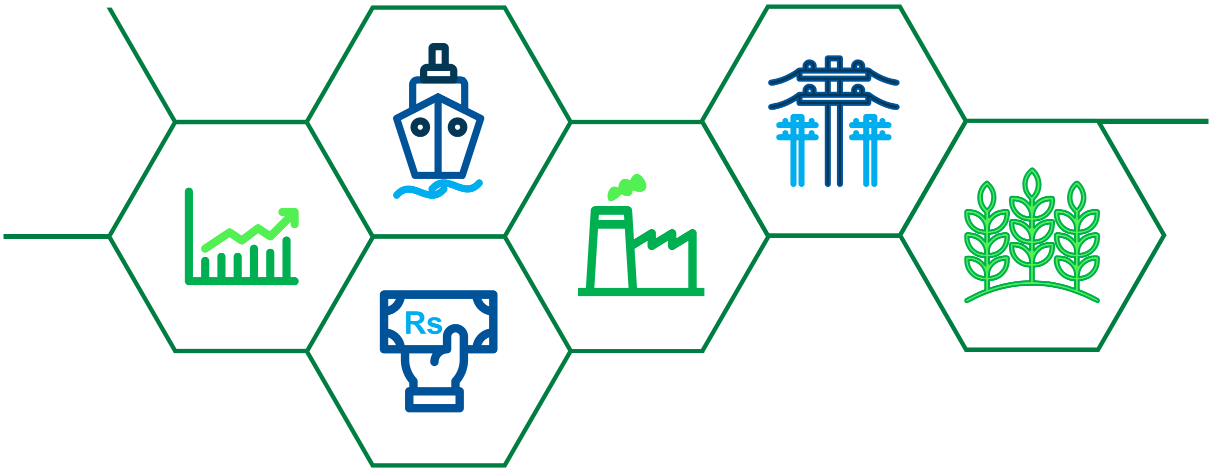


Monthly

ECONOMIC UPDATE & OUTLOOK

September 2022

Government of Pakistan
Finance Division
Economic Adviser's Wing

Contents

Executive Summary

- The global economy is suffering from slow growth, higher inflation and monetary tightening. According to the J.P.Morgan Global Composite Output Index, global economic activity contracted for the first time in August 2022 since June 2020 amid decline in international trade volumes. Global commodity prices showed mixed picture in August. Energy prices increased by 1.3 percent, while agricultural prices eased by 1.0 percent. Food prices declined by 1.6 percent and fertilizers eased by 1.5 percent.
- **Real Sector:** The recent flash flood has adversely affected cotton and other important crops, making the performance of agriculture sector more vulnerable. LSM posted a negative growth of 1.4 percent in July FY2023.
- **Fiscal, Monetary & External:** The fiscal deficit for July 2022 was recorded at 0.3 percent of GDP. The primary balance posted a surplus of Rs 142 billion. During 1st July - 02nd September, FY2023 money supply (M2) shows negative growth of 1.8 percent as compared to negative growth of 1.4 percent last year. During Jul-Aug FY2023, the current account deficit was recorded at $ 1.9 billion.

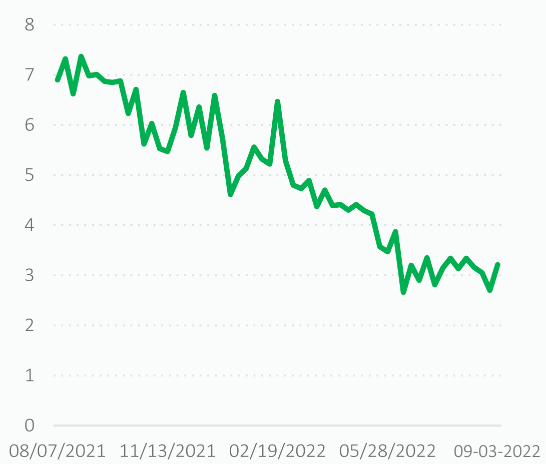
International Performance and Outlook

The global economy is now in its steepest slowdown following a post-recession recovery since 1970. Central banks around the world have been raising interest rates in 2022, a momentum that is likely to continue well into next year. Yet the currently expected trajectory of interest-rate increases, and other policy actions may not be sufficient to bring global inflation down to levels seen before the pandemic. The barometer for world food commodity prices declined for the fifth consecutive month in August. Global commodity exhibited volatility and prices have been on a roller-coaster ride for the past few months. Oil prices stabilized since June due to worsening global economic prospects. Deep and wide cuts to growth forecasts, the European gas crisis, high inflation, and a sharp acceleration in the pace of global monetary policy tightening are taking a heavy toll on economic prospects.

