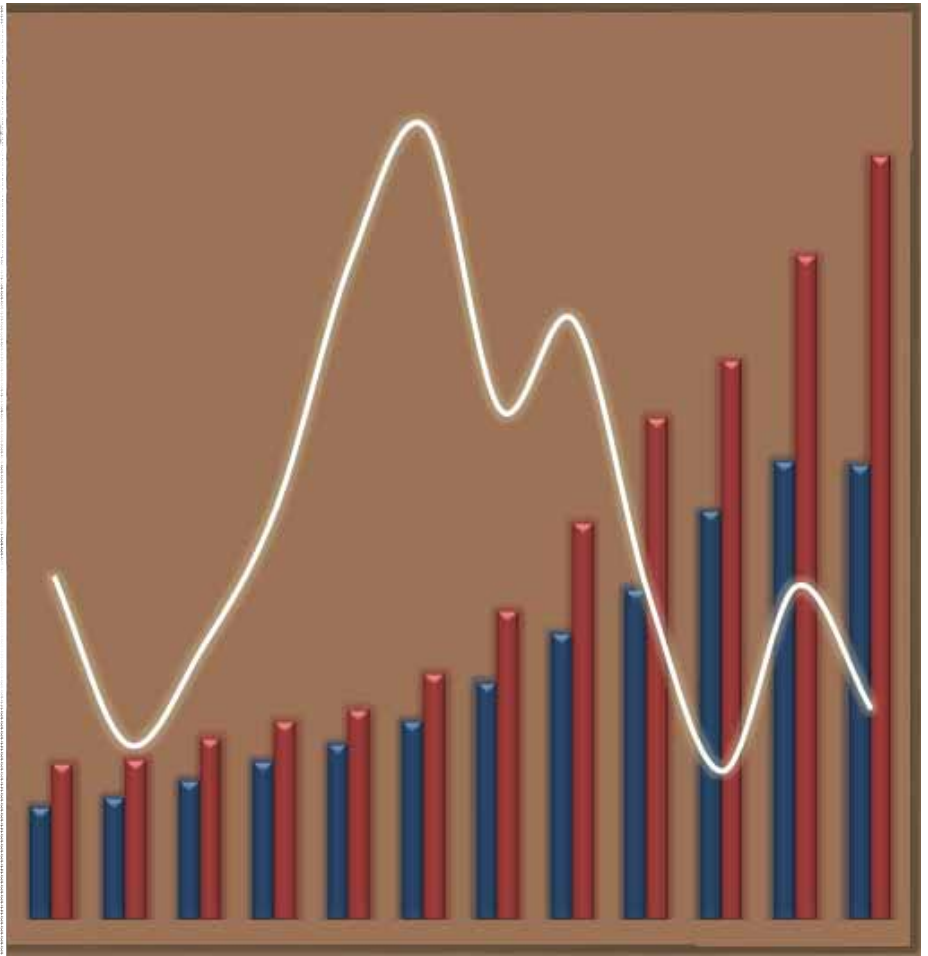


# Fiscal Policy Statement

2011-12



Debt Policy Coordination Office  
Ministry of Finance

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# FISCAL POLICY STATEMENT

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2011-12

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Debt Policy Coordination Office  
Ministry of Finance

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## List of Acronyms

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AJ&K	Azad Jammu & Kashmir
BODs	Board of Directors
BoP	Balance of Payments
BSP	Budget Strategy Paper
CCOR	Cabinet Committee on Restructuring
CDNS	Central Directorate of National Savings
CFAO	Chief Finance & Accounting Officer
CSF	Coalition Support Fund
CVT	Capital Value Tax
DISCOs	Distribution Companies
DPCO	Debt Policy Coordination Office
ENDA	Emergency Natural Disaster Assistance
FATA	Federally Administered Tribal Areas
FBR	Federal Board of Revenue
FED	Federal Excise Duties
FELs	Foreign Exchange Liabilities
FPS	Fiscal Policy Statement
FRDL Act	Fiscal Responsibility and Debt Limitation Act
FY	Fiscal Year
GDP	Gross Domestic Product
GoP	Government of Pakistan
GST	General Sales Tax
IDPs	Internally Displaced Persons
IMF	International Monetary Fund
IRS	Inland Revenue Service
KESC	Karachi Electric Supply Company
MTBF	Medium-Term Budget Framework
NEPRA	National Electric Power Regulatory Authority
NFC	Nation Finance Commission
NTDC	National Transmission & Despatch Company
OGDCL	Oil & Gas Development Company Ltd.
PEPCO	Pakistan Electric Power Company
PSDP	Public Sector Development Programme
PSEs	Public Sector Enterprises
PSO	Pakistan State Oil
PTA	Pakistan Telecommunication Authority
PTCL	Pakistan Telecommunication Company Ltd.
RGST	Reformed General Sales Tax
SBA	Stand by Agreement
SBP	State Bank of Pakistan
SDR	Special Drawing Rights
SED	Special Excise Duty
TPD	Total Public Debt
VAT	Value-Added Tax
WAPDA	Water and Power Development Authority
WHT	Withholding Taxes

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## I. Introduction

A confluence of unfavorable factors including anemic GDP growth, devastating floods, severe energy shortages, hemorrhaging PSEs, high inflation, weak security situation and global economic recession kept the environment very difficult for fiscal policy in 2010-11. Being structural in nature, most of these factors have not yielded any traction and hence the task of fiscal policy remains challenging in 2011-12 and beyond unless structural reforms are implemented quickly and effectively.

Fiscal policy is interrelated with other macroeconomic variables including growth, investment, inflation, monetary policy and external account. Although achieving higher fiscal consolidation remains a key element of government's strategy for maintaining macroeconomic stability, a prerequisite for sustainable growth, the actual fiscal performance of past two years has shown deviation from original targets. While one may question the wisdom of targeting higher fiscal consolidation given the country's low growth envelope, one needs to examine the nature of fiscal deficit to determine whether it is helping higher sustainable growth or working counter to this objective.

After laudable performance in FY2009 wherein fiscal deficit was reduced dramatically to 5.3% from 7.6% in the preceding year, the gains were quickly reversed as fiscal deficit increased sequentially in FY2010 and FY2011. Actual consolidated fiscal deficit for FY2011 came in at 6.6% of GDP, far higher than the original budgeted target of 4.0% for the year. Although the reported deficit figure included payments amounting 0.7% of GDP representing cost of energy subsidies relating to previous years, even excluding it the adjusted fiscal deficit of 5.9% was substantially higher than the original target.

Slippages in both revenues and expenditures led to FY2011 budget deficit missing the target. Gross revenue collection (tax and non-tax) was 12.1% lower than the budgeted target while total expenditures (current and development), adjusted for one off payment of energy subsidies pertaining to previous years, were 2.4% higher than budgetary estimates. FBR tax collection fell 6.4% short of target while non-tax revenues were 23.6% less than target due to non-realization of expected 3G license receipts and lower logistical support receipts from the US. On the other hand, expenditure exceeded the target due to higher subsidies and flood related spending despite PSDP spending being 24% lower than the budgeted target.

A significant positive masked by overall weak fiscal numbers is the distinct uptrend in FBR tax collection since 4QFY2011. Helped by withdrawal of GST exemption on several sectors and levy of one-off flood



surcharge, FBR tax collection grew by 28.7% in 4QFY2011. However, the trend has continued into FY2012 with FBR tax collection increasing by 21% during Jul-Dec'2011 despite shifting of GST collection on certain service to the provinces.

Persisting energy crisis is the common denominator adversely impacting key macroeconomic variables entailing huge social and economic costs in shape of lower GDP growth while being a major drain on fiscal resources. The chronic inter-corporate debt engulfing the entire energy chain and growing energy shortages are dissuading investment not only in the energy sector where it is most needed but in other industrial sectors as well. Moreover, continuing energy subsidies and ensuing high fiscal deficit are inhibiting external inflows especially those from multilateral financial institutions. Slippages in implementing fiscal reforms, particularly implementation of RGST, elimination of electricity subsidies and resolution of circular debt, was a key reason behind IMF's standby agreement staying suspended since June 2010 until it finally lapsed in November 2011.

Power sector subsidies amounted to 1.9% of GDP in FY2011 and it shall be even higher in FY2012 as in addition to tariff differential subsidies, issuance of T-bills/PIBs to repay government guaranteed power sector TFCs shall contribute another 1.5% of GDP to the fiscal deficit. A combination of internal inefficiencies and pricing anomalies is responsible for the circular debt problem confronting the energy sector. Some specific factors include: i) tariff anomalies in power and natural gas sectors, ii) misallocation of natural gas, iii) unfavorable power generation mix, and iv) inefficient operations of public generation and utility companies. Eliminating these problems is imperative for attracting investment in energy and other industrial sectors.

Fiscal policy faces a critical trade-off between short-term inflation and long-term economic growth. Eliminating energy subsidies through tariff rationalization shall spike inflation in the short-term but that is an unavoidable cost to attract the investment needed for higher sustainable economic growth.

The present Fiscal Policy Statement is prepared to fulfill the legal requirement of Section 6 of the FRDL Act 2005. The Act requires that the Fiscal Policy Statement (FPS) shall analyze the performance of key macroeconomic indicators like total revenue collection, total expenditure, fiscal deficit and total public debt along with rationales for any major deviation from fiscal policy targets.

## II. Fiscal Policy Statement

The Fiscal Policy Statement is presented to fulfill the requirement in Section 6 of the Fiscal Responsibility and Debt Limitation (FRDL) Act 2005. The statement provides an overview of government revenues and expenditures during the course of the fiscal year and explains the changes in key macroeconomic indicators during 2009-10. Section 6 of the FRDL Act 2005 requires that:

- 1) The Federal Government shall cause to be laid before the National Assembly the Fiscal Policy Statement by the end of January each year.
- 2) The Fiscal Policy Statement shall, *inter alia*, analyze the following key macroeconomic indicators, namely:-
  - a) Total expenditures;
  - b) Total revenues;
  - c) Total fiscal deficit;
  - d) Revenue deficit; and
  - e) Total public debt
- 3) The Federal Government shall explain how fiscal indicators accord with the principles of sound fiscal and debt management.
- 4) The Fiscal Policy Statement shall also contain:-
  - a) The key measures and rationale for any major deviation in fiscal measures pertaining to taxation, subsidy, expenditure, administrated pricing and borrowing;
  - b) An update on key information regarding macroeconomic indicators;
  - c) The strategic priorities of the Federal Government for the financial year in the fiscal area;
  - d) The analysis to the fullest extent possible of all policy decisions made by the Federal Government and all other circumstances that may have a material effect on meeting the targets for economic indicators for that fiscal year as specified in the Medium-Term Budgetary Statement; and
  - e) An evaluation as to how the current policies of the Federal Government are in conformity with the principle of sound fiscal and debt management and the targets set forth in the Medium-Term Budgetary Statement.

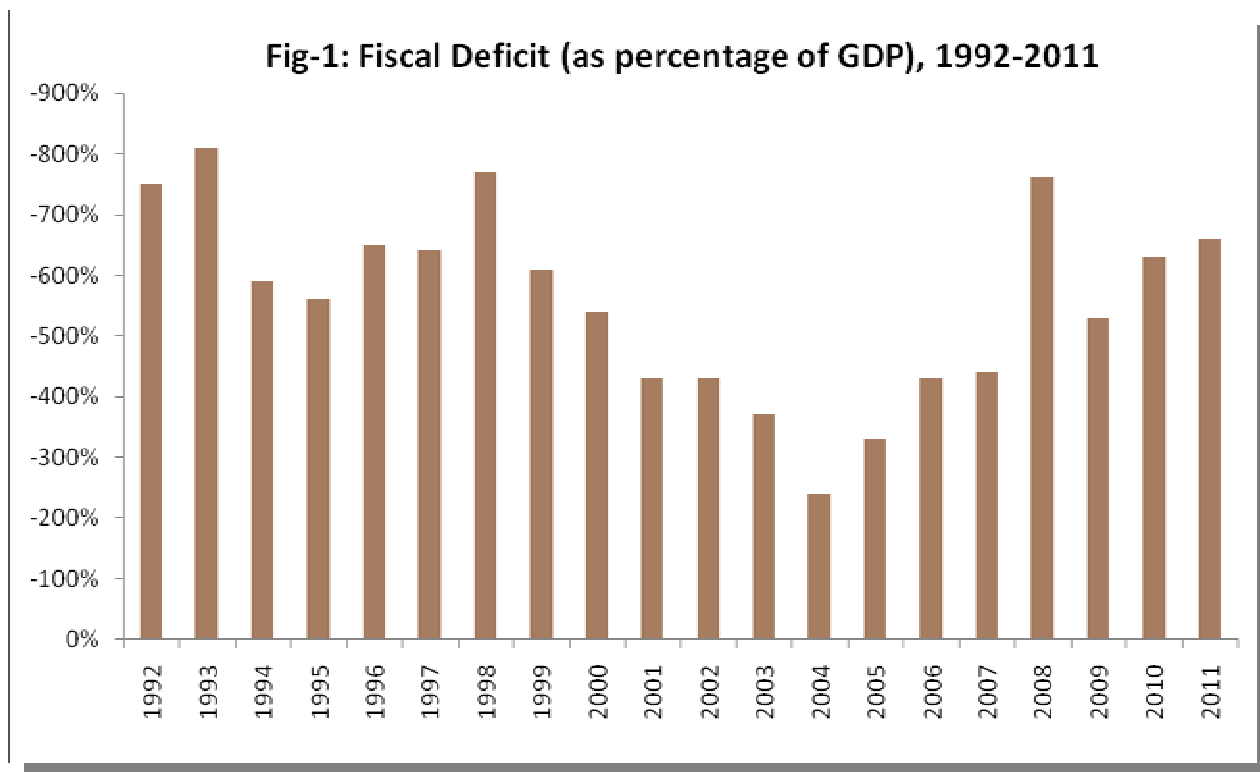
### III. Historical Perspective on Fiscal Developments

Pakistan has had its share of good and bad periods over the last two decades with regards to its fiscal discipline. In order to have a more meaningful comparison between different periods over the last two decades, we represent fiscal numbers as percentage of GDP.

