Debt Policy Statement
2017-18

Debt Policy Coordination Office
Ministry of Finance
Government of Pakistan

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Acknowledgements

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1.0 Introduction

1.1 Progressive public policy always aims to expedite infrastructure development which in-turn facilitate sustainable economic growth. Resource-intensive infrastructure projects remain inextricably contingent on availability of resources. Given the limited financial resources with developing countries, borrowing becomes a necessity to realize development and social welfare goals. Likewise, as a developing country, Pakistan has to maintain a delicate balance – it needs to borrow in order to facilitate its development process while ensuring that level of debt is prudently managed keeping in view of the country's repayment capacity. Therefore, prudent debt management strategy is multidimensional as on one hand it has to reconcile national development goals with sustainable levels of debt, while on the other it has to ensure that optimal financing options are selected in view of cost and risk tradeoffs.

1.2 Pakistan's public debt dynamics witnessed various positive developments during 2016-17, some of them are highlighted below:

- Government continued to adhere to the targets set forth in Medium Term Debt Management Strategy (MTDS) to ensure public debt sustainability;
- Public debt to GDP ratio improved during 2016-17 indicating reduction in relative debt burden of the country;
- Weighted average interest rate on the domestic debt portfolio has further reduced while cost of external debt contracted by the government is not only economical but is also dominated by long term funding. This reduction led to decrease in interest servicing burden as interest servicing as percentage of revenue was recorded at around 27 percent during 2016-17 compared with 33 percent during 2012-13;
- Government successfully issued a 5-year US$ 1,000 million Sukuk in October 2016 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' name with unique features of both the profits paid biannually and the prize money through quarterly draws.

1.3 Government has embarked upon a policy necessary for fiscal consolidation and debt management. Necessary amendments in Fiscal Responsibility and Debt Limitation Act were approved by the parliament to place debt-to-GDP ratio on a firm downward trajectory through sound fiscal and debt management. Accordingly, Federal Government budget deficit shall be reduced at 4 percent of GDP (excluding foreign grants) during the period 2017-18 to 2019-20 and 3.5 percent of GDP thereafter. Similarly, public debt shall be reduced to 60 percent of estimated GDP until 2017-18, and thereafter a 15-year transition has been set to bring down debt-to-GDP ratio to 50 percent.

2.0 Debt Policy Statement

2.1 The Debt Policy Statement is presented to fulfill the requirement of Section 7 of the Fiscal Responsibility and Debt Limitation (FRDL) Act, 2005 which states that:

(1) The Federal Government shall cause to be laid before the National Assembly, the Debt Policy Statement by the end of January each year.

(2) The purpose of the Debt Policy Statement is to allow the assessment of the Federal Government's debt policies against the principles of sound fiscal and debt management and the debt reduction path.

(3) In particular and without prejudice to the provisions of sub-section (2) the Debt Policy Statement shall, *inter alia*, contain –

(a) assessment of the Federal Government's success or failure in meeting the targets of total public debt to estimated gross domestic product for any given year as specified in the debt reduction path;

(b) evaluations of external and domestic borrowing strategies and provide policy advice on these strategies;

(c) analysis of the foreign currency exposure of Pakistan's external debt;

(d) consistent and authenticated information on public and external debt and guarantees issued by the Federal Government;

(e) information of all loan agreements contracted, disbursements made thereof and repayments made thereon, if any, by the Government during the fiscal year; and

(f) analysis of trends in public debt and external debt and steps taken to conform to the debt reduction path as well as suggestion for adjustments, if any, in the Federal Government's overall debt strategy.

3.0 Principles of Sound Debt Management

3.1 Debt is an important measure of bridging the financing gaps. Prudent utilization of debt leads to higher economic growth while helping the government to accomplish its social and developmental goals. Comprehensive debt management is required on part of the government to not only keep current levels of debt under control but to also fulfill the future repayment obligations. This does not subvert the importance of vigilant fiscal and monetary policies. The management of public debt requires effective coordination with macroeconomic policies, including reserve management and exchange rate policy.