Global consumer confidence has already suffered a much sharper decline than in the run-up to previous global recessions. The world's three largest economies the US, China, and Euro Area-have all been experiencing severe slowdowns.

U.S. private-sector business activity contracted for a second straight month in August to its weakest in 27 months. This is due to material shortages, delivery delays, hikes in interest rates, and strong inflationary pressures. US economic situation is also reflected through growth in WEI which has a similar trend as observed in July (Fig-1).

Fig-1: Growth in WEI

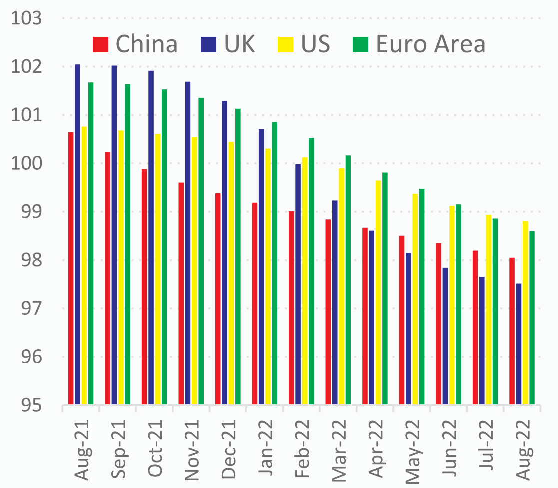


Source: Federal Reserve Bank of New-York

The month of August observed global economic activity contraction for the first time since June 2020, as new order inflows declined, international trade volumes fell, and signs of excess capacity grew. The J.P.Morgan Global Composite Output Index fell to 49.3 in August, from 50.8 in July. Output contracted in both the manufacturing and service sectors.

National PMI data indicated that business activity decreased in five out of the 14 nations covered, all advanced economies. The performance of the US was especially weak, as it observed its rate of steepest decline since May 2020. Japan, Germany, UK, and Italy also witnessed contractions. Manufacturing output and services activity both continued to rise across emerging markets, led by solid expansions in India, Brazil, and China. This is also reflected in the CLI position of Pakistan's main export markets, which shows a declining trend in August 2022 (Fig-2).

Fig-2: Composite Leading Indicator



Source: OECD

Backlogs of work declined at manufacturers and service providers, while stocks of finished products at manufacturers also rose. Subsequently, the rate of job creation eased to a seven-month low.

Global commodity prices showed a mixed picture in August 2022. Energy prices increased by 1.3 percent, led by coal (9.5 percent), and natural gas in Europe by 36.5 percent. Agricultural prices eased 1.0 percent. Food prices declined by 1.6 percent and fertilizers eased by 1.5 percent. Metals gained 3.7 percent and precious metals gained 2.1 percent.

Monthly Performance of Pakistan's Economy

Already confronting inflationary and external sector pressures, the economy of Pakistan is under severe economic and humanitarian crisis due to recent flash floods.

2.1 Real Sector

2.1-a Agriculture

According to FAO's geospatial assessment, an area of over 9.461 million acres (MA) of cultivated crops (Sindh: 4.803 MA (50.8 %), Punjab: 2.715 MA (28.7 %), Balochistan: 1.229 MA (13.0 %), and KP: 0.715 MA (7.5 %)) have been affected/damaged by the recent Floods-2022, increasing the risk of food insecurity. A large number of farmers lost their livestock on way to safe havens and through the non-availability of fodder and exertion. There was hardly a place in the severely affected area that was free of standing water.