<b>Table-1: Fiscal Performance, 1991-2011 (in percent of GDP)</b>					
	<b>Period 1</b>	<b>Period 2</b>	<b>Period 3</b>	<b>Period 4</b>	<b>Period 5</b>
	<b>Improve</b>	<b>Stability</b>	<b>V. improve</b>	<b>Poor</b>	<b>Consolidation</b>
	<b>5 years</b>	<b>3 years</b>	<b>6 years</b>	<b>4 years</b>	<b>3 years</b>
	<b>1991-1995</b>	<b>1996-1998</b>	<b>1999 - 2004</b>	<b>2005 - 2008</b>	<b>2010-2011</b>
<b>TOTAL REVENUES</b>	<b>15.6%</b>	<b>14.0%</b>	<b>13.9%</b>	<b>14.6%</b>	<b>13.7%</b>
Tax Revenues	11.8%	11.6%	10.9%	10.6%	9.7%
Non-Tax Revenues	3.4%	2.3%	3.0%	3.8%	4.0%
<b>TOTAL EXPENDITURE</b>	<b>21.6%</b>	<b>19.9%</b>	<b>18.1%</b>	<b>20.5%</b>	<b>19.7%</b>
Current Expenditure	16.7%	16.5%	15.5%	16.0%	16.3%
Defense	5.3%	4.5%	3.4%	3.0%	2.5%
Debt Servicing	4.8%	5.8%	5.5%	4.1%	4.4%
Current Subsidies	0.5%	0.4%	0.8%	2.0%	1.8%
General Administration	1.4%	1.8%	2.2%	2.7%	3.0%
Development Expenditure	4.8%	3.3%	2.6%	4.5%	3.5%
<b>FISCAL DEFICIT</b>	<b>-6.0%</b>	<b>-5.8%</b>	<b>-4.2%</b>	<b>-5.1%</b>	<b>-6.1%</b>

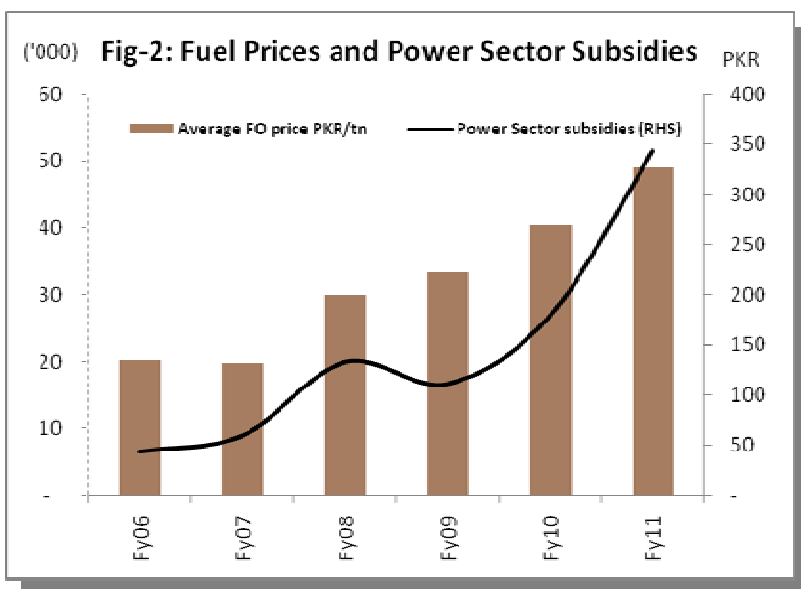
Fiscal deficits have been on a roller coaster ride, with periods of improvement quickly slipping into high deficits and then reverting back to consolidation phase. During the early 1990's fiscal imbalance remained high; however, it started to recover at the end of FY1993. This improvement was again followed by a period of high fiscal constraints (1996-1998). Post FY1999, fiscal performance of the country saw considerable improvement as its fiscal deficit reached to a low of 2.3% of GDP during FY2004. It was after FY2004 that fiscal slippages once again started to widen. During FY2008, fiscal deficit saw a mammoth increase as it reached to 7.6% of GDP.

Breaking up the last two decades into five unequal periods will provide a better picture of fiscal performance. It is safe to say that high subsidies remain a major burden on fiscal account, but it would be unfair not to point out falling percentage of tax to GDP ratio. As seen in Table-1, tax revenue as a percentage of GDP stood at 11.8% during period 1 (1991-1995), which has now decreased to 9.7% during period 5 (2009-2011). Low tax to GDP ratio has also translated into falling total revenues to GDP ratio, as it decreased from 15.6% in period 1 to 13.7% in period 5. Interestingly even during the period of fiscal improvement (1999-2004), tax to GDP ratio continued to slide, it was controlled expenditure that caused the decline in fiscal deficits.

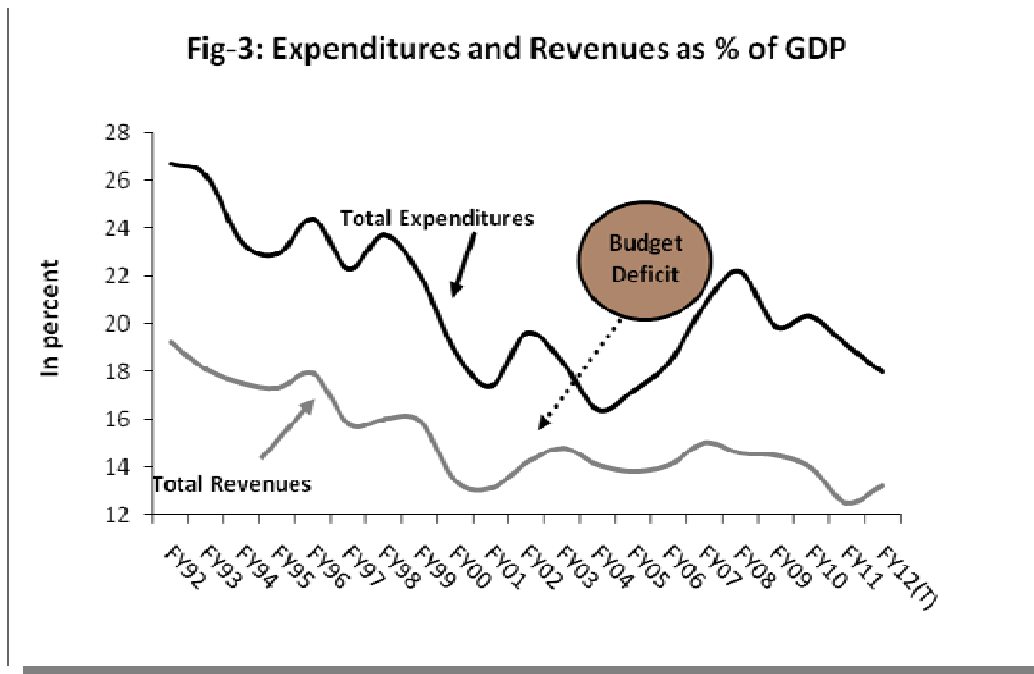


Defense and Debt servicing expenditure has shown a favorable trend over the last two decades, as spending on defense decreased from 5.3% in period 1 to 2.5% in period 5 while debt servicing which had reached to 5.8% during period 2, declined to 4.3% in period 5. Debt servicing as a percentage to GDP is now once again on an upward trend as seen in the latest period.

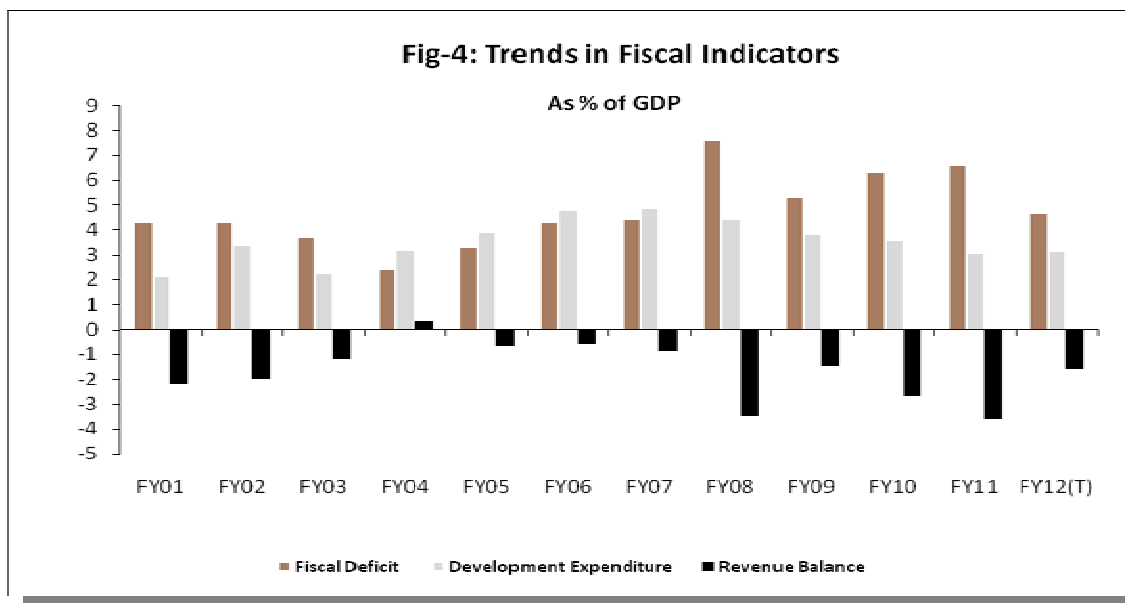
Different factors have contributed towards deteriorating fiscal position during FY2005 to FY2011; however one reason that ignited the fiscal imbalance was higher oil prices in international markets followed by delayed policy response to transfer its impact to consumers. Post FY2005, oil prices in global markets shot up from USD 59/bbl in Jun-2005 to USD 176/bbl in July-2008. Instead of passing this price hike to consumers, government opted to



absorb the price differential by heavily subsidizing energy sector thus burdening its own fiscal account. Subsidies in energy sector alone increased from PKR 49.68 billion in FY2005 to PKR 133.25 billion in FY2008.



The government has started the process of gradually passing on these subsidies to consumers as it increased base electricity tariffs by 90% since March FY2008. However, tariff anomalies still exist that need to be eliminated at the earliest. In FY2011 alone, an amount of PKR 335bn was paid in energy subsidies, equivalent to 1.9% of GDP.



Structural deficiencies in tax system coupled with increasing expenditure on the back of high cost of subsidies have kept fiscal balance under pressure for last few years. It is now imperative to bring untaxed sectors into tax bracket along with improving tax collection mechanism to increase tax to GDP ratio. Restructuring of ailing PSE along with gradually getting rid of subsidies burden is the need of the hour in order to curtail government spending.

#### IV. Recent Fiscal Policy Developments

Pakistan's fiscal deficit over the last two years saw significant variation from its original targets; however government feels confident to meet its projected target of 4.7% during FY2012.