3.2 Domestic and external debt needs to be treated separately owing to their different dynamics. Domestic debt is a charge on budget and must be serviced through government revenues and/or additional borrowings whereas external debt, in addition to charge on revenues, is also a charge on balance of payment and must be serviced from foreign exchange earnings, reserve drawdown and additional borrowings. Therefore, the two should be managed separately to ensure fiscal and external account solvency. Each of these types of debt has its own benefits and drawbacks, with a trade-off between costs of borrowing and exposure to various types of risks that need to be balanced in order to ensure sufficient and timely access to cost efficient funding. A comprehensive approach in managing domestic debt must place a high priority on the development of domestic capital markets and avoid the crowding-out of the private sector.

3.3 As a rule of thumb, as long as the real growth of revenue is higher than the real growth of debt, the debt to revenue ratio will not increase. Crucially, future levels of debt hinge around the primary balance of the government. Mathematically, if the primary balance (fiscal deficit before interest payments) is zero and the growth in revenue is higher than the cost of invested funds, the debt burden will ease. Bridging the gap between revenues and non-interest expenditure and ensuring reduction (generation) in primary deficit (surplus) is an essential pre-requisite that facilitates debt management efforts.

3.4 Managing the levels of external debt and the risks associated with it pose a different set of challenges. In this case, if growth in Foreign Exchange Earnings (FEE) exceeds the growth in external public debt, the ratio of external public debt to FEE will continue to decline. Although external debt expressed as a percentage of GDP and export earnings depicts the levels and burden of external debt, a clear insight into the future path of debt can also be assessed by analyzing the non-interest current account deficit. A nil current account deficit before interest payment and higher growth in FEE compared to the interest rate paid on external public debt will ensure reduction in external public debt to FEE over time. By focusing on limiting the non-interest current account deficit and ensuring that cost of borrowing is kept at a minimum, restricts the increase in debt level in the medium to long-term while partially mitigates the inherent risks of external borrowing.

4.0 Review of Public Debt

4.1 Total public debt is defined as debt of the government (including Federal Government and Provincial Governments) serviced out of consolidated fund and debts owed to the International Monetary Fund. Total debt of the Government is public debt less accumulated deposits of the Federal and Provincial Governments with the banking system. Public debt has two main components, namely domestic debt (incurred principally to finance fiscal deficit) and external debt (raised primarily to finance development expenditure).

4.2 Public debt was Rs.21,407 billion while total government debt stood at Rs.19,634 billion at end June 2017. Public debt increased by Rs.1,729 billion during 2016-17, which was significantly lower than the increase of Rs.2,297 billion recorded during the preceding fiscal year despite higher fiscal deficit witnessed in 2016-17. About 71 percent of the increase in public debt was contributed by domestic debt and 29 percent by external debt. This was in-line with the budget deficit financing as government financed around 71 percent of its budget deficit from domestic sources while the rest of the budget deficit was financed from external sources. In absolute terms, increase in public debt was lower than fiscal deficit financing during 2016-17 which is attributed to:

- Government utilized its deposits held with the banking sector primarily to retire some of the in-year borrowings from State Bank of Pakistan;
- Despite substantial external inflows, the net addition to external public debt (in Pak rupees) was lower than external financing of fiscal deficit, mainly due to revaluation gains on account of appreciation of US dollar against other international currencies.

