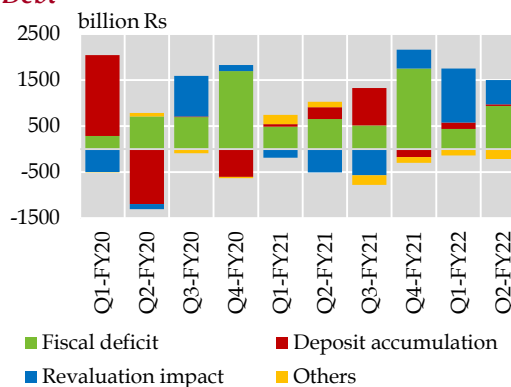
A large part of the increase in public debt i.e., Rs 1.6 trillion out of Rs 2.9 trillion, came in Q1-FY22. The factors underlying the expansion in public debt underwent some change in the two quarters. While Q1-FY22 marked a large Rs 1.2 trillion revaluation loss, the intensity of these losses subsided in Q2-FY22 to Rs 0.5 trillion.³⁸ On the other hand, the financing needs of the government were higher in Q2-FY22 compared to Q1-FY22 (**Figure 4.20**). Nonetheless, a reduction in revaluation losses kept the pace of debt

accumulation lower in Q2-FY22 compared to Q1-FY22.

An important development during Q2-FY22 was the on-lending of the IMF SDR allocation to the government for expenditures related to Covid-19 vaccines. The country received inflow of US\$ 2.8 billion from the IMF under the global SDR allocations during Q1-FY22. In Q2-FY22, with exceptional on-lending of this amount to the government, this amount became part of the government domestic debt (**details in section on domestic debt**).

Most of the increase in domestic debt during H1-FY22, particularly in Q2-FY22, was sourced through long-term instruments, which helped the government lengthen the maturity profile of debt. The government has introduced a number of long term instruments with features like floating rates

Source of Change in Public Debt **Figure 4.20**



Source: State Bank of Pakistan

³⁶ White Paper for FY22. Government of Khyber Pakhtunkhwa

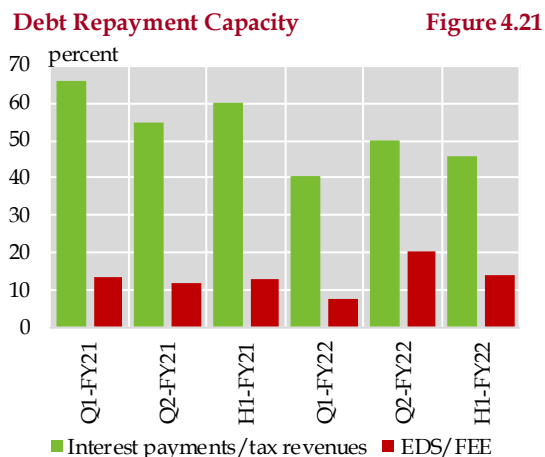
³⁷ Fiscal deficit stood at Rs 1,371.8 billion during H1 FY22 compared to Rs 1,137.5 billion during the same period of last year.

³⁸ PKR depreciated by 7.8 percent against the US dollar in Q1-FY22 (end September 2021 over end June 2021), whereas depreciation in Q2-FY22 (end December 2021 over end September 2021) was around 3.3 percent.

(quarterly and semi-annual coupon payments)^{39,40} and variable rental rates during the last couple of years. Resultantly, the share of floating and variable rental rate long-term instruments in total outstanding domestic debt stock has increased from 28 percent as on end-June 2019 to 41 percent on end-December 2021. Subsequently the share of T-bills and fixed rate instruments has declined. While this has improved the maturity profile of domestic debt, the interest rate risk has amplified as most of the funds are contracted on floating/variable rates. The rising share of variable rate domestic debt amid an increasing interest rate environment translated into a notable increase in debt servicing burden during Q2-FY22 as measured by interest payments-to-tax revenues (Figure 4.21).

Similarly, external debt servicing rose to 18 percent of total foreign exchange earnings of the country during Q2-FY22, compared to 9.4 percent same period last year (Figure 4.21).⁴¹ A scheduled repayment of maturing sovereign bond and commercial loans magnified external debt servicing pressure during Q2-FY22. Going forward, the debt repayments under DSSI relief will also become due.

Furthermore, the government has adhered to its commitment of zero budgetary borrowing from the SBP since the start of FY20, which has led to avoidance of deficit monetization. However, with the absence of this financing



Source: Ministry of Finance, State Bank of Pakistan

window, the government's reliance on commercial banks for budgetary support has scaled up, which has also increased the cost of borrowing. There is a need to introduce reforms to deepen the debt market by diversifying the financing options and keeping a check on the cost of borrowing by focusing on non-bank financing sources e.g., pension funds, corporations etc. Increasing the share of Shariah compliant instruments would also facilitate the government in diversifying the investor base and attracting Islamic Institutions to place their funds in such instruments.

Domestic debt

The pace of buildup in domestic debt slowed down during H1-FY22, with a growth of 1.8 percent compared to 4.4 percent during the

³⁹ Government started issuance of 3-, 5- and 10-Year floating rate PIBs with quarterly coupon payment frequency from October 2020, and 2-Year floating rate PIBs in November 2020 with quarterly coupon payment frequency and fortnightly interest rate re-setting.

⁴⁰ The government at end of FY19 re-profiled its debt held with SBP. Out of its Rs 7.7 trillion debt held with the SBP, roughly Rs 1.2 trillion was re-profiled into fixed PIBs, while the remaining Rs 5.5 trillion was converted into floating rate PIBs, which also increased the share of floating rate instruments in overall outstanding debt stock.

⁴¹ External debt servicing includes principal repayments and interest payments of public debt only.

Instrument-wise Changes in Domestic Debt**Table 4.12**

billion Rs

	H1-FY21	Q1-FY21	Q2-FY21	H1-FY22	Q1-FY22	Q2-FY22
1. Permanent debt	1,565.6	898.6	667.0	1,548.1	(67.2)	1,615.3
GoP Ijara Sukuk	363.2	162.0	201.2	632.5	-	632.5
PIBs	1,216.2	729.8	486.4	584.9	(8.6)	593.5
Prize bonds	(13.8)	6.8	(20.6)	(71.7)	(58.6)	(13.1)
SBP loan to GOP against SDRs allocation	-	-	-	474.9	-	474.9
2. Floating debt	(535.0)	(480.0)	(54.9)	(1,036.9)	250.8	(1,287.7)
MTBs	(535.5)	(480.5)	(54.9)	(1,084.8)	250.8	(1,335.5)
3. Unfunded debt	(3.9)	0.8	(4.7)	(42.0)	(14.0)	(27.9)
NSS	3.9	5.7	(1.8)	(32.6)	(13.5)	(19.2)
4. Naya Pakistan Certificates	5.2	0.7	4.6	10.9	8.4	2.5
5. Others	(7.6)	(4.4)	(3.2)	(33.2)	(0.1)	(33.2)
Domestic debt (1+2+3+4+5)	1,031.6	420.0	611.6	481.1	178.5	302.5

Source: State Bank of Pakistan

same period last year. Adequate availability of external inflows kept the financing needs from domestic sources at lower levels. The increase in the government deposits with the banking system also remained lower than last year. The maturity profile of domestic debt also improved with increasing fund mobilization through long-term instruments such as Pakistan Investment Bonds (PIBs), Ijara Sukuk and Naya Pakistan Certificates (NPCs) (Table 4.12). Nonetheless, as most of the fresh domestic loan is contracted on floating and variables rental rates, repricing risk has edged up.

In terms of ownership, almost the entire increase in domestic debt during H1-FY22 was sourced through commercial banks. The contribution of non-banks was negligible. The government debt owed to SBP declined during H1-FY22.

On-lending of SDR to the government

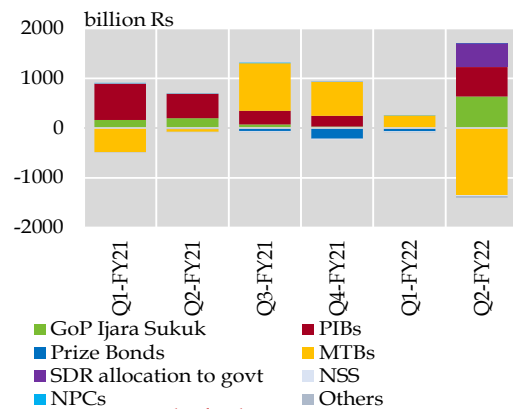
Quarterly analysis indicate that the stock of government debt owed to SBP increased during Q2-FY22. This rise came from the on-

lending of SDRs amounting to Rs 474.9 billion (comprising of US\$ 2.8 billion SDRs) to the government. In November 2021, the IMF allowed exceptional on-lending of this amount to the government for financing of the vaccine drive.⁴² The ceiling on net government budgetary borrowing from the SBP is adjusted upward by the amount of local currency on-lending of the SDRs.⁴³ Excluding the SDR allocation, the government debt stock with SBP declined by Rs 523 billion during H1-FY22.

Instrument-wise Analysis

Most of the increase in domestic debt during H1-FY22 was sourced through long-term instruments such as PIBs, Ijara Sukuk and Naya Pakistan Certificates. The quarterly analysis indicates that whereas most of the increase in domestic debt was sourced through short-term instruments during Q1-FY22, the trend changed in Q2-FY22 (Figure 4.22). The availability of Ijara Sukuk bonds not only facilitated trading of shariah compliant instruments in secondary market

⁴² IMF Sixth review.⁴³ IMF-Sixth review.

Instrument-wise Change in Domestic Debt**Figure 4.22**

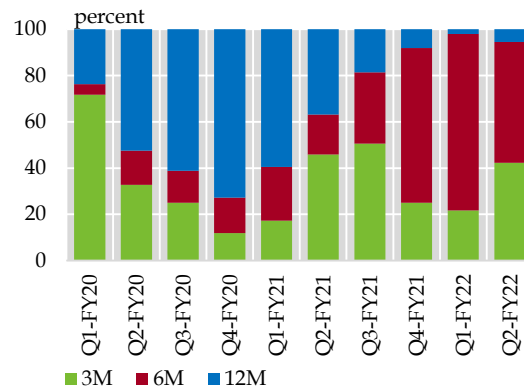
Source: State Bank of Pakistan

but also increased government financing options; hence the government retired its maturing short-term debt in the second quarter.

Market Treasury Bills

The outstanding stock of MTBs declined by Rs 1.1 trillion during H1 FY22 compared to a decline of Rs 0.5 trillion during the corresponding period of last year. A quarterly review indicates that during Q2-FY22 the government made net retirement of MTBs, which more than offset the increase seen in Q1-FY22.

The government set the pre-auction MTB target of Rs 5.96 trillion for Q2-FY22 (Rs 416 billion over and above maturities). Overall, the total offered amount stood at Rs 7.9 trillion. However, the government accepted only Rs 4.2 trillion, during Q2-FY22 and made net retirement of Rs 1.3 trillion MTBs in Q2-FY22. With the reversal in monetary policy stance, market was more inclined towards 3-month MTBs, whereas demand for 6-month MTBs edged down (**Figure 4.23**). This is evident from a total offer of Rs 4.3 trillion in 3-month MTBs, against Rs 1.9

Share in Outstanding Stock of T-Bills**Figure 4.23**

Source: State Bank of Pakistan

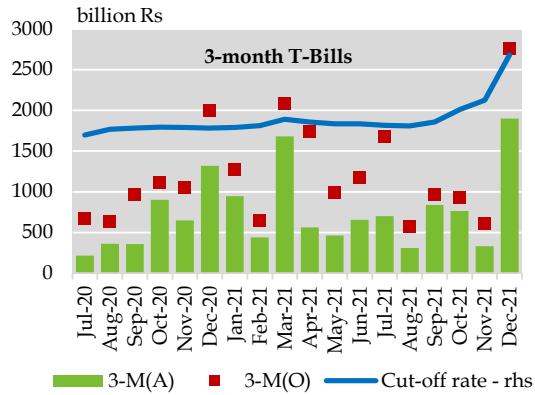
trillion offered in 6-month bills during Q2-FY22.

It is important to highlight here that the cut off rates on 3-M, 6-M, and 12-M T-bills increased by 282 bps, 337 bps and 388 bps during Q2-FY22 with 250 basis points increase in the policy rate (**Figure 4.24**). Hence, to contain the burden of interest payments, the government accepted around 70 percent bids in 3-month T-bills, compared to only 50 percent for 6-month MTBs.

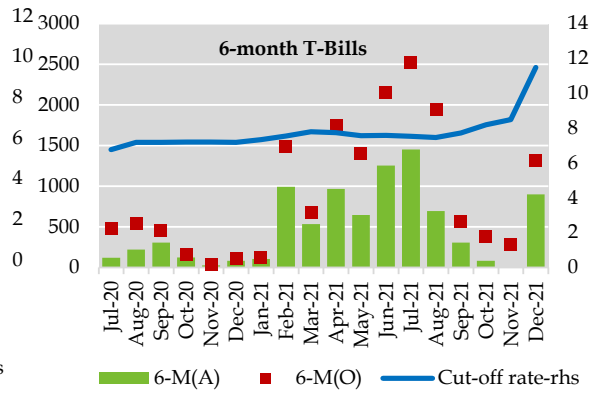
The entire increase in PIBs was concentrated in Q2-FY22

The stock of outstanding PIBs reached Rs 15.2 trillion as on end December 2021 compared to Rs 14.6 trillion as on end June 2021 – reflecting an increase of Rs 0.6 trillion. The entire increase in PIBs was concentrated in Q2-FY22. With the reversal of monetary policy stance and a rise in policy rate, the cut off rates of PIBs also increased sharply during Q2-FY22. On average, the cut off rates during Q2-FY22 were 230-280 bps higher than Q2-FY21 (**Table 4.13**).

Keeping in view the market appetite, the government kept the pre-auction targets for

Bidding Pattern in T-bills

Source: State Bank of Pakistan

Figure 4.24

floaters PIBs higher compared to fixed PIBs. The target for fixed PIBs stood at Rs 750 billion during H1 FY22, while the target of floater PIBs was Rs 1,175 billion for the cumulative period. The accepted amount of floater PIBs was also relatively higher than the fixed PIBs. Rising share of floating rate PIBs increases the repricing risk, particularly in an increasing interest rate environment. The share of floater PIBs in total outstanding stock of PIBs has increased by roughly 13 percentage points to 48 percent as on end December 2021, compared to 35 percent as on end June 2021. Keeping a balance between lengthening of maturity profile and repricing risks is important to ensure debt sustainability.

Monthly auction profile suggests that with the rise in the policy rate, the market's participation has increased in floater PIBs (Figure 4.25). Within floater PIBs, the share of floaters with quarterly coupon payments increased from 20 percent as of end June 2021 to 45 percent as on end June December 2021. Auction profile suggests that the market remained inclined towards floater PIBs with quarterly coupon payments as evident by the higher offered amount in both quarters of

FY22. In line with market's interest, the government also accepted higher amounts in the category of quarterly PFLs (Table 4.14). In Q2-FY22, the government rejected the bids of floaters PIBs with semi-annual coupon payments due to lower participation of the market.

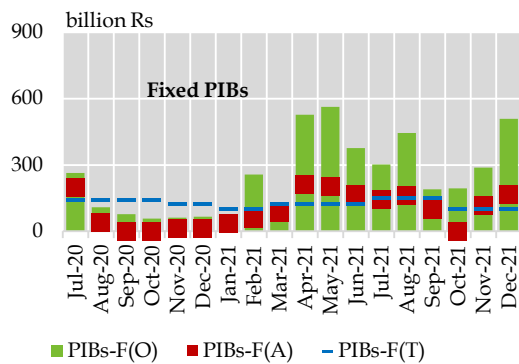
Issuance of GoP Ijara Sukuk

After a gap of two quarters, the government mobilized funds through the issuance of GOP Ijara Sukuk during Q2-FY22 and mobilized Rs 0.6 trillion. In line with the market interest, a large part was issued on the variable rental rate. The offered and accepted amount remained above the pre-auction target (Table 4.15). This helped the government in lengthening the maturity

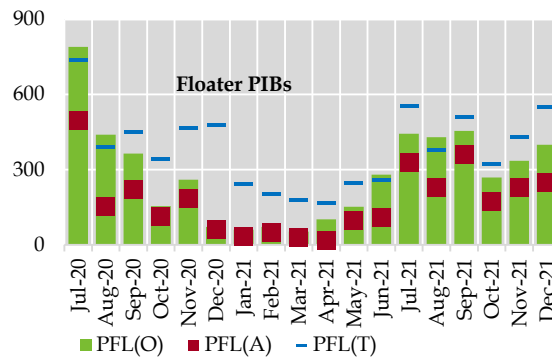
Average Cutoff Rates on PIBs Table 4.13

	3-year	5-year	10-year
H1-FY21	8.1	8.4	9.0
H1-FY22	9.85	10.48	10.80
Q2-FY21	8.2	8.5	9.0
Q2-FY22	11.42	11.58	11.77

Source: State Bank of Pakistan

Auction Profile of PIBs

Source: State Bank of Pakistan

Figure 4.25

O=offered, A=accepted, T=Target

Auction Profile of Floater PIBs Table 4.14

billion Rs	Target	Offered	Accepted
Semi-annual coupon			
Q1-FY22	190.0	175.7	129.5
Q2-FY22	300.0	147.7	-
Quarterly coupon			
Q1-FY22	335.0	1,154.0	787.19
Q2-FY22	350.0	856.7	606.34

Source: State Bank of Pakistan

profile of domestic debt as these instruments have a tenor of 5 years.

Prize bonds and NSS continue to record outflows

Prize bonds recorded net outflows of Rs 72 billion during H1-FY22 – Rs 58 billion in Q1-FY22 and Rs 14 billion in Q2-FY22. Discontinuation of prize bonds of various tenors (7,500, 15,000 and 25,000) and subsequent withdrawals explain the decline in prize bonds. However, monthly analysis shows that the volume of outflows is waning (Figure 4.26). Investment in premium prize bonds increased during the period under review. Gross inflows in premium prize bonds stood at Rs 16.5 billion during H1 FY22 compared to Rs 5.4 billion during the same period of last year.

National saving schemes recorded net outflows during the period under review - Rs 13.5 billion in Q1-FY22 and Rs 19.1 billion in Q2-FY22. Institutions continued to withdraw funds from NSS as they have been barred from participation in such instruments. However, a couple of instruments such as regular income certificates and behbood

Auction Summary Table 4.15

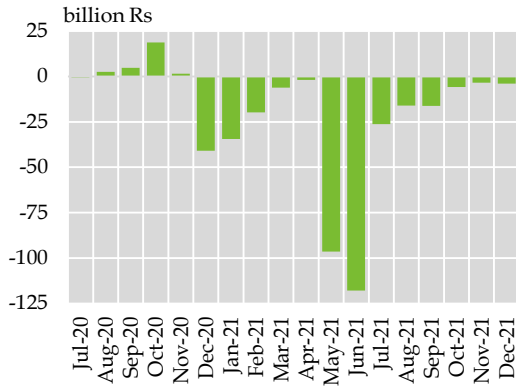
billion Rs	GoP Ijara Sukuk (VRR)		
Date of Settlement	Target	Offered	Accepted
06-10-21	75	193.1	190.5
29-10-21	75	222.7	168.6
17-11-21	75	162.5	148
15-12-21	75	8.1	0.04
GoP Ijara Sukuk (FRR)			
Date of Settlement	Target	Offered	Accepted
06-10-21	25	53.8	12.7
29-10-21	25	22.9	0
17-11-21	25	21.5	0
15-12-21	25	109.8	68

*this does not include Ijara Sukuk issued by GoP to IPPs against their receivables from GoP worth Rs 45 billion.

Source: State Bank of Pakistan

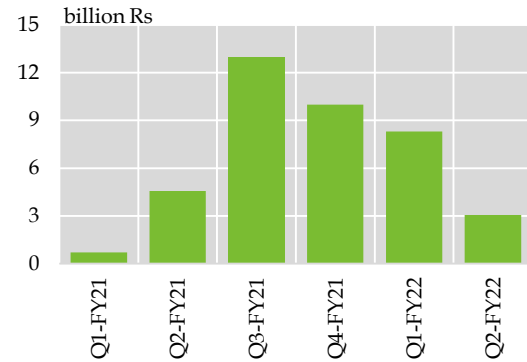
Net Inflows in Prize Bonds

Figure 4.26



Naya Pakistan Certificates Held by Residents - Quarterly Flows

Figure 4.27



Source: State Bank of Pakistan

saving schemes attracted relatively higher inflows due to a hike in profit rates. Recent increase in profit rates in December 2021 will help government in attracting funds through these instruments (Table 4.16).

Naya Pakistan Certificates

The stock of Naya Pakistan Certificates (held by residents) reached Rs 39.2 billion as on end December 2021 compared to Rs 28.3 billion as on end June 2021. The pace of inflows in these certificates slowed down in Q2-FY22 (Figure 4.27).