**Table-2: Consolidated Revenue & Expenditure of the Government (Rs. Billion)**

	Prov. Actual July-June 2009-10	Budget Estimate 2010-11	Prov. Actual July-June 2010-11	Budget Estimate 2011-12
<b>A. Total Revenue</b>	<b>2,078</b>	<b>2,574</b>	<b>2,261</b>	<b>2,871</b>
a) Tax Revenue	1,473	1,859	1,707	2,151
b) Non-Tax Revenue	605	716	554	719
<b>B. Total Expenditure</b>	<b>3007</b>	<b>3259</b>	<b>3455</b>	<b>3721</b>
a) Current Expenditure	2386	2519	2901	2976
b) Development Expenditure	613	734	506	737
c) Net Lending	39	7	8	8
d) Unidentified Expenditure	-32	0	40	0
<b>C. Overall Fiscal Balance</b>	<b>-929</b>	<b>-685</b>	<b>-1194</b>	<b>-851</b>
- As % of GDP	-6.3	-4.0	-6.6	-4.0

Source: Budget Wing, Ministry of Finance

Structural weaknesses like low tax to GDP ratio and high subsidies leave little elbow space for the government to focus on developmental expenditure. With rigid government spending, the onus of fiscal burden falls on developmental expenditure which in return hampers economic growth.

After the lackluster growth of 1.7% in FY2009, economy saw encouraging signs of recovery in FY2010 as GDP

**Table-3: Real Growth of Tax Revenue**

	Tax Revenue (Rs. Billion)	Real Growth of Tax Revenue (%)	Real GDP Growth (%)	Tax-GDP (%)
2006-07	890	2.8	6.8	10.3
2007-08	1,051	1.6	3.7	10.3
2008-09	1,205	-4.5	1.7	9.5
2009-10	1,473	9.2	3.8	9.9
2010-11	1,707	-4.1	2.4	9.5
2011-12*	2,158	12.9	3.6	10.3

\*Projections

Source: DPCO Staff Calculations

growth of 3.8% was recorded. However, floods in FY2011 quickly reversed the gains of previous year and GDP plunged to 2.4%. As a consequence, tax revenue and non tax revenues declined during FY2011 while expenditures remained high.

Generating revenues from taxation remains an uphill task as it was seen in recent trend where tax to GDP ratio fell from 10.1% in FY2010 to 9.5% in FY2011. During FY2010, real growth in tax revenue saw a healthy increase of 11.1%; however, in FY2011 real growth in tax revenue dramatically fell by 4.5%.

Double digit inflation coupled with anemic growth contributed towards dismal real tax revenue growth. Total real revenue collection also suffered from the same hurdles as it posted a negative growth of 8.4% during FY2011.

**Table-4: Selected Fiscal Indicators (in percent)**

	FY06	FY07	FY08	FY09	FY10	FY11
Real Growth of Public Debt	-5.7	2.3	8.3	5.2	4.3	1.1
Real Growth of Revenues	8.3	11.9	-0.6	2.9	0.3	-8.4
Real Growth of Tax Revenue	10.3	2.8	1.6	-4.5	11.1	-4.1
Real Growth in Non-interest Exp.	16.3	14.1	7.5	-11.7	11.6	-1.9
Real Growth of GDP	5.8	6.8	3.7	1.7	3.8	2.4
Saving Investment Gap	-4.4	-5.1	-8.7	-5.6	-2.2	0.4
Primary Balance	-0.7	-1.3	-2.5	-0.1	-1.6	-2.5
Revenue Balance	1.0	-0.6	-3.2	-1.2	-2.4	-3.3
Public Debt/GDP	57.2	55.4	59.0	60.0	60.1	59.3
Public Debt/Revenue	405	370	403	412	429	474
Debt Service/Revenue	29.6	33.8	37.2	46.6	40.4	37.7

Source: Budget Wing, MoF and DPCO Staff Calculations

On non tax revenue front, SBP remains one of the biggest contributors towards national kitty. As SBP's contribution in national exchequer decreased by 20.6% Y/Y in FY2011, non-tax revenue saw a decrease of 9.4% Y/Y during the same period. Increasing Primary Balance (budget deficit in which interest payments on government liabilities are excluded from expenditure) has been an underlying concern that needs to be addressed by increasing tax-GDP ratio.

On Expenditure front, high subsidies to power sector have become a drag on resources. The government has to eliminate the price differential in electricity tariffs that generates circular debt in order create fiscal space for developmental expenditure. In FY2011 alone, 15% of total revenues were consumed in power sector subsidies while back in FY2006, 6% of total revenues were spent on power subsidies.

Table-5: Fiscal Indicators as Percent of GDP

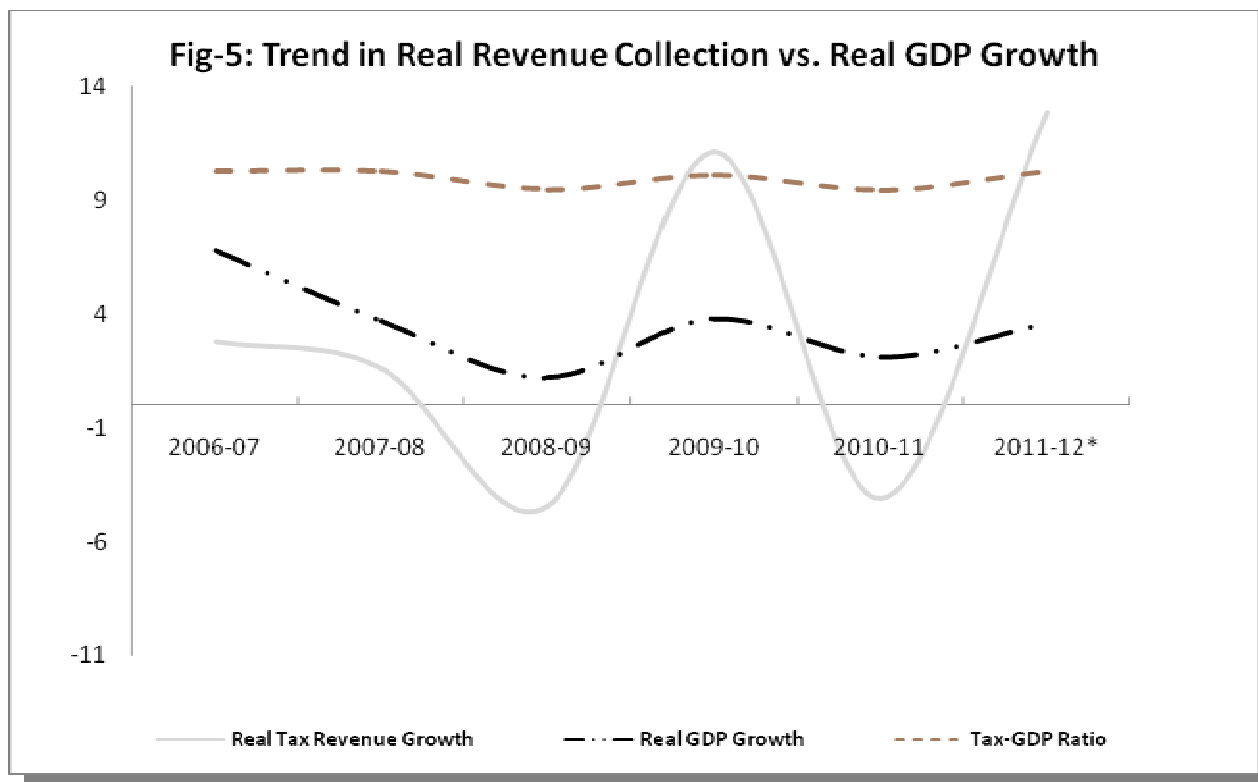
	Real GDP Growth	Overall Fiscal Deficit	Expenditure			Revenue		
			Total	Current	Development	Total	Tax	Non-Tax
FY92	7.6	7.5	26.7	19.1	7.6	19.2	13.7	5.5
FY93	2.1	8.1	26.2	20.5	5.7	18.1	13.4	4.7
FY94	4.4	5.9	23.4	18.8	4.6	17.5	13.4	4.1
FY95	5.1	5.6	22.9	18.5	4.4	17.3	13.8	3.5
FY96	6.6	6.5	24.4	20.0	4.4	17.9	14.4	3.5
FY97	1.7	6.4	22.3	18.8	3.5	15.8	13.4	2.4
FY98	3.5	7.7	23.7	19.8	3.9	16.0	13.2	2.8
FY99	4.2	6.1	21.9	18.6	3.3	16.0	13.3	2.7
FY00	3.9	5.4	18.9	16.4	2.5	13.4	10.6	2.8
FY01	2.0	4.3	17.4	15.3	2.1	13.1	10.5	2.6
FY02	3.1	4.3	19.6	16.2	3.4	14.2	10.7	3.5
FY03	4.7	3.7	18.5	16.2	2.2	14.8	11.4	3.4
FY04	7.5	2.4	16.9	13.7	3.2	14.1	10.8	3.2
FY05	9.0	3.3	17.2	13.3	3.9	13.8	10.1	3.7
FY06	5.8	4.3	18.4	13.6	4.8	14.1	10.5	3.6
FY07	6.8	4.4	20.8	15.9	4.9	15.0	10.3	4.7
FY08	3.7	7.6	22.5	18.1	4.4	14.6	10.3	4.4
FY09	1.7	5.3	19.9	16.1	3.8	14.5	9.5	5.1
FY10	3.8	6.3	20.3	16.7	3.5	14.0	10.1	3.9
FY11	2.4	6.6	19.2	16.1	3.1	12.5	9.5	3.1
FY12(T)	3.6	4.7	18.0	14.8	3.2	13.2	10.3	2.9

Note 1: The base of Pakistan's GDP has been changed from 1980-81 to 1999-2000, therefore, wherever GDP appears in denominator the numbers prior to 1999-2000 are not comparable.

These expenditures are apart from the disguised fiscal deficit that arises from banks funding to public sector enterprises. As privatization looks an unlikely option for now, restructuring of PSE are of utmost importance or else fiscal drainage will continue to increase. The burden of fiscal constraints has been falling on developmental expenditure for some years now. Spending on developmental expenditure in FY2006 stood at 4.8% of GDP while that figure has narrowed down to 3.1% during FY2011.

Government has set an optimistic fiscal deficit target of 4.7% for FY2012. The budgeted target looks achievable as 1HFY12 FBR tax collection of PKR 842bn (up 21% Y/Y) is laudable. FBR should now push for increasing the tax pie by bringing undocumented sectors into tax bracket along with devising policies that close loopholes for tax evasion.





## V. Fiscal Performance 2010-11

### V.i. Revenue

#### V.i.a. FBR Tax Collection and Refunds 2010-11

FBR tax revenue target for the fiscal year 2010-11 was fixed at Rs. 1667 billion at the time of announcement of Federal Budget. The target was higher by 25.6% over actual collection of Rs 1327.4 billion during fiscal year 2009-10. However, floods during August, 2011 and energy shortage have vastly affected the economy and taxation. Thus, the revenue target was revised to Rs.1604 billion and later on further revised to Rs 1587.7 billion.

Despite unfavorable circumstance, FBR has collected Rs 1,558 billion during 2010-11 as against Rs.1327.4 billion in 2009-10 reflecting a growth of 17.4%. The performance is commendable when viewed in the context of higher refunds payments of around Rs.17 billion during 2010-11.

So it may confidently be said that the net collection of Rs 1,588 billion is a significant achievement of FBR despite adverse conditions in the country depicted below:

- Unprecedented floods have vastly affected the economy and resource mobilization efforts in the country.
- Acute shortage of energy has badly affected the tax efforts.
- A huge growth of around 20% in the payment of refunds/rebates has also affected net collection of federal taxes.

The public sector program was slashed down substantially during 2010-11 which has also affected collection of federal taxes collected by FBR.

The transfer of CVT from federal to the provincial governments has also affected the collection of federal taxes.

