Chapter 09

Public Debt

9.1 Introduction

Developing countries like Pakistan need to borrow in order to facilitate their development process. Prudent utilization of debt leads to higher economic growth and helps the government to accomplish its social and developmental goals. On the other hand, unsustainable level of debt coupled with absence of prudent debt management may dampen economic growth by lowering the development expenditure owing to heavy debt servicing requirements. This intricate scenario calls for a comprehensive and prudent debt management strategy which is instrumental in ensuring financial sustainability by mitigating the risks of refinancing, exchange rate fluctuations and debt accumulation.

Government is taking steps to reduce the debt burden of the country. To place the debt-to-GDP ratio on a firm downward trajectory and bolster macroeconomic stability, the government has made amendments to the Fiscal Responsibility and Debt Limitation (FRDL) Act by defining the ceiling for the Federal Government budget deficit at 4 percent of GDP (excluding foreign grants) during the period 2017-18 to 2019-20 and 3.5 percent of GDP thereafter. Public debt shall be reduced to 60 percent of estimated GDP until 2017-18, and thereafter a 15-year transition has been set towards a debt-to-GDP ratio of 50 percent.

Pakistan's public debt dynamics witnessed various positive developments during first nine months of current fiscal year. Some positive developments are as follow:

- Government continued to adhere to the targets set forth in Medium Term Debt Management Strategy (MTDS) to ensure public debt sustainability;
- Weighted average interest rate on the domestic debt portfolio has been further reduced while cost of external debt contracted by the government is not only economical but is also dominated by long term funding;
- Government successfully issued a 5-year US$ 1,000 million Sukuk at the lowest ever rate of 5.5 percent in international capital market;
- In order to facilitate the investors of Central Directorate of National Savings (CDNS), CDNS has been allowed direct membership of Clearinghouse. Accordingly, CDNS became only non-banking member of National Institutional Facilitation Technologies (Pvt.) Limited (NIFT);
- Government launched first-ever registered premium prize bond which is only issued in investors' names with unique features of both the profits paid biannually and the prize money through quarterly draws.

9.2 Public Debt

The portion of total debt which has a direct charge on government revenues as well as the debt obtained from the IMF is defined as public debt. Public debt has two main components, namely domestic debt (which is incurred principally to finance fiscal deficit) and external debt (which is raised primarily to finance development expenditure and balance of payment support).

Gross public debt was Rs.20,873 billion as at end March 2017 while net public debt was Rs.18,893 billion. Gross public debt recorded an increase of Rs.1,194 billion during first nine months of current fiscal year. Out of this total increase, increase in domestic debt was Rs.1,121 billion while government borrowing from domestic sources for financing of fiscal deficit was Rs.1,018 billion. This differential is mainly attributed to increase in government credit balances with the banking system. Similarly, increase in external debt contributed Rs.73 billion in public debt. Revaluation gain on account of appreciation of US Dollar against other foreign currencies reduced the impact of net external inflows on external public debt portfolio. The trend in public debt since 1971 is depicted in Box-1.

Box-1 - Trend in Public Debt

Table-9.1: Year Wise Public Debt Position

Year	Domestic Debt	External Debt	Public Debt	Year	Domestic Debt	External Debt	Public Debt	Year	Domestic Debt	External Debt	Public Debt
(Rs. in billion)											
FY71	14	16	30	**FY87**	248	209	458	**FY03**	1,895	1,800	3,694
FY72	17	38	55	**FY88**	290	233	523	**FY04**	2,028	1,839	3,866
FY73	20	40	60	**FY89**	333	300	634	**FY05**	2,178	2,034	4,211
FY74	19	44	62	**FY90**	381	330	711	**FY06**	2,322	2,038	4,359
FY75	23	48	70	**FY91**	448	377	825	**FY07**	2,601	2,201	4,802
FY76	28	57	85	**FY92**	532	437	969	**FY08**	3,275	2,852	6,126
FY77	34	63	97	**FY93**	617	519	1,135	**FY09**	3,860	3,871	7,731
FY78	41	71	112	**FY94**	716	624	1,340	**FY10**	4,654	4,352	9,006
FY79	52	77	130	**FY95**	809	688	1,497	**FY11**	6,017	4,750	10,767
FY80	60	86	146	**FY96**	920	784	1,704	**FY12**	7,638	5,057	12,695
FY81	58	87	145	**FY97**	1,056	939	1,995	**FY13**	9,522	4,797	14,318
FY82	81	107	189	**FY98**	1,199	1,193	2,392	**FY14**	10,920	5,071	15,991
FY83	104	123	227	**FY99**	1,389	1,557	2,946	**FY15**	12,199	5,182	17,381
FY84	125	132	257	**FY00**	1,645	1,527	3,172	**FY16**	13,627	6,051	19,678
FY85	153	156	309	**FY01**	1,799	1,885	3,684	**FY17 (Mar)**	14,748	6,124	20,873
FY86	203	187	390	**FY02**	1,775	1,862	3,636				

Fig-9.1: Trend in Domestic and External Debt
(Rs. in biliion)

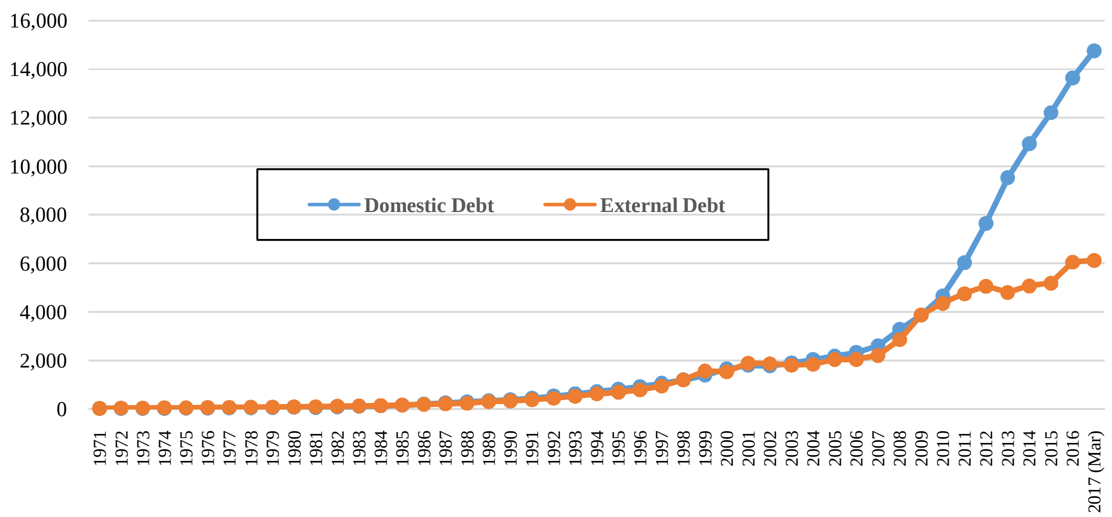


Table-9.2: Public Debt							
	2011	**2012**	**2013**	**2014**	**2015(P)**	**2016(P)**	**2017(P)***
(Rs. in billion)							
Gross Domestic Debt	6,016.7	7,638.1	9,521.9	10,920.0	12,198.9	13,626.9	14,748.1
*Net Domestic Debt	5,173.5	6,831.6	8,686.2	9,551.3	10,804.8	11,773.5	12,768.2
External Debt	4,750.2	5,057.2	4,796.5	5,071.5	5,181.8	6,051.1	6,124.4
Gross Public Debt	10,766.9	12,695.3	14,318.4	15,991.5	17,380.7	19,678.1	20,872.5
***Net Public Debt**	9,923.6	11,888.8	13,482.7	14,622.8	15,986.6	17,824.6	18,892.6
(In percent of GDP)							
Gross Domestic Debt	32.9	38.1	42.5	43.4	44.5	46.8	46.3
*Net Domestic Debt	28.3	34.1	38.8	37.9	39.4	40.5	40.1
External Debt	26.0	25.2	21.4	20.1	18.9	20.8	19.2
Gross Public Debt	58.9	63.3	64.0	63.5	63.3	67.6	65.5
***Net Public Debt**	54.3	59.3	60.2	58.1	58.3	61.2	59.3
Memo:							
Foreign Currency Debt (US$ in billion)	55.3	53.5	48.1	51.3	50.9	57.7	58.4
Exchange Rate (Rs./US$, End of Period)	86.0	94.5	99.7	98.8	101.8	104.8	104.8
GDP[(b)] (Rs. in billion)	18,276.4	20,046.5	22,385.7	25,168.8	27,443.0	29,102.6	31,862.2

*Net of government deposits with the banking system
P: Provisional *end-March, 2017
Source: State Bank of Pakistan, Economic Affairs Division, Budget Wing and Debt Policy Coordination Office

The average cost of gross public debt was reduced by 40 basis points during first six months of current fiscal year owing to smooth execution of the MTDS. The average cost of domestic debt portfolio was reduced by over 50 basis points during first six months of current fiscal year while the average cost of external loans obtained by the present government comes to around 3 percent which is significantly lower than the domestic financing cost even after a margin of capital loss due to exchange rate depreciation is added.

Government was able to mobilize external inflows from multilateral and bilateral development partners and continued its presence in international capital markets through the issuance of Sukuk during first nine months of current fiscal year. An improvement was observed in most of the public debt risks indicators during last three and half years in-line with the objectives set forth in Pakistan's first MTDS (2013). Refinancing risk of the domestic debt portfolio reduced through lengthening of the maturity profile as percentage of domestic debt maturing in one year was reduced to 52.7 percent at the end of December 2016 compared with 64.2 percent at the end of June 2013. Exposure to interest rate risk was also reduced as the percentage of debt re-fixing in one year decreased to 45.5 percent at the end of December 2016 compared to 52.4 percent at the end of June 2013. Similarly, share of external loans maturing within one year was equal to around 31.9 percent of official liquid reserves at the end of December 2016 as compared with around 68.5 percent at the end of June 2013 indicating improvement in foreign exchange stability and repayment capacity.