Table-1: Public Debt

	2013	2014	2015	2016(P)	2017(P)	2018(P)*
(Rs. in billion)						
Gross Domestic Debt	9,521.9	10,920.0	12,198.9	13,626.9	14,855.0	15,375.5
*Net Domestic Debt	8,686.2	9,551.3	10,804.8	11,773.5	13,081.7	13,509.9
External Public Debt	4,796.5	5,071.5	5,181.8	6,051.1	6,552.1	6,683.4
Gross Public Debt	14,318.4	15,991.5	17,380.7	19,678.1	21,407.1	22,058.9
***Total Government Debt**	13,482.7	14,622.8	15,986.6	17,824.6	19,633.8	20,193.3
(In percent of GDP)						
Gross Domestic Debt	42.5	43.4	44.5	46.8	46.6	42.8
*Net Domestic Debt	38.8	37.9	39.4	40.5	41.1	37.6
External Public Debt	21.4	20.1	18.9	20.8	20.6	18.6
Gross Public Debt	64.0	63.5	63.3	67.6	67.2	61.4
***Total Government Debt**	60.2	58.1	58.3	61.2	61.6	56.2
Memo:						
External Public Debt (US$ in billion)	48.1	51.3	50.9	57.7	62.5	63.4
Exchange Rate (Rs./US$, End of Period)	99.7	98.8	101.8	104.8	104.9	105.4
GDP (Rs. in billion)	22,385.7	25,168.8	27,443.0	29,102.6	31,862.2	35,919.0

*Net of government deposits with the banking system

P:Provisional *end-September, 2017

Source: State Bank of Pakistan, Economic Affairs Division, Budget Wing and Debt Policy Coordination Office

4.3 The composition of public debt in terms of maturity profile witnessed slight changes during 2016-17. Both demand and supply factors contributed towards the change in composition of public debt. Demand for medium to long term government securities was relatively lower in anticipation of change in the interest rates, inflation and liquidity conditions while the government was cautious about the cost-risk tradeoff as market participants were seeking higher than usual rates on long-term securities. Accordingly, the share of public debt maturing within one year increased to around 42 percent at end June 2017 compared with around 40 percent at end June 2016 while it was around 46 percent at end June 2013. However, this increase was compensated by reduction in cost of public debt portfolio as evident from the fact that the government's interest expenditure was reduced to 27 percent of total revenue during 2016-17 as compared with 33 percent during 2012-13. It reaffirmed the need to evaluate debt risks indicators in conjunction with cost as Medium Term Debt Management Strategy (MTDS) emphasizes tradeoff between cost and risk indicators.

4.4 Encouragingly, cost and most of the risk indicators of public debt portfolio have witnessed improvement during four years in-line with the objectives set forth in Pakistan's first MTDS (2012/13-2017/18). The average cost of gross public debt was reduced by over 100 basis points during last four years owing to smooth execution of the MTDS. Refinancing Risk of domestic debt portfolio was reduced from 64.2 percent in 2013 to 55.6 percent in 2017. Exposure to interest rate risk was also reduced, as the percentage of debt re-fixing in one year decreased to 47.8 percent in 2017 compared to 52.4 percent in 2013. Similarly, share of external loans maturing within one year was equal to around 27.7 percent of official liquid reserves in 2017 compared with around 68.5 percent in 2013 indicating improvement in foreign exchange stability and repayment capacity.

4.5 One of the objectives of MTDS was to facilitate the development of debt capital market. A well-developed debt market for long term investment is essential for the growth of economy as it provides additional avenues for raising funds besides providing investment opportunities to the investors. Government is taking various steps to provide an efficient and liquid secondary debt market to the investors (Box-1).

BOX-1 - STEPS TAKEN FOR THE DEVELOPMENT OF DEBT CAPITAL MARKET

I. Deployment of automated system for the e-reporting of listed and unlisted debt issues including:
   - Features of each issue of debt securities;
   - Redemption status of issued debt securities;
   - Compliance status of the covenants of the trust deeds.

II. Formulation of Debt Securities Trustee Regulations, 2017;
III. Formulation of Public Offering Regulations, 2017;
IV. Formulation of Bond Pricing Agency Rules, 2017;
V. Formulation of Sukuk (Privately Placed) Regulations, 2017;
VI. Rationalization of fresh issue fee on instruments of redeemable capital charged by Central Depository Company (CDC);
VII. Implementation of Centralized E-PO System (CES) to facilitate investors to submit application for subscription of securities offered through public offer, including debt securities, through internet banking, ATM and mobile phones;
VIII. Tax credit to the public for cost of acquiring Sukuk offered by a public listing company and traded on stock exchange if investor is the original allottee of the Sukuk;
IX. Launch of Fixed Income Securities Certification by Institute of Financial Markets of Pakistan (IFMP);
X. Training program on "Fixed Income Investment & Trading Certification" jointly organized by USAID Financial Market Development Activity and IFMP.