Revenue Heads	Collection		Difference	
	FY11	FY10	Absolute	Percent
<b>Direct Taxes</b>	<b>602.5</b>	<b>526.0</b>	<b>76.5</b>	<b>14.5</b>
<b>Indirect Taxes</b>	<b>955.6</b>	<b>801.4</b>	<b>154.2</b>	<b>19.2</b>
- Sales Tax (GST)	633.4	516.3	117.1	22.7
- Federal Excise	137.4	124.8	12.6	10.1
- Customs Duties	184.8	160.3	24.6	15.3
<b>Total Taxes</b>	<b>1,558.0</b>	<b>1,327.4</b>	<b>230.6</b>	<b>17.4</b>
- As %age of GDP	<b>8.6</b>	<b>8.9</b>		

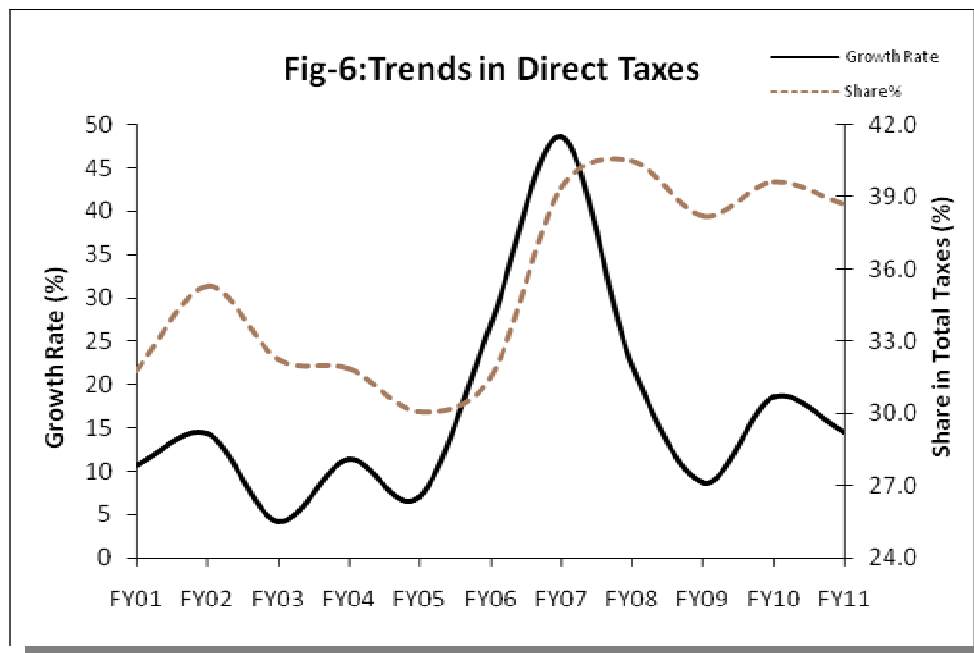
Source: Federal Board of Revenue

### **Direct Taxes**

The net collection has been Rs. 602.5 billion during 2010-11 against the target of Rs. 626.9 billion. An amount of Rs. 46.7 billion refunds has been paid back to the claimants as against Rs.54.2 billion during FY2009-10.

Improved tax effort and relatively effective implementation of tax policy and administrative reforms has geared up the collection over the years. The share of direct taxes in total federal tax receipts has increased from around 15 percent in early 1989-90 to around 32 percent in FY2000-01. Currently, it is around 39 percent in FY2010-11.

It may be recalled that the collection of direct taxes includes income tax and other direct taxes like worker welfare fund, worker profit participatory fund etc. The contribution of income tax in total direct taxes has been around 97 percent. The structure of income tax is based on withholding taxes (WHT), voluntary payments (VP) and collection on demand (COD). The collection during FY2010-11 shows that the shares of WHT, VP and COD in gross collection have been 56.9 percent, 31.2 percent and 11.5 percent respectively.



a. Voluntary Payments

This component includes payments with return and advances. Rs. 196.1 billion have been generated during FY2010-11 as compared to Rs.165.8 billion in the corresponding period last year reflecting 18.3 percent growth has been witnessed in collection. Advance tax is the major component of voluntary compliance. Rs. 184.2 billion

	2009-10	2010-11	Change (%)
Voluntary Payments	166	196	18.3
Collection on Demand	99	72	-26.7
Deductions at Source (WHT)	295	358	21.2
Miscellaneous	0.119	3	2436.1
Gross Income Tax Receipts	560	629	12.4
Refunds	54	47	-13.9
Other DT	20	20	-2.2
<b>Net Direct Taxes</b>	<b>526</b>	<b>602</b>	<b>14.5</b>

Source: FBR Data Bank

has been collected as advance tax as compared to 156.3 billion during 2009-10. The second component of VP is payment with returns which has increased significantly during the period under review. During FY2010-11, Rs. 11.9 billion was collected against Rs. 9.5 billion in FY 2009-10.

b. Withholding Tax

Withholding taxes are the leading source of direct tax receipts. The WHT collection during FY2010-11 has been Rs. 357.8 billion against Rs. 295.2 billion during FY2009-10 indicating a healthy growth of around 21 percent. The nine major withholding taxes contributed around 90 percent of total WHT

collection. These are: contracts, imports, salary, telephone, export, bank interest, electricity, cash withdrawal and dividends.

The growth pattern of various component of WHT collection has been different i.e. exports (42 percent), dividends (29.3 percent), salary (33.8 percent), imports (32.1%), bank interest (18.3 percent),

**Table-8: Withholding Tax Collection (Rs. Billion)**

	2009-10	2010-11	Change (%)
Contracts	91.66	99.24	8.27
Imports	50.25	66.40	32.13
Salary	34.07	45.58	33.77
Telephone	23.12	27.57	19.26
Exports	16.67	23.67	42.01
Bank Interest	19.94	23.58	18.29
Cash Withdrawal	12.89	10.63	-17.51
Electricity	15.47	14.31	-7.48
Dividend	9.28	12.00	29.30
<b>Sub-Total</b>	<b>273.34</b>	<b>322.99</b>	<b>18.16</b>
Other WHT	21.91	34.85	59.09
<b>Total WHT</b>	<b>295.25</b>	<b>357.84</b>	<b>21.20</b>

Source: FBR Data Bank

telephone (19.3 percent), cash withdrawal (-17.5 percent) and contracts (8.3 percent). The highest growth registered in collection from export is due to higher growth in export during FY2010-11. The substantial growth in imports has also improved the collection from imports. A growth of 33.7 percent from salary is mainly on account of increase in the salary of employees.

## 1. Indirect Taxes

### a. Sales Tax

Sales tax has been leading revenue generation source of the country during 2010-11. It has contributed around 41 percent of the collection of federal taxes 2010-11. A growth of around 22.7 percent has been recorded in the net collection of sales tax. The collection is realized from two components i.e. sales tax on imports and sales tax on domestic sector.

**Table-9: Collection and Growth of Sales Tax: Fiscal Year 2010-11 (Rs. Billion)**

Sources of GST	Collection/ Refunds			Growth (%)		
	Gross	Refund	Net	Gross	Refund	Net
Import Stage	308.7	0	309	24.8	0	24.8
Domestic Stage	375.5	50.8	325	26.1	77.0	20.7
<b>Total</b>	<b>684</b>	<b>51</b>	<b>633</b>	<b>25.5</b>	<b>77.0</b>	<b>22.7</b>

Source: FBR Data Bank

*Sales Tax Domestic Collection:* The collection of sales tax has been highly concentrated in some commodities. This is confirmed by the fact that only petroleum products and telecom sector contribute more than three-fifth of the total sales tax domestic. Major ten commodities contributed 89.3 percent of the total net sales tax from domestic. The major revenue spinners of sales tax domestic include

petroleum products, telecom services, natural gas, other services, cigarettes, sugar, electrical energy, beverages, tea and cement.

*Sales Tax at Import Stage:* Sales tax on imports is also a component of federal tax receipts. The collection of sales tax has increased by 24.8 percent during 2010-11 mainly due to higher collection from edible oils, machinery, paper & paper board, plastic, vehicles etc. Like sales tax domestic, the receipts of sales tax on imports have also been concentrated mainly in few sectors. Petroleum products alone contributed around 36 percent of overall collection of sales tax on imports during 2010-11. Similarly, ten major spinners including petroleum shared 80.2 percent of the sales tax import.

#### b. Custom Duty

The customs duty is one of the important components of federal tax receipts. It contributed around 12 percent

**Table-10: Comparison of Sales Tax Domestic (Net) Collection by Major Commodity (Rs. Billion)**

Major Commodities	2010-11	2009-10	Growth Realized (%)	Share (%) 2010-11	Share (%) 2009-10
POL Products	153	116	31.9	47.2	43.2
Telecom Sector	53	45	17.8	16.2	16.6
Natural Gas	18	17	2.1	5.4	6.4
Other Services	21	17	23.0	6.4	6.2
Electrical Energy	8	6	38.8	2.5	2.2
Cigarette	12	11	5.4	3.5	4.1
Beverages	8	7	19.4	2.6	2.6
Sugar	7	9	-22.4	2.2	3.5
Tea	6	5	19.0	1.7	1.8
Cement	5	4	22.6	1.5	1.5
<b>Sub-Total</b>	<b>290</b>	<b>237</b>	<b>22.5</b>	<b>89.3</b>	<b>88.0</b>
Others	35	32	7.4	10.7	12.0
<b>Net Collection</b>	<b>325</b>	<b>269</b>	<b>20.7</b>	<b>100</b>	<b>100</b>

Source: FBR Data Bank

**Table-11: Collection of Sales Tax (Import) - Major Items (Rs. Billion)**

Description	2010-11	2009-10	Realized Growth (%)	Share (%) 2010-11	Share (%) 2009-10
POL Products (27)	111	100	11.1	34.0	37.0
Edible Oil (15)	29	19	52.9	8.8	7.0
Plastic (39)	25	19	29.2	7.6	7.1
Vehicles and Parts (87)	20	16	23.0	6.1	6.0
Iron and Steel (72)	19	18	8.1	5.9	6.5
Mechanical Machinery (84)	13	8	54.8	3.9	3.0
Electrical Machinery (85)	10	7	47.9	3.0	2.4
Organic Chemicals (29)	8	7	23.5	2.6	2.5
Paper & P. Board (48)	8	5	62.2	2.5	1.8
Oil seeds etc (12)	6	6	0.3	2.0	2.4
<b>Sub Total</b>	<b>247.6</b>	<b>203.7</b>	<b>21.5</b>	<b>76.3</b>	<b>75.7</b>
Other	61	44	40.3	18.8	16.2
<b>Gross</b>	<b>309</b>	<b>247</b>	<b>24.8</b>	<b>100.0</b>	<b>100.0</b>
Refund/Rebate	0.05	0.03	70.4		
<b>Net</b>	<b>309</b>	<b>247</b>	<b>24.8</b>		

Source: FBR Data Bank

in total federal tax receipts during 2010-11. The gross and net collection of customs duty has been Rs.193.4 billion and Rs. 184.8 billion respectively during 2010-11. The gross and net collection grew by 16.5 percent and 15.3 percent respectively during 2010-11. Major revenue spinners of customs include automobile, petroleum, edible oils, machinery, plastic, iron & steel etc. Around 70% of gross collection of customs duty is contributed by major fifteen items.

Description	Collection 2010-11	Collection 2009-10	Realized Growth (%)	Share (%) 2010-11	Share (%) 2009-10
1.Vehicles and Parts (87)	28.10	25.23	11.3	14.5	15.2
2. POL Products (27)	21.40	19.02	12.5	11.1	11.5
3.Edible Oil (15)	17.26	15.51	11.3	8.9	9.3
4.Mechanical Machinery (84)	10.93	10.47	4.4	5.7	6.3
5.Electrical Machinery (85)	9.53	9.44	0.9	4.9	5.7
6.Plastic (39)	8.83	7.22	22.3	4.6	4.3
7.Iron and steel (72)	7.57	8.37	-9.5	3.9	5.0
8..Paper & P. Board (48)	7.28	4.86	49.7	3.8	2.9
9.Textile (54)	4.45	2.33	91.0	2.3	1.4
10.Organic Chemical (29)	3.92	3.79	3.4	2.0	2.3
11.Tea and Coffee (9)	3.54	2.74	29.5	1.8	1.6
12.Staple Fibers (55)	3.21	1.74	84.4	1.7	1.0
13. Dairy produce (4)	2.77	1.37	102.0	1.4	0.8
14. Cosmetic and Perfumery(33)	2.75	2.28	20.7	1.4	1.4
15.Dyes and paints (32)	2.68	2.42	10.9	1.4	1.5
<b>Sub Total</b>	<b>134</b>	<b>117</b>	<b>14.9</b>	<b>69.4</b>	<b>70.3</b>
Other	59	49	20.1		29.7
<b>Gross</b>	<b>193</b>	<b>166</b>	<b>16.5</b>	<b>100</b>	<b>100</b>
Refund/Rebate	9	6	47.4		
<b>Net</b>	<b>185</b>	<b>160</b>	<b>15.3</b>		

Source: FBR Data Bank

### c. Federal Excise Duties

Federal excise duty is levied on imports and domestic stages. The major portion of the receipts emanates from domestic sector. The base of the federal excise duty is quite narrow and is limited to few commodities. Despite narrow base, federal excise duty has been an important revenue generation source of federal taxes. Federal excise duty has contributed 8.8 percent of total tax collection during 2010-11. The tax collection has been Rs. 137.4 billion in 2010-11 against Rs. 124.8 billion in 2009-10

reflecting a growth of 10.1 percent. The major revenue spinners of federal excise duty are cigarettes, cements, beverages, natural gas, services and POL products.