The public debt analysis may be incomplete without reporting contingent liabilities. Contingent liabilities are not added to the overall debt of the country, therefore, public disclosure of information about guarantees is an essential component of fiscal transparency. Contingent liabilities of Pakistan are guarantees issued to Public Sector Enterprises (PSEs). During first half of current fiscal year, the government issued fresh/rollover guarantees aggregating to Rs.368 billion or 1.2 percent of GDP. The outstanding stock of government guarantees as at end December 2016 was recorded at Rs.838 billion.

9.3 Public Debt Risks Indicators

It is imperative to have a comprehensive debt management strategy aiming at debt sustainability and enhancing the debt servicing capacity of the country. Owing to its vital importance and indispensable nature, the government updated its MTDS (2015/16-2018/19) which contains a policy advice on an appropriate mix of financing from different sources with the spirit to uphold the integrity of the Fiscal Responsibility and Debt Limitation Act. In accordance with the approved strategy, the government was required to lengthen the maturity profile of its domestic debt and mobilize sufficient external inflows in the medium term.

The public debt risk indicators are on track to achieve the targets set under MTDS. Refinancing, interest rate and foreign currency risks of public debt portfolio have been significantly reduced as at end December, 2016 as compared with end June, 2013.

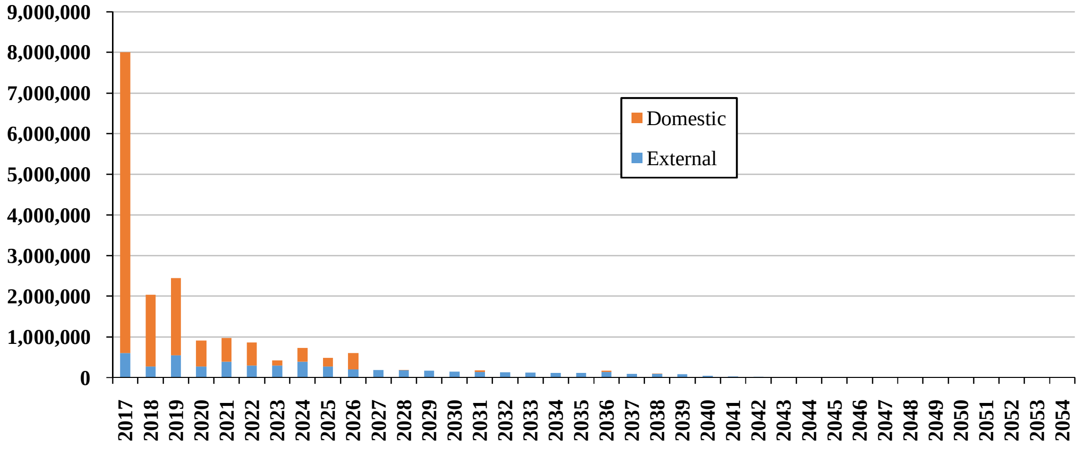
Table-9.3: Public Debt Risk Indicators

Risk Indicators		Indicative Ranges (MTDS 2015/16 - 2018/19)	Domestic Debt	External Debt	Public Debt
			End-December 2016		
FX risk	FX debt (% of total debt)	20% (minimum) and 35%	*	27.8	*
	ST FX debt (% of official liquid reserves)	*	*	31.9	*
Interest rate risk	Debt Re-fixing in 1yr (% of total)	50% and 65% (maximum) - DD 40% and 55% (maximum) -PD	53.6	24.6	45.5
	Fixed rate debt (% of total)	*	54.3	81.5	61.9
	Average Time to Re-fixing (years)	1.5 (minimum) and 2.5 - DD 3.0 (minimum) and 4.5 – PD	2.1	7.8	3.7
Refinancing risk	Debt maturing in 1yr (% of total)	50% and 65% (maximum) - DD 35% and 50% (maximum) -PD	52.7	11.3	41.2
	Average Time to Maturity (years)	1.5 (minimum) and 2.5 - DD 3.0 (minimum) and 4.5 – PD	2.1	8.5	3.9

*** Not Applicable DD: Domestic Debt PD: Public Debt**
Source: Debt Policy Coordination Office, Ministry of Finance

The refinancing risk of the domestic debt was reduced at the end of December 2016 as domestic debt maturing in one year reduced to 52.7 percent as compared with 64.2 percent at the end of 2012-13. This improvement has contributed towards increase in average time to maturity of domestic debt to 2.1 years at the end of December 2016 as compared with 1.8 years at the end of 2012-13. However, average time to maturity of external debt decreased to 8.5 years at the end of December 2016 as compared with 10.1 years at the end of 2012-13. This reduction in average time to maturity of external debt may be mainly attributed to running off the existing long term external debt portfolio over the last three and half years. The redemption profile of domestic and external debt as at end December 2016 is shown in the graph below:

Fig-9.2: Redemption Profile of Public Debt
(Rs. in million) - As at end December 2016



Government has been able to reduce refinancing risk of its domestic debt as compared with end June 2013, still concentration of repayments over the short term are evident in the redemption profile. Government is making concerted efforts to further reduce the refinancing risk of its domestic debt portfolio through more mobilization in the form of medium to long term domestic debt instruments.

Exposure to interest rate risk reduced as percentage of debt re-fixing in one year decreased to 45.5 percent at the end of December 2016 as compared with 52.4 percent at the end of 2012-13. Average time to re-fixing decreased to 3.7 years at the end of December 2016 as compared with 4.2 years at the end of 2012-13. Fixed rate debt as a percentage of total debt increased to 61.9 percent at the end of December 2016 as compared with 54 percent at the end of 2012-13 indicating reduced exposure to interest rate changes.

Around 27.8 percent of total public debt stock was denominated in foreign currency as at end December 2016. Currency wise composition of public debt portfolio is depicted through table below:

Table-9.4: Currency Wise Public Debt[(a)] (in US$)

Currencies	Percentage
Pak Rupee	72.2
US Dollar	12.6
Special Drawing Right	8.6
Japanese Yen	4.5
Euro	2.1
Total	**100.0**

[(a)] As per modalities of MTDS

The improvement in foreign exchange stability and repayment capacity is evident from the fact that share of external loans maturing within one year was equal to around 31.9 percent of official liquid reserves at the end of December 2016 as compared with around 68.5 percent at the end of 2012-13.

9.4 Dynamics of Public Debt Burden

The debt burden can be described with many parameters and there is no single threshold for debt ratios that can delineate the “bad” from the “good” e.g. debt burden can be expressed in terms of the stock ratio i.e. debt to GDP, external debt to GDP or flow ratios i.e. debt to revenue, external debt to foreign exchange earnings etc.

Table-9.5: Selected Public Debt Indicators (in percentage)

	2011	2012	2013	2014	2015	2016
Revenue Balance* / GDP	(3.3)[(a)]	(4.5)[(b)]	(2.9)[(c)]	(0.7)	(1.7)	(0.8)
Primary Balance* / GDP	(2.5)[(a)]	(4.2)[(b)]	(3.6)[(c)]	(0.2)	(0.5)	(0.2)
Fiscal Balance / GDP	(6.5)[(a)]	(8.8)[(b)]	(8.2)[(c)]	(5.5)	(5.3)	(4.6)
Gross Public Debt / GDP	58.9	63.3	64.0	63.5	63.3	67.6
Net Public Debt / GDP	54.3	59.3	60.2	58.1	58.3	61.2
Gross Public Debt / Revenue	477.9	494.7	480.1	439.7	442.1	442.5
Net Public Debt / Revenue	440.5	463.2	452.1	402.0	406.7	400.8
Debt Service / Revenue	38.0	39.9	40.5	40.1	40.4	35.9
Interest Service / Revenue	31.0	34.6	33.2	31.6	33.2	28.4
Debt Service / GDP	4.7	5.1	5.4	5.8	5.8	5.5

*Adjusted for grants

[(a)]includes arrears of electricity subsidies amounting to Rs.120 billion or 0.7 percent of GDP

[(b)]includes "one off" payment of Rs.391 billion on account of debt consolidation or 2 percent of GDP

[(c)] includes payment for the resolution of the circular debt amounting to Rs.322 billion or 1.4 percent of GDP

Source: Debt Policy Coordination Office Staff Calculations, Ministry of Finance

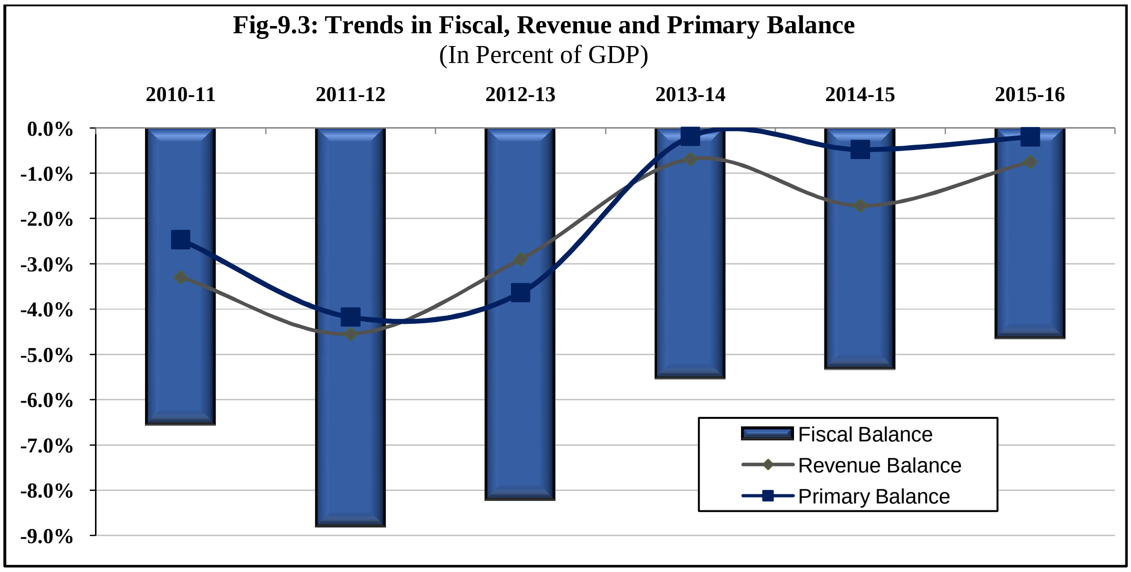
Significant reduction was observed in primary and revenue deficits[1] during 2015-16 as the government adhered strictly to its objective of fiscal consolidation. Revenue deficit was reduced to 0.8 percent of GDP during 2015-16 from 1.7 percent during 2014-15 as the growth in total revenue (13 percent) outpaced the growth in current expenditure (6 percent) during 2015-16. Similarly, primary deficit was reduced to 0.2 percent of GDP during 2015-16 from 0.5 percent during 2014-15 as the growth in total revenue overshadowed the growth in non-interest expenditure during 2015-16. During first nine months of current fiscal year, revenue deficit was recorded at 1.4 percent of GDP while primary deficit was recorded at 0.4 percent of GDP.