Interest payments on domestic debt

Interest payments on domestic debt stood at Rs 1.3 trillion during H1-FY22 compared to Rs 1.4 trillion during the same period of last years.⁴⁴ Specifically, in line with the rising share of variable rate debt, interest payments gained pace in Q2-FY22 amid an increasing interest rate environment. Most of the increase came from the payments on PIBs, as the increasing share of PIB floaters with the unique feature of fortnightly resets and coupon payments on quarterly basis, fed into debt servicing pressure after an increase in policy rate. Similarly, payments on GoP Ijara Sukuk almost doubled in Q2-FY22 compared to the same quarter last year because of the increase in outstanding stock of GoP Ijara Sukuk. On the other hand, payments on

National Savings Schemes

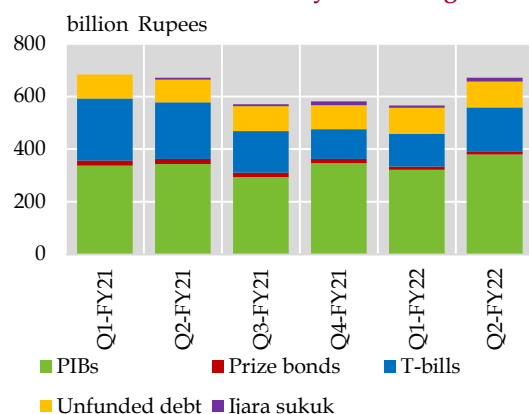
billion Rs, profit rates in percent

Table 4.16

	Net Inflows		Profit Rates	
	Q2-FY21	Q2-FY22	Q2-FY21	Q2-FY22
Defence Savings Certificates	-0.8	-3	8.5	9.4
Special Savings Certificates	6.5	-0.5	7.6	8.2
Regular Income Certificates	4.2	3.6	8	10.8
Behood Savings Certificates	3.3	-2.3	10.3	11

Source: Central Directorate of National Savings

⁴⁴ Source: Ministry of Finance, available at: https://finance.gov.pk/fiscal/July_Dec_2021.pdf, accessed on January 15, 2022

Instrument-wise Interest Payments Figure 4.28

Source: State Bank of Pakistan

prize bonds slowed down in Q2-FY22 as the outstanding stock of prize bonds has been on a decline due to discontinuation of various denominations bonds. Similarly, the payments on MTBs dropped amid a decline in maturing debt stock (Figure 4.28).

Public external debt & liabilities

The stock of outstanding public external debt (excluding liabilities) reached US\$ 90.6 billion on end-December 2021, with increase of US\$ 4.1 billion during H1-FY22 compared to US\$ 4.4 billion during the same period last year (Table 4.17). The fresh disbursements remained higher in H1-FY22 owing to deterioration in the current account balance. However, revaluation gains of US\$ 0.7 billion on the existing stock of external debt (dollar terms) emerging from appreciation of US dollar against other international currencies helped in containing the pace of external debt accumulation.

One-half of revaluation gains due to SDR depreciation

Currency-wise revaluation impact indicates that appreciation of the US dollar against the SDRs constituted more than one-half of the revaluation gains during H1-FY22. It must be recalled that during the same period of last

Change in Public External Debt
million US\$**Table 4.17**

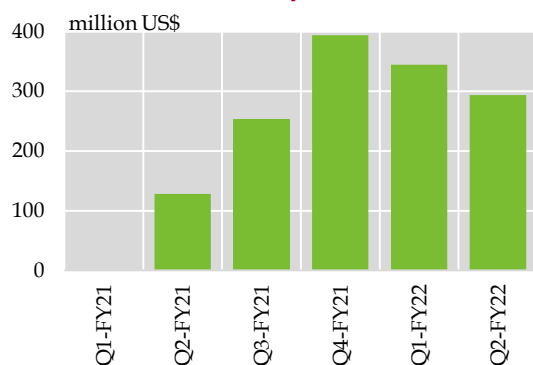
	H1-FY21	H1-FY22	Q2-FY21	Q2-FY22
Public external debt (1&2)	4,412.0	4,099.3	2,499.5	2,475.8
1. Government external debt	4,613.3	4,750.6	2,625.3	2,950.6
of which				
i) Long term (>1 year)	5,239.4	4,441.1	2,881.4	2,816.3
Paris club	622.3	(579.9)	343.9	(198.3)
Multilateral	2,267.2	798.3	779.9	434.2
Other bilateral	1,174.4	3,107.3	190.5	3,041.8
Commercial loans/credits	940.8	522.4	1,366.3	382.1
Naya Pakistan Certificates	128.5	528.9	128.0	159.6
ii) Short term (<1 year)	(626.1)	418.9	(256.1)	(12.2)
Multilateral	(238.8)	561.2	64.9	88.5
Local currency securities	(245.9)	(142.2)	(206.0)	(100.7)
Commercial loans/credits	(141.5)	-	(115.0)	-
2. From IMF	(201.2)	(651.3)	(125.8)	(340.5)
Foreign exchange liabilities	(630.5)	2,879.0	228.9	(3.0)
Central bank deposits	(2,000.0)	-	(1,000.0)	-
Allocation of SDR	63.8	2,739.0	32.3	13.8

Source: State Bank of Pakistan

Major Foreign Economic Assistance during H1
million US\$**Table 4.18**

Donor	Name of project	Purpose	Amount
Total disbursements			9,432.7
<i>of which</i>			
Project and Budgetary Support			
Saudi Arabia	Time Deposit	Budgetary support	3,000.0
ADB	COVID-19 Vaccine Support Project	Project	488.0
IDA	Prog. For Afford. Clean Energy	Budgetary support	397.0
IDB	Short-term credit	Short-term credit	354.4
ADB	Energy Sector Reforms and Finance Sustainable Project	Budgetary support	300.0
China	Karachi Nuclear Power Project	Project	292.0
IDA	Pandemic Response Effectiveness	Project	108.0
IDA	Sindh Barrages Improvement Project	Project	52.2
Euro Bonds			
	5-year Euro Bond	Budgetary support	300.0
	10-year Euro Bond	Budgetary support	400.0
	30-year Euro Bond	Budgetary support	300.0

Source: Economic Affairs Division

Naya Pakistan Certificates Held by Non-Residents - Quarterly Flows **Figure 4.29**

Source: State Bank of Pakistan

year, the country incurred revaluation losses of US\$ 1.9 billion due to depreciation of US dollar against other international currencies, which led to an expansion of external debt stock.

The accumulation of external debt was spread almost evenly across the two quarters. However, the composition of

disbursements slightly changed during Q2-FY22 compared to the same quarter last year. The contribution of bilateral sources increased largely due to inflows of US\$ 3.0 billion from a friendly country for budgetary support. ADB also funded the project "Energy Sector Reforms and Finance Sustainable Project" worth US\$ 300 million during Q2-FY22. Another important area was funding for COVID-19 Vaccine Support Project worth US\$ 487.8 million by ADB, out of which roughly US\$ 173 million were disbursed in the second quarter (**Table 4.18**). Moreover, the government issued Euro bond of various tenors worth US\$ 1.0 billion during Q2-FY22.

Foreign investment in local government securities continued to record outflows

Foreign investment in local government securities recorded net outflows in both quarters of FY22. However, tenor-wise information shows that foreign investment in PIBs recorded net inflows during Q2-FY22.

Naya Pakistan Certificates continued to attract inflows

Naya Pakistan Certificates (held by non-residents) attracted US\$ 0.5 billion inflows during H1-FY22 (**Figure 4.29**). With this increase the stock of NPCs reached US\$ 1.3 billion as on end December 2021 compared to US\$ 0.8 billion as on end June 2021. As most of the inflows under NPCs are long term in nature – maturity of more than one year – these inflows have helped lengthen the maturity profile of government external debt. In addition, these inflows have also helped the government diversify its narrow investor base.

Public External Debt Servicing

Public external debt servicing (principal and interest payments) stood at US\$ 5.0 billion during H1-FY22 compared to US\$ 3.9 billion during the same period of last year.

Quarterly analysis indicates that both components of public external debt servicing (principal and interest payments) increased during Q2-FY22, after showing a slight decline in Q1-FY22 (**Figure 4.30**). This was because of the repayment of a maturing

Sukuk bond worth US\$ 1 billion during Q2-FY22.

Subsequently the outstanding stock of Euro/Sukuk global bonds fell to US\$ 7.8 billion as on end December 2021 compared to US\$ 8.8 billion as on end September 2021. In addition, the government also repaid its maturing commercial loans worth US\$ 1.2 billion during Q2-FY22.

Debt relief under DSSI continued in Q2-FY22

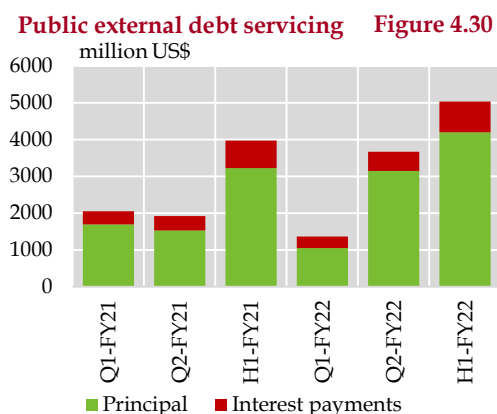
On a cumulative basis during H1 FY22, the country secured debt relief of US\$ 1.1 billion (US\$ 0.8 principal and US\$ 0.3 billion interest payments) under DSSI.

During Q2-FY22, the country received debt relief of US\$ 0.5 billion (principal amount US\$ 0.4 billion and interest component US\$ 0.1 billion) compared to relief of US\$ 0.9 billion in Q2-FY21. Without this relief, public external debt servicing would have been higher in Q2-FY22.

In total (May-2020 till December 2021), the country secured relief of US\$ 3.8 billion. Under this initiative, the debt repayments were postponed till December 2021. The repayment period for the restructured principal and interest amounts is 4-6 years.

Debt repayment capacity slightly weakens in Q2 due to higher debt servicing

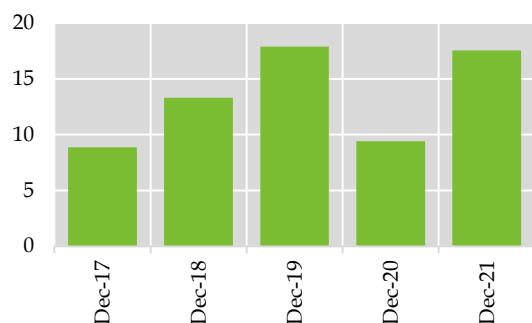
The indicators of debt repayment capacity came slightly under pressure in Q2-FY22 compared to the same period last year. The ratio of public external debt servicing-to-foreign exchange earnings rose to 17.5 percent by the end of December 2021, whereas the ratio of public external debt



Source: State Bank of Pakistan

EDS as Percent of FEE

Figure 4.31a

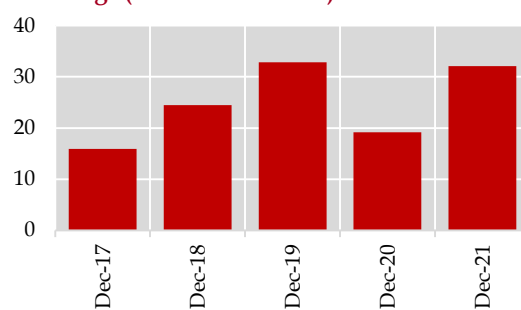


* EDS external debt servicing (principal component);
FEE foreign exchange earnings

Source: State Bank of Pakistan

EDS as Percent of Export Earnings (Goods & Services)

Figure 4.31b



* EDS external debt servicing (principal component);
Exports of goods & services

servicing-to-exports of goods and services increased to 32.1 percent in December 2021 (Figure 4.31 a & b).⁴⁵

⁴⁵ Public external debt servicing includes principal component of long term and short-term government external debt plus debt repayments to the IMF. It does not include foreign exchange liabilities and interest payments.

5 External Sector

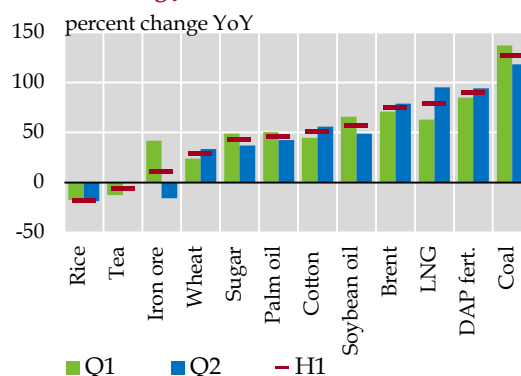
The continued surge in global commodity prices in response to supply-side bottlenecks and buoyant global demand had largely negative consequences for Pakistan's external account during H1-FY22. This surge in prices was the dominant factor behind the sharp increase in import payments during the period. 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.

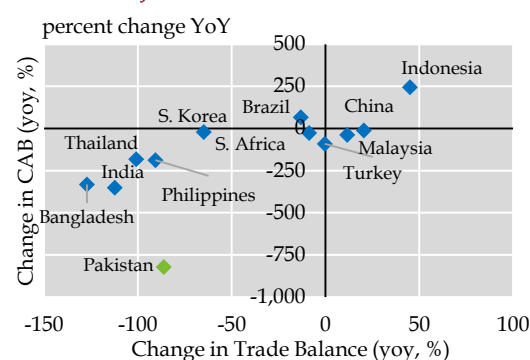
In addition to Pakistan, multiple other net oil importing emerging markets (EMs) also witnessed a deterioration in their current account balances, mainly due to a higher trade deficit (**Figure 5.2**). In Pakistan's case, higher international commodity prices had a more pronounced impact on the trade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

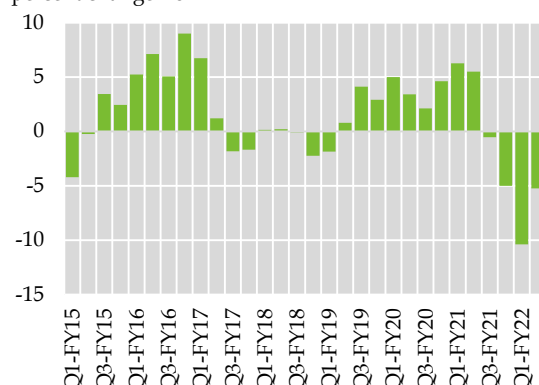
The recent growth in import payments is primarily responsible for the worsening in Pakistan's current account balance during H1-FY22. This box analyzes the major drivers of this import growth, and finds that global and domestic factors have both contributed to the increase. Specifically, there are three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

percent change YoY

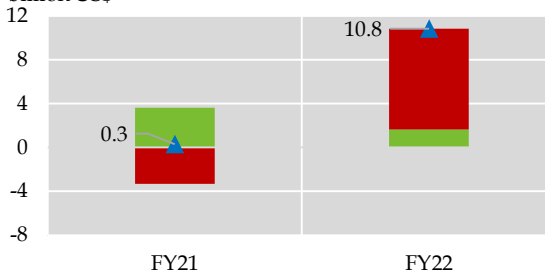


Source: Pakistan Bureau of Statistics

Figure 5.1.1a

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

billion US\$



■ Volume impact ■ Price impact ▲ Change in imports

*for items with both volume and value data available

Figure 5.1.1b

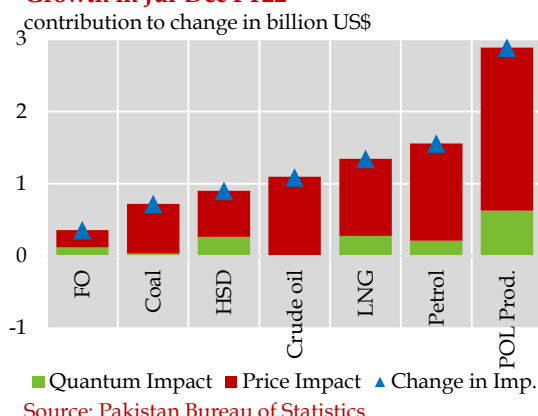
² In **Figure 5.1.1b**, the breakdown of volume and price impact is shown for only those items for which both import volume and value data is available. These items had a 59.3 percent share in overall imports during H1-FY22.

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

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



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

5.5). Among other raw materials, the import demand for industrial and agricultural inputs and intermediates, such as fertilizer and plastic, also stayed elevated.

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 (IITFC) 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/IITFC 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.

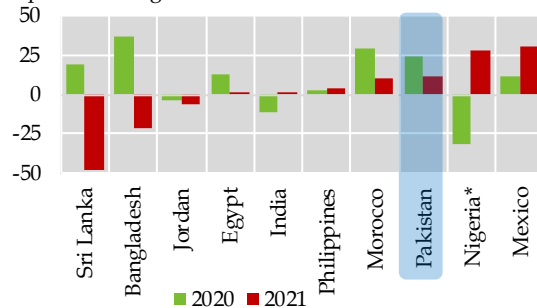
5.2 Current Account

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 merchandise 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
<i>Saudi Arabia</i>	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
<i>Other GCC</i>	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

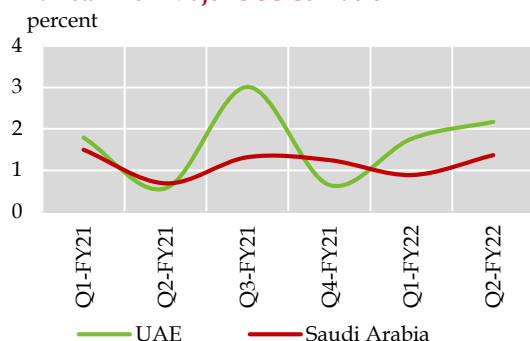
At the same time, some differences in remittance trends to Pakistan can be seen within Q1-FY22 and Q2-FY22. Specifically, remittances from the GCC countries slightly declined on YoY basis in Q2, with an 8.2 percent drop in inflows noted from the UAE (Table 5.2). The resumption in international air travel 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 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 merchandise 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

Breakdown of Services Balance during H1-*

million US Dollars

Table 5.3

	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

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.

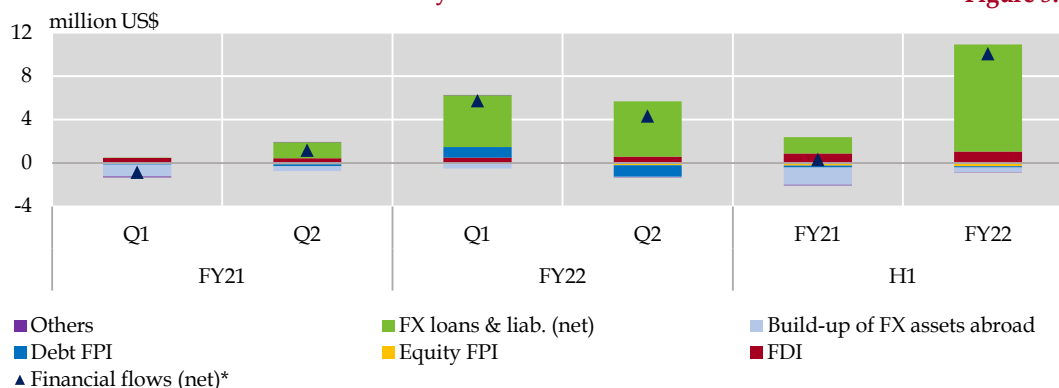
Nonetheless, on an encouraging note, the country's exports of information and

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.

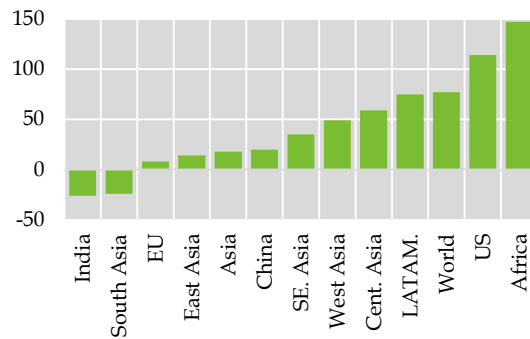
Foreign direct investment

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

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

percent change YoY



Source: UNCTAD Investment Trends Monitor (Jan 2022)

digital innovations as well as into microfinance institutions.

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

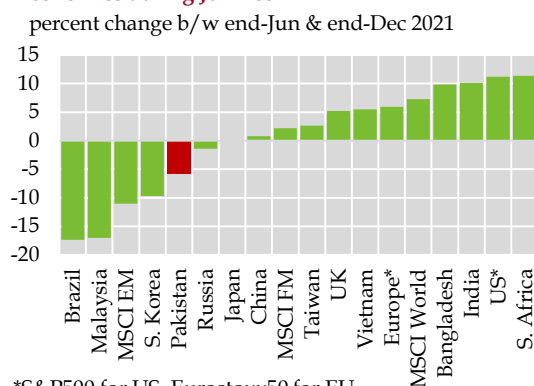
Sector-wise Net FDI inflow in H1 **Table 5.4**
million US Dollars

	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**



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.

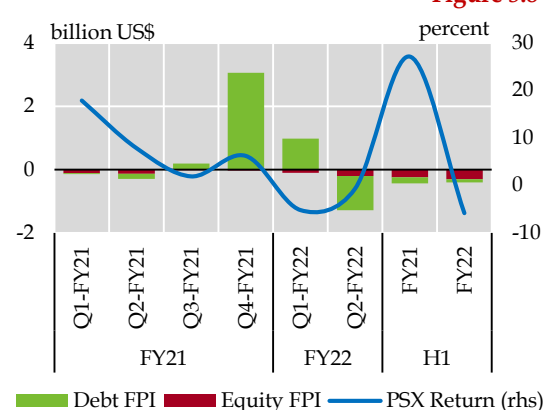
Foreign portfolio investment

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.

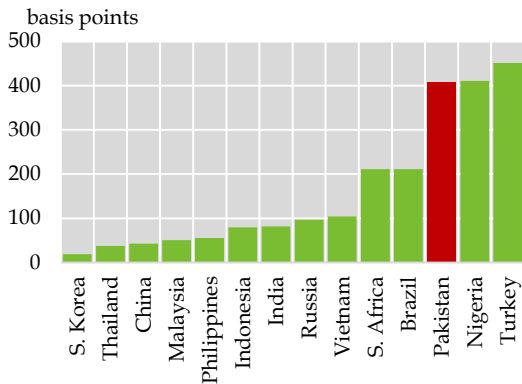
FPI into Pakistan and PSX Returns **Figure 5.8**



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.

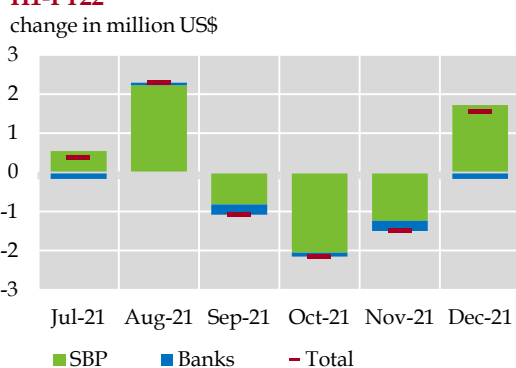
The breakdown shows that the SBP's FX reserves had risen by a substantial US\$ 2.0 billion in ssQ1-FY22, mainly in response to the receipt of Eurobond proceeds in July 2021 and the additional SDR allocation from the IMF in August 2021 (**Figure 5.10**). However, maintaining the reserves position proved 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.