FUTURE PLANS WITH REGARD TO DEVELOPMENT OF DEBT CAPITAL MARKET:

I. Establishment of Bond Pricing Agency;
II. Formulation of Shariah Advisors Regulations, 2017;
III. Review of the Companies (Asset Backed Securitization) Rules, 1999;
IV. Rationalization of rate of stamp duty applicable on the issuance of debt instruments;
V. Review of the Regulations for listing of debt securities issued to the Qualified Institutional Buyers (QIBs);
VI. Development of a Shariah Governance Framework for development of Islamic capital markets (including debt market);
VII. Facilitation of Pakistan Mortgage Refinance Company (PMRC) in fund raising from debt capital markets;
VIII. Training sessions on fixed income trading/ capacity building of market participants;
IX. Study on Exchange Traded Funds (ETF) on fixed income securities.

Source: Securities and Exchange Commission of Pakistan

4.6 Government was required to meet Pakistan Investment Bonds (PIBs) maturity amounting to Rs.1,427 billion during the first quarter of 2016-17. Given the impact of maturing amount on appetite of domestic debt market, the government planned well in time and started mobilizing more through fresh issuance of PIBs and Government Ijara Sukuk (GIS) to cover 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 neutralize the overall impact of PIBs maturity on domestic debt sustainability indicators, however, the entire PIBs amount was challenging to re-finance during first quarter through fresh issuance of PIBs which resulted in positive quarterly borrowing from the SBP. However, the reliance on SBP borrowing was reduced in subsequent quarters of 2016-17 as government retired some of its borrowing from SBP which enabled the government to meet its net zero quarterly limit under the amended SBP Act 1956 during last three quarters of 2016-17. However, borrowings from SBP remained positive during first quarter of 2017-18 as the government required to meet PIBs maturity amounting Rs.597 billion which could not be refinanced from medium to long term instruments due to demand and supply side factors mentioned earlier. It is worth noting here that net zero quarterly borrowing was tied with fixation of ways and means limit which is yet to be finalized.

4.7 Public debt was Rs.22,059 billion while total government debt was Rs.20,193 billion at end September 2017. Gross Public debt increased by around Rs.652 billion during first quarter of 2017-18. Out of this total increase, increase in domestic debt was Rs.521 billion while government borrowing from domestic sources for financing of fiscal deficit was Rs.433 billion. This differential is mainly attributed to increase in government credit balances with the banking system. Similarly, external public debt recorded an increase of around Rs.131 billion which was predominantly driven by translational losses on account of appreciation of international currencies against US Dollar and depreciation of Pak Rupee against US Dollar.

4.8 In US Dollar terms, external public debt increased by around US$ 0.9 billion during first quarter of 2017-18 and recorded at US$ 63.4 billion at end September 2017. Government mobilized US$ 1,468 million during first quarter of 2017-18, mainly from multilateral sources (US$ 642 million), commercial loans (US$ 472 million) and bilateral sources contributed US$ 354 million (mainly from China amounting US$ 317 million). Government also repaid US$ 1,349 million during the first quarter of 2017-18.

5.0 Dynamics of Public Debt Burden

5.1 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”. Debt burden can be expressed in terms of the stock ratio i.e. in terms of GDP or flow ratios i.e. in terms of revenues.