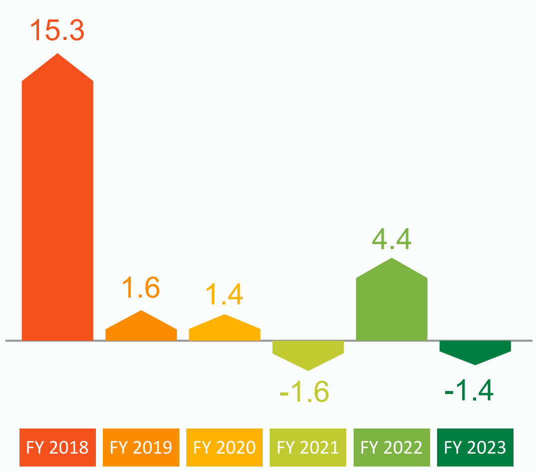
For Jul-Aug FY2023, farm tractor production declined by 37.3 percent to 5,810 and its sales also dropped by 18.5 percent to 6,230 compared to the same period last year. During Jul-Aug FY2023, the agriculture credit disbursement increased by 31.8 percent to Rs 226.1 billion as compared to Rs 171.6 billion during same period last year. During Kharif 2022 (Apr-Aug), urea and DAP offtake was 2,629 thousand tonnes (5.1 percent less than Kharif 2021) and 428 thousand tonnes (35.8 percent less than Kharif 2021).

2.1-b Manufacturing

Amid elevated inflationary pressures,

monetary tightening, and uncertainty in the financial market, a flood has further aggravated the supply chain disruptions and dragged down LSM to negative growth of 1.4 percent in July FY2023 against 4.4 percent growth in the corresponding period last year. On MoM, LSM nosedived by 16.5 percent in July 2022 against 0.6 percent in June 2022. During the period, only 8 out of 22 sectors witnessed growth which includes, Beverages, Wearing Apparel, Iron & Steel products, Wood Products, Paper & Paperboard, Furniture, and others, while it decreased in Food, Textile, Tobacco, Automobiles, Chemicals, Rubber Products and Other Transport Equipment.

Fig-3: LSM Growth (%) July



During Jul-Aug FY2023, Car production and sale decreased by 26.6 percent and 49.8 percent, respectively, Trucks & Buses production and sale decreased by 22.2 percent and 48.9 percent.

Cement dispatches, in August 2022, suffered a decline of 24.0 percent to 3.29 mn tonnes (4.33 mn tonnes in August 2021) as a massive decline of 23.7 percent observed in local cement dispatches and 25.7 percent in export dispatches. Cumulatively, during Jul-Aug FY2023, total cement sales were 5.34 mn tonnes, which were 35.2 percent lower than sales of 8.23 mn tonnes in the corresponding period of last year. Meanwhile, the sale of petroleum products plunged by 24 percent to 2.9 mn tonnes from 3.9 mn tonnes in the same months of last fiscal year.

2.2 Inflation

CPI inflation is recorded at 26.1 percent during Jul-Aug FY2023 as against 8.4 percent in the same period last year. CPI inflation for August FY2023 is recorded at 27.3 percent as compared to 8.4 percent in the same month last year.

Food prices have risen globally due to a shortage of supply of commodities and high demand. Pakistan has also been affected by global price hikes as the country is net importer of food items especially wheat, pulses, and edible oil. Hence, food inflation is not a domestic phenomenon only. Along with an increase in international commodity prices, depreciation of the exchange rate against the US dollar and the recent floods have further amplified domestic inflation.