**Table-13: FED Collection from Major Commodities (Rs. Billion)**

Commodities	2010-11	2009-10	Difference		Share(%) 2010-11	Share(%) 2009-10
			Absolute	Percent		
Cigarettes	47	45	2	5.2	34.3	35.9
Cement	15	16	0	-1.9	11.3	12.6
Services	11	16	-5	-31.4	8.0	12.9
Beverages & Concentrates	9	11	-2	-19.6	6.7	9.1
Natural Gas	12	6	5	87.5	8.5	5.0
POL Products	5	5	0	6.5	3.7	3.8
1% SED	25	16	9	53.0	17.9	12.9
<i>Sub Total</i>	<i>124</i>	<i>115</i>	<i>9</i>	<i>7.9</i>	<i>90.3</i>	<i>92.2</i>
Other	13	10	4	36.0	9.7	7.8
<b>Total</b>	<b>137</b>	<b>125</b>	<b>13</b>	<b>10.1</b>	<b>100</b>	<b>100</b>

Source: FBR Data Bank

### V.i.b. Non Tax Revenue

Federal non tax revenue in FY2011 reached Rs 491 billion lower than the budget target by Rs 125 billion. Receipts under the head of defense were budgeted at Rs 133.5 billion during FY2011 originating mainly from logistic support services provided to the coalition forces. However, Rs. 70.7 billion could be realized under this head leaving the receipts under the head of defense below the target by Rs. 62.8 billion. The dividends receipts from financial and non financial institutions remained below the budget target by Rs 13.6 billion. Interest receipt from on-lending to Public Sector Enterprises was lower by Rs.28.2 billion against the budgeted estimates. Non materialization of Rs. 60 billion earmarked against issuance of 3 G licenses was primarily compensated by unbudgeted foreign grants of Rs. 41 billion and higher collection of levies on petroleum and gas sectors.

### V.ii. Expenditure

As originally envisaged in budgetary targets for FY 2010-11, enhanced revenue generation would be used to fuel additional outlays on socio-economic development and social protection. Containment of current expenditure was targeted in order to keep the fiscal deficit at sustainable level. However, the government witnessed massive slippages against the budgeted current expenditure targets, making an adjustment to development spending goals.

Details of government expenditure are given below:

**Table-14: Consolidated Budgetary Position of the Government (Rs. Billion)**

	Prov.	Budget	Prov.	Budget
	Actual		Actual	
	July-June 2009-10	Estimate 2010-11	July-June 2010-11	Estimate 2011-12
<b>A. Total Revenue</b>	<b>2,078</b>	<b>2,574</b>	<b>2,261</b>	<b>2,871</b>
<b>a) Tax Revenue</b>	<b>1,473</b>	<b>1,859</b>	<b>1,707</b>	<b>2,151</b>
- Federal	1,418	1,779	1,643	2,074
<i>of which FBR Revenue</i>	1,327	1,667	1,558	1,952
- Provincial	55	80	65	77
<b>b) Non-Tax Revenue</b>	<b>605</b>	<b>716</b>	<b>554</b>	<b>719</b>
- Federal	537	616	491	642
- Provincial	68	100	62	77
<b>B. Total Expenditure</b>	<b>3,007</b>	<b>3,259</b>	<b>3,455</b>	<b>3,721</b>
<b>a) Current Expenditure</b>	<b>2,386</b>	<b>2,519</b>	<b>2,901</b>	<b>2,976</b>
- Federal	1,759	1,769	2,088	2,016
<i>of which: Interest Payments</i>	642	699	698	791
- Domestic	578	622	630	715
- Foreign	64	77	68	76
<b>Defense Expenditure</b>	<b>375</b>	<b>442</b>	<b>451</b>	<b>495</b>
- Provincial	627	750	813	960
<b>b) Development Expenditure</b>	<b>613</b>	<b>734</b>	<b>506</b>	<b>737</b>
- PSDP	518	610	462	640
Federal	259	290	216	300
of which ERRA		10	9	10
Provincial	258	340	246	340
<b>Less Operational Shortfall</b>		<b>-20</b>		
- Other Development Expenditure	96	124	45	97
<b>c) Net Lending</b>	<b>39</b>	<b>7</b>	<b>8</b>	<b>8</b>
<b>d) Unidentified Expenditure</b>	<b>-32</b>	<b>0</b>	<b>40</b>	<b>0</b>
<b>C. Overall Fiscal Balance</b>	<b>-929</b>	<b>-685</b>	<b>-1,194</b>	<b>-851</b>
- <i>As % of GDP</i>	-6.3	-4.0	-6.6	-4.0
<b>D. Financing of Fiscal Balance</b>	<b>929</b>	<b>685</b>	<b>1,194</b>	<b>851</b>
<b>a) External Sources</b>	189	186	108	135
<b>b) Domestic</b>	<b>740</b>	<b>499</b>	<b>1,087</b>	<b>716</b>
- Non-Bank	436	333	472	413
- Bank	305	167	615	304
<b>c) Privatization Proceeds</b>				
<b>E. GDP at Market Prices</b>	<b>14,837</b>	<b>16,975</b>	<b>18,063</b>	<b>21,041</b>
<b>Memo Items</b>				
<b>Revenue Balance</b>	<b>-308</b>	<b>55</b>	<b>-594*</b>	<b>-106</b>
- <i>As % of GDP</i>	-2.1	0.3	-3.3	-0.5
<b>Primary Balance</b>	<b>-286.8</b>	<b>13.6</b>	<b>-450.7*</b>	<b>-59.7</b>
- <i>As % of GDP</i>	-1.9	0.1	-2.5	-0.3

\* Adjusted for grants

Source: Budget Wing, Ministry of Finance

Total expenditure for 2010-11 approximated to Rs. 3,455 billion; Rs. 198 billion above the spending targets while the growth over the previous fiscal year remained 15 percent. A 10 percent slippage on



account of current expenditure, excluding flood relief, has been the main culprit. The outgoing fiscal year underwent a significant downward adjustment in respect of development expenditure, that was 24.3 percent lower than the budgeted estimates and 10.8 percent lower than FY2010.

### V.ii.a. Current Expenditure

For the fiscal year 2010-11, current expenditure, adjusted for one-off previous years power subsidy, over-run reached an alarming magnitude of Rs. 260 billion or 10 percent. About Rs. 2,901 billion were consumed on current spending, almost 17 percent more than the previous year. Major heads are explained as follows:

	<b>Prov.Actual July-June</b>	<b>Budget Estimate</b>	<b>Revised Estimate</b>
<b>Federal</b>	<b>2,088.1</b>	<b>1,769.1</b>	<b>2,114.4</b>
<b>General Public Service</b>	<b>1,434.0</b>	<b>1,158.9</b>	<b>1,474.1</b>
Serving of Domestic Debt	629.7	621.8	653.6
Serving of Foreign Debt	68.4	76.8	74.4
Superannuation Allowances & Pension	106.6	90.7	92.7
Grants to Others	232.1	172.8	245.9
Others General Public Services	397.1	196.9	407.4
<b>Defense Affairs and Services</b>	<b>450.6</b>	<b>442.2</b>	<b>444.6</b>
<b>Public Order and Safety Affairs</b>	<b>64.2</b>	<b>51.3</b>	<b>58.7</b>
<b>Economic Affairs</b>	<b>77.7</b>	<b>66.9</b>	<b>80.0</b>
<b>Others</b>	<b>61.6</b>	<b>49.9</b>	<b>57.0</b>
<b>Provincial</b>	<b>812.7</b>	<b>750.0</b>	<b>810.0</b>
<b>Current Expenditure</b>	<b>2,900.8</b>	<b>2,519.1</b>	<b>2,924.4</b>
<b>PSDP</b>	<b>461.5</b>	<b>610.0</b>	<b>420.9</b>
Federal	215.9	270.0	196.0
Provincial	245.6	340.0	224.9
<b>Other Development Expenditure (inclusive of floods)</b>	<b>44.6</b>	<b>123.5</b>	<b>45.5</b>
<b>Development Expenditure</b>	<b>506.1</b>	<b>733.5</b>	<b>466.5</b>
<b>Net Lending</b>	<b>7.9</b>	<b>6.6</b>	<b>-4.9</b>
<b>Total Expenditure</b>	<b>3,455.1</b>	<b>3,259.3</b>	<b>3,386.0</b>

Source: Budget Wing, Ministry of Finance

#### 1. General Public Service

Originally, expenses with regards to general public service were budgeted at Rs. 1,159 billion for FY 2010-11. However, this category ended up with an escalation to the tune of Rs. 275 billion mainly on account of poorly targeted subsidies and growing security expenditures. This also includes Rs. 120 billion unpaid power tariff differential subsidy of previous years that was paid in FY2011.

a. Interest Payments:

A major chunk of Pakistan's scarce resources are dedicated to making hefty payments in respect of debt obligations. For FY 2010-11, nearly 31 percent of total revenues have been consumed in servicing of domestic and foreign debt against a ratio of 31 percent and 33 percent in 2009-10 and 2008-09 respectively. Even though this indicator has improved in the fiscal year 2010-11, an increasing concentration of financing mix towards internal sources and higher domestic interest rates on account of tight monetary policy indicate a persistent burden of servicing expense on the government's budgetary position.

b. Grants:

During the fiscal year 2010-11, transfer by the federal government to provinces in the form of grants aggregated to Rs. 53.4 billion. When analyzing the break-up of grants provided to other institutions, it becomes clear that security related expenses in the wake of deteriorating security situation contributed a huge portion to the expenditure bottom line.

c. Subsidies:

During 2010-11, government subsidized the power sector by a large amount. Out of a total subsidy of Rs. 381 billion, Rs. 335 billion or 88 percent were granted to WAPDA/PEPCO and KESC against a budgeted target of Rs. 87 billion for the fiscal year 2010-11.

A whopping slippage of 146 percent, adjusted for one-off payment of Rs.120 billion related to previous years, in this respect underlines the absence of prominent reforms in the power sector during the previous fiscal year.

Organization	Prov.Actual July-June	Budget Estimate	Revised Estimate
Power Sector	334.8	87.3	343.1
Food & Agriculture	25.7	26.1	32.1
Oil Refineries	10.8	10.8	10.8
Others	9.3	2.5	9.8
<b>Total</b>	<b>380.6</b>	<b>126.7</b>	<b>395.8</b>

Source: Budget Wing, Ministry of Finance

Restoring fiscal sustainability will require addressing with greater vigor existing challenges in the resource-stricken power sector to reduce unnecessary and unproductive burden on government budgets. Table 16 shows a break-up of subsidies for 2009-10.

## 2. Other Current Expenditures

Defense affairs accounted for 15.5 percent of current expenditure for the fiscal year 2010-11. Rs. 64.2 billion were spent on public order and safety affairs against a budgeted estimate of Rs. 51.3 billion. Economic affairs registered Rs. 77.7 billion, an increase of 16 percent in comparison to budget.

**Table-17: Social Spending, 2010-11(Rs. Billion)**

	Prov.Actual July-June	Budget Estimate	Revised Estimate
Environment Protection	0.5	0.4	0.4
Health	8.4	7.3	7.5
Education Affairs and Services	43.9	34.5	40.3
<b>Total</b>	<b>52.8</b>	<b>42.2</b>	<b>48.2</b>
- As % of GDP	0.3	0.2	0.3

Source: Budget Wing, Ministry of Finance

On the contrary, government spending on social safety nets had been abysmally low and access to social services by the vulnerable remains a challenge. A combined total of only Rs.53 billion was incurred on education, health and environment sector. This spending translated into only 0.3 percent of GDP for FY2010-11, indicating the government's lack of attention towards targeted social transfers. Government

must ensure intergenerational equity and an adequate social safety net, and provision of public services that allow a level playing field, regardless of conditions at birth.

### V.ii.b. Development Expenditure

Development spending was contained for the fiscal year 2010-11 in relation to budgetary targets to mitigate the damage done to the fiscal account in the form of higher than projected non-development outlays.