Table-2: Selected Public Debt Indicators (in percentage)

	2013	2014	2015	2016	2017
Revenue Balance* / GDP	(2.9)**	(0.7)	(1.7)	(0.8)	(0.7)
Primary Balance* / GDP	(3.6)**	(0.2)	(0.5)	(0.2)	(1.5)
Fiscal Balance / GDP	(8.2)**	(5.5)	(5.3)	(4.6)	(5.8)
Gross Public Debt / GDP	64.0	63.5	63.3	67.6	67.2
Total Government Debt / GDP	60.2	58.1	58.3	61.2	61.6
Gross Public Debt / Revenue	480.1	439.7	442.1	442.5	433.6
Total Government Debt / Revenue	452.1	402.0	406.7	400.8	397.7
Debt Service / Revenue	40.5	40.1	40.4	35.9	38.3
Interest Service / Revenue	33.2	31.6	33.2	28.4	27.3
Debt Service / GDP	5.4	5.8	5.8	5.5	5.9

*Adjusted for grants
[a] 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

5.2 The revenue deficit[1], which excludes development expenditure, recorded at 0.7 percent of GDP in 2016-17 compared with 0.8 percent during the preceding fiscal year. This reduction in revenue deficit shows that growth in revenue outpaced the growth in current expenditure during 2016-17. Thus, from expenditure side, fiscal deficit was driven largely by an increase in development expenditures and recorded at 5.8 percent during 2016-17 compared with 4.6 percent during the preceding fiscal year. Similarly, the primary deficit[2], which excludes interest payments, increased to 1.5 percent of GDP during 2016-17 from 0.2 percent during 2015-16 owing to the same reason. The consolidated development expenditures

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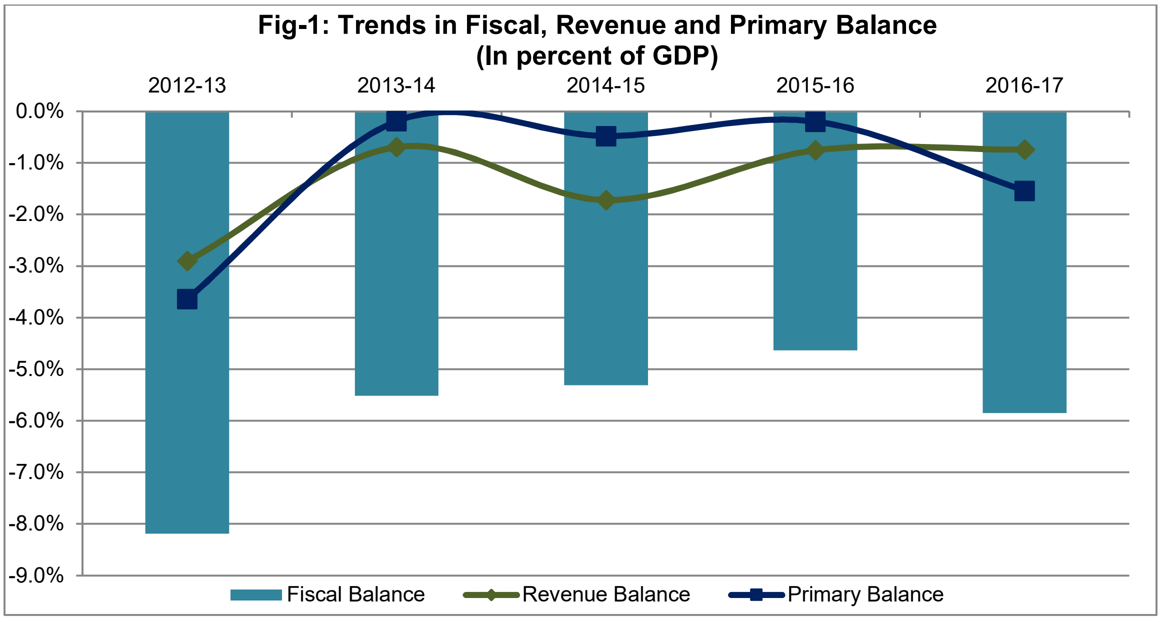
[1] Revenue balance is the total revenues minus current expenditure. The persistence of revenue deficit indicates that the government is not only borrowing to finance its development expenditure, but partially to finance its current expenditure.