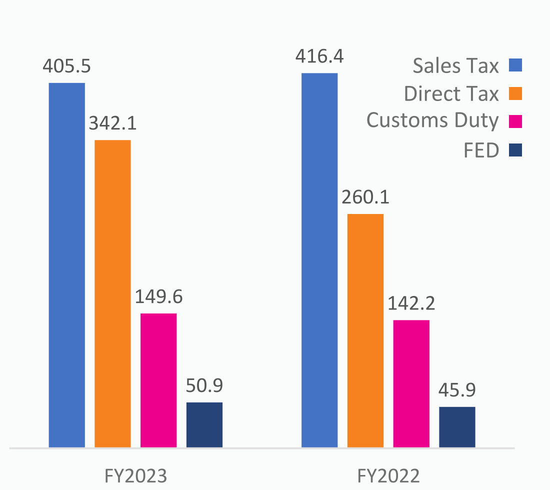
2.3 Fiscal

Net federal revenues in July FY2023 increased by 9.3 percent to Rs 229 billion against Rs 209 billion in the same period last year. Total expenditures increased by only 3.7 percent to reach Rs 536 billion in July FY2023 compared to Rs 517 billion in the same month last year. Within the total, current expenditures increased by 8.0 percent to Rs 531 billion in July FY2023 as compared to Rs 492 billion in the same period last year. Thus, the fiscal deficit has been contained to 0.3 percent of GDP in July FY2023 against 0.4 percent last year. Whereas the primary balance posted a surplus of Rs 142 billion in July FY2023 against the deficit of Rs 5 billion last year.

FBR Tax Collection

During Jul-Aug FY2023, provisional net revenue collection grew by 9.7 percent to reach Rs 948.1 billion against Rs 864.5 billion in the comparable period of last year. While in the month of August, the provisional net collection increased by 9.4 percent to Rs 489.7 billion against Rs 447.6 billion in August last year. Despite floods, a zero rating on POL products, and import compression, FBR has been able to surpass the target by 22.5 billion during Jul-Aug FY2023.

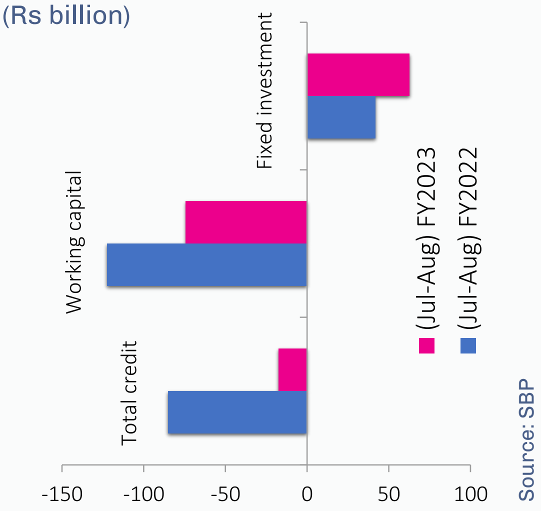
Fig-4: FBR Tax Collection (Rs. Billion) Jul-Aug



2.4: Monetary

In the last monetary policy decision held on 22nd August 2022, SBP maintained the policy rate at 15.0 percent. The decision is based on recent inflation developments in line with expectations, domestic demand beginning to moderate and the external position showing some improvement. Looking ahead, the MPC intends to remain data-dependent, paying close attention to month-on-month inflation, inflation expectations,

Fig-5: Loans to Private Sector Businesses (Rs billion)



developments on the fiscal and external fronts, as well as global commodity prices and interest rate decisions by major central banks.

During 1st July - 02nd September, FY2023 money supply (M2) shows negative growth of 1.8 percent as compared to negative growth of 1.4 percent last year. Private Sector has retired Rs 111.8 billion as compared to the retirement of Rs 145.0 billion last year.

2.5 External Sector

The Current Account posted a deficit of $ 1.9 billion for Jul-Aug FY2023 as against a deficit of $ 2.4 billion last year, mainly due to an increase in exports and contraction in imports. However, the current account deficit shrank to $ 703 million in August 2022 as against $ 1.2 billion in July 2022, largely reflecting an improvement in the trade balance. Exports on fob grew by 11.3 percent during Jul-Aug FY2023 and reached $ 5.1 billion ($ 4.6 billion last year). Imports on fob declined by 2.1 percent during Jul-Aug FY2023 and reached $ 11.1 billion ($ 11.3 billion last year). Resultantly, the trade deficit (Jul-Aug FY2023) reached $ 6.0 billion as against $ 6.8 billion last year.