Fiscal consolidation remained on track as fiscal deficit continued to fall for the fourth year in a row. Fiscal deficit was contained at 8.2 percent in 2012-13 (down from a projected 8.8 percent), due to the concerted efforts by the government soon after assuming the office. Fiscal deficit was reduced significantly in 2013-14 and recorded at 5.5 percent of GDP (lower than its budgeted target of 6.6 percent) and recorded at 5.3 percent of GDP in 2014-15. Fiscal deficit was reduced further at 4.6 percent of GDP during 2015-16 mainly owing to the following:

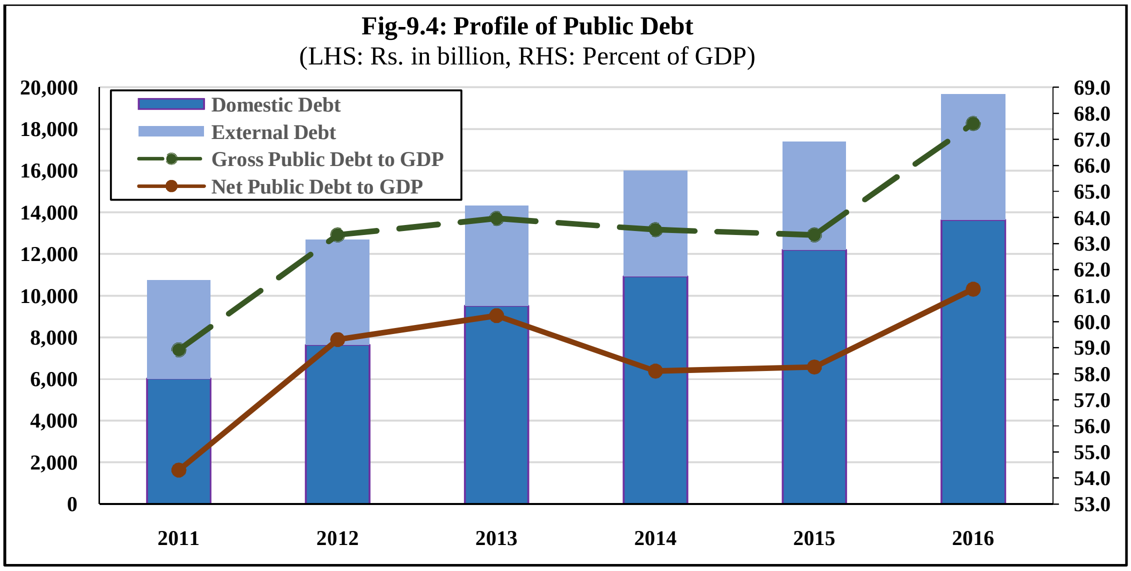
- FBR tax collections witnessed growth of over 20 percent during 2015-16;
- Interest payments recorded a significant decline and stood at 28 percent of government revenue during 2015-16 as compared with 33 percent in 2014-15 mainly due to low interest rate environment, downward revision of coupon rates of Pakistan Investment Bonds (PIBs) and higher growth in revenue as mentioned above;
- While deficit reduction was already visible at the federal level, surpluses in provincial accounts further consolidated the fiscal position.

Fiscal deficit was recorded at 3.9 percent of GDP during first nine months of current fiscal year as compared with 3.5 percent in the corresponding period of last year. The increase may be attributed to lower growth in tax revenues owing to various tax incentives provided to promote investment and economic activity in the country.

[1] Revenue balance is the total revenues minus current expenditure. The persistence of revenue deficit indicates that the government is not only borrowing to finance its development expenditure, but partially to finance its current expenditure. Primary balance is the total revenues minus non-interest expenditure or fiscal deficit before interest payments. Primary balance is an indicator of current fiscal efforts since interest payments are predetermined by the size of previous deficits.



The net public debt to GDP ratio was recorded at 61.2 percent as at end June, 2016 slightly higher than 60.2 percent recorded at end June 2013 despite reduction in fiscal deficits over this period. The non-fiscal deficits factors like revaluation losses on account of cross currency movements and loans from IMF contributed to this increase. The IMF loans are only applied towards Pakistan's balance of payments, add to foreign currency reserves and do not come as an extra resource in the budget. In fact, net public debt to GDP ratio was prevailing at the same level of 60.2 percent at end June 2016, however, this ratio went up to 61.2 percent due to downward revision of nominal GDP. As at end March 2017, net public debt to GDP ratio stood at 59.3 percent as compared with 59.6 percent in the corresponding period of last year. The gross and net public debt position since fiscal year 2011 (both in absolute and GDP term) are depicted in the following graph:



Public debt levels against actual government revenues measures debt repayment capacity of the country. There was around 6 percentage point reduction in net public debt to government revenues ratio which stood at 401 percent in 2015-16 as compared with 407 percent in 2014-15, indicating some easing in government indebtedness. Whereas, gross public debt to government revenues increased slightly by 0.4 percentage point during 2015-16 as compared with previous fiscal year. Government is committed to reduce this ratio to a generally acceptable threshold of 350 percent by increasing its revenues and rationalizing current expenditures which will reduce the debt burden and improve the debt carrying capacity of the country to finance the growing development needs.

9.5 Servicing of Public Debt

Public debt servicing was recorded at Rs.1,410 billion during first nine months of current fiscal year against the annual budgeted estimate of Rs.1,945 billion. Public debt servicing consumed nearly 45 percent of total revenues during first nine months of current fiscal year against a ratio of 46 percent during the same period last year.

Table-9.6: Public Debt Servicing (Rs. in billion)

	2016-2017*			
	Budgeted	**Actual**	**Percent of Revenue**	**Percent of Current Expenditure**
Repayment of External Debt	585.2	315.6	10.0	8.8
Total External Principal Repayment (A)	**585.2**	**315.6**	**10.0**	**8.8**
Servicing of External Debt	113.0	84.6	2.7	2.3
Servicing of Domestic Debt	1,247.0	1,009.9	32.1	28.0
Total Interest Servicing (B)	**1,360.0**	**1,094.5**	**34.8**	**30.4**
Total Servicing of Public Debt (A+B)	**1,945.2**	**1,410.0**	**44.8**	**39.1**

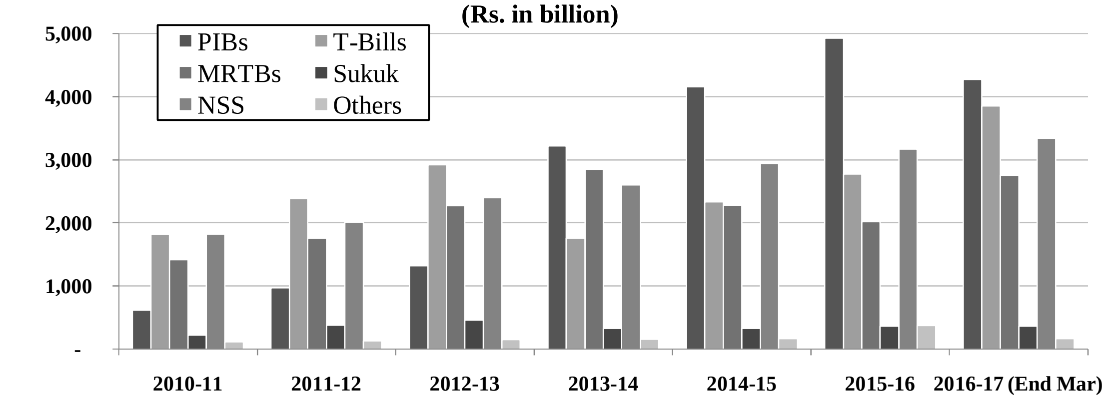
*: July-March
Source: Budget Wing and Debt Policy Coordination Office Staff Calculations, Ministry of Finance

Domestic interest payments constituted around 72 percent of total debt servicing which is due to higher volume of domestic debt in public debt portfolio. Domestic interest payments were recorded at Rs.1,010 billion during first nine months of current fiscal year as compared with Rs.1,003 billion during the same period last year. This slight increase in interest payments (despite lower interest rates) was mainly driven by increase in domestic debt stock during the period. Out of total domestic interest payments, large portion was paid against PIBs (Rs.457 billion), National Savings Schemes (Rs.203 billion), T-Bills (Rs.164 billion) and Market Related Treasury Bills (Rs.119 billion). Furthermore, due to re-profiling of the domestic debt by the government, the domestic interest cost is expected to remain almost at the same level in the upcoming year despite increase in domestic debt volume.