[2] 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.

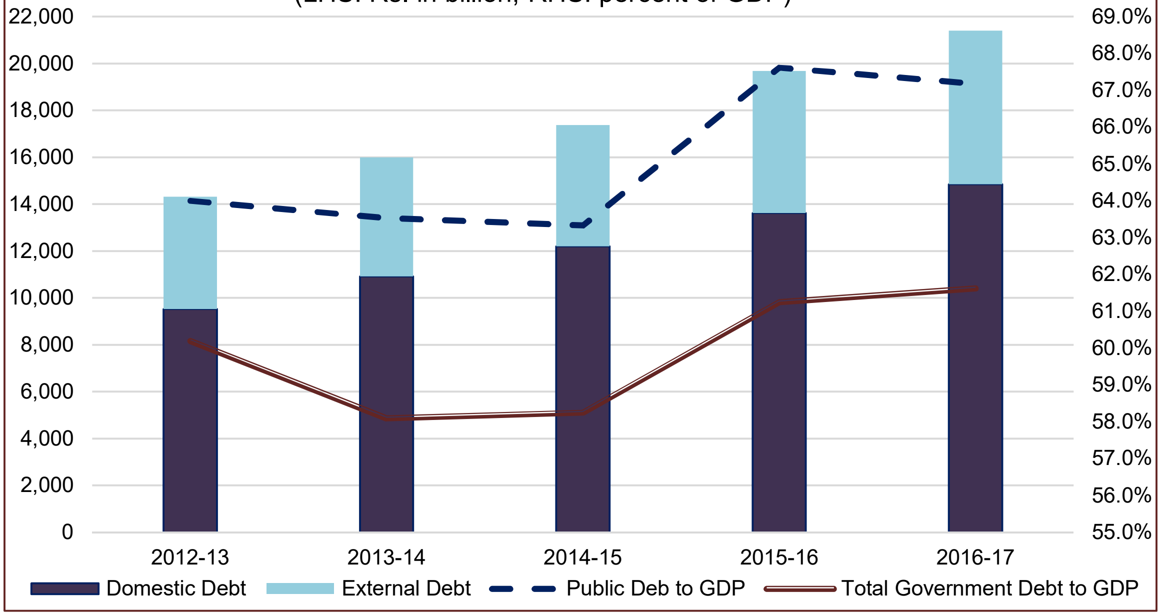
maintained the momentum observed during the last few years owing to ongoing number of infrastructure projects. Accordingly, actual PSDP spending at federal level and annual development plan at provincial level cumulatively grew from Rs.695 billion in 2012-13 to Rs.1,577 billion in 2016-17. Furthermore, relatively contained interest payment during the last few years created additional fiscal space for increased development spending. The trends in fiscal, revenue and primary balance are depicted in the graph below:



5.3 It is to be noted that the debt burden is better understood in comparison to its relation with GDP instead of absolute debt numbers. The government debt was as high as over 100 percent of its GDP at the end of 2001 while it is hovering around 60 percent during last 15 years. Another way to gauge the increase in public debt burden of the country is to compare that with relevant global debt statistics. In this regard, Pakistan witnessed a marginal increase of 1.4 percent (from 60.2 percent in 2013 to 61.6 percent in 2017) in its total government debt to GDP ratio during last four years while during the same period global debt to GDP ratio increased by about 8 percent[3]. The public debt position since fiscal year 2013 (both in absolute and GDP terms) are depicted in the following graph:

[3] Source IMF World Economic Outlook

Fig-2: Profile of Public Debt
(LHS: Rs. in billion, RHS: percent of GDP)



The table below shows the summary of debt to GDP ratio of few developed and developing economies:

Table-3: Country Wise Total Government Debt to GDP Ratio (in percentage)