Rs. 506 billion was spent for development purposes in FY 2010-11 in comparison to Rs. 613 billion during 2009-10. Out of it, Public Sector Development Programme (PSDP) was slashed to Rs. 462 billion as against a budgeted estimate of Rs. 610 billion, while other development expenditures summed to Rs. 45 billion and witnessed a cut of 64 percent (in comparison to budget estimates) in the fiscal year 2010-11. Among PSDP, provincial share decreased by 28 percent in comparison to budgeted outlay whereas federal portion was curtailed by a massive 20 percent in the period under review.

It is worth noting here that such a fiscal adjustment largely compromises on the development prospects

for future generation in a country like Pakistan that needs to build upon its existing social sector.

### **V.iii. Fiscal Deficit**

Adverse developments in the fiscal sector during the fiscal year 2010-11 finally culminated to a budget deficit of Rs. 1,194 billion or 6.6 percent of GDP. The weakening fiscal performance can be gauged by the fact that the fiscal balance deteriorated by a huge 100 bps against a revised target of 5.4 percent of GDP. A slippage of 1.2 percent in terms of GDP was observed in comparison to budget projections. The fiscal deficit was higher by Rs. 265 billion over the deficit recorded in 2009-10 or Rs.145 billion adjusted for one-off payment against unpaid power sector subsidies of previous years. This under-performance chiefly stemmed from a narrow tax base and the inability to tap this base fully on the revenue side, with rigid and non-priority current spending patterns taking a toll on these scarce resources.

Notwithstanding, the fiscal consolidation witnessed in 2008-09 appeared to be vanishing in last two fiscal years. Unless serious corrective measures to induce flexibility in government expenditure especially subsidies are taken, the fiscal outlook is bound to remain fragile in the near term. Similarly, enhanced revenue generation efforts need to be the top-most priority going forward.

The current trajectory of fiscal deficit is a recipe to future external account crisis and will fuel inflationary expectations in the economy as it creates demand in the system. Simultaneously, meeting the financing requirement placed by the higher deficit will limit the prospects of private sector growth and the economic benefits it brings.

### **V.iv. Financing of Fiscal Deficit**

Drying-up of external inflows exacerbated the already lackluster fiscal performance during the fiscal year 2010-11. A widening fiscal balance, was, therefore, mainly financed through domestic sources in the absence of any proceeds accruing from privatization. This avenue is costly as this borrowing is conducive to inflationary pressures and at the same time, translates into higher debt servicing in view of higher domestic interest rates. Moreover, such practice crowds out the private sector credit demands.

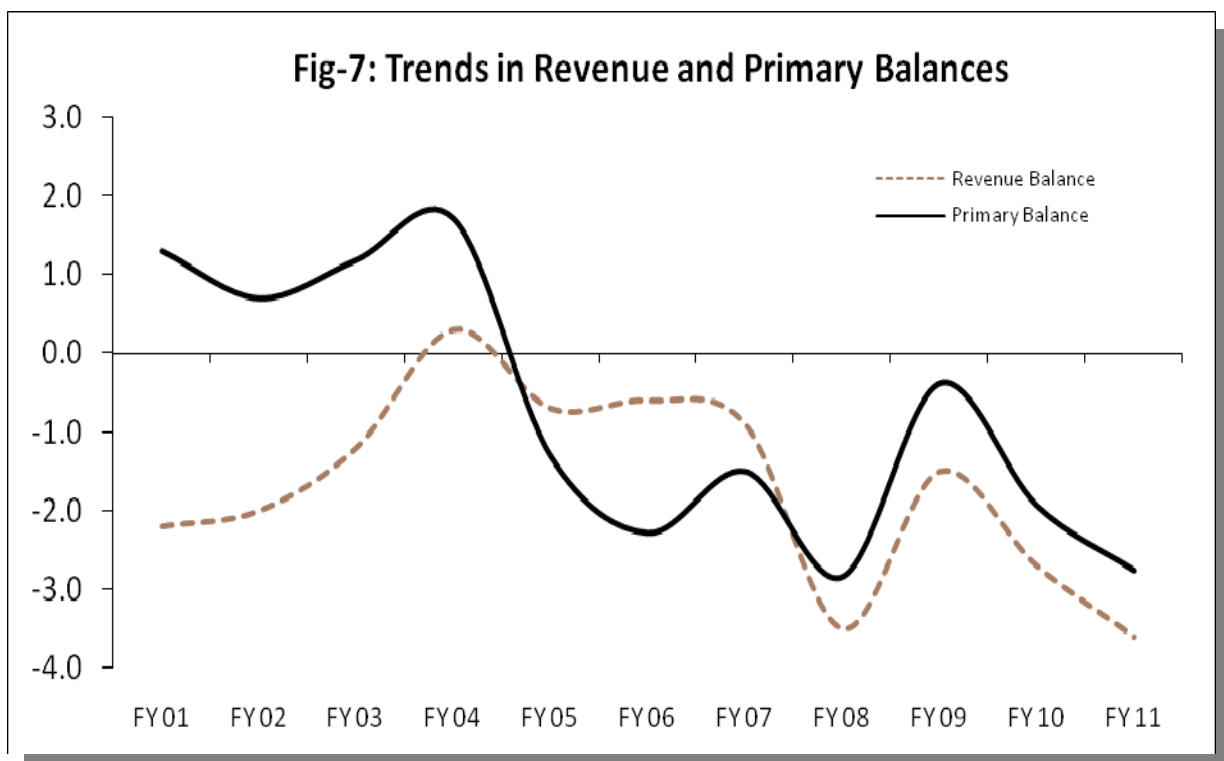
In the course of the fiscal year 2010-11, Rs. 1,086 billion was generated from internal avenues against a budgeted target of Rs. 499 billion. Bulk of the domestic financing came from Banking sources (56.6 percent of the domestic borrowing), whereas government was able to borrow the rest from non-bank sources. It is encouraging to note that government was able to retire SBP credit by Rs. 32 billion during FY2011 in line with its policy of net zero quarterly borrowing from SBP. Government was able to adhere

to this policy at the end of quarters ending in March, June and September 2011. This trend has helped reduce the inflationary pressures and allowed SBP to reduce the policy rate by 2 percent during the first half of FY2012.

The non-bank inflows amounted to Rs. 471 billion, 41.4 percent higher than the estimated magnitude. This segment of deficit financing underwent an amplification of nearly Rs. 35 billion as compared to FY 2009-10. Huge accruals in retail instruments offered by the Central Directorate of National Savings (CDNS), large issuance of Islamic Instruments (Government Ijara Sukuk) coupled with a resurgence of non-banking financial institutions’ interest in government papers were the prime reasons behind this strong growth.

**V.v. Revenue Deficit**

Revenue balance is the total revenue adjusted for current expenditure. Governments require fiscal space to spur development activities in the economy. For development spending, however, governments need to generate a revenue surplus or at least maintain revenue balance. In Pakistan, the government has not been able to achieve a zero revenue balance by June 30, 2008, a critical provision of FRDL Act 2005. In fact, the revenue deficit mushroomed to Rs. 358.2 billion or 3.5 percent of GDP during 2007-08.



While the same indicator improved sharply by 200 bps in 2008-09 over 2007-08, the fiscal year 2010-11 saw a reversal of this declining tendency and recorded a revenue deficit of 595 billion approximating to 3.3 percent of GDP. Government has not been able to achieve a surplus of 0.2 percent of GDP as envisioned in the Federal Budget 2010-11. This is an alarming situation and by no means, a sustainable scenario.

The existence of a high and persistent revenue deficit points out the government's inability in maintaining fiscal discipline and instilling austerity measures in order to curtail increasing current expenditures. Moral hazards in the form of subsidies have meant that "government is creating debt obligations for financing inefficiency in the economy"<sup>1</sup>. So far, government has been helpless in bringing current expenditures in line with the revenues. On the contrary, persistent revenue deficit implies that the borrowed money is mostly being spent on current outlays that otherwise should be available solely for development purposes. This practice needs to be put to halt by undertaking an aggressive expenditure reform action plan. At the same time, it calls for greater emphasis on exploiting other avenues in terms of resource mobilization.

#### **V.vi. Primary Deficit**

Primary balance is the total revenue adjusted for non-interest expenditure. In line with the revenue deficit, the primary deficit aggregated to Rs. 450 billion or 2.5 percent of GDP in FY 2010-11 against a budgeted target of primary surplus of Rs. 110 billion or 0.6 percent of GDP. This indicator has eroded by a large margin when compared to the FY 2009-10 position of 1.6 percent of GDP.

A negative primary balance essentially means that the government is borrowing monies to pay interest payment on the debt stock, debt trap. Action to arrest such a trend is politically difficult, but the effects of the needed measures could be phased in over time. Indeed, to the extent that long term spending trends are ameliorated by structural reforms, a smaller improvement in the primary balance could then be targeted.

### **VI. Fiscal Performance July-September 2011-12**

First quarter fiscal year 2011-12 performance is laudable as FBR managed to collect PKR 381bn (up 30% Y/Y) revenues against PKR 293bn during the same period in the corresponding year.

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<sup>1</sup> "Public Finance and Fiscal Policy", State Bank of Pakistan Annual Report FY10

<b>Table-18: Consolidated Government Budget, July-Sept 2011 (Rs. Billion)</b>		
	<b>Prov. Actual July-Sept 2010-11</b>	<b>Prov. Actual July-Sept 2011-12</b>
<b>A. Total Revenue</b>	<b>406</b>	<b>542</b>
<b>a) Tax Revenue</b>	<b>323</b>	<b>417</b>
- Federal	309	398
<i>of which FBR Revenue</i>	293	381
- Provincial	14	19
<b>b) Non-Tax Revenue</b>	<b>83</b>	<b>125</b>
- Federal	74	106
- Provincial	9	19
<b>B. Total Expenditure</b>	<b>683</b>	<b>800</b>
<b>a) Current Expenditure</b>	<b>567</b>	<b>657</b>
- Federal	419	436
<i>of which:</i> <b>Interest Payments</b>	162	177
- Domestic	147	165
- Foreign	15	12
<b>Defense Expenditure</b>	93	107
- Provincial	148	220
<b>b) Development Expenditure</b>	<b>59</b>	<b>90</b>
- PSDP	48	80
Federal	27	47
ERRA	5	1
Provincial	16	32
- Other Development Expenditure	16	10
<b>c) Net Lending</b>	<b>3</b>	<b>(1)</b>
<b>d) Unidentified Expenditure</b>	<b>53</b>	<b>55</b>
<b>C. Overall Fiscal Balance</b>	<b>(276)</b>	<b>(259)</b>
- <i>As % of GDP</i>	(1.5)	(1.2)
<b>D. Financing of Fiscal Balance</b>	<b>276</b>	<b>257</b>
<b>a) External Sources</b>	57	(4)
<b>b) Domestic</b>	219	262
- Bank	98	142
- Non-Bank	121	120
<b>c) Privatization Proceeds</b>	-	-
<b>E. GDP at Market Prices</b>	<b>18,063</b>	<b>20,905</b>
<b>Memo Items</b>		
<b>Revenue Balance</b>	<b>-160</b>	<b>-115</b>
- <i>As % of GDP</i>	-0.9	-0.5
<b>Primary Balance</b>	<b>-115</b>	<b>-73</b>
- <i>As % of GDP</i>	-0.6	-0.3

Source: FBR, Budget Wing, Ministry of Finance

The first quarter of the current fiscal year observed a budget deficit of 1.2 percent of GDP. Expenditures increased by 16.5% Y/Y during 1QFY2012, mainly driven by higher current expenditure (up 15% Y/Y). The

total amount of tax collection has now reached to PKR 417bn in the first quarter of fiscal year 2011-12 as against PKR 313bn in the corresponding period last year.

### VI.i. Tax Revenue

Recent collection of taxes by government is admirable as FBR managed to gather PKR 374bn during first quarter 2011-12 against PKR 287bn collected during the corresponding period last year. Direct taxes grew by

**Table-19: FBR Tax Collection, July-September 2011 (Rs. Billion)**

Revenue Head	Target 2011-12	July-Sept		% Change
		2010-11	2011-12	
Direct Tax	743.6	96	125	30.1
Sales Tax	836.7	134	185	38.6
Federal Excise	165.6	27	28	5.7
Customs Duty	206.4	37	43	14.4
<b>Total Collection</b>	<b>1,952</b>	<b>293</b>	<b>381</b>	<b>29.7</b>

Source: FBR

35.2%, customs by 16.3%, FED by 18.5% and most notable increase was seen in sales tax which grew by 32.5% during first quarter fiscal year 2011-12. Despite shifting of GST collection on certain service to the provinces, total collection grew by 30% during first quarter fiscal year 2011-12.