9.6 Domestic Debt

Pakistan's domestic debt comprises permanent debt (medium and long-term), floating debt (short-term) and unfunded debt (primarily made up of the various instruments available under the National Savings Schemes). Domestic debt increased by Rs.1,121 billion during first nine months of current fiscal year which was lower than Rs.1,200 billion witnessed in the same period last year. The composition of domestic debt witnessed some changes as most of the increase came from short-term debt while net retirement was witnessed in medium to long term debt during the said period owing to significant PIBs maturities. Accordingly, share of floating debt in total domestic debt increased to 45 percent at the end of March 2017 as compared with 37 percent at the end of last fiscal year while share of permanent debt in total domestic debt decreased to 36 percent at the end of March 2017 as compared with 44 percent at the end of last fiscal year.

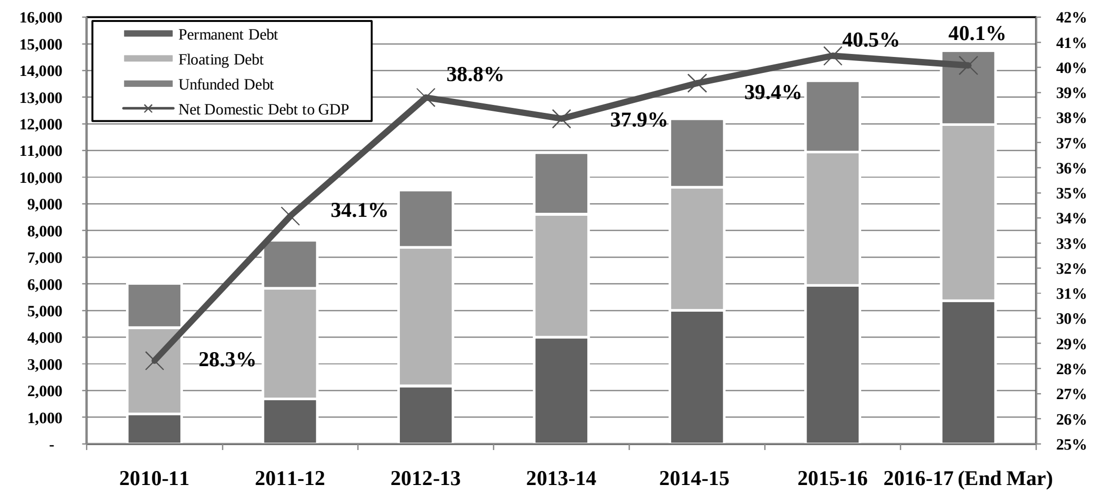
Fig-9.5: Evolution of Domestic Debt
(Rs. in billion)



9.6.1 Outstanding Domestic Debt

Gross domestic debt was Rs.14,748 billion while net domestic debt was Rs.12,768 billion as at end March 2017. Gross domestic debt registered an increase of Rs.1,121 billion during the year while government borrowing from domestic sources for financing of fiscal deficit was Rs.1,018 billion. This differential is mainly attributed to increase in government credit balances with the banking system. Most of the incremental mobilization was recorded in floating debt while net retirement was witnessed in permanent debt. Despite significant PIBs maturities of Rs.1,427 billion, marginal net retirement was witnessed owing to proactive debt management that brought down the interest rates on long term domestic debt portfolio significantly, thus bringing down the overall cost of domestic debt portfolio.

Fig-9.6: Evolution of Domestic Debt (LHS: Rs. in billion, RHS: Percent of GDP)



The following section highlights the developments in the various components of domestic debt during first nine months of outgoing fiscal year:

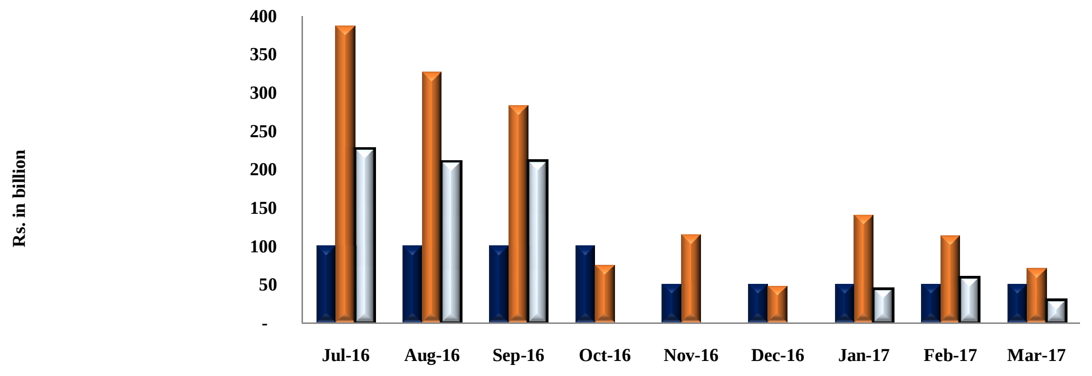
I. Permanent Debt

Permanent debt mainly consists of medium to long term instruments including PIBs, Government Ijara Sukuk (GIS), Prize Bond etc. PIBs are non-callable instruments with fixed and semi-annual coupon payment. PIBs are issued in tenors of 3, 5, 10 and 20 years maturity. The 3, 5 and 10 years tenors are most liquid. Government Ijara Sukuk are medium term Shariah compliant bonds currently issued in 3 years tenor. The purpose of issuance was to raise money from Islamic financial institutions which have grown substantially in Pakistan in past few years.

The amount of permanent debt in total domestic debt stood at Rs.5,379 billion as at end March 2017, representing decrease of Rs.565 billion as compared with the stock at the end of last fiscal year. This decrease was driven by PIBs maturity amounting to Rs.1,427 billion which was repaid during the first quarter of 2016-17. Given the impact of maturing amount on the appetite of domestic debt market, the government planned well in time and started mobilizing more through fresh issuance of PIBs and GIS to cover up the existing PIBs maturities i.e. the government issued Rs.2,271 billion from January 2015 to September 2016 and that too at lower yield and higher duration. Although the government was able to more or less neutralize the overall impact of PIBs maturity on domestic debt sustainability indicators, it was envisaged that the entire PIBs amount would be challenging to re-finance during the first quarter of 2016-17 through fresh issuance of PIBs given the local market appetite for long term paper.

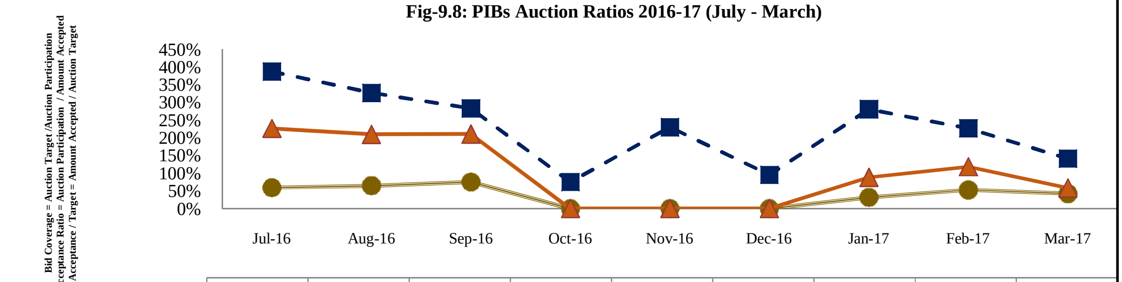
Auction profile of government securities witnessed varied patterns of investment by the commercial banks during first nine months of 2016-17, mainly depending on their perception of changes in interest rates, inflation, liquidity conditions and external sector developments. The policy rate remained unchanged throughout first nine months of current fiscal year, however, unlike the first quarter, when the government (in gross terms) raised more than twice the combined targeted amount of Rs.300 billion, all bids received against PIBs auctions during second quarter of 2016-17 were rejected as the rates quoted by commercial banks were on a higher side. Any acceptance in these PIBs auctions may have signalled a reversal in long-term interest rates, which, in turn, would have had implications for the market's short-term interest rate expectations. The market was expecting an increase in interest rates due to increase in inflation and widening of the current account deficit. Nonetheless, as the actual inflation consistently turned out to be lower than market expectations (especially in November and December 2016) and accordingly some correction in the longer segment of the yield curve was observed during third quarter of 2016-17. The auctions wise details and PIBs yields are depicted through following graphs:

Fig-9.7: PIBs Auction Profile 2016-17 (July - March)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17
Auction Target (Rs. in billion)	100	100	100	100	50	50	50	50	50
Auction Participation (Rs. in billion)	386	326	283	75	115	48	140	113	70
Amount Accepted (Rs. in billion)	226	210	210	-	-	-	44	59	29

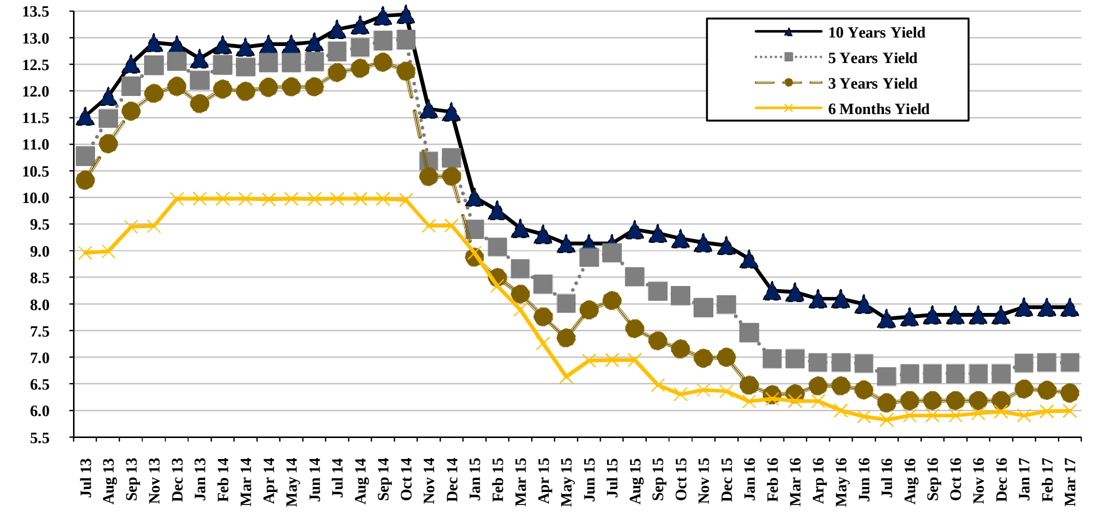
Fig-9.8: PIBs Auction Ratios 2016-17 (July - March)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17
Bid Coverage	386%	326%	283%	75%	229%	95%	280%	226%	141%
Acceptance Ratio	59%	64%	74%	0%	0%	0%	31%	52%	42%
Acceptance/ Target	226%	210%	210%	0%	0%	0%	88%	118%	58%