As per PBS, during Jul-Aug FY2023, exports increased by 3.3 percent to $ 4.7 billion ($ 4.6 billion last year). The major export commodities which have shown tremendous performance include Readymade garments (8.5 percent in value & 60.9 percent in quantity), Cotton Cloth (2.6 percent in value despite 32.8 percent decline in quantity), Knitwear (16.9 percent in value & 66.4 percent in quantity), Carpet, Rugs & Mats (21.1 percent in value & 6.8 percent in quantity) Footwear (20.9 percent in value), Foot Balls (56.5 percent in Value & 52.9 percent in quantity) and Others rice (9.5 percent in value despite a decline of 2.2 percent in quantity).

The total imports in Jul-Aug FY2023 decreased by 8.9 percent to $ 11.1 billion ($ 12.1 billion last year). The main commodities imported were Petroleum products ($1658.6 million), Medicinal products ($ 202.7 million), Petroleum crude ($ 904.5 million), Liquefied Natural gas ($ 629.4 billion), Palm Oil ($ 716.3 million), Plastic materials ($ 452.9 million) and Iron & Steel ($ 344.5 million).

2.5.1 Foreign Investment

FDI reached $ 169.5 million during Jul-Aug FY2023 ($ 229.5 million last year) decreased by 26.1 percent. On MOM basis, FDI was recorded at $ 110.7 million in August 2022 as against an inflow of $ 58.9 million in July 2022. FDI received from China $32.7 million (21.5 percent of total FDI), U.A.E $ 25.5 million (19.6 percent), Switzerland $ 23.3 million (11.0 percent), and the Netherland $ 16.8 million (10.6 percent). The power sector attracted the highest FDI of $ 80.4 million (47.4 percent of total FDI), Financial Business $ 50.7 million (29.9 percent), and Communication $ 25.0 million (14.7 percent).

Foreign Private Portfolio Investment has registered a net outflow of $ 6.7 million during Jul-Aug FY2023. Foreign Public Portfolio Investment recorded a net outflow of $ 18.4 million. The total foreign portfolio investment recorded an outflow of $ 25.1 million during Jul-Aug FY2023 as against an inflow of $ 961.6 million in the corresponding period last year. Total foreign investment during Jul-Aug FY2023 reached $ 144.4 million ($ 1191.1 million last year).

2.5.2 Worker's Remittances

In Jul-Aug FY2023, workers' remittances were recorded at $ 5.2 billion ($ 5.4 billion last year), decreased by 3.2 percent, however continued to remain above the $2 billion mark since June 2020. Share of remittances (Jul-Aug FY2023) from Saudi Arabia remained 24.2 percent ($ 1272.4 million), U.A.E 18.8 percent ($ 987.6 million), U.K 14.9 percent ($ 781.3 million), USA 10.5 percent ($ 548.7 million), other GCC countries 11.1 percent ($581.4 million), EU 10.8 percent ($ 294.7 million), Malaysia 0.5 percent ($ 25.9 million), and Other Countries 9.2 percent.

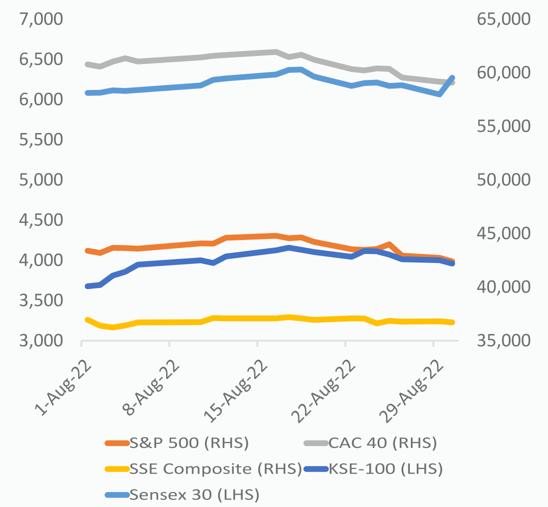
2.5.3 Foreign Exchange Reserves

Pakistan's total liquid foreign exchange reserves stood at $13.8 billion on Sep 21, 2022, with the SBP's reserves recorded at $8.1 billion, while commercial banks' reserves remained at $5.7 billion.