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

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



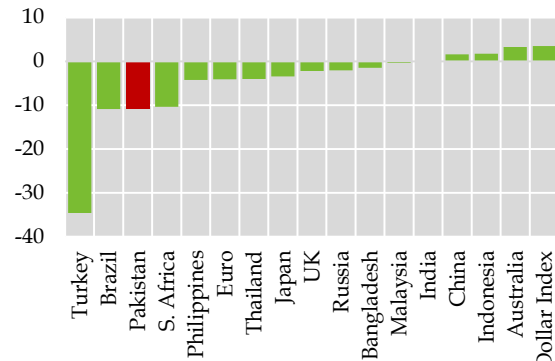
Source: State Bank of Pakistan

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

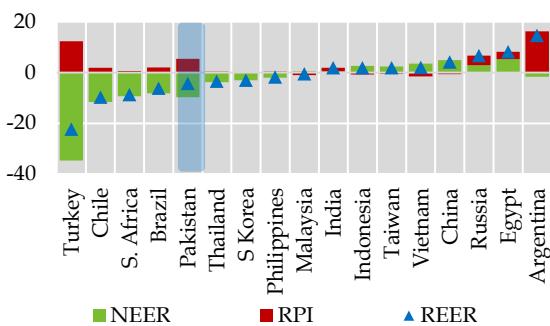
percent change b/w end-Jun & end-Dec 2021



Source: Bloomberg

Figure 5.11**Change in REERs of Major EMs during H1-FY21***

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



*JP Morgan Effective Exchange Rates (deflated by CPI)

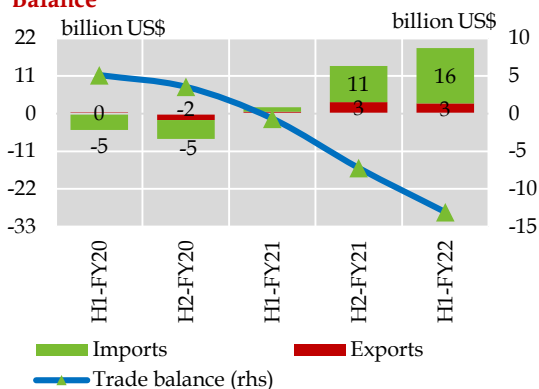
Source: Haver Analytics

Figure 5.12

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**

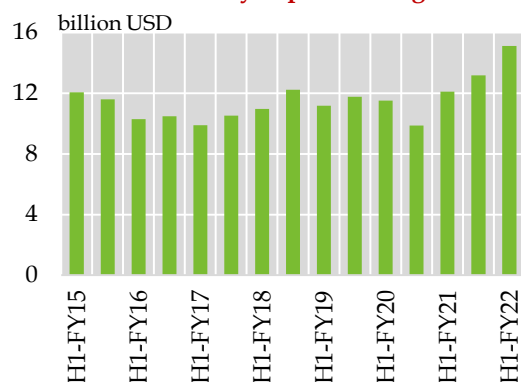
Source: Pakistan Bureau of Statistics

5.5 Trade Account¹⁷

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

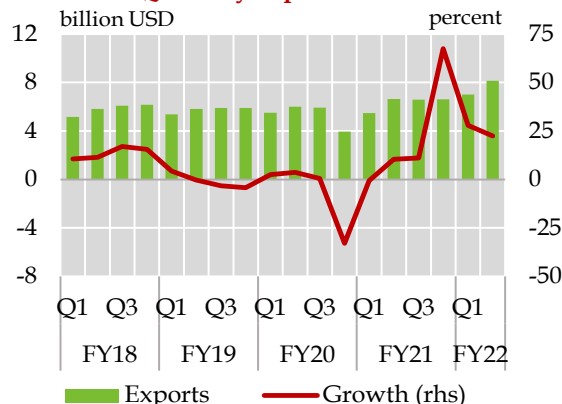
¹⁷ This section is based on customs data reported by the PBS. The information in this section does not tally with the payments record data, which is reported in **Section 5.1**. To understand the difference between these two data series, see Annexure on data explanatory notes.

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

Source: PBS

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.

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

Source: PBS

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
million US Dollars

Table 5.6

	FY17- FY20 avg.	FY21	FY22	YoY change in FY22
EU-27	2,971	3,453	4,082	629
<i>Netherlands</i>	438	623	768	145
<i>Spain</i>	459	446	585	139
<i>Italy</i>	343	362	463	101
<i>Germany</i>	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	-	-

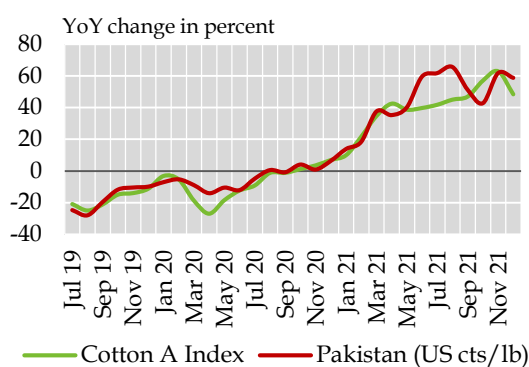
Note: 1) Apparel = Hosiery (Knitwear) + Readymade Garments; Home Textiles = Bed wear + Towels

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}

To put things in perspective, Pakistan's average monthly cotton fiber price in 2021

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

Source: Emerging Textiles

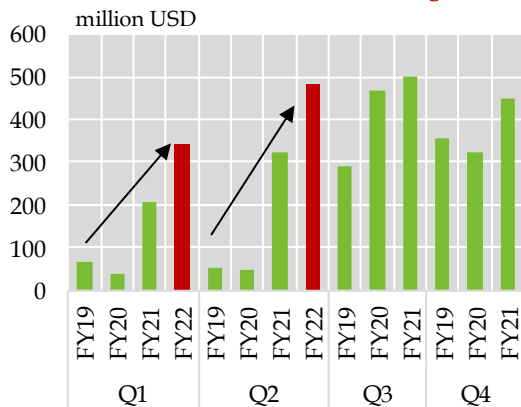
stood at 98 cents per pound, which was almost 1.5 times the 2020 average, and ranked highest in a decade. Same is true for the cotton A index, that evaluates the cotton prices in the international market.²¹

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**.

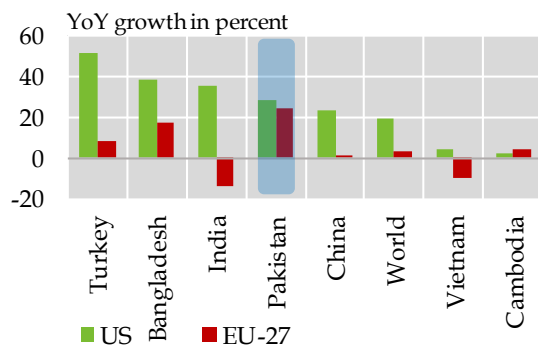
²⁰ It may be noted that world cotton production had declined by 7.6 percent YoY to 24.3 million MT in 2020/21. Source: Cotton: World Markets and Trade, February 2022, USDA

²¹ Source: Emerging Textiles

Raw Cotton Imports of Pakistan Figure 5.15b

Source: PBS

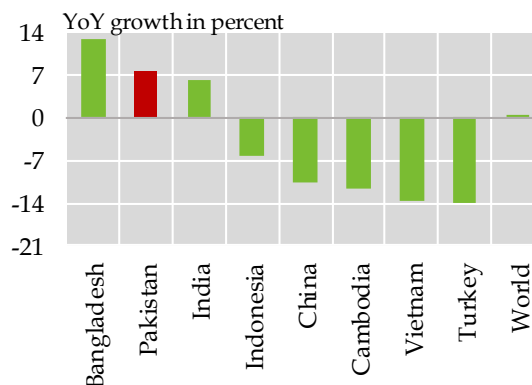
industry, which helped realize and sustain higher orders from the major buyers. This phenomenon partly reflected in much higher working capital offtake by the textile and apparel industry. In H1-FY22, the industry registered net borrowing of working capital loans (including the trading finance) to the 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

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

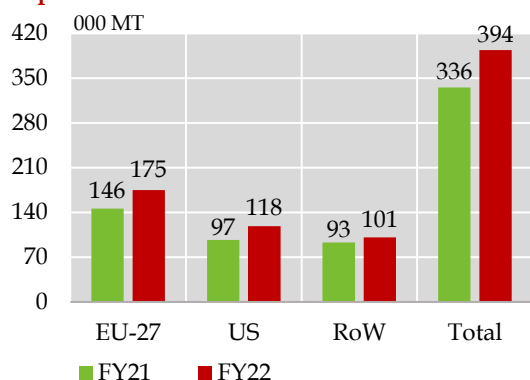
Growth in Quantum Apparel Imports of the UK in H1-FY22 Figure 5.16b

Source: UK Trade Info

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

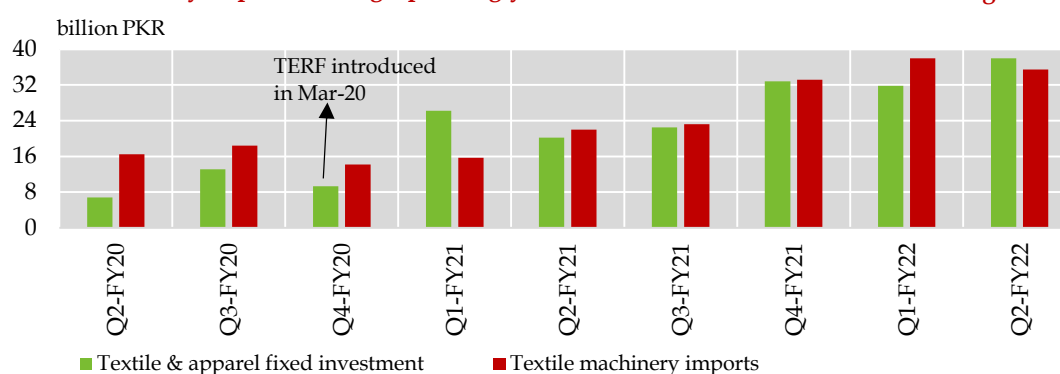
Pakistan's Quantum Home Textiles Exports in H1 Figure 5.17



Source: PBS

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 KWh²³ – 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

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

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

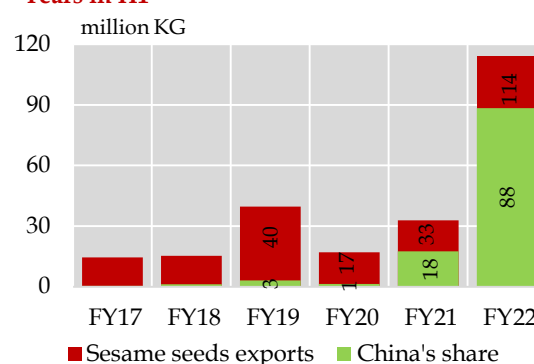
Source: PBS

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

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

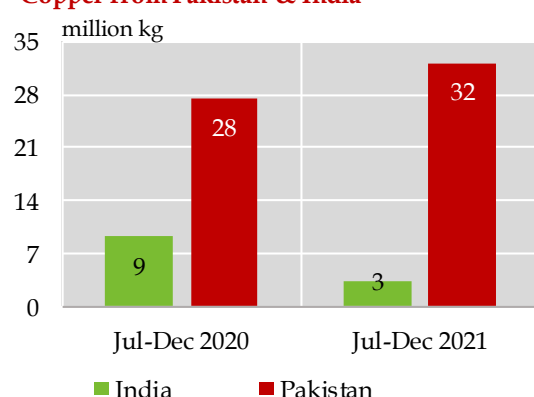
was maize (corn), as its exports jumped by US\$ 9 million to US\$ 89 million in H1-FY22. This massive jump came on the back of higher shipments to Malaysia, Vietnam, and Oman.

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

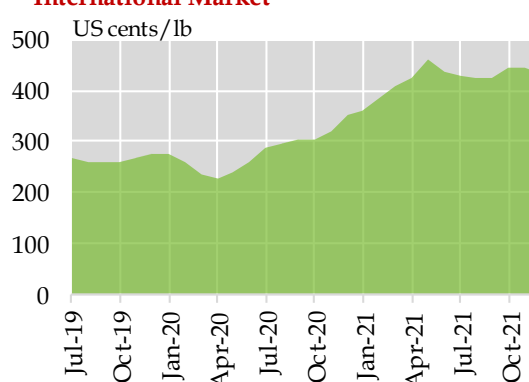
Figure 5.20a



Source: China Customs Statistics

Price of Copper in the International Market

Figure 5.20b

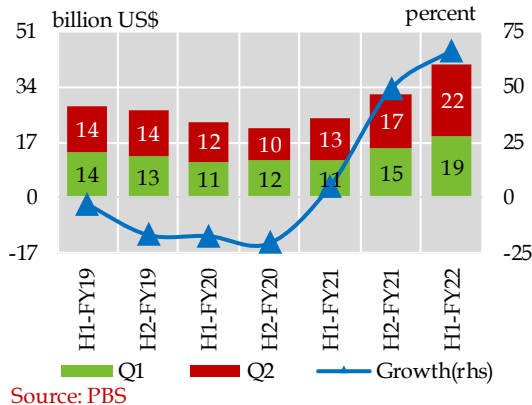


Source: Haver Analytics

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

Quarterly and Half-yearly Trend in Imports Figure 5.21

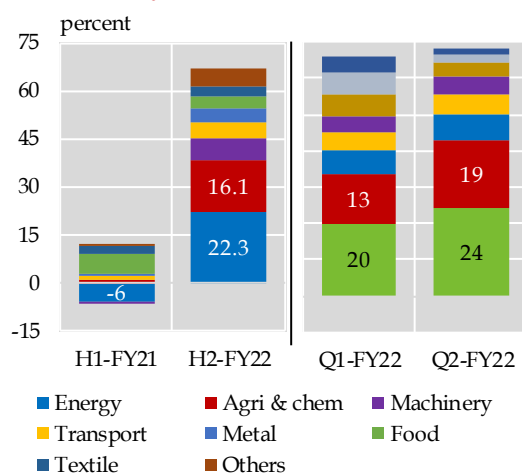


percent to US\$ 106.8 million, partly due to the low base effect. Soaring crude prices also complemented higher volumes. Lastly, exports of ethyl alcohol (undenatured) increased by US\$ 72 million to US\$ 201 million in H1-FY22.²⁹ All of this increase came on the back of higher shipments to China.

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 driving the Half-yearly and Quarterly Imports Figure 5.22



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

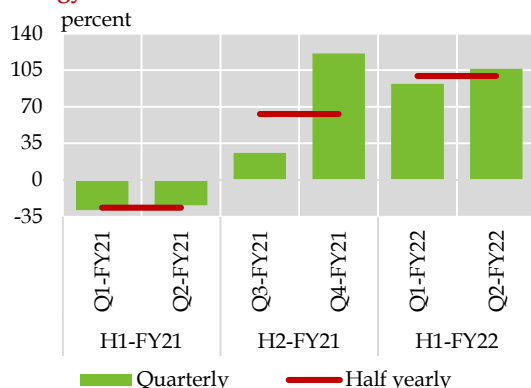
²⁹ Undenatured ethyl alcohol is the pure form of the chemical.

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.

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



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.

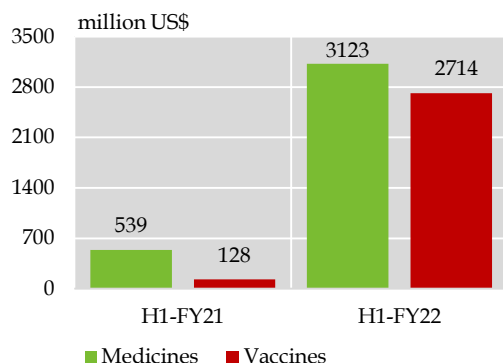
Medicines, including vaccines to control Covid spread, supported the sharp increase in imports

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**).

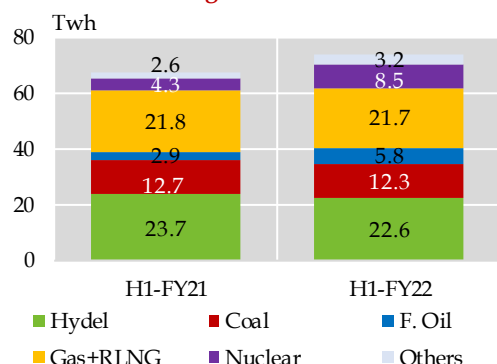
Key Petroleum Product Imports during H1-FY22**Table 5.9**

	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).

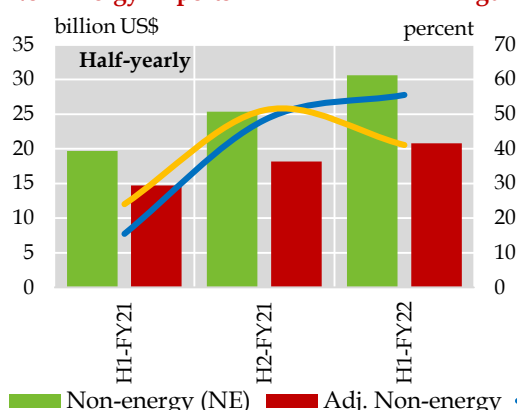
Importantly, power generation during H1-FY22 has increased by 8.7 percent YoY to 74 Twh (Terra watt hour) from 68 Twh generated in this period of FY21, despite a 4.8 percent YoY decrease in Hydel generation during H1-FY22.³⁶ To mitigate the impact of higher international energy prices and lower hydropower 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

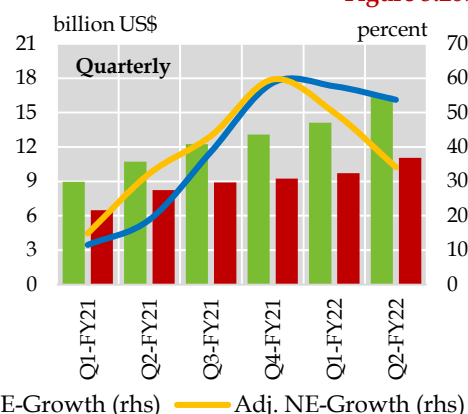
Non-Energy Imports

Figure 5.26a



Source: PBS

Figure 5.26b



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.

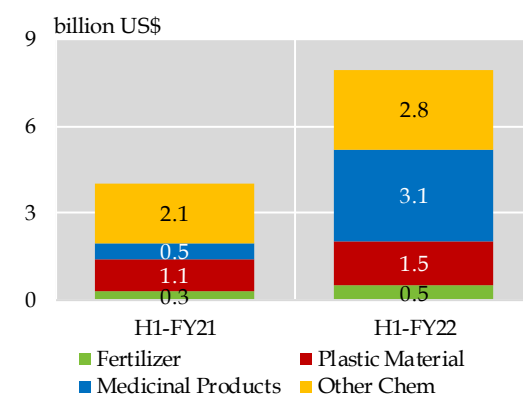
Fertilizer imports, on the other hand, increased by 60.8 percent YoY to US\$ 523.4 million in H1-FY22, from US\$ 325.5 million in H1-FY21. However, in term of quantum,

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

Agricultural and Chemical Imports Figure 5.27



Source: PBS

non-energy imports. This volume of machinery imports is only bettered by 6.1 billion of these imports in H2-FY17 and H2-

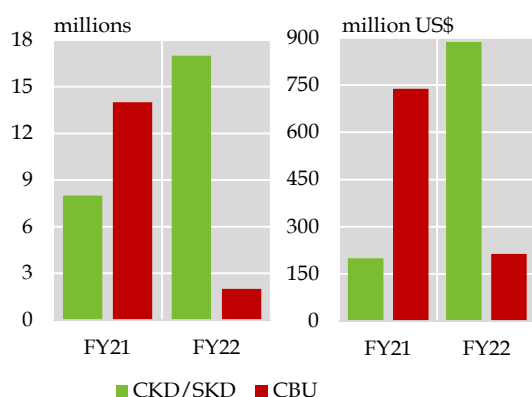
³⁸ DMMD Circular No. 20 of 2021, available at: <https://www.sbp.org.pk/dmmd/2021/C20.htm>

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

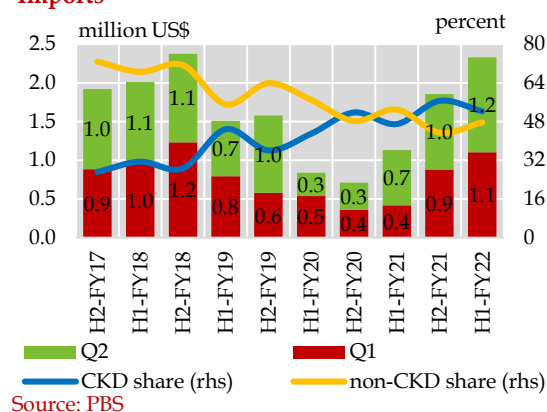
Transport imports increased by 105.8 percent to US\$2.3 billion during H1-FY22; marginally lower from peak imports of US\$ 2.4 billion seen H2-FY18 (Figure 5.29). At that time, record imports of ships and vessels for breaking, and aircrafts and its parts, besides CKD/SKD vehicles with 29 percent share 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



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>.

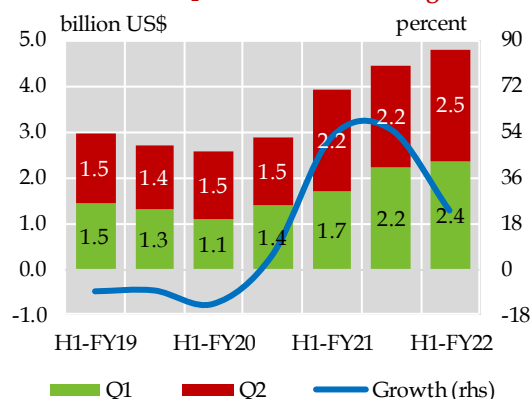
⁴⁸ Pakistan imported US\$ 262.8 million of photosensitive semiconductor in H1-FY22, while this amount was only US\$ 126.2 million in the same period of last year.