As depicted in the graph above, against the target of Rs.650 billion, government received participation of Rs.1,556 billion against which government accepted Rs.779 billion during first nine months of current fiscal year. The yields (6 months T-bills, 3, 5 and 10 years PIBs) from July 2013 to March 2017 are depicted through following graph:

Fig-9.9: T-Bills PIBs Yields (6 Months, 3, 5 & 10 Years) - In Percent



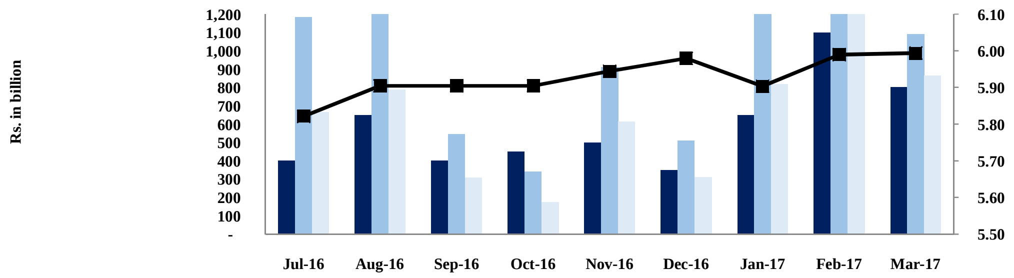
II. Floating Debt

Floating debt consists of short term domestic borrowing instruments such as Market Treasury Bills (MTBs) and State Bank borrowing through the purchase of MRTBs. Treasury Bills are zero coupon or discounted instruments issued in tenors of 3 months (introduced in 1997), 6 months (introduced in 1990) and 12 months (introduced in 1997). In order to raise short term liquidity, the government borrows from the domestic banks through auction in the form of Treasury Bills. The auction of Treasury Bills is arranged by the SBP twice a month.

Floating debt recorded an increase of Rs.1,602 billion during first nine months of current fiscal year and stood at Rs.6,604 billion at end March 2017. The share of floating debt in overall public debt and domestic debt stood at 32 percent and 45 percent respectively at end March 2017 while it was at 36 percent and 55 percent respectively at the end of 2012-13. During July-March 2016-17, net mobilization through T-bills and MRTBs stood at Rs.1,080 billion and Rs.735 billion respectively, while the government retired maturing Sukuk (Bai-Muajjal) of Rs.213 billion. The increase in floating debt was mainly driven by refinancing of portion of PIBs maturity during first quarter of 2016-17. Further, banks started offering higher amounts in T-bills auctions while participation and acceptance in PIBs auctions remained subdued in second and third quarter of 2016-17 owing to rising interest rate expectations. The share of 3 months, 6 months and 12 months maturity in total T-Bills portfolio was 30 percent, 41 percent and 29 percent respectively as at end-March 2017.

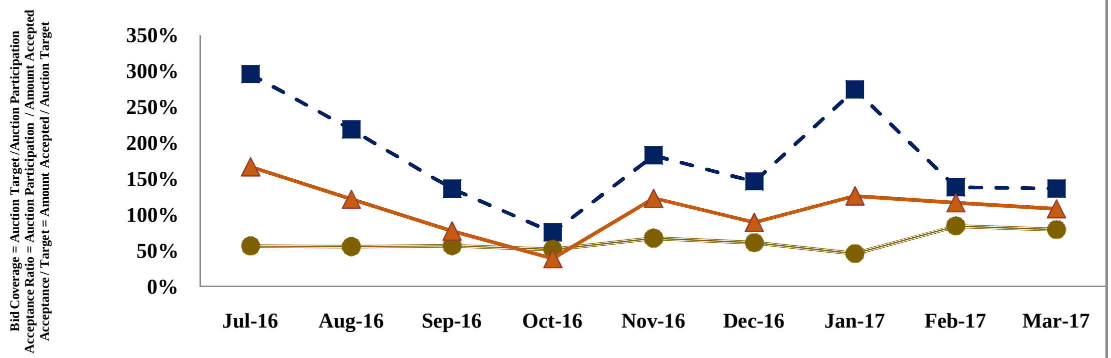
Government received massive participation of Rs.9,308 billion in the auctions of T-Bills against the target of Rs.5,300 billion including maturity of Rs.4,759 billion. However, the government mobilized Rs.5,829 billion resulting in additional mobilization of Rs.1,070 billion (net of maturity) against the targeted additional requirement of Rs.541 billion. The auctions wise details and relevant ratios related to T-bills are depicted through following graphs:

Fig-9.10: T-Bills Auction Profile 2016-17 (July - March)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17
Auction Target (Rs. in billion)	400	650	400	450	500	350	650	1,100	800
Auction Participation (Rs. in billion)	1,183	1,422	545	339	912	512	1,783	1,521	1,091
Amount Accepted (Rs. in billion)	666	789	309	175	613	312	819	1,281	865
6 month T-Bill Yield (%)	5.82	5.90	5.90	5.90	5.94	5.98	5.90	5.99	5.99

Fig-9.11: T-Bills Auction Ratios 2016-17 (July - March)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17
Bid Coverage	296%	219%	136%	75%	182%	146%	274%	138%	136%
Acceptance Ratio	56%	55%	57%	52%	67%	61%	46%	84%	79%
Acceptance/Target	167%	121%	77%	39%	123%	89%	126%	116%	108%

III. Unfunded Debt

The return offered on National Savings Schemes (NSS) instruments remained relatively lower than previous year which mainly contributed towards decrease in net mobilization of Rs.85 billion during first nine months of current fiscal year as compared with

Rs.96 billion mobilized during the same period last year. Most of the incremental mobilization went into Bahbood Savings Certificates (Rs.45 billion) and Special Savings Certificates and Accounts (Rs.26 billion). The total share of unfunded debt in the government's domestic debt stood at Rs.2,766 billion or 19 percent as at end March 2017. The rates on NSS revised three times during first nine months of current fiscal year to align them with the market rates.

Over a period of time, government took various measures to transform CDNS from merely a retail debt raising arm of the government to an effective vehicle for financial inclusion and a provider of social security net to the vulnerable sections of the society. CDNS launched Rs.40,000 Premium Prize Bond which is issued to only registered investors with unique features of both the profits paid biannually and the prize money through quarterly draws. Both the profits and the prize money are also directly credited into investors' bank accounts. CDNS also became the only non-banking member of National Institutional Facilitation Technologies (Pvt.) Limited ("NIFT") – the Banking Clearinghouse. With this initiative, the profits can be credited directly into investor's bank accounts, thereby offering safety and security along with access to other banking services.

CDNS is planning to introduce innovative products in order to increase financial inclusion of small savers and contribute towards the social safety net of deserving segments of the society. In this respect, extension of Bahbood Savings Certificates ("BSCs") to the disabled persons, launch of Shuhadas' Family Welfare Accounts ("SFWAs") for family members of the martyrs and introduction of Overseas Pakistanis Certificates ("OPCs"), an exclusive scheme for non-resident Pakistanis are under consideration. Shariah compliant products are taking firm roots in Pakistani society and accordingly CDNS is working on the possibility of launching Shariah Compliant Savings Certificates.

Table-9.7: Outstanding Domestic Debt - (Rs. in billion)

	2011	2012	2013	2014	2015(P)	2016(P)	2017(P) *
Permanent Debt	**1,125.6**	**1,696.9**	**2,179.2**	**4,005.3**	**5,016.0**	**5,944.2**	**5,378.8**
Market Loans	2.9	2.9	2.9	2.9	2.8	2.8	2.8
Government Bonds	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Prize Bonds	277.1	333.4	389.6	446.6	522.5	646.4	729.5
Foreign Exchange Bearer Certificates	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Bearer National Fund Bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Federal Investment Bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Special National Fund Bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign Currency Bearer Certificates	0.0	0.0	0.0	0.0	0.0	0.0	0.0
U.S. Dollar Bearer Certificates	0.0	0.0	0.0	0.0	0.1	0.1	0.1
Special U.S. Dollar Bonds	1.0	0.9	4.2	4.4	4.4	4.5	4.5
Government Bonds Issued to SLIC	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Pakistan Investment Bonds (PIBs)	618.5	974.7	1,321.8	3,223.5	4,158.3	4,925.0	4,276.5
GOP Ijara Sukuk	224.6	383.5	459.2	326.4	326.4	363.9	363.9
Floating Debt	**3,235.4**	**4,143.1**	**5,196.2**	**4,610.9**	**4,612.6**	**5,001.8**	**6,603.7**
Treasury Bills through Auction	1,817.6	2,383.4	2,921.0	1,758.6	2,331.3	2,771.6	3,851.4
Rollover of Treasury Bills discounted SBP	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Market Related Treasury Bills (MRTBs)	1,417.3	1,759.2	2,274.7	2,851.8	2,280.9	2,017.1	2,751.7
Bai Muajjal	-	-	-	-	-	212.6	-
Unfunded Debt	**1,655.8**	**1,798.0**	**2,146.5**	**2,303.8**	**2,570.3**	**2,680.9**	**2,765.7**
Defence Savings Certificates	234.5	241.8	271.7	284.6	300.8	308.9	326.0
Khas Deposit Certificates and Accounts	0.6	0.6	0.6	0.6	0.6	0.6	0.6
National Deposit Certificates	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Savings Accounts	17.2	21.2	22.3	22.6	26.4	29.2	31.8
Mahana Amdani Account	2.1	2.0	2.0	1.9	1.8	1.8	1.7
Postal Life Insurance	67.1	67.1	67.1	67.1	67.1	67.1	67.1