2.6 Performance of KSE Index

The KSE-100 index closed at 42,351 points as on 31st Aug 2022 while market capitalization settled at Rs 7,035 billion. The trend of major world indices is depicted in Fig-6:

Fig-6: Major World Indices



2.7 Social Sector

- The government has decided to increase the flood relief assistance under BISP from the existing Rs 28 billion to Rs 70 billion. The compensation amount of Rs 25,000 is being given to each flood-affected family to help them recover their financial losses.
- Till 14th September 2022 the government has disbursed Rs 24 billion among 965,248 families in flood-affected areas, which is almost 81 percent of the total identified beneficiaries.
- According to WHO, more than 1,400 health facilities had been fully or partially destroyed and that access to

health facilities, health workers, and essential medicines and medical supplies are the main challenges.

- The UNFPA reported that at least 650,000 pregnant women and girls, 73,000 of whom are expected to deliver in the next month. These women lack access to the healthcare facilities and support they need to deliver their children safely.
- Government of Pakistan received relief goods for flood-affected people from French Government on September 3, 2022. The relief aid consists of 83 very high-capacity motor pumps, 200 family tents as well as survival, hygiene, and protection equipment along with a team of doctors and experts.
- Bureau of Emigration and Overseas Employment has registered 72,173 emigrants during August 2022 for overseas employment in different countries.

Economic Outlook

Geopolitical conflicts continue to exist. Global and domestic uncertainties surround the economic prospects. High inflation, aggressive monetary tightening, and uncertainty from the Ukraine war and pandemic have hampered the global outlook in 2022. Soaring food and energy prices are eroding real earnings, generating a global cost-of-living catastrophe for vulnerable communities. The US, China, and the EU are slowing, which is affecting other countries. Rising government borrowing costs and capital outflows exacerbate fiscal and BOP pressures in many developing countries on the basis of forward looking indicators, further slowdown in global growth is expected. Therefore, Pakistan's external environment faces rising challenges. Recent floods brought on by extremely strong monsoon rains have negatively impacted crops, altering the economic outlook mostly through agriculture performance.

3.1 Inflation

Inflation has started reverting as the MoM price increases have been on a declining path during the last two months. Though the YoY inflation has shown significant acceleration from June till August. One reason is a steady decline in international food and oil prices during the last 2 months. Further M2 has also posted a negative MoM growth rate in this period.

On the other hand, since March, the Pakistani rupee is depreciating against the USD. One worrisome problem is the devastating effects of recent floods which have destroyed a substantial part of crops. However, their effects on inflation are being alleviated by prompt Government measures to counter forms of price speculation and to provide sufficient supplies by allowing trade from neighboring countries. Still, the risk of second-round effects of recent inflationary shocks persists which may work themselves through the markets. It can also be observed that in recent years, the month of August shows a positive seasonality in the MoM inflation rate. All in all, September may show a halt to the recent drastic accelerations of the YoY inflation rate.

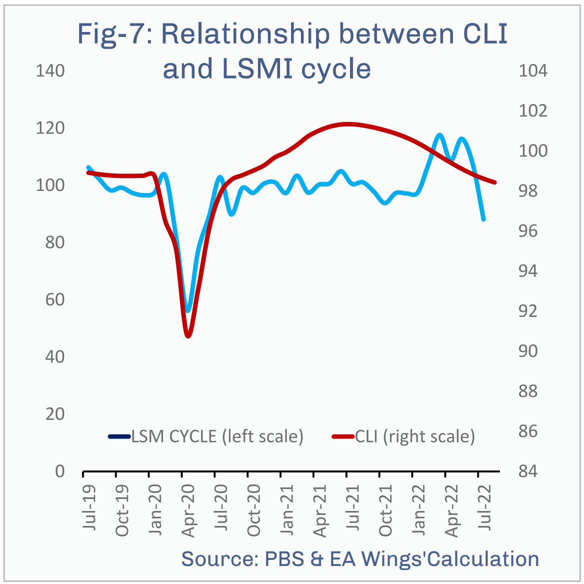
3.2 Agriculture

The agricultural outlook is still not clear as the output of both important and other Kharif crops has suffered significantly due to recent floods and unprecedented heavy monsoon rains. The stay of water in the cropping area may also affect the sowing of Rabi crops.