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

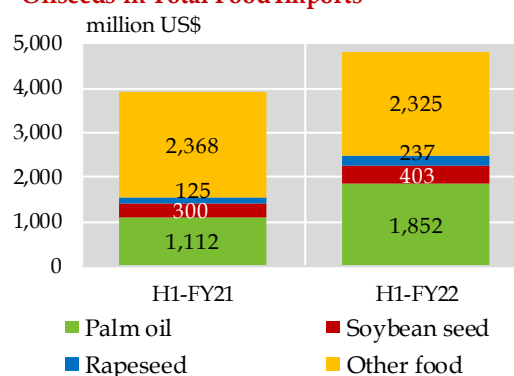
of Soybean seed and Rapeseed, have increased by 34.5 percent and 89 percent YoY respectively in this period.⁵³

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\$ 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).

Special Section: Role of Trade Organisations in Economic Growth and Development: Understanding the Dynamics in Pakistan

Public-private dialogue (PPD) is important for economic growth and development, where the role of Trade Organisations (TOs) is important given their collective representation of private sector. In addition to evidence-based policy advocacy, an essential element of business reform initiative, TOs also provide market complementing services to their members, the revenues from which help TOs to become financially sustainable. The TOs in Pakistan have been established with aforementioned reasons, and are accordingly engaged by the public sector. After shedding light on international best practices of TOs, this Special Section takes a look at the state of TOs in Pakistan, from the perspective of PPD and the services they offer to their members. Based in part on a survey, the key finding is that although TOs are engaged in PPD through limited arrangements, their contribution vis-à-vis evidence-based advocacy is limited and their range of services for members is not comprehensive. Lastly, it offers broad policy suggestions and raises some points for deliberations on how TOs can enhance their contribution to Pakistan's economic growth and development.

S1.1 Introduction

Economic growth and transformation requires interactive strategic cooperation between the public and private sectors; wherein collective action by chambers of commerce and business associations (Trade Organizations)¹ plays a constructive role. Research on emerging economies, such as East Asia of 1980s onward, as well as developed economies shows that public-private dialogue (PPD) has helped shape effective economic and sectoral policies,

improved productivity, developed consensus on future pathways, and gained competitive advantages in products, markets, and innovation strategies. Increasingly, leading global central banks also engage with Trade Organizations (TOs) on various aspects of monetary policy.²

Collaboration with the private sector is necessary for governments because the private sector has better access to market signals: profitability; business cycles; business processes; global competition;

¹ Under Pakistan's Trade Organization Act 2013, chambers and associations are referred to as Trade Organizations (TOs), whereas in academic literature these are often referred to as Business Membership Organizations. This Special Section refers to global and local chambers and associations as TOs.

² E. Fernandez-Arias, C. Sabel, E. H. Stein and A. Trejos (2016). *Two to Tango: Public-Private Collaboration for Productive Development Policies*. Washington, DC: Inter-American Development Bank; R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3; D. Rodrik (2004). *Industrial Policy for 21st Century*, Special Publication for UNIDO. Cambridge, MA: Harvard University; Devlin R. (2014). *Towards Good Governance of Public Private Alliance Councils Supporting Industrial Policies in Latin America*, Inter-American Development Bank technical Note No. IDB-TN-615; and Cornick J. (2013). *The Organization of Public-Private Cooperation for Productive Development Policies*. IDB Working Paper Series, IDB-WP-437. Respective websites of central banks of Canada, Australia, New Zealand, and the US.

avenues of opportunities and challenges; etc. The public sector on the other hand, cannot be expected to have adequate knowledge to assess the need for reform, and design appropriate policy intervention, because a lot of the knowledge is held by individual firms.³

For the purpose of design, implementation, feedback, and redesign of economic, industrial and business policies, the public sector needs to recurrently engage the private sector whose members reveal their information about market signals and their preferences, which the public sector validates and integrates into the policy cycle. Effective and regular PPD, therefore, helps reduce policy uncertainty. However, regular exchange of information can only take place if formal mechanisms exist where the public and private sector engage with each other.⁴

By collaborating with the private sector, the public sector risks being captured by special interests that may use the opportunity for rent-seeking.⁵ However, these risks exist

covertly even without a formal PPD mechanism. Engagements with the private sector through a formal institutional framework, on the other hand, reduces those risks.

The right institutional setting for PPD involves well represented, well organized and well-functioning TOs with which the public sector collaborates, instead of overtly or covertly collaborating with few individual businesses. Other key aspects of the institutional setting for PPD are its transparency with due public disclosure, and a mechanism to ensure that policy advocacy by TOs is evidence-based, as is the policymaking by the public sector. These aspects help academic institutions, competing TOs, and other stakeholders to apply checks and balances.^{6,7}

In light of this, the role of TOs becomes paramount, provided they appropriately represent the interests of their respective constituencies; have sufficient participation to avoid free rider problem; and are

³ E. Fernandez-Arias, C. Sabel, E. H. Stein and A. Trejos (2016). *Two to Tango: Public-Private Collaboration for Productive Development Policies*. Washington, DC: Inter-American Development Bank Washington, DC: Inter-American Development Bank; D. Rodrik (2004). *Industrial Policy for 21st Century*, Special Publication for UNIDO. Cambridge, MA.: Harvard University.

⁴ R. Hausmann, and D. Rodrik (2006). *Doomed to Choose: Industrial Policy as Predicament*. Paper prepared for Blue Sky seminar organized by the Center for International Development at Harvard University. Cambridge, MA: Harvard University. K. Sen and D. W. Te Velde (2009). "State Business Relations and Economic Growth in Sub-Saharan Africa." *The Journal of Development Studies*, 45:8, 1267-1283.

⁵ A. Sinha (2005). "Understanding the Rise and Transformation of Business Collective Action in India" *Business and Politics*: Vol. 7: Iss. 2, Article 2.

⁶ R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3.

⁷ The essence of economic and business policy is not always the outcome, but rather the process because it helps the policy gain legitimacy. In other words, the best policy in wrong institutional setting is likely to do considerably less good in the long run, than the second-best policy in the right institutional setting. D. Rodrik (2004). *Industrial Policy for 21st Century*, Special Publication for UNIDO. Cambridge, MA.: Harvard University.

financially sustainable to effectively contribute to PPD.⁸ Organizational capabilities of TOs, therefore, is a prerequisite to effective cooperation between its members, the PPD process, and successful policymaking.⁹

In addition to PPD and other facets of public private collaboration, such as organizing trade fairs or hiring trade lobbyists, TOs also offer various services to their members. These include exploring new markets; labour training; encouraging innovation; providing arbitration/mediation; ensuring standardization – and other collective activities that help increase exports, efficiency and productivity, or improve the business environment. Unlike the PPD activities, from which the TOs do not earn revenues, these services help them to be financially sustainable.¹⁰

In Pakistan too, TOs are engaged by the

public sector through a variety of mechanisms. For example, the Ministry of Commerce consulted some TOs for the purpose of drafting Strategic Trade Policy Framework 2018-2023; the ministry had also sought policy suggestions from textile TOs to improve the sector's competitiveness in early waves of Covid-19. In addition, TOs are consulted by Federal Board of Revenue on taxation affairs. The Planning Commission also recommends implementing access to finance programmes for SMEs in collaboration with the TOs.¹¹

Similarly, the leadership of TOs are ex-officio members of the boards of several government bodies, such as Punjab Board of Investment and Trade, and Board of Approval for special economic zones, whereas international donors also engage TOs as part of their technical sectoral policy assistance to federal and provincial

⁸ R. Hausmann, and D. Rodrik (2006). *Doomed to Choose: Industrial Policy as Predicament*. Paper prepared for Blue Sky seminar organized by the Center for International Development at Harvard University. Cambridge, MA: Harvard University.

⁹ E. Fernandez-Arias, C. Sabel, E. H. Stein and A. Trejos (2016). *Two to Tango: Public-Private Collaboration for Productive Development Policies*. Washington, DC: Inter-American Development Bank; R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others" *Business and Politics*, Vol. 2, No. 3; K. Sen (2015). "State-Business Relations", Topic Guide. Birmingham, UK: GSDRC, University of Birmingham

¹⁰ OECD (2018). "How can Private Sector Organisations Contribute to Economic Resilience in Fragile and Conflict-Affected Contexts in The Middle East and North Africa?". Background note for the MENA-OECD Economic Resilience Task Force. Paris: OECD; R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3; M. Boleat (1996). "Trade Association Strategy & Management", Association of British Insurers.

¹¹ USAID (2018). "Pakistan Quarterly Trade Bulletin", Fourth Quarter Review FY18 & STPF Issue Volume 1, Issue 2. Washington D.C.: USAID. A. Khaver, et al (2021). "Using stakeholder dialogues for strengthening evidence use to inform government decision-making during COVID-19", SEDI Learning Brief 4. Strengthening Evidence Use for Development Impact, Oxford. London: UKaid. S.A.H. Shah (2018). "Framework for SME Sector Development in Pakistan", Planning Commission of Pakistan. MoC. Strategic Trade Policy Framework 2015-18. Islamabad: MoC. FBR press release, dated April 9, 2012 (www.fbr.gov.pk/pr/chairman-fbr-holds-meetings-with-oicci-fpcci/700/2012 accessed on May 19, 2022)

governments.¹² The SBP Banking Services Corporation in partnership with various TOs has started working under a new mechanism in which, in addition to awareness sessions, it facilitates businesses and their employees to apply for bank loans under various concessional credit schemes.¹³

In light of these realities, and the fact that the government wants to improve PPD,¹⁴ the objective of this Special Section is to assess the state of TOs in Pakistan; whether or not they have the capacity to effectively engage in PPD and other facets of public-private collaboration; and the nature of services they offer to their members.

A 2010 study showed that TOs in Pakistan had weak organizational capacity with the staff lacking necessary analytical skills; dormant committees initially formed to analyze and advocate policy reforms; and

lack of consensus among leadership of TOs.¹⁵ Recent diagnostic studies to this effect do not exist; nor do case studies of the contribution of leading TOs in Pakistan under the archetypal roles of TOs.^{16,17}

In the absence of these studies, therefore, this Special Section is based on semi-structured interviews with representatives of TOs across major cities, and key manufacturing and service sectors, with particular focus on textile (*Annexure I*). The discussions were facilitated by a survey designed to gather insights on the organizational affairs of TOs; the services they offer; and the mechanism of PPD (*Annexure II*). Accordingly, the responses from these stakeholder discussions form a key part of the findings.

The Special Section proceeds as follows. Section S1.2 sheds light on key characteristics of TOs and showcases a variety of examples

¹² USAID (2013). "Pakistan Non-Agricultural Value Chain Assessment", Asia and the Middle East Economic Growth Best Practices Project. Washington D.C.: USAID; USAID (2018). "Pakistan Regional Economic Integration Activity (PREIA)", Monthly Progress Report, April 2018. Washington D.C.: USAID; World Bank (2017). "Boosting Pakistan's Export Competitiveness: Private Sector Perspectives", Proceedings from Round Table Meetings held in Islamabad, Peshawar, Karachi and Lahore September - November 2017. Washington D.C. World Bank

¹³ State Bank and Multan Chamber organize a two-day SME Mela in Multan (SBP press release dated January 26, 2022 available at www.sbp.org.pk/press/2022/Pr-26-Jan-2022.pdf accessed on May 19, 2022)

¹⁴ K. Ahmed, V. Ahmed, M. Arshad, S.A. Javed, A. Jillani, A. Khan, A.A. Khaver, U. Nadeem, A. Pellini, Q. Shah, L. Shaxon, A.Q. Suleri, and A. Zaidi (2021). "The Role Of Evidence In Policymaking In Pakistan: A Political Economy Analysis Report", Strengthening Evidence Use for Development Impact. London: UKaid.

¹⁵ A. Salman (2010). *Trade Bodies in Pakistan: Trends, Challenges and Opportunities*. A Diagnostic Study by Centre for International Private Enterprise (CIPE). Karachi: CIPE Pakistan

¹⁶ For instance, Lahore chamber provides mediation services, Karachi chamber organizes a business-to-business event in the form of MyKarachi, and Sialkot chamber with the help of its members has successfully led formation of a dry port and an airport. However, impact assessment of these activities in the form of published research does not exist, nor do case studies of such endeavors.

¹⁷ Diagnostic studies and case studies of impact evaluation are important given the peculiar nature of the contribution of TOs, which manifests itself over long periods of time often waxing and waning during quiet periods between major breakthroughs. These breakthroughs may be legislative, achieved through policy advocacy or new markets explored or innovation patented courtesy research funded by TOs.

of how TOs contribute towards economic growth and development. Section S1.3 discusses the brief history and structure of TOs in Pakistan. It also discusses the state of local TOs, where the key finding is that TOs in Pakistan have weak organizational capacity to engage in PPD. Nor, with some exceptions, do they pool in resources or offer services that help improve exports, investments, productivity, and business environment. This finding is also evident in textile sector, discussed in Section S1.4. Lastly, Section S1.5 offers suggestions to improve the dynamic and raises policy questions for deliberations aimed at strengthening the TOs in Pakistan.

S1.2 Characteristics and Examples of Economic Footprint of TOs

TOs can be defined as non-profit and democratically guided organizations formed and financed by entrepreneurs and companies to promote and support business interests of its members. While TOs are diverse in goals, objectives and functions, they can be classified in two broad categories: business associations, and chambers of commerce.

Business associations typically represent businesses of homogenous industries and firm size and may take different forms based on underlying objectives of associations. For instance, trade/industry associations represent interests of trade or industrial sector and actively participate in policy advocacy, quality upgrading, product

standardization, etc. Similarly, SME associations assist SMEs in obtaining services, such as access to finance, consulting, training and/or group marketing instruments.¹⁸

The chambers of commerce are more comprehensive in nature and comprise businesses from diverse sectoral backgrounds. The underlying objective of chambers is much broader such as promoting conducive business environment by research and advocacy on cross-sectoral challenges, investor matchmaking, foreign trade, arbitration and consultancy (**Table S1.1**).

Both categories of TOs play a critical role in economic growth and development of both developing and advanced economies. They do so by taking a host of measures that can be grouped in two broad sets of activities: (a) market supporting, and (b) market complementing services.¹⁹

Through market-supporting services, TOs ensure the provision of public goods, strong property rights, effective public administration, and infrastructure to all firms. This is achieved by means of evidence-based policy advocacy via PPD, participating in reforms process, and other means of collaboration with public authorities.

With market complementing services, TOs try to reduce market imperfections by encouraging coordination among member

¹⁸ D. McCormick, Winnie Mitullah and M. Kinyanjui (2003). *How to Collaborate: Associations and Other Community Based Organisations among Kenyan Micro and Small-Scale Enterprises*. Occasional Paper 70, Institute for Development Studies. Nairobi: Institute for Development Studies, University of Nairobi

¹⁹ R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3.

Typology, Characteristics and Services Offered by Different TOs

Table S1.1

TOs			
• Nonprofit organizations • Democratically guided by the decisions of their members • Operations are financed by a mix of membership fees, service charges, voluntary grants, and public subsidies.			
Business Associations	Common characteristics	Services offered	Types
	• concentrating on specific industries, firm size • homogeneous membership structures, or functions • corresponding interests and similar problems and needs	• arbitration • industry standard setting • evidence-based policy advocacy • quality upgrading, training and consulting • trade promotions, trade fairs • matchmaking • facilitating market research	• trade or industry associations • small-scale enterprises' associations • women's organizations • employers' associations • bi-national associations
Chambers of Commerce	Common characteristics	Services offered	Types
	• representing the business interests of a certain geographic region. • heterogeneous membership structures, or functions • may perform functions delegated by the government	• delegated government functions • arbitration courts • basic information services • policy research & surveys • matchmaking • local economic development	• regional chambers • international chambers • multilateral chambers • city chambers • national chambers
Source: World Bank (2005). "Building the Capacity of Business Membership Organizations, Guiding Principles for Project Managers", Second Edition			

firms to help bring economic reforms; streamlining interdependent production and investment decisions in a value chain; lowering cost of information; setting industry standards; and promoting quality upgradation.

TOs also act as a service firm to lower the transaction costs of infrastructure and various services obtained by member companies. This is particularly useful when individual member firms are not large enough to set up their own infrastructure or buy services on their own. **Box S1.1** briefly

defines these functions and discusses how TOs in different countries have assisted the process of economic progress by conducting these activities.

Two conditions enhance activities of TOs: (a) state discipline, and (b) increased deregulation and competition in markets or any shock, such as the end of protectionism. The former depends on legislation and bureaucratic capacity, while the latter prompts TOs to upgrade their market supporting and market complementing services. For instance, after liberalization,

Mexican footwear producer associations collaborated with suppliers to standardize measurements, the lack of which had been hurting the industry's prospects. Likewise, to compete with the London market, splintered brokers in New Zealand formed Wool Brokers Association to standardize auction procedures and address issues of insurance, warehousing, on-boarding etc. Similarly, prior to economic liberalization in 1980s, TOs

in Nigeria were inactive. But after liberalization, Manufacturers Association of Nigeria and Kano's chamber of commerce became active, which set-up research offices to assess the state of economy and advocate for policy reforms, such as research on anti-dumping; strengthened their organizational capacity; and raised additional funds to document their own efforts.²⁰

Box S1.1: Examples of Market Supporting and Market Complementing Services by TOs

Establishing a causal link between economic growth and development, and market supporting and complementing services of TOs is a significant challenge because the presence of TOs services at the time of economic reform or spurts of growth and development is not sufficient evidence of causality.^a However, the following examples showcase some ways and means of how TOs contribute towards economic growth and development.

Effective State-Business Relations: This is an important role in supporting the process of economic development across different facets of public policy, from trade and industrial development to taxation and public expenditures. Sen and Velde (2009) documented positive impact of effective state-business relationships on economic growth in 19 sub-Saharan African countries more specifically due to: improved institutional relations by creating umbrella business associations and formalized PPD.^b

In case of an individual country, Kuwait Chamber of Commerce and Industry helped bridge differences between public and private sector. Accompanied by Kuwaiti central bank, the chamber actively participated in preparing and implementing the post Kuwait-Iraq war debt resolution plan for commercial banks. After the bailout package, the chamber opened a debate on non-performing loans and pressurized authorities to initiate financial reforms. The country finally adopted legislation in 1995, which tackled the debt crisis, initiated financial reforms and the privatization process.^c

Implementing Industrial Policies: The industrialization experience in South Korea during 1960-1970s is a prominent example of how governments engage TOs as policy implementing agents in achieving goals (such as export targets), in which the Korea Chamber of Commerce & Industry (KCCI) played a key role. Currently, KCCI performs an intermediary function between the government and businesses by channelling evidence-based advocacy, such as carrying out economic diagnosis, conducting surveys on the condition and opinion of businesses, and participating in major government forums to represent the business sector. The chamber also prepares roadmaps for reform and gives recommendations to the government and the National Assembly. In 2008, a deregulatory taskforce was jointly established by the

²⁰ R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3. S. Ville (2007). "Rent seeking or market strengthening? Industry Associations in New Zealand Wool Broking", University of Wollongong. A. Olukoshi (1996). "Economic crisis, structural adjustment and the coping strategies of manufacturers in Kano, Nigeria," United Nations Research Institute for Social Research. DP77. J Lucas (1994). "The State, Civil Society and Regional Elites: A Study of Three Associations in Kano, Nigeria". *African Affairs* Vol. 93, No. 370 (January 1994), pp. 21-38

KCCI and the Presidential Council on National Competitiveness, with the task of conducting fieldwork to identify business concerns and drafting solutions in consultation with relevant government authorities.^d

Arbitration: Traditionally TOs offer dispute resolution services to settle business disputes outside the traditional courts through negotiation, mediation, and arbitration. Arbitration offers cheaper and less time-consuming dispute resolution where parties may appoint arbitrators with specialized expertise and technical knowledge. Many chambers across different countries provide arbitration services for domestic as well as international parties. These include Federation of Indian Chambers of Commerce and Industry (FICCI), Bangladesh Chamber of Commerce, the Chamber of Commerce and Industry of Romania, the Oslo Chamber of Commerce, Chamber of Commerce of Milan, and many others.^e

In Austria, Austrian Federal Economic Chamber established Vienna International Arbitral Centre in 1975 as an attached department. The institute is now among the leading tribunal institutions in Europe and top seven global venues for international arbitration. It also partners research with Austrian and foreign law schools.^f

Providing Intellectual Property Rights (IPRs): Due to growing importance of IPRs, TOs, especially chambers of commerce, are increasingly engaged in the provision of IPR support services to their members. In many countries such as Germany, Argentina, Austria, Finland, France, Ireland, India, Russia, and UAE, TOs provide IPR services to their members. For instance, the FICCI has established an IPR Division to resolve business concerns related to IPRs. In addition, FICCI also set up an Intellectual Property Facilitation Centre to support micro, small and medium enterprises in IPR tools and technologies.^g

Promoting Evidence-Based Policy Making: In Romania, the five leading ICT business associations formed an alliance, the Tech 21 Coalition, which developed a business agenda with reform priorities and solutions, organized public hearings on specific legislative reform proposals and offered advice to Romanian public authorities on the design of public policies to make the industry more competitive. The Romanian ICT Ministry and the ICT Commission in the Parliament started an open dialogue with Tech 21 Coalition, which resulted in several key reforms. This included introduction of zero salary tax for software developers aimed at curbing the brain drain from Romanian ICT industry; amendment of leasing legislation to encourage software acquisitions across industries; the establishment of technology parks and adoption of an e-signature law for businesses. As a result, the Romanian ICT sector became one of the most competitive in Eastern Europe's ICT industry.^h

Supporting R&D and innovation: For an effective PPD, TOs conduct research on various economic and business affairs with outputs ranging from business and economic outlook surveys, economic updates, in-depth sector specific research and reports. TOs also offer industry-specific and market research services to their members. In addition, TOs facilitate innovation and technology adoption. For instance, the Knowledge Innovation Market, developed by Barcelona Chamber of Commerce, promotes innovation through technology evaluation of companies, transferring technology, conducting commercial feasibility of technology development and implementation, and technology prototyping. The institute also collaborates with universities, research centers, technology parks, public administrations, and disseminates emerging scientific technologies.ⁱ

Similarly, in initial development stages of Malaysia's automotive industry, Malaysian Automotive Component Parts Manufacturers Association pressurized industry to adopt mandatory deletion programme that encouraged local assembly of automobile parts and restricted imports. Later, the association shifted its focus from localization to technology promotion.^j

Standardization and codes of practice: Some TOs draft industry standards and codes for compulsory adoption by the industry in collaboration with government. Others set up organizations to test and certify standards. For instance, the Pharmaceutical Manufacturers Association of Canada through the creation of the Pharmaceutical Advertising Advisory Board and the use of its own Code of Marketing Practice has assumed responsibility for the regulation of the advertising of ethical drugs.^k

Similarly, since in export markets of basic food products, like rice and coffee, the failure of one supplier to meet minimum standards can undermine the reputation of all the country's producers, there have been examples of TOs coming together to ensure standardization of local produce. For example, in 1950s, Thailand's Board of Trade, apex association of agricultural export merchants, organized its rice-exporting members to develop and adhere to product standards, following which Thai government granted export licenses only to those members belonging to the associations and complying with these standards. In Columbia, National Federation of Coffee Growers of Colombia, a growers' association, devised various labelling protocols to distinguish different types of coffees, and ensured proper labelling through sanctions.^l

Labour training & upskilling of workers: TOs also collaborate with technical and traditional institutes and industry to develop and upgrade human resource skills according to dynamic industrial needs. For instance, Thai Embedded Systems Association in Thailand, which links corporate and individual developers and with public and private users of embedded computing technology, trains university students in developing software systems for automotive components.^m Similarly, the Malaysian Rubber Products Manufacturers' Association collaborates with local universities to offer technical and vocational training courses to labour on various aspects of rubber production, such as compounding, extrusion, injection moulding.ⁿ

References:

^a B. Herzberg and L. Sisombat (2016). *State of Play – Public-Private Dialogue. Public-Private Dialogue (PPD)*. Practical Note Series. Washington DC: World Bank

^b K. Sen (2015). *State-Business Relations: Topic Guide*. GSDRC International Development Department, University of Birmingham: U.K.; K. Sen and D. W. T. Velde (2009). "State Business Relations and Economic Growth in Sub-Saharan Africa", *Journal of Development Studies*, Vol. 45(8) pp. 1267-1283.