Table-9.7: Outstanding Domestic Debt - (Rs. in billion)	2011	2012	2013	2014	2015(P)	2016(P)	2017(P) *
Special Savings Certificates and Accounts	529.1	537.4	734.6	738.8	867.5	896.5	922.2
Regular Income Scheme	182.6	226.6	262.6	325.4	376.0	359.8	339.1
Pensioners' Benefit Account	146.0	162.3	179.9	198.4	214.1	234.7	250.9
Bahbood Savings Certificates	428.5	480.8	528.4	582.4	628.3	692.1	737.4
National Savings Bonds	3.6	3.6	0.2	0.2	0.1	0.1	0.1
G.P. Fund	44.3	54.6	73.1	80.5	85.8	88.3	85.8
Short Term Savings Certificates	-	-	4.0	1.3	1.7	1.9	2.8
Total Domestic Debt	**6,016.7**	**7,638.1**	**9,521.9**	**10,920.0**	**12,198.9**	**13,626.9**	**14,748.1**

P: Provisional *end-March, 2017

Source: Budget Wing, Finance Division

9.6.2 Secondary Market Activities of Government Securities

An important role of secondary market for government securities is to assist in development of a reliable yield curve and the term structure of interest rates, thus facilitating new issuance. Government bond market in Pakistan is large, liquid and growing in size. The growth in trading activity, as reflected in the increased daily trading volume of government securities in secondary market, shows that the depth and efficiency of the market has increased over time. Banks and non-banks financial institutions also use secondary market trading of government securities as a source of liquidity management.

Secondary Market Outright Trading

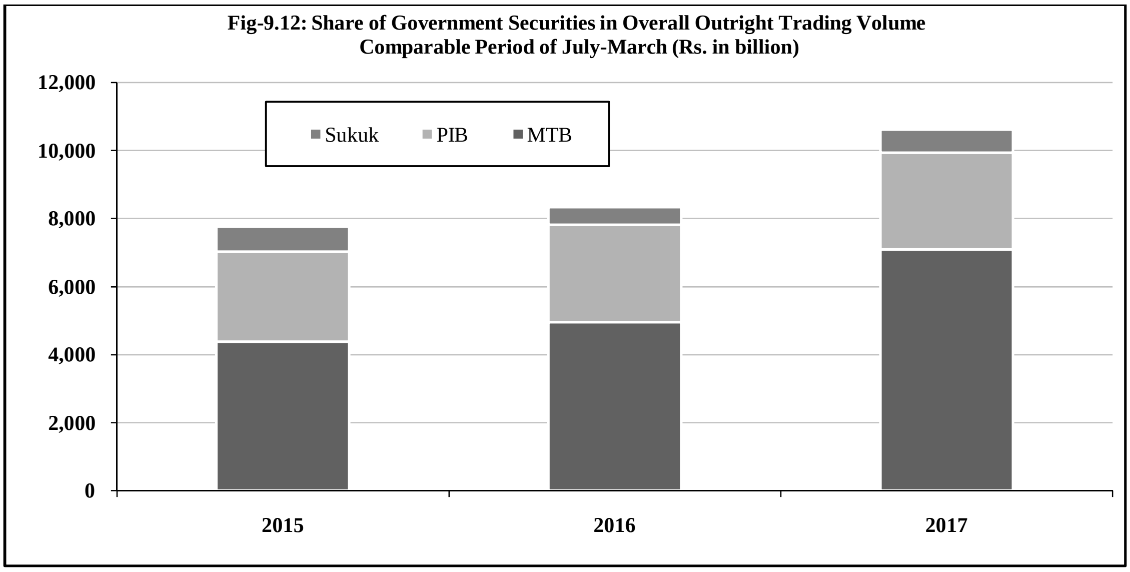
In Pakistan, outright trading of government securities, which include MTBs, PIBs and GIS has been growing steadily. The secondary market for these securities is liquid, efficient and deep with Rs.11.3 trillion and Rs.10.7 trillion traded outright in 2015-16 and 2014-15, respectively. During first nine months of 2016-17, the outright trading volume in the secondary market is recorded at Rs.10.6 trillion, compared to Rs.8.3 trillion during the same period of last year. Additionally, the growth in outright segment of secondary market can also be viewed from increase in daily trading volumes which has also increased from Rs.44.4 billion in July-March period of 2015-16 to Rs.56.5 billion during July-March, 2016-17.

Table-9.8: Secondary Market Outright Trading Volume (Rs. in billion)

	Full Year		July-March		
Securities	**2016**	**2015**	**2017**	**2016**	**2015**
MTB-3M	1,369	1,550	2,502	1,027	1,294
MTB-6M	2,142	2,156	2,432	1,851	1,325
MTB-12M	2,720	2,325	2,156	2,076	1,763
PIB-3Yr	2,387	1,753	1,209	1,520	1,417
PIB-5Yr	959	741	974	651	511
PIB-10Yr	1,018	1,014	641	682	692
PIB-20Yr	10	34	19	6	31
GIS-3Yr	653	1109	682	526	732
Total	**11,257**	**10,683**	**10,616**	**8,338**	**7,765**
Daily Volume	45.0	43.2	56.8	44.4	43.4
Memo:					
Government securities (end period stock)	8,199	6,955	8,620	7,969	6,828
Turnover	1.37	1.54	1.23	1.05	1.14

Source: State Bank of Pakistan

The share of MTBs in the overall outright secondary market volume of government securities increased to 46 percent in the period July-March, 2016-17 compared to 35 percent in the same period of 2015-16, mainly on account of increased volume of MTBs issued in the primary market. On the other hand, the share of PIBs reduced to 50 percent from 60 percent during the period under consideration. A major reason for this shift is the greater primary issuances of MTBs as market interest shifted towards short tenor government securities. The shift possibly reflects market perception of interest rate bottoming out.



The turnover ratio (represented by ratio of trading volume to outstanding stock of Government securities) increased to 1.23 during July-March, 2016-17 compared to 1.05 and 1.14 in the same period of 2015-16 and 2014-15, respectively. Increased issuance of MTBs, as discussed above, during 2016-17 has improved the turnover ratio, as the market tend to trade short term securities more frequently for their liquidity management compared to buy and hold behaviour for PIBs and GIS.

Repo Market Trading

Repo market continues to dominate the secondary market trading activities of government securities in Pakistan. In the first nine months of 2016-17, 57 percent of the overall secondary market trades were generated in the repo market, having a trading volume of Rs.13,938 billion. The significantly large trade volumes and high liquidity in the repo market for government securities allow the market participants to swiftly meet their temporary liquidity requirements.

Table-9.9: Government Security based Transactions (July-March)

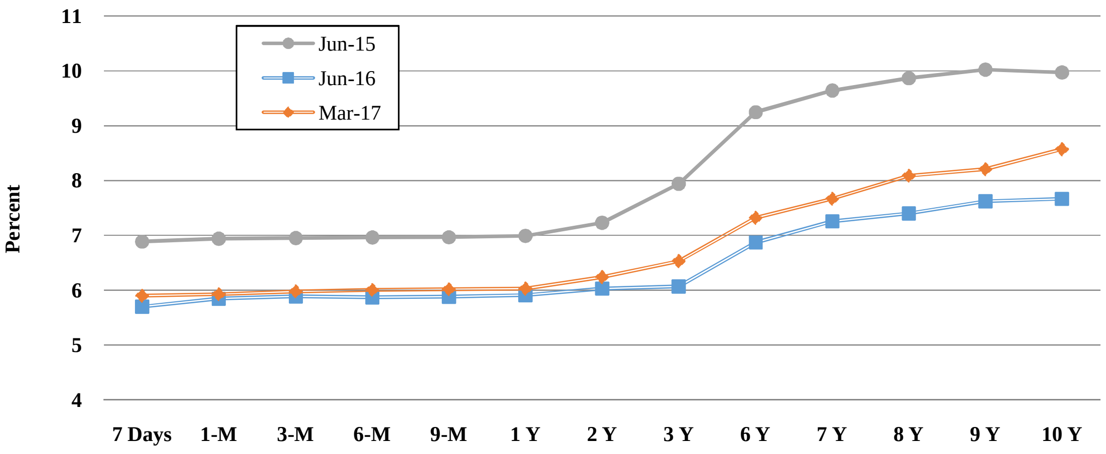
Type	Volume (Rs. in Billion)			Percentage Share		
	2017	2016	2015	2017	2016	2015
Repo	13,938	9,820	10,453	57%	54%	57%
Outright	10,616	8,338	7,765	43%	46%	43%
Total	24,554	18,158	18,218	100%	100%	100%

Source: State Bank of Pakistan

Yield Curve

In continuation to easy monetary policy stance, SBP cut its policy rate by a cumulative 75 bps from June-2015 to June-2016, which is reflected in the downward movement in the yield curve of June 2016. However, SBP kept its policy rate at 5.75 percent during July-March, 2016-17. The upward movement in the yield curve of March 2017 reflects market view regarding the direction of policy rate, going forward.

Fig-9.13: Secondary Market Yield Curve



9.7 External Debt and Liabilities

Pakistan's External Debt and Liabilities (EDL) include all foreign currency debt contracted by the public and private sector as well as foreign exchange liabilities of SBP. Out of EDL, external public debt of the government is defined as debt which is serviced out of consolidated fund and debt owed to the International Monetary Fund. External public debt is obtained to supplement the domestic resources required to accelerate the pace of economic development and make positive contribution towards developing the country's infrastructure base. The receipts are used for balance of payment support, reducing domestic borrowing and covering the repayment obligations. The external inflows, altogether, help in building foreign exchange reserves, provide stability to exchange rate vis-à-vis other currencies and help in achieving accelerated economic growth.