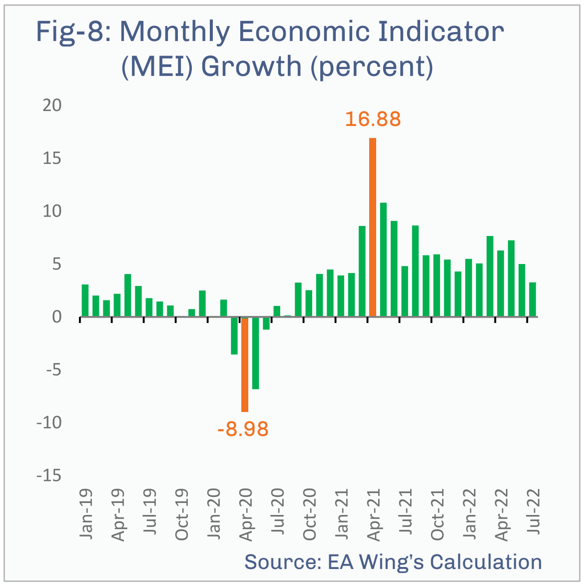
3.3 Industrial Activities

Industrial activity, measured by the LSM index (rebased on prices of 2015-16) is the sector which is most exposed to the developments in international markets is illustrated in Fig-7.

The LSM cycle is following the cyclical movements in the main trading partners,



Source: PBS & EA Wings'Calculation



Source: EA Wing's Calculation

but since it is focused on the main industrial sectors and not on total GDP, it is somewhat more volatile than the cyclical component of GDP in Pakistan's main export markets. Nevertheless, LSM's cyclical pattern is well positively correlated with the cyclical position of Pakistan's main trading partners. Most recent data show a convergence of Pakistan's cyclical position to that of its main trading partners. As expected, in July, international economic slowdown and domestic negative seasonal effects dragged down LSM as compared with its level recorded in June, whereas on a YoY basis, LSM showed relative stability. For August moderate growth both on MoM and YoY basis can be expected, unless the effects of the recent floods would jeopardize this scenario.

3.4 Overall economic activity

The Monthly Economic Indicator (MEI) is based on combining monthly data of indicators that are proven to be correlated with GDP at constant prices. Fig-8 presents the MEI on monthly basis since January 2019. It should be noted that some of the data underlying the August MEI are still provisional and may be revised next month. The MEI has also been adjusted to the new rebased National Accounts.

Since the start of the current FY, economic activity seems to have fallen to a lower growth path. Contributing indicators to this observation are the growth slowdown in the rest of the world, limited YoY growth in manufacturing, high domestic inflation, eroding real incomes, and raising production costs. Probably the data do not yet incorporate the economic costs of the recent floods.

3.5 External

According to BOP data, the trade deficit in goods and services expressed in USD declined marginally in July. Both exports and imports gained strength. For the coming months, the baseline scenario is moderation in imports, following a domestic growth slowdown. At the same time, exports would stabilize, helped by a relatively stable REER at historically low levels. As a result, the trade balance could be expected to improve.

Remittances are expected to stabilize at around current levels. This together with the expected path of the trade balance and other primary and secondary income transactions would guide the current account balance towards further improvement.

But this scenario may be perturbed significantly by the consequences of the recent floods. These may limit export capacity and at the same time require more imports to satisfy the demand for products and harvests foregone.