^c P. W. Moore (2001). "What Makes Successful Business Lobbies? Business Associations and the Rentier State in Jordan and Kuwait", *Comparative Politics*, Vol. 33(2) pp. 127-147

^d Source: International Chamber of Commerce Case Studies, available at www.iccwbo.org/chamber-services/chamber-resources/chamber-case-studies-library/#1486743201254-492800dd-d6c1 accessed on May 19, 2022;

Korean Chamber of Commerce and Industry, available at www.english.korcham.net/nChamEng/Service/About/appl/03.asp accessed on 19 May, 2022. ; Korean Development Institute (2016). *Strategies for Effective Implementation of Second Growth and Transformation Plan (GTP 2)*. Senior Policy Dialogue and Final Reporting Workshop. Seoul: Korean Development Institute

^e Source: www.international-arbitration-attorney.com/arbitral-institutions-and-arbitration-courts/ accessed on May 19, 2022

^f Source: Vienna International Arbitral Centre, available at www.viac.eu accessed on May 19, 2022.

^g ICC and WIPO (2011). *Handbook for Chamber of Commerce and Business for Setting up Intellectual Property Services*. Paris: ICC and Geneva: WIPO

^h K. Frauscher and C. Bulat (2009). *The power of business advocacy and ICT reforms*. The Business and Development Discussion Papers. Paper No. 10. Washington DC: World Bank

ⁱ Source: Knowledge Innovation Market Barcelona, available at www.kimglobal.com/en/kimbcn/, accessed on May 19, 2022

^j ILO (2016). *Analysis of the Economic Development Role of Sectorial Business Associations: In the Rubber, Electronics and Electrical and Automotive Sectors in Malaysia, Thailand and Viet Nam*. Working Paper Series 16. Geneva: ILO

^k W. Coleman and W. Grant (1984). "A Comparison of Organizational Development in Britain and Canada", *Journal of Public Policy*, Vol. 4(3) pp. 209-235.

^l R. Doner and B. R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others", *Business and Politics*, Vol. 2(3) pp. 261-288

^m P. Intarakumnerd, P. Chairatana and P. Chaiyanajit (2015). "Global Production Networks and Host-Site Industrial Upgrading: The case of the semiconductor in Thailand", *Asia Pacific Business Review*, Vol. 22(2) pp. 289-306.

ⁿ ILO (2016). *Analysis of the Economic Development Role of Sectorial Business Associations: In the Rubber, Electronics and Electrical and Automotive Sectors in Malaysia, Thailand and Viet Nam*. Working Paper Series 16. Geneva: ILO

S1.3 Trade Organizations in Pakistan

As discussed in Section S1.1, TOs in Pakistan have been engaged in PPD. Some TOs also further the cause of business community and contribute to achieving a desirable economic outcome for the country. An example of this are the efforts of the Surgical Instruments Manufacturers Association in response to restrictions on Pakistani-made surgical imports by the US Food and Drug Authority in 1994. The association, with aid from the government, hired a US-based quality assurance firm for the technical training of local manufacturers. As a result, by January 1997, 75 local firms became certified by FDA, allowing them to export to the US.²¹

There are other instances of local TOs' positive contribution to the private sector's interest by employing advocacy tools and facilitating business-to-business (B2B) events. However, in certain areas, such as research and development, evidence-based policy advocacy, alternative dispute resolution (ADR) mechanisms, and resource pooling for the common benefit of members, TOs lag behind international best practices. The underlying reason for this is the lack of professional staff and, in some cases, the

limitation of funds. To understand the prevalence of these issues, it is necessary to understand the organizational structure of local TOs.

Regulatory and Organizational Structure

The history of trade organizations operating in Pakistan dates back to pre-independence. Overseas Investors Chamber of Commerce & Industry, formerly known as Karachi Chamber of Commerce, was formed in 1860. Also, the Lahore Chamber of Commerce & Industry was established in 1923 under the name of the Northern Indian Chamber of Commerce.²² However, the first legislation to monitor and regulate TOs in Pakistan was the Trade Organization Ordinance (TOO) 1961.

However, since TOO 1961 did not demark the regulator's role, and there was a vacuum in the licensing process and evaluation mechanism, the government formed a committee in 2006 to overhaul TOs legal landscape. The committee revealed that the TOs did not act like think-tanks to guide policy on trade and industry. Due to a lack of professional management, their capacity

²¹ K. Nadvi (1999). "Collective Efficiency and Collective Failure: The Response of the Sialkot Surgical Instrument Cluster to Global Quality Pressures", *World Development*, Vol. 27, No. 9, pp. 1605-1626.

²² OICCI, www.oicci.org/about-the-oicci/, accessed on May 19, 2022; LCCI, www.lcci.com.pk/mediation/, accessed on May 19, 2022

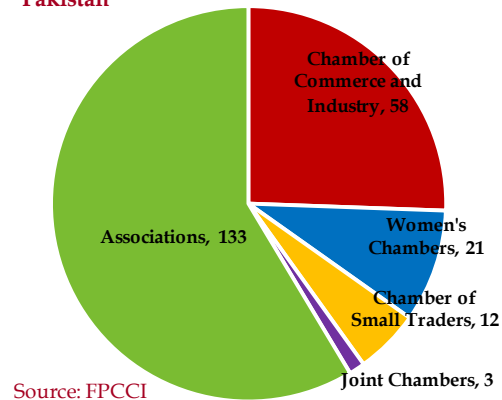
to present well researched views on policy matters was also limited. It emphasized that for TOs to work efficiently, it is imperative to have defined roles, responsibilities, and an operational framework. The committee also recommended that a new law be formed, which provides for an independent regulatory body and licensing fees to discourage fake trade bodies.²³ These recommendations were implemented in the shape of the Trade Organization Ordinance, 2007, later enacted as the Trade Organization Act (TOA) 2013, the current regulation in place.

The 2013 Act provides for the regulator in the Director General Trade Organization (DGTO) and an apex body in the Federation of Pakistan Chamber of Commerce and Industry (FPCCI), whose members include all the trade bodies registered with DGTO. It is important to note that all bodies within the ninety days of getting the license from the DGTO have to incorporate as non-profit company with the SECP.²⁴

The law along with a mechanism to form associations and chambers, also allows for establishing separate chambers for women and small traders on the basis of voluntary membership. As of January 2022, 227 trade organizations are members of FPCCI, including 21 women chambers and 12

chambers for small traders (**Figure S1.1**).²⁵ All trade organizations are based on the democratic principle, with the general body of all members electing the key office-bearers.²⁶ For the FPCCI, there are fourteen office bearers, including a president, a senior vice president, and twelve vice presidents, with representation from TOs across the spectrum. It is worth noting that none of FPCCI's office bearers come from the companies listed on Pakistan Stock Exchange (PSX) even though those companies are members of different TOs. This is also true for Karachi, Islamabad, Lahore, Faisalabad, and Sialkot chambers.²⁷ This points towards low level of active participation in TOs by relatively larger companies.

Number of Trade Organizations in Pakistan **Figure S1.1**



²³ Recommendations of Committee on Revision of Trade Organizations Ordinance, 1961 formed under MoC vide notification No.12 (1) 2006. T.O dated April 27, 2006.

²⁴ Rule 6 (e) of Trade Organizations Rules, 2013.

²⁵ FPCCI, www.fpcci.org.pk/, accessed on January 23, 2022

²⁶ General body elects executive committee, which in turn elects president, senior vice president, and vice president, in case of associations office bearers are titled as chairman, senior vice chairman, and vice-chairman. (Source: Rule 21 of Trade Organizations Rules, 2013)

²⁷ The office bearers' details were obtained from the relevant chambers' website to cross-check it on the Pakistan Stock Exchange website. (All the websites were accessed on January 25, 2022.)

Apart from FPCCI and its member bodies, there has been a recent trend of another form of business coalition in Pakistan in the shape of Pakistan Business Council (PBC), Pakistan Agriculture Coalition (PAC) and Pakistan Textile Council (PTC). These bodies are formed by leading companies, many of which are listed at the PSX and are also members of different TOs. The members of these coalitions do not represent the wider business community, but their contribution to the economy is dominant. For instance, combined turnover of PAC's sponsors is around US\$ 10 billion and PTC's members account for US\$ 4.5 billion of textile's exports.²⁸

These coalitions are not registered with the DGTO and legally do not qualify as a chamber or association under the TOA 2013. However, despite their legal status, they perform functions similar to traditional TOs with a role in the public-private dialogue. For instance, the PAC frequently engages government officials and the PBC advocates economic reforms such as tariff liberalisation under its Make in Pakistan initiative.²⁹ The government also grants these bodies seats on important boards. For example, the PBC is represented on the Board of Approval for Special Economic Zones.³⁰

The Current State of TOs in Pakistan

The primary reason of existence of TOs is to create a collective platform to steer policy by advocating the agenda of the private sector. However, the ambit of activities they perform has widened. Now, in an effort to ensure financial sustainability and retain their membership, these bodies perform the function of research and development, take active steps in facilitating technological adoption, and contribute to improving the overall business environment by providing ADR mechanisms and protecting intellectual property rights (IPR).³¹

As mentioned in Section S1.1, in the absence of updated diagnostic studies and case studies on the role of TOs in Pakistan, this section is based on semi-structured interviews of representatives of leading TOs from a cross-section of regions and sectors. The interviews were facilitated by a survey questionnaire (**Annexure-II**), designed on the basis of academic literature. The TOs for this section were chosen to reflect prominent regional chambers and a few associations from vital and emerging sectors (**Table A, Annexure I**).³² The survey results and other key findings from literature review are as follows.

²⁸ Similarly, PBC joining fee and annual fee is Rs 3 million and Rs 2 million respectively to ensure serious business participation. Source: PAC, www.pac.com.pk/about-us/, accessed on May 19, 2022; PTC, www.ptc.org.pk/about-ptc/mission-and-vision/, accessed on May 19, 2022; PBC, www.pbc.org.pk/about-pbc/, accessed on May 19, 2022; www.pbc.org.pk/wp-content/uploads/PBC-Profile.pdf, accessed on May 19, 2022

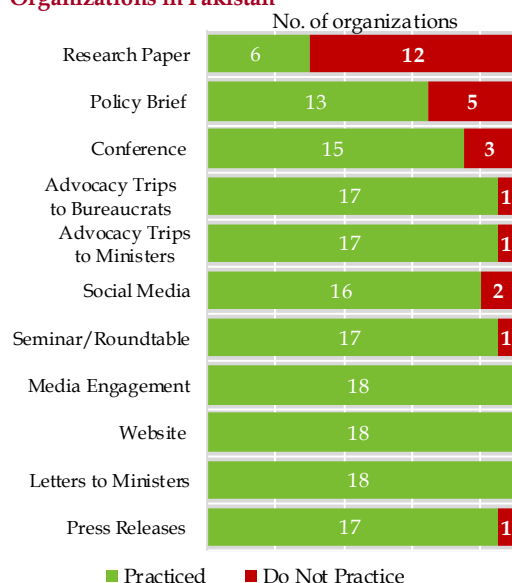
²⁹ Pakistan Business Council, www.pbc.org.pk/wp-content/uploads/PBC-Profile.pdf; PAC, www.pac.com.pk/news/, accessed on May 19, 2022

³⁰ Special Economic Zones Act, 2012, as amended up to December 31, 2015

³¹ International Chamber of Commerce, history of the chamber movement, www.iccwbo.org/chamber-services/world-chambers-federation/history-chamber-movement/, accessed on January 27, 2022.

³² In addition to the TOs listed in Annexure I, the section draws on discussions with Mr. Riaz Ahmed Director General Trade Organisation, Ministry of Commerce; and Mr. Moin Fudda, former country director, Center for International Private Enterprise (CIPE), Pakistan.

Advocacy Tools Practiced by Trade Organizations in Pakistan **Figure S1.2**



■ Practiced ■ Do Not Practice
 *Total 18 organizations were surveyed
 Source: Survey conducted as per Annexure II

Advocacy with lack of research-based tools and gazetted forums

To gauge the performance of the advocacy function, participants were asked to identify the tools they use. All 18 participants engaged with media, and scribed letters to ministers to influence a policy outcome (Figure S1.2). However, the tools associated with evidence-based advocacy were less widely employed. For instance, only 33 percent published research papers to back their advocacy with evidence.

In the case of sector-specific associations, advocacy can be more effective if trade bodies across the value chain make a concerted effort for an outcome. Out of 9 associations, only 2 had a formal mechanism to connect with their counterparts across the value chain.³³ However, the majority claimed to take joint action if their interest over a policy issue aligned.

Public-Private Dialogue

As identified in Section S1.1, the two essential aspects of PPD are advocacy to ensure effective communication, and research to ensure informed dialogue. Whilst TOs in Pakistan pursue various means of advocacy and lobbying, the absence of an effective institutional framework and the nature of instruments used for advocacy point towards a weak environment of evidence-based policymaking.

There was also a lack of formal gazetted joint advisory boards to facilitate PPD between TOs and the government. TOs are also not given adequate representation at high-level advisory councils. For instance, of the 15 private sector members of CPEC Business Council only two are from TOs, and the rest are by-name appointees. Similarly, of the 13 private sector members of Economic Advisory Council (EAC) there are no ex-officio appointees from TOs; instead there

³³ This question was not asked from chamber of commerce, as by nature they can have members from multiple sectors and industries across the value chains.

are by-name appointees from the business community.^{34, 35}

With exception of government-led Sugar Advisory Board and Pakistan Software Export Board where Pakistan Sugar Mills Association (PSMA) and Pakistan Software Houses Association (PASHA) contribute to sectoral policy as board members, respectively, instances of joint advisory boards as structured mechanism for PPD and sectoral policymaking are not common.³⁶ Although the government engages and often seeks responses from different associations and chambers, the boards with the mandate to regularly meet and officially weigh on the sectoral policies can systematize these efforts.

Another feature that is largely missing from the TOs ecosystem is the delegation of public function from the government. As associations are close to players in their respective sectors, they are well poised to perform certain public functions. Due to this unique position, states worldwide sometimes delegate a public function to them. For instance, the Columbian government empowered a coffee association to collect

export tax and spend it on infrastructure development.³⁷ Also, when the restriction was levied by the US on Taiwanese footwear, the government delegated the Taiwan Footwear Manufacturers Association to manage the export quota.³⁸ However, no surveyed participant has been put in charge of such functions in Pakistan.

Weak research amid low demand for evidence-based policymaking

Research and surveys, especially to ascertain market dynamics, have become one of the key features for business associations around the world.³⁹ For instance, under US African Growth and Opportunity Act (AGOA), some sub-Saharan African countries were granted better market access to the US. Initially, Kenyan apparel was also included under AGOA, but it was to be excluded before the program's conclusion. However, due to evidence-based policy position presented by the African Cotton and Textile Industry Federation, the apparel products remained on the list. Resultantly, over the next 13 years, the economy of Kenya benefitted by

³⁴ Source: Finance Ministry, Notification No.F.I(27)/DEA (SS)/EAW2022 dated April 27, 2022; Board of Investment <https://invest.gov.pk/about-us/cpec-business-council>, accessed on May 19, 2022

³⁵ In the previous EAC constituted in April 2021, there were no ex-officio appointees from TOs among its 13 private members. (Finance Ministry, Notification F.No.13 (5)IERU/EAC/2018 dated April 3, 2021.)

³⁶ Source: World Bank (2017). "Boosting Pakistan's Export Competitiveness: Private Sector Perspectives", Proceedings from Round Table Meetings held in Islamabad, Peshawar, Karachi and Lahore September - November 2017. Washington D.C.: World Bank.

³⁷ R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others", *Business and Politics*, Vol. 2, No. 3.

³⁸ L. Cheng (1996). "Embedded Competitiveness: Taiwan's Shifting Role in International Footwear Sourcing Networks." Ph.D. Thesis, Department of Sociology Duke University. Durham: Duke University

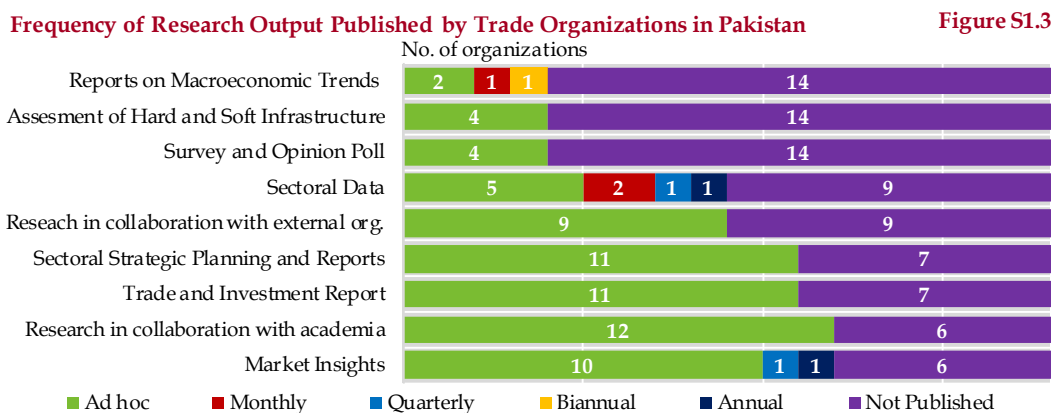
³⁹ R. Strohmeier, M. Pilgrim, F. Luetticken, R. Meier, H.G. Waesch, and I. Arias (2005). *Building the Capacity of Business Membership Organizations: Guiding Principles for Project Managers*. A Handbook by Small and Medium Enterprise Department, World Bank. Washington D.C.: World Bank.

US\$ 1.9 billion.⁴⁰

Similar to their international counterparts, TOs in Pakistan are also adopting the research and evidence function, as 13 out of 18 TOs surveyed have a separate research and development department. However, most respondents acknowledged that their research department needed professionals to function properly. The same was reflected in the research output, which, with some exceptions, is limited in scope and nature. TOs submit the budget recommendations before the announcement of the federal and provincial budgets and some also publish annual sectoral reports and quarterly journals, but the rest of the research is published mostly on ad hoc basis (**Figure S1.3**).

Since TOs are closely associated with businesses, they can also support the state agencies by acting as evidence producers in the form of published data. Although some TOs, for instance PAMA and APCMA, regularly publish sectoral data, majority only report it when requested by government agencies.

In addition to weak in-house research functions, TOs in Pakistan also do not create a demand for research from universities, even though business leaders in Pakistan acknowledge the lack of market research.⁴¹ Being privy to their needs, businesses are better placed to drive the industry-academia linkage from the demand side. The role of TOs is vital in this context given their ability to pool resources for the common good of its members and because it is easier for



Note: Total 18 organizations were surveyed
Source: Survey conducted as per Annexure II

⁴⁰ International Trade Centre (2021). *Reforming Public Policy — Step By Step. An Introduction to Dialogue and Advocacy for Women's Business Associations*. Guide is prepared under the Shetrades In The African Continental Free Trade Area project. Geneva: International Trade Centre.