EDL stock was US$ 75.7 billion as at end March 2017 out of which external public debt was US$ 58.4 billion. External public debt recorded an increase of US$ 0.7 billion during first nine months of current fiscal year. The impact of net fresh external borrowing was partially offset by revaluation gains during first nine months of current fiscal year. Within external debt, the largest component is the multilateral debt and bilateral debt, constituting around 87 percent of the external public debt as at end March, 2017. The loans from multilateral and bilateral development partners are primarily aimed at removing structural bottlenecks from Pakistan's economy. These concessional loans are primarily utilized towards implementing structural reforms in the areas of energy, taxation, doing businesses, trade facilitation, education and promotion of small and medium enterprises (SMEs). Such concessional lending programs are instrumental in enhancing Pakistan's potential output by promoting efficiency and productivity. These loans are, thus, simultaneously adding to the debt repayment capacity of the country. It may also be highlighted that these loans are also dominated by long term maturities and, therefore, do not add much to the country's debt servicing burden. Furthermore, these concessional external loans have been used to retire relatively more expensive domestic debt.

During first nine months of 2016-17, disbursements against external public debt stood at US$ 4,955 million. Details of gross inflows from main creditors during the period are as follows:

- Pakistan mobilized US$ 1,000 million as proceed of the international Sukuk;
- Disbursements from ADB US$ 757 million included US$ 188 million under the Social Protection Development and remaining portion was dominated by the proceeds against power sector programs;

- Disbursements from China reached at US$ 1,033 million and recorded an increase of US$ 432 million as compared with the comparable period last year. This occurred in tandem with a pickup in CPEC-related economic activities in the country;
- Government borrowed US$ 1,315 million from commercial lenders.

Table-9.10: Pakistan External Debt and Liabilities

	2011	2012	2013	2014	2015(P)	2016(P)	2017(P) *
(US Dollar in billion)							
PUBLIC EXTERNAL DEBT							
1. Public Debt (i+ii+iii)**	**55.3**	**53.5**	**48.1**	**51.3**	**50.9**	**57.7**	**58.4**
i). Medium and Long Term(>1 year)	**45.7**	**45.6**	**43.5**	**47.7**	**45.8**	**50.0**	**51.3**
Paris Club	15.5	15.0	13.5	13.6	11.7	12.7	11.9
Multilateral	25.8	25.3	24.2	25.8	24.3	26.4	25.9
Other Bilateral	1.9	2.5	2.9	3.4	3.9	4.4	5.2
Euro Bonds/Saindak Bonds	1.6	1.6	1.6	3.6	4.6	4.6	5.6
Military Debt	0.1	0.1	0.1	0.0	-	-	-
Commercial Loans/Credits	-	-	-	0.2	0.3	0.9	2.2
Local Currency Bonds**	0.0	-	0.0	0.0	0.0	0.0	-
Saudi Fund for Development	0.2	0.2	0.2	0.1	0.1	0.1	0.0
SAFE China Deposits	0.5	1.0	1.0	1.0	1.0	1.0	0.5
NBP/BOC Deposits	0.1	-	-	-	-	-	-
ii). Short Term (<1 year)	**0.6**	**0.5**	**0.3**	**0.7**	**1.0**	**1.7**	**1.1**
Commercial Loans/Credits			-	0.2	-	0.6	-
Multilateral	0.6	0.5	0.3	0.4	1.0	1.1	1.1
Local Currency Securities**	0.0	0.0	0.0	0.1	0.0	0.0	0.0
iii). IMF	**8.9**	**7.3**	**4.4**	**3.0**	**4.1**	**6.0**	**6.0**
of which Central Government	2.0	1.9	1.5	0.9	0.1	-	-
Monetary Authorities	6.9	5.4	2.9	2.1	4.1	6.0	6.0
PUBLICLY GUARANTEED DEBT							
2) Publicly Guaranteed Debt	**0.1**	**0.2**	**0.6**	**0.5**	**1.0**	**1.3**	**1.2**
i). Medium and Long Term(>1 year)	**0.1**	**0.2**	**0.6**	**0.5**	**1.0**	**1.3**	**1.2**
Paris Club	-	-	-	-	-	-	-
Multilateral	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Bilateral	0.0	0.2	0.6	0.5	1.0	1.3	1.2
Commercial Loans/Credits	-	-	-	-	-	-	-
Saindak Bonds	-	-	-	-	-	-	-
ii). Short Term (<1 year)	-	-	-	-	-	-	-
NON PUBLIC DEBT							
3. Private Sector Debt	**4.4**	**3.6**	**3.1**	**3.0**	**3.0**	**3.3**	**4.3**
4. Public Sector Enterprises (PSEs Debt)	**1.3**	**1.3**	**1.2**	**1.7**	**1.5**	**1.5**	**1.6**
5. Banks	**1.1**	**1.8**	**1.6**	**2.0**	**2.3**	**2.7**	**3.7**
Borrowing	0.4	0.9	0.7	1.1	1.3	1.6	2.6
Non-resident Deposits (LCY & FCY)	0.7	1.0	0.8	0.9	1.0	1.1	1.2
6. Debt liabilities to direct investors - intercompany debt	**1.6**	**2.7**	**3.1**	**3.4**	**2.7**	**2.9**	**3.0**
Total External Debt (1 through 6)	**63.8**	**63.1**	**57.8**	**62.1**	**61.4**	**69.5**	**72.2**
FOREIGN EXCHANGE LIABILITIES							
7. Foreign Exchange Liabilities	**2.6**	**2.4**	**3.1**	**3.3**	**3.7**	**3.6**	**3.5**
Total External Debt & Liabilities (1 through 7)	**66.4**	**65.5**	**60.9**	**65.4**	**65.1**	**73.1**	**75.7**
Memo:							
GDP (Rs. in billion)	18,276.4	20,046.5	22,385.7	25,168.8	27,443.0	29,102.6	31,862.2
Exchange Rate (Rs./US$, End of Period)	86.0	94.5	99.7	98.8	101.8	104.8	104.8
GDP (US$ in billion)	213.8	224.6	231.4	244.7	270.9	279.2	304.4

P: Provisional *end-March,2017

**excluding local currency bonds/securities since they are already included in domestic debt

Source: State Bank of Pakistan, Economic Affairs Division & Debt Policy Coordination Office

9.7.1 External Debt Servicing

External public debt servicing declined to US$ 4,340 million during 2015-16 as compared with US$ 4,475 million during 2014-15. This decline in public debt servicing was mainly due to lower principal repayments made to the IMF.

Servicing of external public debt was recorded at US$ 3,883 million in first nine months of 2016-17. A segregation of this aggregate number shows a repayment of US$ 3,008 million in respect of maturing external public debt stock while interest payments were US$ 875 million. Among the principal repayments, US$ 1,000 million of multilateral debt and US$ 500 million of Safe China Deposit accounted for most of the share.

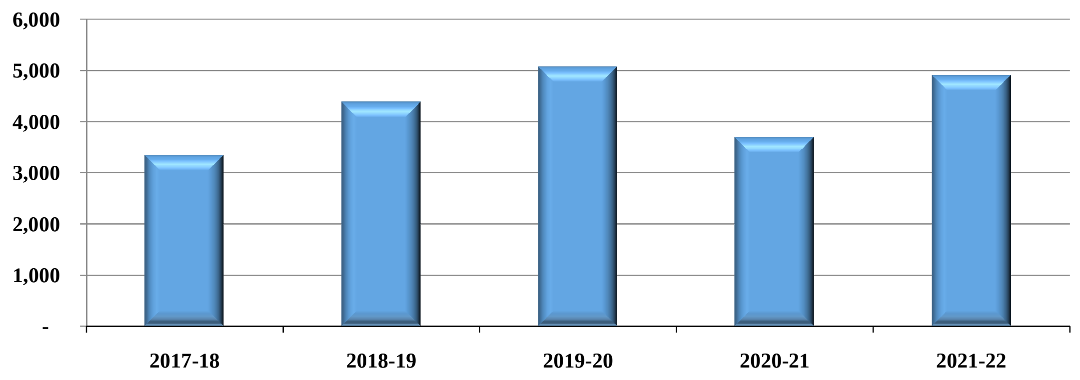
Table-9.11: Public External Debt Servicing

Years	Principal	Interest	Amount Rolled Over	Total
(US Dollar in million)				
2010-11	2,084.7	930.0	488.0	3,502.7
2011-12	2,700.0	880.9	543.0	4,123.9
2012-13	4,794.6	800.4	500.0	6,095.1
2013-14	5,220.0	774.6	1,000.0	6,994.5
2014-15	3,500.3	974.5	1,000.0	5,474.8
2015-16	3,213.1	1,126.7	1,248.3	5,588.1
2016-17*	3,008.4	875.0	-	3,883.3

*July-March, 2016-17
Source: Source: State Bank of Pakistan and Debt Policy Coordination Office , Ministry of Finance

Going forward, there is limited pressure from external debt repayments in the medium term. Projected principal repayments to the IMF against Extended Fund Facility (EFF) are stretched over a longer timeframe, starting at US$ 0.2 billion in 2018 and rising to US$ 0.8 billion in 2020, with the final payment due in 2025. An amount of US$ 0.75 billion due in this fiscal year is the only Eurobond maturing until 2019. Repayments for Official Development Assistance from the Paris Club began in 2016 which are spread over a 23-year period. The projected external public debt repayments based on outstanding as at end March, 2017 is presented through the graph below:

Fig-9.14: Public External Debt Payments - US$ in million (Based on Outstanding as on March 31, 2017)



As depicted in the graph above, external debt repayment obligations for Pakistan are not more than an average of US$ 4.3 billion per annum until 2022 based on outstanding external public debt as at end March, 2017. Keeping in view the track record of the country, this amount of repayments should not raise any concern. Pakistan has successfully met higher repayment obligations of US$ 4.8 billion and US$ 5.2 billion in 2013 and 2014 respectively, even with much smaller volume of foreign exchange reserves. Furthermore, it is anticipated that average yearly external inflows would be around US$ 6.7 billion until 2022 against expected annual average repayment obligations of US$ 4.3 billion (based on outstanding external public debt as at end March, 2017) i.e. inflows are expected to be sufficient to meet repayment obligations.