### VI.ii. Non Tax Revenue

Non tax revenue also posted a healthy growth of 42% Y/Y during first quarter fiscal year 2011-12. Major contributions came from SBP profits and dividends. SBP continues to remain a major contributor in non tax revenues.

SBP profits reached PKR 54bn during first quarter 2011-12 against PKR 40bn in the corresponding period last year.

Dividends increased by PKR 12.5bn

**Table-20: Non-Tax Revenue, July-Sept 2011 (Rs. Billion)**

	Prov. Actual July-Sept 2010-11	Prov. Actual July-Sept 2011-12
<b>Non-Tax Revenue</b>	<b>78</b>	<b>110</b>
Interest (PSEs & Others)	4.4	5.0
Dividend	0.5	13.0
SBP Profit	40.0	54.0
Defence	1.4	1.8
Citizenship, Naturalization & Passport Fee	2.1	1.9
Development Surcharge on Gas	5.0	5.7
Discount Retained on Crude Oil	3.0	4.3
Royalty on Oil/Gas	19.6	15.0
Others	2.4	9.1

Source: Budget Wing, Ministry of Finance

in first quarter fiscal year 2011-12 against last year small dividends of PKR 500mn during 1QFY2011 owing to higher corporate profitability. Government is now taking important measures for the issuance



of 3G license to Pakistani telecom sector which is likely to generate revenue of around USD 800mn during this fiscal year.

### **VI.iii. Expenditure**

Current expenditure slippages continue to burden limited resources of the country. Current expenditure soared by 15% during first quarter fiscal year 2011-12. Current spending was PKR 657bn in July-September 2011 with interest payments of PKR 177bn. Continued subsidies remain a major drain on financial resources, during first quarter fiscal year 2012, PKR 32bn were spent on subsidies with PKR 26bn amount coming from power sector subsidies. Major heads of expenditure have increased during first three month of fiscal year 2012. Meanwhile on the positive front, spending in PSDP increased by 167% to reach at PKR 80bn during first quarter fiscal year 2011-12 against PKR 48bn during the corresponding period last year.

Government has initiated reforms for tightening of expenditures along with effective management of financial resources. It remains an uphill task in the presences of tariff anomalies, inefficient operations of public utilities and misallocation of natural resources. With limited options available to the government, painful policy options of structural changes need to be adopted in order to create fiscal space for social and developmental expenditures.

### **VI.iv. Fiscal, Revenue and Primary Deficit**

A budgeted deficit of PKR 257bn was recorded in first quarter fiscal year 2011-12 against a deficit of PKR 276bn in the corresponding period last year. Fiscal deficit for first quarter of current fiscal year stood at 1.2% of GDP. This improvement in fiscal balance should be interpreted with caution as conversion of power holding TFC are yet to show their effect on fiscal balance.

Revenue deficit improved to PKR 115bn or 0.6% of GDP during first three months of current fiscal year against revenue deficit of PKR 161bn or 0.9% of GDP in the same period last year. Similarly primary deficit also showed improvement as it reached to PKR 82bn in 1QFY2012 against PKR 114bn in 1QFY2011. Improvements in these fiscal indicators are commendable, showing governments desire to improve spending patterns along with increased revenue collection. On the back of improved tax collection, the government now needs to push for greater tax and structural reforms.

### **VI.v. Financing of Fiscal Deficit**

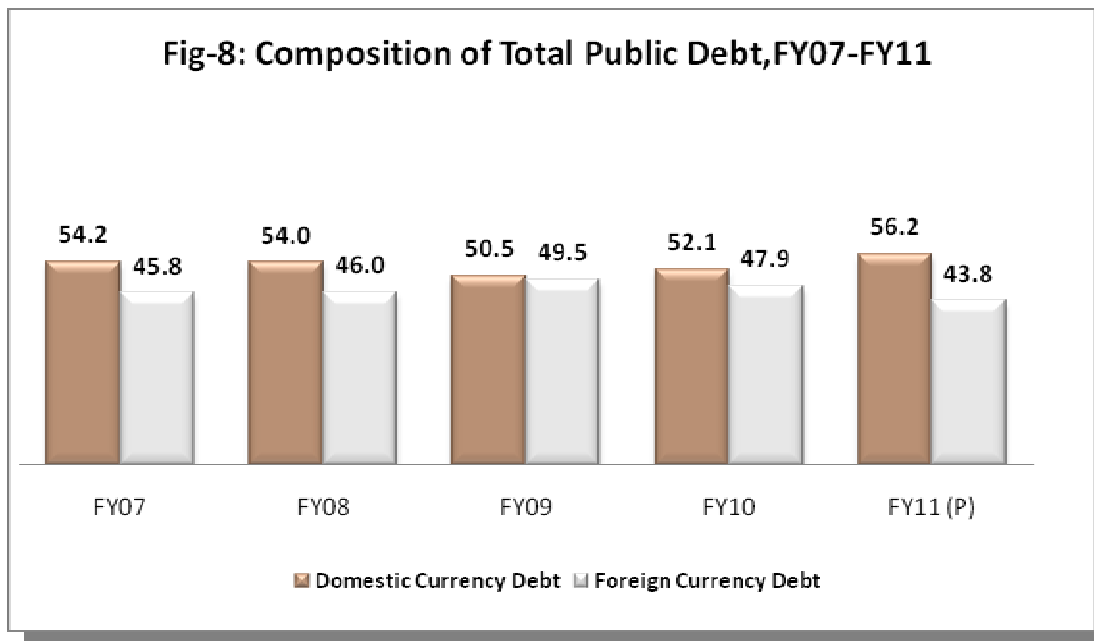
With external inflows drying out, government reliance on domestic avenues for budgetary support has greatly increased. During the first three months of fiscal year 2012, no external sources were used for budgetary support and the onus felt on domestic borrowings. More importantly, banks remained the major source for financing. Total domestic borrowing for first quarter fiscal year 2011-12 stood at PKR 261bn, 45% of this borrowing was met from banks while the rest of 55% was met from non-bank sources. This financing mix has dramatically changed as during first quarter of fiscal year of 2010-11, borrowing from banks stood at 55%, while non banks sources contributed 45% of domestic sources. Increasing reliance on banks is not an applaud able policy, because it results in crowding-out of private sector credit. The impact of crowding-out of private sector credit will be more severe once private sector credit demand restores.

### **VII. Review of Public Debt**

Pakistan entered the 21 Century with serious financial constraints; public debt was as high as 83 percent of its GDP at the end of FY2001. Pakistan's economy has experienced a turnaround since 2000, growth has accelerated, and most macroeconomic indicators have improved. Public debt indicators have also shown significant improvement. Modest growth in public debt, coupled with the strong growth in nominal GDP, led to a significant reduction in public debt to GDP ratio, from 79% in fiscal year 2001-02 to 55.4 percent by the end of FY2007. However since FY07, fiscal policy became subservient to political exigencies as government extended whole-sale subsidies on oil, electricity, food and fertilizer to protect the more vulnerable sections of the society from the effects of global commodity shock. Higher security related expenditures supplemented by policy inaction on key expenditures plus increased expenditures due to natural disasters led to rapid escalation of Total Public Debt as a percentage of GDP, reaching 60 percent by the end of FY2010. However, the same was 59.3 percent at the end of fiscal year 2011; this would have been 58.2 percent had the government not maintained credit balance with SBP on June 30, 2011.

The total public debt stood at Rs.10.709 billion as at June 30, 2011, an increase of Rs.1.788 billion or 20 percent higher than the debt stock at the end of last fiscal year. Government borrowed Rs.1.086 billion from domestic sources and Rs.62 billion from external sources to finance the fiscal operations. Approximately, US\$ 3.3 billion were added to the external debt stock owing to depreciation of US Dollar against other major international currencies and around Rs.27 billion were added by depreciation of Pak

Rupee against US Dollar by meagre 0.6 percent. In May 2011, government paid Rs. 120 billion against the un-paid tariff differential subsidy of past years to PEPCO.



Developments in TPD during 2010-11 have been driven mainly by a combination of five distinct factors. Increased demands on the government budget during 2010-11 for purposes of security meant that expenditure was fairly rigid even in the face of a committed effort to rationalize expenditure and curtail the fiscal deficit. Secondly, lower than expected GDP growth, acute energy shortages, and a high cost of doing business led to a revenue shortfall, situation was further complicated by the devastating floods that put additional burden on fiscal operations. Higher international prices for textile products had a positive impact on Pakistan’s trade balance. In addition to these external developments, import compression measures restricted the import bill significantly despite higher oil prices and shift of power generation mix towards furnace oil.

Slippages in both revenues and expenditures led to FY2011 budget deficit missing the target. Gross revenue collection (tax and non-tax) was 12.1% lower than the budgeted target while total expenditures (current and development), adjusted for one off payment of energy subsidies pertaining to previous years, were 2.4% higher than budgetary estimates. FBR tax collection fell 6.4% short of target while non-tax revenues were 23.6% less than target due to non-realization of expected 3G license receipts and lower logistical support receipts from the US. On the other hand, expenditure exceeded the target due

to higher subsidies and flood related spending despite PSDP spending being 24% lower than the budgeted target.

The primary source of increase in public debt during 2010-11 has been a rapid increase in local currency component that accounted for almost 76 percent of the total increase in TPD. The main reasons for this shift in borrowing were the non-materialization of privatization proceeds, slow disbursement from multilateral and bilateral donors, and higher than budgeted fiscal deficit.

The external debt component grew by Rs. 424 billion or 24 percent due to increased foreign public debt inflows on the one hand, and depreciation of US dollar against other major currencies on the other hand. Rupee lost approximately 0.6 percent of its value against the US dollar during 2010-11. Depreciation of the US Dollar against other major currencies caused the foreign currency component of public debt to increase by approximately US \$3,300 million. This capital loss on foreign currency debt, however, is mitigated by the strong concessionality element associated with Pakistan's external loans. The impact of any currency shock should not be looked at in isolation, but rather be analyzed in the context of interest rate differential.

**Table-21: Public Debt, FY07-FY12\***

	FY07	FY08	FY09	FY10	FY11(P)	FY12*
	(In billions of Rs.)					
Domestic Currency Debt	2,601	3,266	3,852	4,651	6,014	6,223
Foreign Currency Debt	2,201	2,778	3,776	4,270	4,694	4,773
<b>Total Public Debt</b>	<b>4,802</b>	<b>6,044</b>	<b>7,629</b>	<b>8,921</b>	<b>10,708</b>	<b>10,996</b>
	(In percent of GDP)					
Domestic Currency Debt	30.0	31.9	30.3	31.3	33.3	29.8
Foreign Currency Debt	25.4	27.1	29.7	28.8	26.0	22.8
<b>Total Public Debt</b>	<b>55.4</b>	<b>59.0</b>	<b>60.0</b>	<b>60.1</b>	<b>59.3</b>	<b>52.6</b>
	(In percent of Revenue)					
Domestic Currency Debt	200	218	208	224	266	250
Foreign Currency Debt	170	185	204	205	208	192
<b>Total Public Debt</b>	<b>370</b>	<b>403</b>	<b>412</b>	<b>429</b>	<b>474</b>	<b>442</b>
	(In percent of Total Debt)					
Domestic Currency Debt	54.2	54.0	50.5	52.1	56.2	56.6
Foreign Currency Debt	45.8	46.0	49.5	47.9	43.8	43.4
<b>Memo:</b>						
Foreign Currency Debt (in US\$ Billion)	36.4	40.7	46.4	50.0	54.6	54.6
Exchange Rate (Rs./US\$, E.O.P)	60.4	68.3	81.4	85.5	86.0	87.5
GDP (in Rs. Billion)	8,673	10,243	12,724	14,837	18,063	20,905
Total Revenue (in Rs. Billion)	1,298	1,499	1,851	2,078	2,261	2,485

P : Provincial

\*end-September 2011

Source: EAD, SBP, Budget Wing, MoF and DPCO staff calculations

TPD stood at Rs. 10,996 billion at the end of first quarter FY2012, registering an increase of Rs. 287 billion or 2.7 percent in first three months of the current fiscal year. During the first quarter FY2012, US \$ appreciated against other major currencies and registered a meagre capital gain of approximately US \$ 50 million, however Pak Rupee lost its value against US Dollar by 1.7%. Government was able to contain the fiscal deficit for the first quarter at 1.2 percent of GDP against 1.6 percent in same period last fiscal year that helped restricted the growth in public debt.