3.6 Fiscal

For FY2023, the fiscal deficit is budgeted to reduce to 4.9 percent of GDP, while the primary balance is a surplus of Rs 153 billion. The budget for FY2023 was prepared to achieve the goals of stabilizing economic growth, increasing revenues, rationalizing expenditures through prudent expenditure management, enhancing exports, and protecting the vulnerable segments of society through relief measures and pro-poor initiatives. However, the economy of Pakistan has been affected severely by widespread destruction brought by extreme flooding. Consequently, there will be a detrimental impact on the government's fiscal situation from both the revenue and expenditure sides.

Way Forward

In March 2022, international oil and food prices broke out the upper bound of the margins observed in the last two decades. These tendencies have impacted significantly inflation in Pakistan. Even if international commodity prices would mean-revert in the near future, domestic inflation may still suffer from delayed adjustments and second-round effects. Also, the depreciation of the PKR continues to exert upward pressure on domestic prices.

At the same time, recent exceptional floods have destroyed human, physical, and livestock capital and deprived many families of their assets and incomes. Besides the cost in terms of lost lives and capital, these events will certainly affect the creation of gross value added and hence economic growth. The latter was already under pressure due to unstable economic conditions in the rest of the world and due to the necessary fiscal consolidation, high rates of interest, and inflation. The economic outlook for Pakistan in the current fiscal year has become uncertain and will likely to remain below the target. Macroeconomic imbalances may ease with the expected slowdown in the economic growth.

Economic Indicators

30th September, 2022

External Sector			
	2021-22 Jul-Aug	2022-23 Jul-Aug	% Change
Remittances ($ billion)	5.4	5.2	↓3.2
Exports FOB ($ billion)	4.6	5.1	↑11.3
Imports FOB ($ billion)	11.3	11.1	↓2.1
Current Account Deficit ($ billion)	2.4	1.9	↓
FDI ($ million)	229.5	169.5	↓26.1
Portfolio Investment-($ million)	961.5	-25.1	↓
Total Foreign Investment ($ million)	1,191.1	144.1	↓87.8
Forex Reserves ($ billion)	26.037 (SBP: 19.222) (Banks: 6.815) (On 28th Sep 2021)	13.582 (SBP: 7.885) (Banks: 5.697) (On 28th Sep 2022)	
Exchange rate (PKR/US$)	169.97 (On 28th Sep 2021)	232.12 (On 28th Sep 2022)	

Source: SBP

Fiscal (Rs Billion)			
	2021-22 (July)	2022-23 (July)	% Change
FBR Revenue(Jul-Aug)	864	948	↑9.7
Non-Tax Revenue	47	41	↓13.0
PSDP (incl. grants to provinces)	25	5	↓80.0
Fiscal Deficit	238	210	↓11.7
Primary Balance	-5	142	↑

Source: FBR & Budget Wing

Monetary Sector			
	2021-22	2022-23	% Change
Agriculture Credit (provisional) (July-Aug)	171.6	226.1	↑31.8
Credit to private sector (Flows)	-145.0 (1st Jul to 3rd Sep FY22)	-111.8 (1st Jul to 2nd Sep FY23)	↑
Growth in M2 (percent)	-1.4 (1st Jul to 3rd Sep FY22)	-1.8 (1st Jul to 2nd Sep FY23)	
Policy Rate (percent)	7.25 (20-Sep-2021)	15.0 (22-Aug-2022)	

Source: SBP

Inflation			
	2021-22	2022-23	% Change
CPI (National) (percent)	8.4 (Aug) 8.4 (Jul-Aug)	27.3 (Aug) 26.1 (Jul-Aug)	

Real Sector			
Large Scale Manufacturing (LSM) (percent)	4.4 (July)	-1.4 (July)	
PSX Index*	41630 (On 1st Jul 2022)	41435 (On 28th Sep 2022)	↓0.47
Market Capitalization (Rs trillion)	6.96 (On 1st Jul 2022)	6.81 (On 28th Sep 2022)	↓2.16
Market Capitalization ($ billion)	33.99 (On 1st Jul 2022)	29.36 (On 28th Sep 2022)	↓13.62
Incorporation of Companies (Jul-Aug)	3991	4057	↑1.65

*: Formerly Karachi Stock Exchange (KSE)

Source: PBS, PSX & SECP