⁴¹ N. Haque, M. Mahmood, S. Abbas, and C.S. Jones (2020). "The University Research System in Pakistan." *A Knowledge Platform Project In Collaboration with the British Council In Pakistan*. Karachi: British Council

academia to solicit funding for research from TOs as representative bodies rather than from individual businesses.⁴²

Even though some TOs in Pakistan have signed MoUs with universities, they generally do not translate into a regular publication feature or materialize into tangible results. Instead, most TOs in Pakistan are focused on networking and lobbying without providing evidence, thus creating little research demand. TOs in Pakistan are also not active producers of market surveys and benchmarking data.⁴³

While these factors limit the TOs' ability to contribute towards public-private dialogue through a systematic gathering of evidence and analysis and policy proposals thereof, policymakers in Pakistan also have little demand for evidence-based policymaking amid a lack of government funding for economic and business policy research. Accordingly, businesses and policymakers' weak demand for research makes the public-private dialogue process less effective and more susceptible to rent-seeking by interest groups.⁴⁴

This is a matter of concern since one of the many reasons developing countries' reform experiences show mixed results is that they

do not pursue evidence-based policymaking, which is necessary for producing unique governance solutions to localize international best practices. To this end, active participation by TOs in evidence-based public-private dialogue is an essential factor.⁴⁵

Market Complementing Services

In addition to the function of advocacy and research, chambers and associations offer a host of services to their members. Whereas, advocacy and research are expenditure items on TOs' financial statements, the services they offer are revenue sources. Accordingly, TOs in Pakistan offer different services to their members. Some organize international trips for members, while almost all offer visa facilitation by issuing referral letters against service fees. TOs have also set up helpdesks to answer members' queries and accommodate new members, while some provide certificates of origin (COOs) (**Figure S1.4**).⁴⁶

TOs in the country are also active in B2B events. Every chamber and association interviewed organized either a conference, seminar, exhibition, or standard matchmaking service to connect suppliers and buyers. Some regular and noticeable

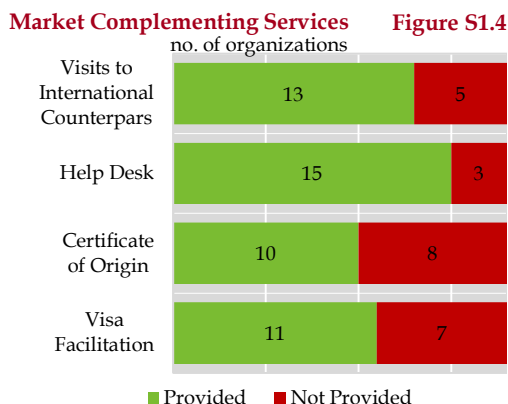
⁴² B. Pourdeyhi (2021). "University research funding: Why does industry funding continue to be a small portion of university research, and how can we change the paradigm?", *Industry and Higher Education*.

⁴³ N. Haque, M. Mahmood, S. Abbas, and C.S. Jones (2020). "The University Research System in Pakistan." *A Knowledge Platform Project In Collaboration with the British Council In Pakistan*. Karachi: British Council

⁴⁴ N. Haque and D. Orden (2020). "Developing Research and a Research Culture: Results from a Pilot Project in Pakistan", *The Pakistan Development Review*. 59:3 pp. 553-570

⁴⁵ Andrews, M. 2013. *The Limits of Institutional Reform in Development*. Cambridge: Cambridge University Press; Yaamina Salman (2021). "Public management reforms in Pakistan", *Public Management Review*, 23:12

⁴⁶ Certificate of origin is a trade document verifying the origin of exported goods.

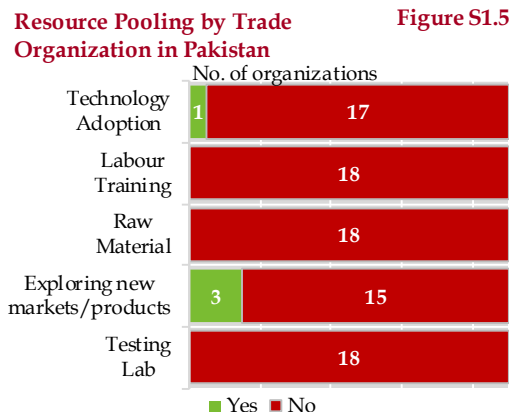


Note: Total 18 organizations were surveyed

Source: Survey conducted as per Annexure II

events include KCCI's My Karachi exhibition, which attracts local and international businesses, and RCCI's All Pakistan Chambers Presidents' Conference, which gathers leaders of all chambers and focuses on different themes every year.^{47,48} The conference also calls for participation from the government and acts as a PPD forum to evaluate economic policies for the betterment of the business community.⁴⁹

However, when it comes to the more sophisticated market complementing services such as setting industry standards, establishing testing labs, exploring new export markets, improving productivity, or offering arbitration and mediation services to improve the business environment, TOs in



Note: Total 18 organizations were surveyed

Source: Survey conducted as per Annexure II

Pakistan seem to fall behind. On the one end, TOs lack professionally staffed departments for these services. At the other end, TOs' members do not pool in resources, i.e., funds in addition to membership fees, to offer such services to their members. (Figure S1.5, S1.6).

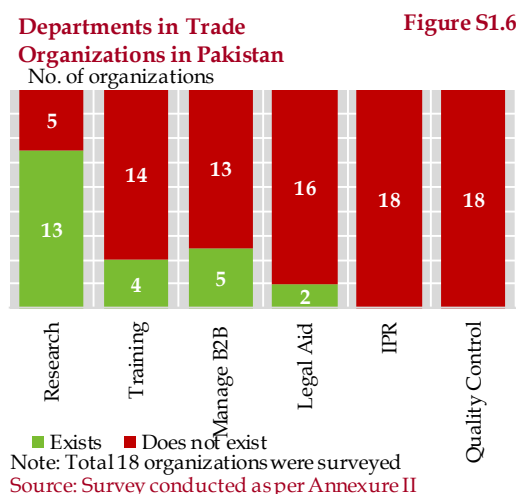
One of the noticeable exceptions to this trend is the Sialkot Chamber of Commerce and Industry (SCCI). In 1997 and onwards, the SCCI contributed both financially and administratively to monitor and eliminate child labour from Sialkot's football industry in collaboration with international agencies.⁵⁰ In 1999, the SCCI in collaboration with other private and public sector stakeholders led the Sialkot City Package Programme to improve

⁴⁷ RCCI, www.rcci.org.pk/apcpc/, accessed on May 19, 2022

⁴⁸ KCCI, www.kcci.com.pk/my-karachi/, accessed on May 19, 2022

⁴⁹ B. Herzberg and L. Sisombat (2016). "State of Play – Public-Private Dialogue. Public-Private Dialogue (PPD)", *Practical Note Series*. Washington D.C.: World Bank.

⁵⁰ SCCI collaborated with International Labour Organisation under Atlanta Agreement to eliminate child labour. (Source: S. Becker and Z.U. Ahmed (1999). *Elimination of Child Labour in the Soccer Ball Industry in Sialkot, Pakistan*. Evaluation Report PAK/97/MO1/USA. Geneva: ILO; P.L. Thomsen and K. Nadvi (2010). "Global Value Chains, Local Collective Action and Corporate Social Responsibility: A Review of Empirical Evidence." *Business Strategy and the Environment*. Vol. 19, issue 1.



the city's infrastructure.⁵¹ Similarly, it played a lead role in building Pakistan's first private airport in Sialkot and the setting up of Airsial airline.⁵² Other exceptions include LCCI's mediation centre formed in collaboration with the International Finance Corporation (IFC).⁵³ Apart from this, there have been instances of members pooling resources to acquire land or building for their TO's secretariat but rarely for technology adoption, testing labs, or joint research to explore new markets.

Besides these, services like arbitration and legal aid are provided by some other TOs.

However, these are through sub-committees whose members work voluntarily rather than through professionally staffed departments or separate centres established and owned by TOs for these purposes. This is unlike international best practices as shown in **Table S1.2**, which compares Pakistan's apex body, FPCCI, with its peers in the region.

The absence of these services has a two-pronged impact. At the one end, the absence of professionally managed services against adequate fees leaves the TOs with little finances and dependent on funding by the government, such as through the Export Development Fund or by bilateral donor agencies.⁵⁴ At the other end, it prevents the TOs from fulfilling their roles towards improving the business environment and economic growth as per the objectives of the Trade Organization Act, 2013.⁵⁵

Organizational Constraints

Business associations must have professionally trained staff to strengthen their organization and successfully execute their functions.⁵⁶ In the case of TOs in Pakistan, the administrative head is the general secretary, a paid employee. In addition, a research department and, in some

⁵¹ SCCI, www.scci.com.pk/sialkot-city-package/, accessed on May 19, 2022.

⁵² SCCI (2021). Annual Report 2020-21. Sialkot: SCCI; and Sialkot International Airport, available at www.sial.com.pk/about, accessed on May 19, 2022)

⁵³ LCCI, www.lcci.com.pk/mediation/index.php, accessed on May 19, 2022

⁵⁴ UKaid (2021). "The Role of Evidence in Policymaking in Pakistan. A Political Economy Analysis Of: Planning and Reform for Economic Development; Child Labour; and Education Pathways into Employment". London: UKaid.

⁵⁵ Trade Organisation Act 2013, available at www.na.gov.pk/uploads/documents/1562222010_669.pdf accessed on May 19, 2022.

⁵⁶ R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others", *Business and Politics*, Vol. 2, No. 3.

Comparison of Key Services & Activities by Apex Chambers of Commerce in Different Countries

Table S1.2

	FPCCI (Est. 1950)	FICCI (Est. 1927)	FBCCI (Est. 1973)	FCCISL (Est. 1973)	VCCI (Est. 1963)	TOBB (Est. 1950)
Trade Helpdesks/ B2B Networking	Helpdesks established	Trade helpdesks in East Asia, East Africa, Caribbean etc. Has B2B web portal with searchable directories	Facilitate international delegations, fairs & exhibitions etc.	Facilitate international delegations, fairs & exhibitions etc.	B2B e-site: searchable directory of companies	
Research Department/ Output	Policy briefs, trade reports, sectoral reports; surveys and polls on ad-hoc basis	State of economy reports, policy briefs, surveys, sectoral policy research plans, collaboration with ministries, KPMG, Nielson	Handbooks, Study Reports, position papers, country profiles	Research papers, proposals, e-surveys	Sectoral research, monthly magazines, annual reports, surveys	Annual reports, production capacity reports, sectoral policies
Intellectual Property Rights (IPR)		IPR Division; cooperation agreement with World Intellectual Property Rights Organization			VCCI IP Co Ltd, incorporated as a separate IPR company.	
Arbitration Centre		Indian Council of Arbitration, cooperation agreement with 40 major arbitral centres	Bangladesh Council of Arbitration	Sri Lanka National Arbitration Centre	Vietnam International Arbitration Centre	TOBB Arbitration center
Training & Development		Engages industry leaders in skilling activity; collaborates with government in skill development	FBCCI Skill Lab-part of the FBCCI Impact 4.0 Initiative, to prepare for 4th Industrial Revolution under the 2041 Vision	Training programs range from seminars and workshops to advanced certificate and diploma courses	Vocational training in collaboration with international organizations	Works with Turkish Employment Agency on Vocational Education & Employment; Set-up Insurance Training Center with Turkish Insurance Association
Quality Certifications, Testing labs etc.		FICCI Research & Analysis Centre for industry-wide quality standard for food, nutraceutical, pharmaceutical etc.				Quality management applications & standards in collaboration with EU chambers of commerce
Technology Adoption		Various innovation programs e.g. India-Rwanda Innovation Growth Program, DST-Lockheed Martin-Tata Trusts India Innovation program	Tech centers that promote FinTech, Agriculture Tech, Education Tech etc.	SMED project for industrial engineering, enterprise & agribusiness development, tech transfer etc.		
Industry-Academia Linkage	MOUs with universities, e.g. collaboration with DHA Suffa University; arranged webinar for SMEs on supply chain, e-commerce etc.	Various initiatives e.g. National Knowledge Functional Hub initiative with the UK's Royal Academy of Engineering	FBCCI Institute & FBCCI University established. Agreements with Massachusetts Institute of Technology, University of Toronto, etc. to train local startups.	Boot camps for development of startups on topics i.e. design thinking, financing, compliance	Collaborates with academia; provides them sectoral statistics, arranges workshops related to the research area	Has 81 academic advisors who contribute to local data production; Collaboration with universities, researchers & companies

FPCCI: Federation of Pakistan's Chamber of Commerce, FICCI: Federation of India's Chamber of Commerce, FBCCI: Federation of Bangladesh Chamber of Commerce and Industry, FCCISL: Federation of Chambers of Commerce and Industry of Sri Lanka, VCCI: Vietnam Chamber of Commerce and Industry, TOBB: The Union of Chambers and Commodity Exchanges of Turkey

Source: Respective websites of these chambers of commerce; in case of FPCCI, findings as per website and semi-structured interview with officials

cases, separate training and B2B departments also exist (**Figure S1.6**).

However, anecdotal evidence suggests that these departments are inadequately staffed both in terms of the number of employees as well as their skill and experience. The same, as mentioned earlier, is reflected in TOs' limited scope and nature of research output and services offered. Other functions are performed by subcommittees headed by members working voluntarily instead of individual departments staffed with full-time paid professionals.

The main limitation flagged by the majority of the participants behind the lack of professional staff, quality of research and advanced services was the shortage of funds. With some income generated from the issuance of visa recommendations and COOs, TOs heavily rely on membership fees for their revenues. However, because membership retention and recruitment of new members is also a problem for some organizations, the funding source becomes unstable.

An effective strategy to improve overall revenues and retention of members may be to introduce the concept of tiered membership.⁵⁷ This system enables business

associations to attract businesses from different sectors by offering tailored packages where different fees are charged to different members depending on the scope and extent of services they wish to avail from the TOs. However, in Pakistan, TOs are limited by law to have only two classes of membership – corporate and associate – that are charged different membership fees without any difference in the services offered to them.⁵⁸

In addition, to increase member density, membership for businesses belonging from a specific sector and a particular region may be made compulsory to relevant associations and chambers. Such a model allows for increased membership and solves the problem of membership retention. However, since the TOs will be guaranteed to get members, motivation to create additional services to attract members is affected.⁵⁹

Another burden on TOs is the conduct of elections every year. This becomes a frequent expenditure for TOs in terms of finances and time spent on managing elections rather than focusing on the organization's core functions.⁶⁰ The annual election of office bearers also makes the task of long-term planning a major challenge in the absence of a well-staffed secretariat and strong organizational capacity.

⁵⁷ CIPE (2019). "Business Associations for the 21st Century. Guides and Tools", Washington D.C.: CIPE

⁵⁸ The main difference between the two categories is that the corporate members are either a sales-tax registered manufacturing or business company or corporate body or a multinational. In contrast, associate members do not qualify as either of those. (Rule 11, Sub rule 7 of Trade Organizations Rules 2013.)

⁵⁹ M. Heseltine (2012). "No Stone Unturned: Chamber Of Commerce International Comparisons", BIS/12/1214. London: Dept. for Business, Innovation and Skills.

⁶⁰ Discussions with TOs' office bearers and management reveal that each year the secretariat of the TOs spends on average 70 to 90 days on various aspects of election management, depending on the size of the TO's membership.

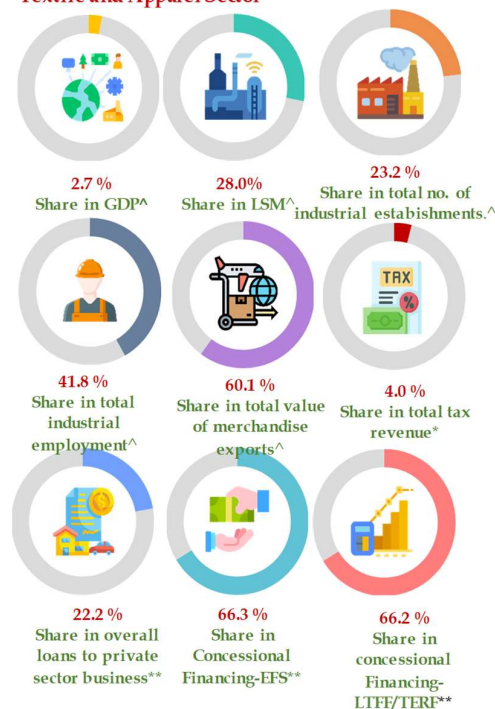
The annual election is a legal requirement stemming from the Trade Organization Act, 2013, which defines the tenure of the office-bearers to be one year.⁶¹ Such a short term means a frequent change in leadership, which is a hurdle in the smooth functioning of TOs. In recognition of this problem, a bill has been tabled in the parliament, but it has not been passed yet.⁶² However, the idea behind the one-year term is to rotate the leadership, and because these office bearers are industry players with their businesses to run, they prefer a shorter term.

The discussion in the preceding paragraphs reflects the cross-sectional view of TOs representing various regions and business clusters in Pakistan. However, a closer look at TOs from Pakistan's textile sector, one of the most important industries, strengthens the view that these challenges are deep-rooted across different regions and business clusters (represented by TOs) in the country.

S1.4 Case Study: Role of TOs in Textile Sector

By most key metrics, textile industry is one of the biggest contributors to Pakistan's economy; be it exports, industrial production or non-farm employment, the sector has a dominant footprint (**Figure S1.7**). In addition to underlying macroeconomic challenges, the textile sector is exposed to a host of challenges across its supply chain.

The State of Activity in Pakistan's Textile and Apparel Sector **Figure S1.7**



Sources: *FBR; **SBP; [^]PBS. Share in LSM; no. of industrial establishments; and industrial employment have been taken from CMI2015-16.

This includes protectionism, weak R&D, low-skilled labor, weak industry-academia linkages and inability to diversify into new export markets.⁶³ As discussed in preceding sections, PPD as well as coming togetherness of the textile sector through well organized

⁶¹ Article 11 (1) of the Trade Organization Act, 2013

⁶² Trade Organizations (Amendment) Act, 2021

⁶³ Tanveer, M. and Zafar, Sarah (2012). "The stagnant performance of textile industry in Pakistan", *European Journal of Scientific Research*; Kazmi, S.A.Z. and Takala, J. (2014). "An Overview of Pakistan's Textile Sector from Operational Competitive Perspective – A Suggestive Analysis", *World Journal of Engineering and Technology*; SMEDA (2005). "Textile Vision", available at www.tco.com.pk/documents/aecddb9e4c.PDF, accessed on May 19, 2022.

and well-functioning TOs can help address these challenges.

The textile sector has a large number of associations that represent different sub-sectors within its value chain - from raw materials to various categories of finished products. There are a total of 19 textile and apparel associations in Pakistan that are listed with DGTO as against 6 in chemicals, 8 in metal and 14 in the engineering sector.⁶⁴ Some of the textile TOs date back to several decades; e.g. Karachi Cotton Association was established in 1933, whereas All Pakistan Textile Mills Association (APTMA) and Pakistan Silk & Rayon Mills Association (PSRMA), were setup in late 1950s.⁶⁵ A recent addition to TOs in textile sector is the formation of Pakistan Textile Council (PTC), which describes itself as a research and advocacy platform.⁶⁶ Albeit as mentioned in previous section it is not a formally registered TO with the DGTO. It is important to note that member companies at the board of PTC are also members of different conventional DGTO registered textile TOs, but only some of them play an active role as office bearers of registered textile TOs.⁶⁷

To assess the role of textile sector TOs in PPD, and the delivery of market complementing services, this section is based

on discussions with representatives of leading textile sector associations (*Table B-Annexure I*) and other public and private sector stakeholders.⁶⁸

Public-Private Dialogue

The state of PPD in textile sector TOs does not appear different from the state of PPD in TOs of the country. Textile sector TOs are strong on advocacy. However, the instruments used for the same do not point towards an environment of evidence-based policy advocacy, whereas institutional framework of PPD also appears to be weak.

Weak Evidence-based Advocacy

Most of the textile TOs use basic advocacy tools such as press releases, letters, media engagement and visits to bureaucrats to steer the government's macroeconomic, sector specific and related policies. Only a few associations employ more sophisticated and deliberation-oriented advocacy measures such as research papers, conferences, and policy briefs (**Figure S1.8**).

As per survey results, textile associations in Pakistan lack a robust research environment to fulfill the dynamic needs across its value chain. Only four out of 13 associations host a research department with dedicated staff to

⁶⁴ Source: DGTO, www.dgto.gov.pk, accessed on May 19, 2022.

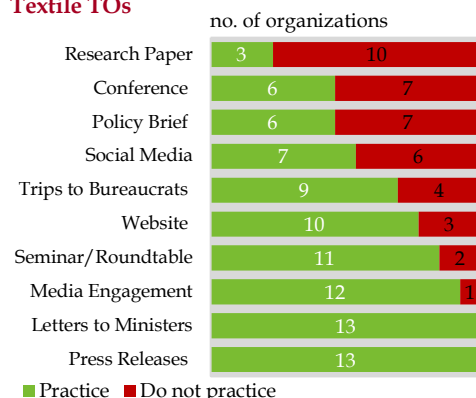
⁶⁵ Source: Websites of respective associations, accessed on January 25, 2022.

⁶⁶ Source: Pakistan Textile Council, www.ptc.org.pk, accessed on May 19, 2022.

⁶⁷ The office bearers' details of textile TOs were obtained from the relevant TOs website and cross-checked on Pakistan Textile Council website. Websites were accessed on January 25, 2022.

⁶⁸ There are 19 textile TOs registered with the DGTO (excluding those pertaining to canvas, tents and carpet manufacturing). Of these, 3 associations did not respond whereas 3 others representing small power looms, hand looms and yarn merchant business could not be contacted. As a result 13 out of 19 TOs were surveyed. Moreover, this section draws on discussions with office bearers from Textile Commissioner Office, Textile Division (Ministry of Commerce), the DGTO office and other private sectors associations, not listed with the DGTO, namely Pakistan Textile Council and Pakistan Apparel Forum.

Advocacy Tools Practiced by Textile TOs **Figure S1.8**



Note: Total 13 associations were surveyed

Source: Survey conducted as per Annexure II

contribute to any research output in terms of exploring market emerging trends, product diversification, innovation, or strategic policymaking. The research output of textile sector TOs is also limited in its scope – both in terms of the nature of the evidence gathered and in terms of collaboration with academia and other research institutions (Figure S1.9).