A significant positive masked by overall weak fiscal numbers is the distinct uptrend in FBR tax collection since 4QFY2011. Helped by withdrawal of GST exemption on several sectors and levy of one-off flood surcharge, FBR tax collection grew by 28.4% in 4QFY2011. However, the trend has continued into FY2012 with FBR tax collection increasing by 21% during Jul-Dec'2011 despite shifting of GST collection on certain service to the provinces.

### VIII. Servicing of Public Debt

Increases in the outstanding stock of Total Public Debt have implications for the economy in the shape of a greater amount of resource allocation towards debt servicing in the future. In order to meet debt servicing obligations, an extra burden is placed on limited government resources and might have costs in the shape of foregone public investment or expenditure in other sectors of the economy.

**Table-22: Public Debt Servicing, 2010-11**

	Budgeted (in billions of Rs.)	Actual	% of Govt Revenues	% of Current Expenditure
Servicing of Foreign Debt	76.8	68.4	3.0	2.4
Repayment of Foreign Loans	174.4	154.2	6.8	5.3
Servicing of Domestic Debt	621.8	629.7	27.9	21.7
<b>Servicing of Public Debt</b>	<b>872.9</b>	<b>852.2</b>	<b>37.7</b>	<b>29.4</b>

Source: DPCO staff calculations

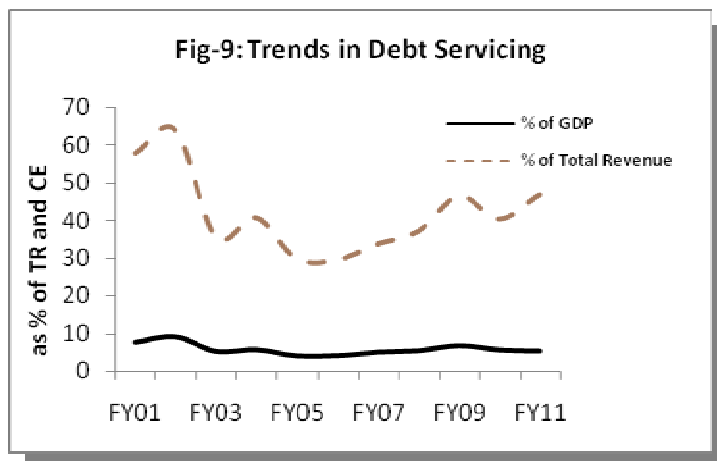
During the year 2010-11, servicing of public debt amounted to Rs 852.2 billion as opposed to a budgeted amount of Rs 872.9 billion (See Table 22). The saving of Rs 20.7 billion has mostly been due to stable dollar rupee parity, which reduced the amount used for interest and principal repayments of foreign loans in rupee terms. Repayment of foreign loans stood at Rs 154.2 billion as opposed to a target of Rs 174.4 billion; while interest payments on foreign loans, which were budgeted at Rs 76.8 billion, reached to Rs 68.4 billion by end-June 2011. An amount of Rs 629.7 billion was spent on account of servicing of domestic debt against the budgeted estimate of Rs 621.8 billion. The increase in domestic debt servicing

is partly the result of a tight monetary stance taken in order to arrest the monetary overhang caused by previous policies.

The increase in the total public debt has implications for the economy in the form of increased debt servicing in the future.

In order to meet these obligations an

additional burden is placed on the limited resources of the government which may result in extraction of resources from the developmental programmes and hence hamper growth.



## IX. Economic Reforms

The Government has continued to strengthen the process of structural reforms in the economy focusing on power sector and three key Public Sector Enterprises (PSEs). Implementation of Power Sector Reform Plan 2010 has been expedited and upgraded under the Power Sector Recovery Plan 2011. Dissolution of PEPCO was completed on 30<sup>th</sup> October, 2011 with transfer of operational functions to National Transmission & Dispatch Company (NTDC) and Central Power Purchase Authority (CPPA). CPPA has been operationalized and Board of Directors (BODs) for all nine distribution companies (DISCOs) and GENCO Holding Company have been reconstituted and professional management is being inducted.

The timely payment of subsidy and improvement in recovery for public and private sector has resulted in improvement in liquidity. Private sector running defaulters have been reduced. Load Management and conservation measures to save about 1000MW are under implementation.

Board of Directors of **Pakistan Steel Mills (PSM)** has been strengthened and implementation of a Business Plan for revitalization of PSM approved by Cabinet has started. A restructuring framework for **Pakistan Railways** has been operationalized. Freight operations and route rationalization is being pursued. Under the financial restructuring plan, commercial borrowing has been obtained to repair 96 locomotives. Restructuring plan for **Pakistan International Airlines** has been finalized which addresses corporate governance, human resource rationalization, financial and operational restructuring, engineering improvement, procurement and logistics, marketing and fleet, airport services and dispatch reliability.

Government's efforts have resulted in relative stability in these key sectors and fiscal discipline is being maintained. The focus remains on improving overall corporate governance, curtailing haemorrhaging, improving service delivery and reducing fiscal burden and moving to a structural surplus and increased public sector savings.

## X. Report on Compliance with FRDL Act 2005

The Fiscal Responsibility and Debt Limitation (FRDL) Act, 2005 was approved on 13 June 2005. The FRDL Act, 2005 requires that the federal government take measures to reduce total public debt and maintain it within prudent limits thereof. The following sections identifies the various limits prescribed by the FRDL Act 2005 and reports on progress thereof.

The FRDL Act 2005 requires the following:

***(1) Reducing the revenue deficit to nil not later than the thirtieth June, 2008 and thereafter maintaining a revenue surplus***

As of June 30, 2011, the revenue deficit approximated to Rs. 595 billion or 3.3 percent of GDP.

	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11
Revenue Balance	-1.5%	0.3%	0.5%	1.0%	-0.6%	-3.2%	-1.2%	-2.4%	-3.3%

***(2) Ensure "that within a period of ten financial year, beginning from the first July, 2003 and ending on thirtieth June, 2013, the total public debt at the end of the tenth financial year does not exceed sixty percent of the estimated gross domestic product for that year and thereafter maintaining the total public debt below sixty percent of gross domestic product for any given year."***

As of 30<sup>th</sup> June 2011, the total public debt stood at 59.3 percent of GDP. It must be noted here that the limit of 60 percent of total public debt-to-GDP is applicable from the fiscal year 2012-13 onwards.

	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11
	(Rs. Billion)								
Domestic Currency Debt	1,852	1,995	2152	2322	2601	3266	3852	4651	6015
Foreign Currency Debt	1,771	1,816	1,913	2,038	2201	2778	3776	4270	4694

Total Public Debt	3,623	3,810	4,065	4,359	4,802	6,044	7,629	8,921	10,709
GDP	4,876	5,641	6,500	7,623	8,673	10,243	12,724	14,837	18,063
Total Public Debt (as % of GDP)	74.3	67.6	62.5	57.2	55.4	59.0	60.0	60.1	59.3

**(3) Ensure “that in every financial year, beginning from the first July, 2003, and ending on the thirtieth June 2013, the total public debt is reduced by no less than two and a half percent of the estimated gross domestic product for any given year, provided that social and poverty alleviation related expenditures are not reduced below 4.5 percent of the estimated gross domestic product for any given year and budgetary allocation to education and health, will be doubled from the existing level in terms of percentage of gross domestic product during the next ten years.”**

During the fiscal year 2010-11, the Debt to GDP ratio was reduced by 0.8 percent. Social and poverty alleviation related expenditure (as given by pro-poor budgetary expenditure excluding non-development outlays on law and order) remained at 6.9 percent of GDP in 2010-11. Additionally, expenditure on health and education in 2010-11 amounted to 0.6 percent and 1.8 percent of GDP respectively.

	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11
Social sector and poverty related expenditure (as % of GDP)	3.6	3.9	4.2	4.9	4.9	9.3	6.9	6.7	6.9
Expenditure on education (as % of GDP)	1.6	1.7	1.8	1.9	1.9	1.8	1.9	1.8	1.8
Expenditure on health (as % of GDP)	0.5	0.5	0.5	0.5	0.6	0.6	0.7	0.8	0.6

**(4) Not issue “new guarantees, including those for rupee lending, bonds, rates of return, output purchase agreements and all other claims and commitments that may be prescribed, from time to time, for any amount exceeding two percent of the estimated gross domestic product in any financial year: Provided that the renewal of existing guarantees shall be considered as issuing a new guarantee.”**

New guarantees issued by the government in 2010-11 amounted to Rs. 62.4 billion or 0.35 percent of GDP. The government also issued letter of comfort equivalent to 0.5 percent of GDP against commodity finance.



Since last few years Pakistan is faced with serious challenges both at domestic and international fronts. Serious internal security situation, energy shortages, severe floods and rising inflation combined with global economic & credit crises and higher commodity prices have all put enormous pressure on government's limited fiscal resources. Given the severity of these constraints the government has been able to manage the fiscal deficits at reasonable levels though was unable to fully comply with some provisions of FRDLA 2005. However, the government remains fully committed to adhere to all the provisions of FRDLA 2005 in future.

### **XI. Concluding Remarks**

Pakistan's fiscal deficit increased to 6.6 percent of GDP in FY2010-11 against the budgeted target of 4.0 percent whereas fiscal deficit for FY2009-10 was 6.3 percent. Lower revenue collection and higher than budgeted expenditure on security and subsidies were the main reasons for this undesirable increase in fiscal deficit. Reported deficit figure for FY2011 include payment amounting 0.7 percent of GDP representing cost of energy subsidies relating to previous years, the adjusted fiscal deficit is 0.4 percent lower compare to last fiscal year. This fiscal adjustment is commendable in light of loss of revenue, lower GDP growth and cost incurred owing to floods in Sindh.

Generating revenues from taxation remains an uphill task as it was seen in recent trend where tax to GDP ratio fell from 10% in FY2010 to 9.5% in FY2011. During FY2010, real growth in tax revenue saw a healthy increase of 11.1%; however, in FY2011 real growth in tax revenue dramatically fell by 4.5%. Double digit inflation coupled with anemic growth contributed towards dismal real tax revenue growth. Total real revenue collection also suffered from the same hurdles as it posted a negative growth of 8.4% during FY2011. Furthermore, real growth of -3.2 percent in expenditure has been higher than the real growth of revenues which has had significant consequences for the fiscal deficit. Persistent divergence between growth of revenues and expenditure has led to escalating revenue deficit to the tune of 3.3 percent of GDP. The primary balance also remains in deficit by 2.5 percent of GDP. Going forward, significant growth in real revenues is essential to maintain fiscal sustainability, and to finance the government's economic plans.

The implementation of the government's recovery efforts and gradual resurgence of economic stability has been remarkable. However, in the course of the recent economic performance, a few key issues have emerged. Firstly, the importance of addressing key structural issues during times of relative fiscal soundness has been highlighted. While giving due credit to the government's crisis management efforts,

it must be noted that had there been an implementation of resource management and revenue generation efforts in periods of relative stability. By shifting from a reactionary stance to reform and efficiency oriented resource management policies, the government will be able to rid the system of the inefficiencies that are painfully brought to the surface in times of crisis.

Secondly, emphasis must be placed on revenue generation, instead of adjustments made through cuts in expenditure. Inability to translate relative economic prosperity into a structural advancement of revenue generation has meant that fiscal adjustments have been made by reduction in outlays, which hampers future prospects and might have dire consequences for socio-economic development. Changes in the tax structure to include major sectors of the economy that have so far not matched their contribution to economic growth by a proportionate increase in tax revenue will be a significant step in this regard.

A considerable drain on government resources has been an increasing burden of contingent liabilities in order to cover the losses incurred by public sector enterprises (PSEs). Accordingly, the contingent responsibility of the government has, most of the times, transformed to a reality as these bodies lacked the capacity to service their obligations. In order to allow efficient fiscal adjustments, the root cause of these public sector entities' losses must be tackled by comprehensive restructuring and introduction of corporate management structures, rather than absorbing their liabilities into the government budget.

It was for the first time after fiscal year 2003-04 that Pakistan managed to post a current account surplus. External account is a vital part of any economy; however the factors affecting it are mainly exogenous, apart from structural discrepancies. There is a need to strengthen the external account by promoting positive trade balance especially in the coming years as ceasing of IMF inflows coupled with increasing oil and other commodity prices will continue to put pressure on the current account. Government needs to take proactive measures to combat this. On top of it, there's a strong need to promote non debt creating foreign inflows to decrease the dependence on external loans.

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