9.7.2 Impact of Exchange Rate Fluctuations

In Pakistan, external loans are contracted in various currencies but disbursements are effectively converted into Pak Rupee. As Pak Rupee is not an internationally traded currency, the other currencies are bought and sold via selling and buying of US Dollar. Hence, the currency exposure of foreign debt originates from two sources: US Dollar/other foreign currencies and Pak Rupee/US Dollar. This two pronged exchange rate risk has been a major source of fluctuation in the stock of public external debt over a period.

During first nine months of current fiscal year, appreciation of US Dollar against other major currencies resulted in decrease in foreign currency component of public debt mainly driven by Japanese Yen which depreciated around 16 percent against US dollar. However, Pak Rupee remained almost at the same level of end June, 2016 against US Dollar which resulted in negligible increase in external public debt in Pak Rupee terms.

9.7.3 External Debt Sustainability

The external debt sustainability can be assessed with two types of indicators; (i) solvency indicators and (ii) liquidity indicators. Solvency indicator such as external debt-to-GDP ratio shows debt bearing capacity while liquidity indicators such as external debt servicing to foreign exchange earnings ratio shows debt servicing capacity of the country

Table-9.12: External Debt Sustainability Indicators

	2011	2012	2013	2014	2015	2016
ED/FEE (times)	1.2	1.1	1.0	1.0	1.0	1.1
ED/FER (times)	3.0	3.5	4.4	3.6	2.7	2.5
ED/GDP (Percentage)	25.9	23.8	20.8	21.0	18.8	20.7
ED Servicing/FEE (Percentage)	6.3	7.4	11.1	11.7	8.5	8.4

FEE: Foreign Exchange Earnings; **ED:** External Public Debt; **FER:** Foreign Exchange Reserves
Source: Debt Policy Coordination Office Staff Calculations, Ministry of Finance

External public debt to GDP ratio increased from 18.8 percent at the end of 2014- 15 to 20.7 percent at the end of 2015-16. Apart from next external inflows, translational losses on account of depreciation of US Dollar against other foreign currencies contributed to increase in this ratio. Similarly, ED to FEE ratio increased slightly and recorded at 1.1 times at the end of June, 2016 as compared with 1 times at the end of preceding fiscal year. However, external debt to GDP ratio of 20.7 percent was still lower when compared with 20.8 percent recorded at the end of June 2013. By end March 2017, this ratio stood at 19.2 percent.

A decrease in external debt in relation to foreign exchange reserves reflects the consolidation of foreign exchange reserves and a general improvement of the country's repayment capacity or vice versa. This ratio started improving since 2013-14 and recorded at 2.7 times in 2014-15 as compared with 4.4 times at the end of 2012-13. This ratio improved further and recorded at 2.5 times as at end June, 2016 despite increase in external public debt which shows that growth in foreign exchange reserves outpaced the growth in external public debt in 2015-16. As at end March 2017, this ratio stood at 2.7 times.

External public debt servicing to foreign exchange earnings ratio dropped to 8.5 percent in 2014-15, from 11.7 percent in 2013-14 due to decline in external debt repayments coupled with strong growth in the remittance. This ratio improved further and recorded at 8.4 percent during 2015-16 mainly on account of decline in external public debt servicing. During first nine months of current fiscal year, external public debt servicing to foreign exchange earnings ratio stood at around 10 percent.

A pragmatic and realistic approach is to measure the "net external indebtedness" of the country which is the difference between external public debt and official FX reserves. As at end June 2013, the SBP FX reserves were around US$ 6 billion, out of which US$ 2 billion were through short term FX swap with a friendly country maturing in less than 60 days. Therefore, practically SBP's true FX reserves were US$ 4 billion as at end June 2013 against which external public debt stood at US$ 48.1 billion, thus net external indebtedness on June 30, 2013 was US$ 44.1 billion (US$ 48.1 billion - US$ 4.0 billion). As at end March 2017, the FX reserves of SBP were US$ 16.5 billion and external public debt stood at US$ 58.4 billion, thus net external indebtedness was US$ 41.9 billion (US$ 58.4 billion - US$ 16.5 billion). Therefore, net external indebtedness of the country improved by US$ 2.2 billion by end March 2017 compared with end June 2013.

9.8 Pakistan's Link with International Capital Market

The issuance of Eurobonds has great significance for Pakistan as it not only introduced Pakistan back in the international capital market but also allowed access to foreign resources for building country's reserves, which have paved the way for exchange rate stability Further, the proceeds from Eurobonds were utilized to retire the expensive domestic debt.

Sukuk is referred as a 'Sharia compliant' bond. It represents an undivided proportionate ownership interest in an asset with the corresponding right to the Sharia acceptable income streams generated by the asset. These income streams are established and translated into tradable securities which can be issued in the capital markets for investors' participation. The issuance of Sukuk is one of the most significant mechanisms for raising finances in the domestic/international capital markets. It is being used extensively in the world as an alternative to conventional syndicated financing. In October 2016, the government successfully issued 5-year US$ 1,000 million Sukuk at the rate of 5.5 percent, the lowest rate ever achieved by the government in the international capital market. The order book saw solid momentum from the start with strong demand from international investors and reached over US$ 2.4 billion. About 57 percent of the subscription for the Sukuk came from Investment Advisors, Hedge/Mutual/Pension Funds while the remaining was from banks and other financial institutions. In terms of geographical spread, 38 percent of subscription came from Europe, 27 percent each from North American and Middle East and 6 percent from Asia. The proceeds of Sukuk were utilized for balance of payments and budgetary support.

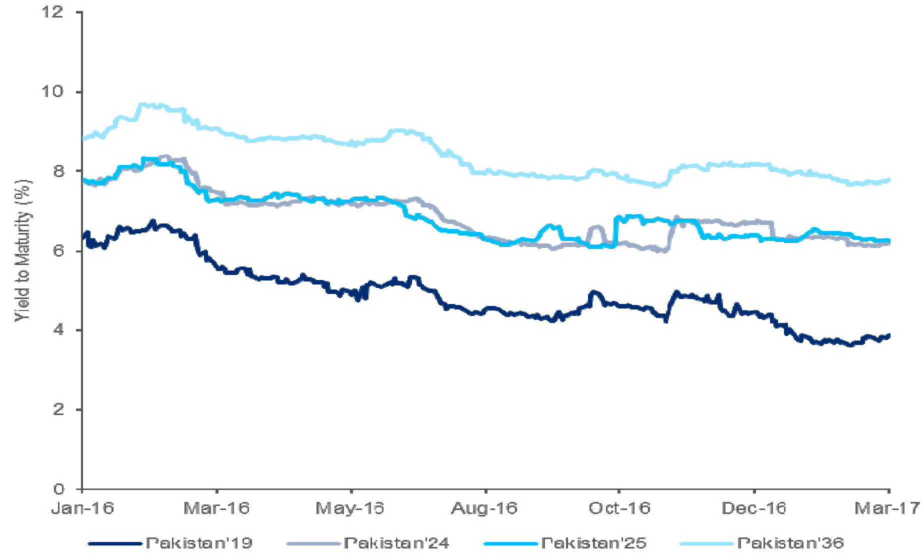
Pakistan's international Eurobonds have traded well since issuance and levels have remained relatively stable since the start of 2015, other than intermittent impact for broad based market wide volatility. Pakistan's 19s, 24s, 25s and 36s Eurobonds have broadly traded at a premium since February 2016.

Table-9.13: Secondary Trading Levels

Bond	Ratings			Maturity	Size	Coupon	Price (Bid/Ask)	Yield (%)
	M	S&P	F		($ in million)	(%)		
EM Sovereign Bonds								
Pakistan	B3	B	--	Jun-17	750	6.875	100.38/ 100.44	3.050
Pakistan	B3	B	--	Apr-19	1,000	7.250	106.13 / 106.50	3.990
Pakistan (Sukuk)	B3	B	--	Dec-19	1,000	6.750	105.13 / 106.50	4.240
Pakistan (Sukuk)	B3	B	B	Oct-21	1,000	5.500	103.75 / 104.13	4.560
Pakistan	B3	B	--	Apr-24	1,000	8.250	111.88 / 112.38	6.130
Pakistan	B3	B	B	Sep-25	500	8.250	112.88 / 113.38	6.260
Pakistan	B3	B	--	Mar-36	300	7.875	102.38 / 103.13	7.630

Source: Reuters, 20th April 2017

Fig-9.15: Pakistan Eurobonds – Historic Yield Performance:



Source: Bloomberg, April2017

9.9 Conclusion

Government is committed to accomplish objectives outlined in FRDL Act, 2005. Going forward, the prime objectives of public debt management include: (i) fulfilling the financing needs of the government at the lowest possible cost, consistent with prudent degree of risk; (ii) broadening the investor base and have a well-functioning domestic debt capital market; (iii) lengthening of maturity profile of its domestic debt portfolio to reduce the re-financing and interest rate risks; and (iv) mobilization of concessional external financing to enhance potential output by promoting efficiency and productivity, thus, simultaneously adding to the debt repayment capacity of the country. Further, it is important for the government to adopt an integrated approach for economic revival and debt reduction which will require trade-offs in the short-term, thus implementing structural reforms that boost potential growth which is a key to ensure public debt sustainability.