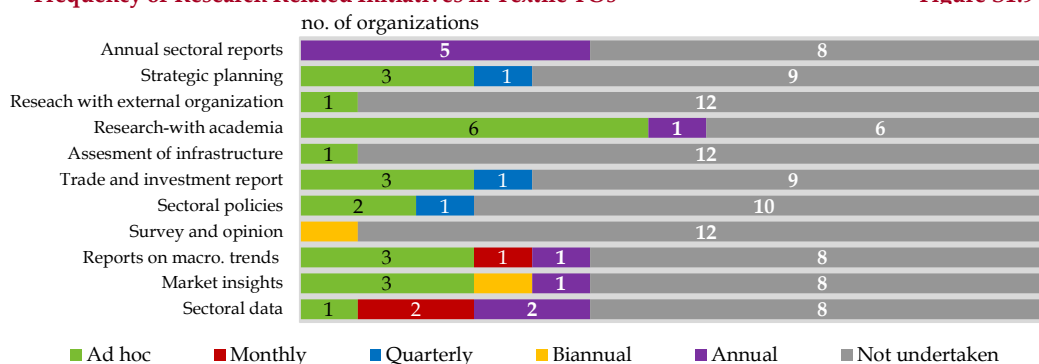
Institutional design

While leading textile sector TOs are engaged by the government at the time of policy design or implementation, there is an absence of a joint advisory board to steer sector specific policy. In 2002, the government had notified the composition of Federal Textile Board (FTB) with representation from public and private stakeholders.⁶⁹ The public sector was represented by relevant ministries and public sector organizations such as Textiles; Industries, Production & Special Initiatives; Commerce; Finance, the SBP etc. From the private sector, the government nominated individual persons and firms from textile clusters located in Faisalabad, Karachi, and Lahore. However, there was no representation from textile TOs.

The main objective of the FTB was continuous monitoring of the state of textile industry across value chain from cotton farming to high value added exports as well as the debottlenecking of growth prospects of

Frequency of Research Related Initiatives in Textile TOs

Figure S1.9



Note: Total 13 associations were surveyed

Source: Survey conducted as given in Annexure II

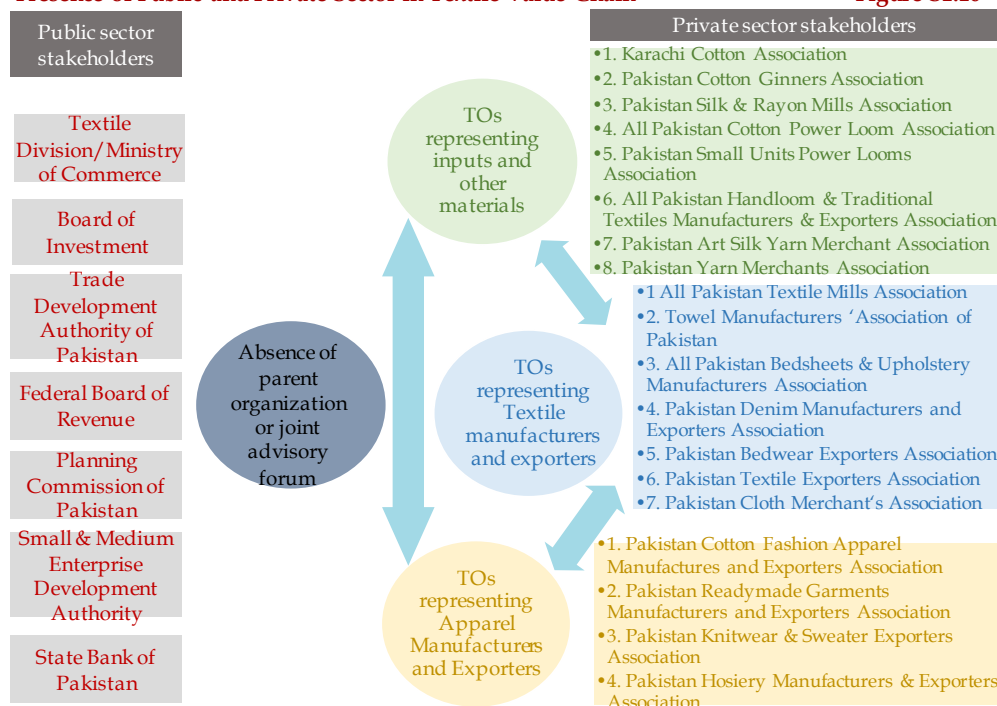
⁶⁹ Source: Year Book (2005-06), Ministry Of Textile Industry, Government of Pakistan.

the sector. Along with strategic level industry-centric functions,⁷⁰ the board was also responsible for bridging the gap between industry stakeholders and government bodies on operational basis by meeting at least once a month. In addition, the FTB was to restructure the role and activities of textile TOs so they could actively participate in fixing the information gap.

However, the textile board remained largely inoperative after merging of Ministry of Textile Industry with Ministry of Commerce. It was inactive at the time of formulation of Textile Policy 2009-14, and while the 2014-19 Textile Policy mentioned the restructuring and re-notification of the FTB, it has stayed inactive since then.⁷¹ Although, under the Textiles and Apparel Policy 2020-25, the

Presence of Public and Private Sector in Textile Value Chain

Figure S1.10



Note: The associations are categorized on the basis of the nature of member firms. The first category captures activity of manufacturing and supplying of inputs used in textile and apparel manufacturing; the second shows fabric manufacturing and their exports (some of these outputs are used as inputs in apparel industry); whereas the third category represents apparel manufacturing and exports.

Source: DGTO's Website and websites of different textile associations

⁷⁰ The board was mainly responsible for: 1) implementation and monitoring of textile policy; 2) performance monitoring; 3) analysis for technology up gradation, quality standards and training needs; 4) bridging of coordination gap between government and industry; 5) provision of business advisory services; 6) investment promotion; and 7) human resource development

⁷¹ Source: Textile Policy 2009-14 and Textile Policy 2014-19, Textile Division.

government aims to consult textile TOs, and strengthen their role for a variety of sectoral affairs, the policy does not envisage a joint advisory board ala the FTB.⁷²

In addition, there is an absence of an umbrella body to represent the combined interests of textile sector TOs, or any large sub-sector thereof. One exception to this is Pakistan Apparel Forum, which represents multiple manufacturing and exporter associations including PHMA, PAKSEA, PRGMEA, and PCFA. However, the forum is not registered with the DGTO, and operates on ad hoc basis. The absence of an umbrella

body means that a large number of TOs representing different yet overlapping mandates across textile value chain engage various government departments independently, which impairs optimal policy making process (**Figure S1.10**).

In contrast to the institutional design in Pakistan, India has an Apparel Export Promotion Council that acts as a public-private joint advisory board, whereas Sri Lanka has an umbrella organization called Joint Apparel Association Forum (JAAF), a permanent body to represent the interests of multiple value-added textile TO (**Box S1.2**).

Box S1.2 : Examples of Umbrella Bodies in Apparel Sector of India and Sri Lanka

In comparison to Pakistan, the institutional structures of India and Sri Lanka offer useful insights.

India: India has several sectoral export promotion councils, one of which is the Apparel Export Promotion Council (AEPC) formed in 1978. It is a public private industry implementation body that promotes garment exports. The AEPC was set up by private sector leaders from within India's textile and apparel industry to standardize and promote apparel exports, with representation of the government in its executive council. While AEPC's leadership comes from the private sector, it reports to the Indian Ministry of Textile.^a

Due to AEPC's efforts, India has strategized to focus on higher value and specialized products like manmade fibre apparels, medical textile and technical textiles. It has a dedicated R & D cell. It also publishes the semi-monthly periodical, which offers insights from experts and industry leaders. The body also organises the twice-yearly India International Garment Fair.^b Most apparel export firms register with the AEPC to seek its guidance on exploring new market, international fairs and technical guidance.

The organization works closely with various government departments, including Indian foreign office, for technology upgradation, attracting FDI in textile sector, becoming focal body for foreign buyers, and improving the country's infrastructure, such as power, port, transport, water and labor.^c The AEPC also operates 14 training institutes, which have played a critical role to train textile operators, but also developed managerial skills within textile industry and relevant government bureaucracy.^d

⁷² Under the new policy, the Ministry of Commerce plans to consult textile TOs for the sector's regulatory reforms, and targets strengthening their role as TOs for numerous matters including productivity, technology up-gradation, Industry 4.0, quality & standards, resource efficiency, product & market diversification, digitization, and building Pakistan's image abroad. (Source: Textiles and Apparel Policy 2020-25, Ministry of Commerce)

Sri Lanka: In 2002, five textile associations formed to work closely with the government on long term strategic plan, and to deal with the dismantling of quota allocation policy in the post Multi-Fiber Arrangement era. The associations - namely Sri Lanka Apparel Exporters Association; the Fabric and Apparel Accessory Manufacturers Association; the Sri Lanka Chamber of Garment Exporters; the Sri Lanka Sourcing Association; and the Free Trade Zone Manufacturers Association - came from varied background and therefore represented wide range of sectoral interests under one apex body.

Formed with the objective of strengthening forward linkages, solidifying alliances with buyers and suppliers, Joint Association Apparel Forum (JAAF) focusses on strategic issues such as bilateral and multilateral issues; international marketing, and productivity. Among these, various programmes were carried out by JAAF focusing on market development, and international image building - to provide competitive edge to these establishments.

In addition, JAAF has helped facilitate, negotiate, and draft trade policy framework related to Sri Lanka's apparel sector. For instance, because of JAAF's efforts, Sri Lanka initiated the bilateral Free Trade Agreement with the US in 2014. JAAF has taken initiatives to improve worker productivity, such as training programmes in marketing in collaboration with Chartered Institute of Marketing in UK; degree courses in fashion development with North Carolina State University College of Textiles; and design courses in textile technology jointly with London School of Fashion Design. It is also working on automation of Sri Lanka's textile industry, and has conducted successful programmes to promote Sri Lanka's name as an ethical clothing source.^e

References:

- ^a C. Hall (2018). "The AEPC: Learning More About India's Apparel Export Promotion Council", *The Sourcing Journal*; Apparel Export Promotion Council, Memorandum of Association: (www.aepcindia.com/system/files/20170915_Memorandum_Articles_of_Association_of_the_council.pdf) accessed on January 28, 2022); US Department of Labour: (www.dol.gov/sites/dolgov/files/ILAB/submissions/20091210c.pdf) accessed on January 28, 2022); Dr. G. Yoganandan (2015). "Textile Export Promotion in India-Salient Features", *Bonfring International Journal of Industrial Engineering and Management Science*, Vol. 5(1) pp. 1-4.
- ^b India Country Study (2019). Amsterdam: Fair Wear Foundation
- ^c D Das (2014). "India, the next China? Analysis of the unique firm resources claimed by Indian apparel export firms", *Journal of Fashion Marketing and Management*, Vol. 18(4) pp. 378-393.
- ^d M. Tewari (2008). "Varieties of Global Integration: Navigating Institutional Legacies and Global Networks in India's Garment Industry", *Competition & Change*, Vol. 12(1) pp. 49-67.
- ^e A. Khattak (2015). "Environmental upgrading of apparel firms in global value chains: Evidence from Sri Lanka", SAGE Publications, Vol. 19(4) pp. 317-335; D. Weerakoon and J. Thennakoon (2006). "Trade Liberalization in Sri Lanka: A Case Study of the Garments Industry", Institute of Policy Studies of Sri Lanka; S. Kelegama (2004). "Readymade garment industry in Sri Lanka: Facing the Global Challenge" Institute of Policy Studies of Sri Lanka; H. Jayatilake and A. Withanarachchi (2016). *Industry 4.0 in the Apparel-Manufacturing Sector: Opportunities for Sri Lanka*, 1st Interdisciplinary Conference of Management Researchers, at Sabaragamuwa University of Sri Lanka. Sabaragamuwa: Sabaragamuwa University of Sri Lanka; P. Athukorala (2018). "Repositioning in the global apparel value chain in the post-MFA era: Strategic issues and evidence from Sri Lanka", *Development Policy Review*, Vol. 36 pp. 247-269.

Market Complementing Services & Organizational Constraints

Most of the textile TOs offer basic services, such as visa facilitation, and issuing COO, to

their members (**Figure S1.11**). Some also offer opportunities for networking or exploring new markets, such as B2B matching making services and trade exhibitions (**Figure S1.12**). However, market

Provision of Services to Members in Textile TOs

Figure S1.11



Note: Total 13 associations were surveyed

Source: Survey conducted as per Annexure II

complementing services that can help TOs become financially sustainable are largely absent.

This is also evident from the fact that most textile sector TOs lack separate departments staffed with relevant professionals to perform various functions (such as research) and to offer various services (such as training, legal aid & arbitration/mediation,

Presence of Seperate Departments in Textile TOs

Figure S1.13

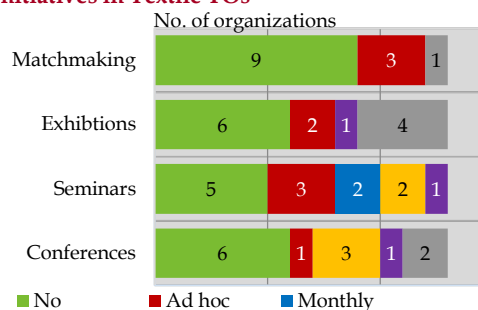


Note: Total 13 associations were surveyed

Source: Survey conducted as per Annexure II

Frequency of Networking Initiatives in Textile TOs

Figure S1.12



Note: Total 13 associations were surveyed

Source: Survey conducted as per Annexure II

quality testing) against fees. Instead, these functions and services are carried out by different committees on voluntarily basis, which doesn't help TOs become financially sustainable organizations to be able to perform the real function of effective public-private collaboration (Figure S1.13).

Moreover, resource pooling is also very limited in case of textile TOs in Pakistan. Members of only few associations pool in their funds, in addition to membership fees, to provide for the setting up, and/or running of high value added services such as labor training, testing labs, technology adoptions etc. (Figure S1.14). In the absence of significant pooling mechanism, TOs primarily run their training programs in collaboration with bilateral donor funded agencies, whenever the latter initiate their respective programs.⁷³

⁷³ For instance various textile TOs have conducted labour skill training under various donor funded programmes. SMEDA, Industry Support Programme, available at www.smeda.org/index.php?option=com_content&view=article&id=16&Itemid=118, accessed on May 19, 2022; PRGMEA, www.prgmea.org/documents/10.pdf, accessed on May 19, 2022

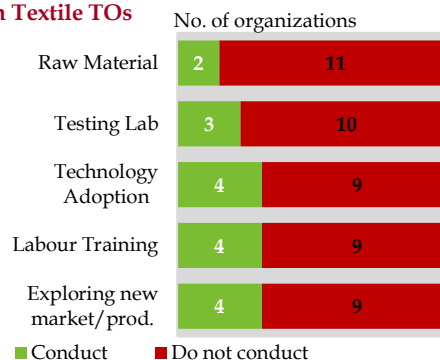
Lately, however, some of the leading associations have started to take some research initiatives to support the industry's value chain. For example, APTMA has laid the foundation of APTMA Cotton Foundation, which, in liaison with public and private research institutes, will introduce corporate farming model for cotton production on a large scale.⁷⁴ The foundation will establish model farms, where the farmers will use the cutting-edge technology, such as drones and satellite imagery to monitor the crop health. In addition, the project also aims to establish knowledge centers, bio-tech labs and research institutions with the collaboration of international counterparts.

S1.5 Final Remarks

TOs offer important market supporting and market complementing services that directly and indirectly benefit the public and private sectors. Under Pakistan Vision 2025, the government also identifies TOs as catalyst of change with an important role in guiding government policy and economic programs.⁷⁵ However, in Pakistan, as preceding sections show, the purpose of existence of TOs is not being adequately fulfilled.

In part, this is because the framework for PPD in the country is weak. Here, as mentioned earlier, the absence of joint advisory forums in general is worth noting, as is the fact that TOs are not given due

Resource Pooling for Services in Textile TOs **Figure S1.14**



Note: Total 13 associations were surveyed

Source: Survey conducted as per Annexure II

representation at high-level government advisory councils such as the EAC and CPEC Business Council. This prevents the development of a vibrant PPD process as an institution. Another reason why TOs in Pakistan are unable to play an effective role is the weak state of their organizational capabilities, which is a prerequisite for TOs to be able to engage in effective PPD and to offer various sorts of market complementing services to their members. As a result of these gaps, TOs have had a weak role in demanding reforms.⁷⁶

The following paragraphs offer seven recommendations intended as broad policy suggestions and bring to fore some points for deliberations between public and private sector stakeholders on how to build strong, effective, and sustainable TOs that can contribute to economic growth and development of Pakistan.

⁷⁴ Source: APTMA, www.aptma.org.pk/better-days-for-cotton/, accessed on May 19 2022

⁷⁵ Planning Commission (2014). *Pakistan Vision 2025*. Islamabad: Planning Commission, Ministry of Planning, Development and Reforms.

⁷⁶ Source: World Bank (2017). "Boosting Pakistan's Export Competitiveness: Private Sector Perspectives", Proceedings from Round Table Meetings held in Islamabad, Peshawar, Karachi and Lahore September - November 2017. Washington D.C.: World Bank

First, from the perspective of public sector, the government needs to set up institutional mechanisms for public private dialogue where bureaucracy can effectively engage the private sector on matters relating to both short- and long-term economic/ business policymaking and its implementation. These may take the shape of joint advisory councils across major sectors and regions where due representation is given to sectoral and regional TOs. These may also require a phased approach where in the first phase the public sector may set up such platforms, ensure their effective organization through collaborative leadership, and facilitate their funding before gradually letting the private sector take leadership and be responsible for financial sustainability of such platforms. Since there are no standardized solutions to these, a trial-and-error way of doing reforms would be the way forward.⁷⁷

Second, an equally important step is to move towards evidence-based policymaking helped in part by demanding the evidence behind policy advocacy by TOs. To this end, the legal framework of TOs may be reassessed with the objective of nudging TOs to improve their research capacities needed for effective PPD.

Third, legal framework also needs to be looked at from the aspect of improvement in organization affairs of TOs. These may include increasing the term of office for office bearers to give TOs a long-term sense of

direction, and the strengthening of TOs' secretariat with separate departments staffed by professionals. In addition, compulsory membership of TOs may be considered to strengthen the membership base, and accordingly, the finances of TOs. A framework for tiered membership, allowing TOs to offer different scope of services to different tiers of members against varied fees, may also be deliberated.

Fourth, as discussed in earlier sections, the government's relationships with the private sector needs to be legitimized through mechanisms of accountability and transparency. To this end, PPD and documents thereof need to be made public, with sufficient time and space allowed for their formal analysis and evaluation by both economic/ industrial bureaucracy and other stakeholders such as TOs from competing sectors, academia, media, etc. The objective is to identify opportunities for coordination and public deliberation while reducing rent-seeking.⁷⁸

Fifth, while compulsory membership of TOs may also help towards improving representation, the subject of advocacy forums by large businesses also requires attention. Advocacy forums by large businesses, such as the PBC, the PTC and PAC formed by leading local conglomerates, business groups and multi-national corporations, represent large scale industrial and financial sectors needed for driving

⁷⁷ B. Herzberg and A. Wright (2005). "Competitiveness Partnerships: Building and Maintaining Public-Private Dialogue to Improve the Investment Climate", The World Bank Group, Policy Research Working Paper Series, no. 3683. *The PPD Handbook: "A Toolkit for Business Environment Reformers"*, available at www.publicprivatedialogue.org/papers accessed on May 19, 2022.

⁷⁸ D. Rodrik (2004). "Industrial Policy for 21st Century", Special Publication for UNIDO. Cambridge, MA: Harvard University

economic growth and development. Although large businesses are also a part of various conventional TOs – i.e., chambers and associations – they are outnumbered by small and medium enterprises, because of which the interests of large scale industrial and financial sector is elbowed out. At the same time the interests of SMEs that mostly populate TOs are also important, whereas when large businesses are inactive in TOs or are less active, it leads to fragmented private sector representation and thereby complicates government-business relations.⁷⁹ Therefore, striking the balance in representation of the interests of both and ensuring effective functioning of TOs is what policymakers need to strive for.

Sixth, the private sector also needs to make TOs effective. The level of competition in Pakistan has been low, with little incentive for research, innovation, and efficiency. As a result, private sector has not faced pressure to improve productivity or search for new markets and products.⁸⁰ The corollary of this

has been low demand for archetypical market complementing services from TOs, and a failure to achieve economies of scale by pooling in resources using TOs as an institutional platform. However, Pakistan is taking gradual steps towards liberalization, which, as discussed in section S1.2, may encourage business community to reform the TOs.⁸¹ To that end, TOs will need to explore various business models for financial sustainability since strong business associations should be self-funded and offer market complementing services alongside the PPD function. As previously mentioned, funding for these may come from higher membership fees, tiered memberships, or pooling resources to offer demand-driven services like arbitration centres, quality testing labs, and labour training.

Lastly, academia and think-tanks may be encouraged to conduct periodic impact assessments and case studies on the nature and extent of the contribution of various TOs to Pakistan's economy.

⁷⁹ Schneider, B. R. (2015). "Designing industrial policy in Latin America: Business-state relations and the new developmentalism", New York, NY: Palgrave Macmillan US

⁸⁰ State Bank of Pakistan (2020). "Special Section: Technical and Vocational Education and Training (TVET) in Pakistan: Issues and Challenges for Productivity Enhancement, www.sbp.org.pk/reports/quarterly/fy20/Third/Special-Section.pdf

⁸¹ For instance, the country has moved towards market-based mechanism of exchange rate. Furthermore, the import tariffs are being rationalized under National Tariff Policy (2019) on capital goods, intermediate products and raw materials to encourage competition in the domestic market. Source: Ministry of Finance (2020-21), Economic Survey of Pakistan

Annexure I – List of Trade Organizations Surveyed⁸²

Table A: Leading chamber & association surveyed for Section 3

S. No	Associations and Chambers	Acronym	S. No	Associations and Chambers	Acronym
1	Federation of Pakistan Chambers of Commerce and Industry	FPCCI	10	Pakistan Chemical Manufacturers Association	PCMA
2	Karachi Chamber of Commerce and Industry	KCCI	11	Rice Exporter Association Pakistan	REAP
3	Quetta Chamber of Commerce and Industry	QCCI	12	Surgical Instrument Manufacturers Association Pakistan	SIMAP
4	Sarhad Chamber of Commerce and Industry	SCCI	13	Pakistan Banks' Association	PBA
5	Lahore Chamber of Commerce and Industry	LCCI	14	Pakistan Software House Association	PASHA
6	Faisalabad Chamber of Commerce and Industry	FCCI	15	Pakistan Sugar Mills Association	PSMA
7	Rawalpindi Chamber of Commerce and Industry	RCCI	16	Pakistan Vanaspati Manufacturers Association	PVMA
8	Sialkot Chamber of Commerce and Industry	SCCI	17	Pakistan Automotive Manufacturers Association	PAMA
9	Islamabad Chamber of Commerce and Industry	ICCI	18	All Pakistan Cement Manufacturers Association	APCMA

Table B: Leading textile associations surveyed for Section 4

1	All Pakistan Textile Processing Mills Association	APTMA	8	Pakistan Denim Manufacturers and Exporters Association	PDMEA
2	All Pakistan Bed Sheets & Upholstery Manufacturer's Association	APBUMA	9	Pakistan Hosiery Manufacturers & Exporters Association	PHMA
3	All Pakistan Cotton Power Looms Association	APCPLA	10	Pakistan Readymade Garments Manufacturers And Exporters Association	PRGMEA
4	Pakistan Bedwear Exporters Association	PBEDWEA R	11	Pakistan Silk & Rayon Mills Association	PSRMA
5	Pakistan Knitwear & Sweaters Exporters Association	PAKSEA	12	Pakistan Textile Exporters Association	PTEA
6	Pakistan Cotton Ginners Association	PCGA	13	Towel Manufacturers Association of TMA Pakistan	
7	Pakistan Cloth Merchants Association.	PCMA			

⁸² The TOs were surveyed in January, 2022. In addition to the organizations listed, a few other TOs were also approached but they did not respond.

Annexure II – Questionnaire⁸³

Basic Information	
Name of Organization:	Year Founded:
Name & Designation of Respondent:	Date:
Membership, Structure, Organization, Finances	
1)	Do you have different tiered membership pricing and service levels? (Tick one)
	a) Yes, we have different pricing plans and categories for different members ☐
	b) No, we charge all our members the same, and tiers or categories do not exist ☐
2)	Are there separate departments for each of the following activities: each dept. with its own full-time paid staff of relevant professional qualification? (Tick those that apply)
a)	Research ☐
b)	Intellectual Property Rights ☐
c)	Legal Aid ☐
d)	Training and development of members ☐
e)	Organize & Manage B2B networking and corporate affairs ☐
f)	Managing Quality Certification, Labelling, Testing Labs etc. ☐
3)	Does your organization formulate a long-term strategic business plan (3-5 years) with specific targets and goals as milestones during the plan period? (Tick one)
a)	Yes, shared with DGTO, only ☐
b)	Yes, shared with public ☐
c)	No ☐
4)	Does your organization publish annual reports with details about organization's performance, activities, initiatives and financial expenditure? (Tick one)
a)	Yes, and made public ☐
b)	Yes, but not made public ☐
c)	No ☐
5)	How many subcommittees/councils exist in your organization that focus on special issues relating to the area/industry represented by your organization? (Tick one)
a)	None ☐
b)	1-3 ☐
c)	3-5 ☐
d)	5-7 ☐
e)	More than 7 ☐
Advocacy and External Relations	

⁸³ The questionnaire is based from preliminary discussions with TOs representatives and a review of following papers: R. Strohmeyer, M. Pilgrim, F. Luetticken, R. Meier, H.G. Waesch, and I. Arias (2005). *Building the Capacity of Business Membership Organizations: Guiding Principles for Project Managers*. A Handbook by Small and Medium Enterprise Department, World Bank. Washington D.C.: World Bank; OECD (2018). "How can Private Sector Organisations Contribute to Economic Resilience in Fragile and Conflict-Affected Contexts in The Middle East and North Africa?". Background note for the MENA-OECD Economic Resilience Task Force. Paris: OECD; R. Doner and B.R. Schneider (2000). "Business Associations and Economic Development: Why Some Associations Contribute More Than Others." *Business and Politics*, Vol. 2, No. 3; L. E. McCormick (2000). *An Analysis of the Economic Development Role of Business Associations and Other Intermediary Organizations Serving Appalachian Industries*. Volume 1 of Report submitted to the Appalachian Regional Commission. Washington D.C.: Appalachian Regional Commission.

6) Do your organization have joint advisory boards with various government ministries and departments?
(Tick one)

- a) Yes ☐ b) No ☐

7) Does your sector have joint advisory board for all associations representing all businesses upstream and downstream? (Note: This question applies to association and not on chambers) (Tick one)

- a) Yes ☐ b) No ☐

8) What are the tools used by your organization to steer government's macroeconomic, sectoral policy and other related policies? Kindly also mention the average number of times the tool is used in a year. (Tick only those that apply)

Tools		
a)	Press releases	☐
b)	Letters to ministers/secretaries	☐
c)	Website presence	☐
d)	Social media presence (Linked, Twitter, etc.)	☐
e)	Direct engagement with media (newspaper columns, interviews to TV channels, press conferences etc.)	☐
f)	Policy briefs (for e.g. short one or two page summary of key issues/solutions)	☐
g)	Research papers (detailed studies)	☐
h)	Conferences	☐
i)	Seminars & Roundtable discussions	☐
j)	Advocacy trips: members' meetings with ministers	☐
k)	Advocacy trips: members' meetings with bureaucrats	☐

How many times tools f-k have been used in the last 3 years

9) Has the government delegated (or collaborated for the delivery) any of public function to you?

- a) Yes, on temporary basis ☐ a) Yes, on permanent basis ☐ b) No ☐

10) If yes, which of the following (Tick those that apply)

- a) Distribution of exports quota ☐
b) Collection of Cess, and/or any other type government taxes or charges ☐
c) Assist in ensuring that quality standards are followed ☐
d) Assist in monitoring labor laws ☐ e) Others

Services

11) Which of the following services are provided by your organization? (Tick those that apply)

- a) Visa Facilitation ☐
b) Certificate of Origin ☐
c) Help desk (for e.g. providing information & assistance to current/potential new members) ☐
d) Exchange visits to international counterparts ☐

12) Does your organization offer resource pooling for its members for any of the following? (Tick only those that apply)

- a) Testing labs ☐
b) Research to explore new export markets; new products. ☐
c) Combined raw material purchase (for e.g. to lower per unit prices) ☐
d) Labour training ☐
e) Technology adoption ☐

13) Is there an arbitration/mediation centre within your organization?

	Yes	No	If yes, then	
			Date of formation	Total cases/disputes resolved to date
Arbitration centre	☐	☐		

Mediation centre ☐ ☐

14) Which of the following B2B networking events do you organize? Please also mention the frequency of the event.

Event	No	If yes, what is the frequency (tick all that apply)					
a) Conferences	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
b) Seminars	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
c) Trade Fairs & Exhibitions	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
d) Matchmaking service (to connect companies with common business interests, complementary services, expertise, technologies etc.)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	

15) Which of the following reports and research initiatives are published or conducted by your organization?

Research Initiatives	No	If yes, what is the frequency (tick all that apply)					
a) Sectoral Data (for instance sales, employment data for the relevant industry)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
b) Market Insights (for instance market sizing, analysis of demand/supply drivers)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
c) Reports on Macroeconomic Trends and Challenges	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
d) Survey and Opinion Polls (for instance on employment situation, interest rate, etc.)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
e) Trade and Investment Reports (research on new potential markets, information on regulatory laws and certification requirement of new markets)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
f) Assessment of Hard (road, rail, etc.) and Soft (education, health system etc.) Infrastructure	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
g) Research in collaboration with academia (for e.g. for product R&D or market research)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
h) Research in collaboration with external research organizations (e.g. KPMG, AC Nielson, etc.)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
i) Conducting sectoral strategic planning for relevant industry (planning for future changes in markets, technologies, labor needs, and consumer/product trends.)	☐	Ad hoc ☐	Monthly ☐	Quarterly ☐	Biannually ☐	Annually ☐	
j) Annual Sectoral Reports	☐			Yes ☐			
k) Daily Briefs	☐			Yes ☐			

Annexure A: Data Explanatory Notes

- 1) **GDP:** In case of an ongoing year, for which actual GDP data is yet not available, SBP uses the GDP target given in the Annual Plan by the Planning Commission in order to calculate the ratios of different variables with GDP, e.g., fiscal deficit, public debt, current account balance, trade balance, etc. SBP does not use its own projections of GDP to calculate these ratios in order to ensure consistency, as these projections may vary across different quarters of the year, with changing economic conditions. Moreover, different analysts may have their own projections; if everyone uses a unique projected GDP as the denominator, the debate on economic issues would become very confusing. Hence, the use of a common number helps in meaningful debate on economic issues, and the number given by the Planning Commission better serves this purpose.
- 2) **Inflation:** There are three numbers that are usually used for measuring inflation: (i) period average inflation; (ii) YoY or *yearly* inflation; and (iii) MoM or *monthly* inflation. Period average inflation refers to the percent change of the *average* CPI (national, urban, or rural) from July to a given month of the year over the corresponding period last year. YoY inflation is percent change in the CPI of a given month over the same month last year; and monthly inflation is percent change of CPI of a given month over the previous month. The formulae for these definitions of inflation are given below:

$$\text{Period average inflation } (\square_{\text{Ht}}) = \left(\frac{\sum_{i=0}^{t-1} I_{t-i}}{\sum_{i=0}^{t-1} I_{t-12-i}} - 1 \right) \times 100$$

$$\text{YoY inflation } (\square_{\text{YoYt}}) = \left(\frac{I_t}{I_{t-12}} - 1 \right) \times 100$$

$$\text{Monthly inflation } (\square_{\text{MoMt}}) = \left(\frac{I_t}{I_{t-1}} - 1 \right) \times 100$$

Where I_t is consumer price index in t^{th} month of a year. The CPI can be national, urban or rural.

For detailed information on the methodology, please see:

<http://www.pbs.gov.pk/content/methodology-2>

- 3) **Change in debt stock vs. financing of fiscal deficit:** The change in the stock of gross public debt does not correspond with the fiscal financing data provided by the Ministry of Finance. This is because of multiple factors, including: (i) The stock of debt takes into account the gross value of government borrowing, whereas financing is calculated by adjusting the government borrowing with its deposits held with the banking system; (ii)

changes in the stock of debt also occur due to movements in exchange rates, both PKR and other currencies against US Dollar, which affect the rupee value of external debt.

4) **Government borrowing:** Government borrowing from the banking system has different forms and every form has its own features and implications, as discussed here:

(a) Government borrowing for budgetary support:

Borrowing from State Bank¹: The federal government may borrow directly from SBP either through the “Ways and Means Advance” channel or through the purchase (by SBP) of Market Related Treasury Bills (MRTBs). Ways and Means Advance allows government to borrow up to Rs 100 million at a time in a year at an interest rate of 4 percent per annum; higher amounts are realized through the purchase of 6-month MTBs by SBP at the weighted average yield determined in the most recent fortnightly auction of treasury bills.

Provincial governments and the Government of Azad Jammu & Kashmir (AJK) may also borrow directly from SBP by raising their debtor balances (overdrafts) within limits defined for them. The interest rate charged on the borrowings is the three month average yield of 6-month MTBs. If the overdraft limits are breached, the provinces are penalized by charging an incremental rate of 4 percent per annum. However, the Federal Government has taken over from the State Bank of Pakistan (SBP) the business of direct credit to provincial governments on 29th June 2020. In this regard, the federal government has executed tripartite agreements with four provincial governments and SBP (as executer) for extension of Ways and Means loans on account of Federal Government Central Account No.I (non-food) on 29th June 2020.

Borrowing from scheduled banks: This is mainly through (i) fortnightly auction of 3, 6 and 12-month Market Treasury Bills (MTBs); (ii) monthly auction of 3, 5, 10, 15, 20 and 30 year fixed rate Pakistan Investment Bonds (PIBs); (iii) fortnightly auctions of 2, 3, 5, 10 year floating rate PIBs; (iv) Sukuk and (v) Bai Muajjal of Sukuk (on deferred payment basis). However, provincial governments are not allowed to borrow from scheduled banks.

(b) Commodity finance:

Both federal and provincial governments borrow from scheduled banks to finance their purchases of commodities e.g., wheat, sugar, etc. The proceeds from the sale of these commodities are subsequently used to retire commodity borrowing.

¹ This was applicable before the amendments in the SBP Act in January 2022. According to Section 9C (1) of the SBP Act (as amended up to 28 January, 2022), the SBP “shall not extend any direct credits to or guarantee any obligations of the Government, or any government owned entity or any other public entity.”

- 5) **Differences in different data sources:** SBP data for a number of variables, such as government borrowing, foreign trade, etc – often do not match with the information provided by MoF and PBS. This is because of differences in data definitions, coverage, etc. Some of the typical cases have been given below.
- (a) **Financing of budget deficit (numbers reported by MoF vs. SBP):** There is often a discrepancy in the financing numbers provided by MoF in its quarterly tables of fiscal operations and those reported by SBP in its monetary survey. This is because MoF reports government bank borrowing on a cash basis, while SBP's monetary survey is compiled on an accrual basis, i.e., by taking into account accrued interest payments on T-bills.
 - (b) **Foreign trade (SBP vs PBS):** The trade figures reported by SBP in the *balance of payments* do not match with the information provided by the Pakistan Bureau of Statistics. This is because the trade statistics compiled by SBP are based on banking data, which depends on the actual receipt and payment of foreign exchange, whereas the PBS records data on the physical movement of goods (customs record).

List of Acronyms

A

ADB	Asian Development Bank
ADR	Alternative Dispute Resolution Mechanism
AE	Advanced Economy
AEPC	Apparel Export Promotion Council
AGOA	African Growth and Opportunity Act
AIIB	Asian Infrastructure Investment Bank
AJK	Azad Jammu and Kashmir
AML	Anti-Money Laundering
APCMA	All Pakistan Cement Manufacturers Association
APTMA	All Pakistan Textile Processing Mills Association

B

BCS	Business Confidence Survey
BDI	Baltic Dry Index
BISP	Benazir Income Support Program
bln	billion
bps	Basis points
BSC	Behood Savings Certificate

C

CAD	Current Account Deficit
CAN	Calcium Ammonium Nitrate
CBU	Completely Built Unit
CCS	Consumer Confidence Survey
CDMP	Circular Debt Management Plan
CDNS	Central Directorate of National Savings
CFT	Combating the Financing of Terrorism
CIPE	Center for International Private Enterprise
CIT	Corporate Income Tax
CKD	Completely Knocked Down
CMI	Census of Manufacturing Industries

CNIC	Computerized National Identity Card
COO	Certificate of Origin
CPEC	China Pakistan Economic Corridor
CPFTA	China-Pakistan Free Trade Agreement
CPFTA II	China Pakistan Free Trade Agreement Phase II
CPI	Consumer Price Index
CRR	Cash Reserve Requirement

D

DAP	Diammonium Phosphate
DGTO	Director General Trade Organization
DI	Diffusion Index
DNFBP	Designated Non-Financial Business and Professions
DSSI	Debt Service Suspension Initiative

E

EAC	Economic Advisory Council
EAD	Economic Affairs Division
EDS	External Debt Servicing
EFF	Extended Fund Facility
EFS	Export Finance Scheme
EM	Emerging Market
ESP	Economic Stimulus Package
EU	European Union

F

FAO	Food and Agriculture Organization
FATF	Financial Action Task Force
FBR	Federal Board of Revenue
FCA	Federal Committee on Agriculture
FCCI	Faisalabad Chamber of Commerce and Industry
FCTC	Framework Convention on Tobacco Control

FDA	Food and Drug Administration
FDI	Foreign Direct Investment
FED	Federal Excise Duty
FEE	Foreign Exchange Earnings
FI	Financial Institution
FICCI	Federation of Indian Chambers of Commerce and Industry
FMCG	Fast Moving Consumer Goods
FO	Furnace Oil
FPCCI	Federation of Pakistan Chambers of Commerce and Industry
FPI	Foreign Portfolio Investment
FRR	Fixed Rental Rate
FTB	Federal Textile Board
FX	Foreign exchange
FY	Fiscal Year

G

GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GIDC	Gas Infrastructure Development Cess
GOP	Government of Pakistan
GST	General Sales Tax
GSTS	General Sales Tax on Services

H

H1	First Half
HS	Harmonized System
HSD	High Speed Diesel

I

IBRD	International Bank for Reconstruction and Development
IBA	Institute of Business Administration
ICC	International Chamber of Commerce
ICT	Islamabad Capital Territory

ICT	Information and Communication Technology
IDA	International Development Association
IDB	Islamic Development Bank
IFC	International Finance Corporation
IH&SMEFD	Infrastructure, Housing & SME Finance Department
ILO	International Labour Organization
IMF	International Monetary Fund
IPPs	Independent Power Producers
IPR	Intellectual Property Rights
IREN	Inland Revenue Enforcement Network
IT	Information Technology
ITFC	International Islamic Trade Finance Corporation
ITP	Illicit Trade in Tobacco Products

J

JAAF	Joint Association Apparel Forum
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K

KCCI	Karachi Chamber of Commerce and Industry
KP	Khyber Pakhtunkhwa
KTP	Karachi Transformation Plan

L

LCCI	Lahore Chamber of Commerce and Industry
LNG	Liquefied Natural Gas
LPG	Liquefied Petroleum Gas
LSM	Large Scale Manufacturing
LTFF	Long Term Financing Facility

M

12MMA	12 Month Moving Average
MA	Moving Average
MAF	Million Acre Feet

MMBtu	Metric Million British Thermal Unit
MMT	Million Metric Ton
MNFSR	Ministry of National Food Security and Research
MPC	Monetary Policy Committee
MSCI	Morgan Stanley Capital International
MT	Metric Ton
MTB	Market Treasury Bill

N

NCCPL	National Clearing Company of Pakistan
NCPI	National Consumer Price Index
NDA	Net Domestic Assets
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Assets
NFDC	National Fertilizer Development Center
NFNE	Non-food-non-energy
NIA	National Income Accounts
NICOP	Smart National Identity Card for Overseas Pakistanis
NP	Nitro Phosphate
NPK	nitrogen, phosphorus and potassium
NSER	National Socio Economic Registry
NSS	National Savings Scheme
NTR	Non Tax Revenue

O

OCAC	Oil Companies Advisory Council
OECD	Organization for Economic Co-operation and Development
OGDCL	Oil and Gas Development Company Limited
OICCI	Overseas Investors Chamber of Commerce and Industry
OMO	Open Market Operation
OPEC	Organization of the Petroleum Exporting Countries

P

PAC	Pakistan Agriculture Coalition
PACRA	Pakistan Credit Rating Agency
PAKSEA	Pakistan Knitwear & Sweaters Exporters Association
PAMA	Pakistan Automotive Manufacturers Association
PASHA	Pakistan Software House Association
PBC	Pakistan Business Council
PBS	Pakistan Bureau of Statistics
PCFA	Pakistan Cotton Fashion Apparel Manufacturers and Exporters Association
PDL	Petroleum Development Levy
PE	Price Effect
PFL	Pakistan Investment Bond Floating Rate
PHMA	Pakistan Hosiery Manufacturers & Exporters Association
PHPL	Power Holding Private Limited
PIA	Pakistan International Airlines
PIB	Pakistan Investment Bond
PKR/Rs.	Pakistan Rupee
PMKJ-YES	Prime Minister's Kamyab Jawan Youth Entrepreneurship Scheme
POL	Petroleum, Oil and Lubricants
POS	Point of Sales
PPD	Public-Private Dialogue
PPL	Pakistan Petroleum Limited
PRGMEA	Pakistan Readymade Garments Manufacturers And Exporters Association
PSDP	Public Sector Development Program
PSMA	Pakistan Sugar Mills Association
PSW	Pakistan Single Window
PSX	Pakistan Stock Exchange
PTA	Pakistan Telecommunication Authority
PTC	Pakistan Textile Council

Q

Q1	First Quarter
Q2	Second Quarter
Q3	Third Quarter
Q4	Fourth Quarter
QE	Quantum Effect
QIM	Quantum Index of Manufacturing
R	
RCCI	Rawalpindi Chamber of Commerce and Industry
REER	Real Effective Exchange Rate
rhs	Right Hand Side
ROA	Return on Assets
ROE	Return on Equity
RPI	Retail Price Index
S	
SBP	State Bank of Pakistan
SCCI	Sialkot Chamber of Commerce and Industry
SDR	Special Drawing Rights
SDRP	Sohni Dharti Remittance Program
SECP	Securities & Exchange Commission of Pakistan
SIMAP	Surgical Instrument Manufacturers Association Pakistan
SKD	Semi Knocked-Down
SME	Small and Medium Enterprise
SMEDA	Small and Medium Enterprises Development Authority
SSP	Single Superphosphate
ST	Sales Tax
SUPARCO	Space and Upper Atmosphere Research Commission
SUV	Sports Utility Vehicle
T	
TDAP	Trade Development Authority of Pakistan
TERF	Temporary Economic Refinance Facility

TO	Trade Organization
TOA	Trade Organization Act
TOO	Trade Organization Ordinance
TTS	Track and Trace System
U	
UAE	United Arab Emirates
UIM	Unique Identification Mark
UK	United Kingdom
UNIDO	United Nations Industrial Development Organization
US/USA	United States of America
USD/US\$	US Dollar
USDA	United States Department of Agriculture
V	
VAT	Value Added Tax
VRR	Variable Rental Rate
W	
WALR	Weighted Average Lending Rate
WAONR	Weighted Average Overnight Rate
WC	Working Capital
WCI	World Container Index
WHO	World Health Organization
WHT	Withholding tax
WPI	Wholesale Price Index
Y	
YoY	Year on Year