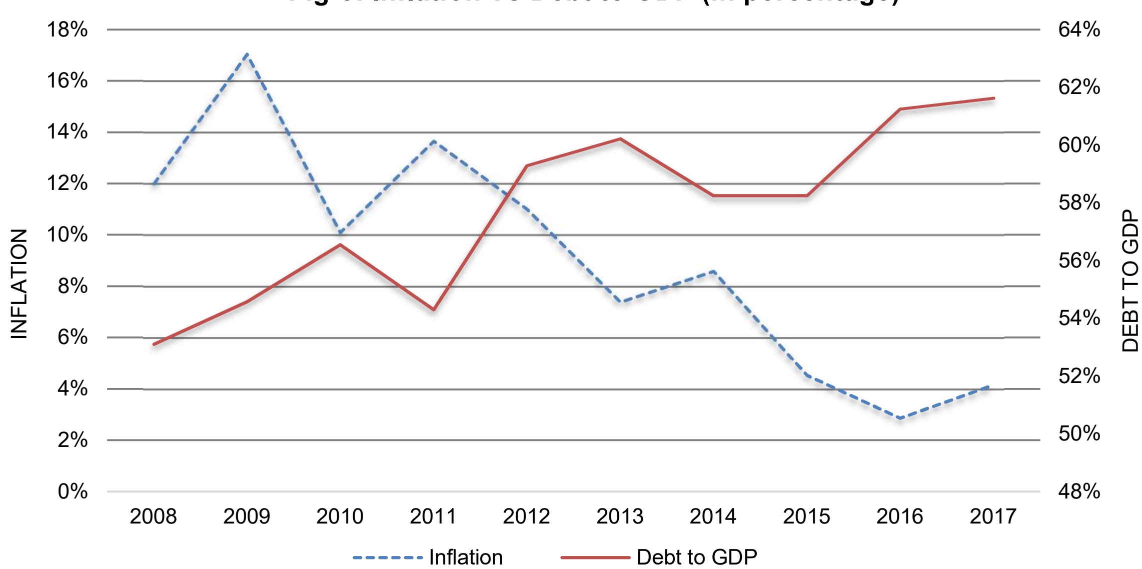
Country	2013	2014	2015	2016	2017
United States	81.5	80.9	80.5	81.4	82.4
United Kingdom	77.7	79.6	80.4	80.7	80.4
Japan	117.3	118.9	118.3	119.7	119.9
India	68.5	68.5	69.5	69.5	67.7
Srilanka	70.8	70.7	76.0	77.3	79.5
Egypt	73.7	77.1	78.8	88.1	93.6
Pakistan	60.2	58.1	58.3	61.2	61.6

Source: IMF World Economic Outlook

5.4 It is evident from the table above that developed countries like USA, UK and Japan also carry debt and maintain levels as high as 80 to over 100 percent of their GDPs, well over Pakistan debt to GDP levels. Even in the developing country peer group, Egypt, Srilanka and India carry higher debt to GDP levels than Pakistan.

5.5 The analysis of debt to GDP ratio during past years reveals that in the period of high inflation, debt to GDP ratio performed relatively better as the denominator becomes larger and this ratio remained below 60 percent even when real GDP growth was merely half a percent e.g. 2008-09. While higher inflation could help reducing the debt-to-GDP ratio yet it has other repercussions for the economy. Therefore, economic managers would always prefer high real GDP growth coupled with low inflation rather than low real GDP growth coupled with high inflation. During 2016-17, actual inflation stood around 4 percent against target of 6 percent, causing nominal GDP at Rs.31,862 billion against target Rs.33,509 billion. Therefore, debt to GDP went slightly up mainly owing to lower than anticipated inflation.

Fig-3: Inflation Vs Debt to GDP (in percentage)



*Correlation coefficient (ρ) between inflation and debt to GDP ratio = - 0.82

5.6 Public debt levels against actual government revenues reveal important information about debt repayment capacity of the country. There was around 9 percentage point reduction in public debt to government revenues ratio which stands at 434 percent in 2016-17 as compared with 443 percent in 2015-16 while total government debt to government revenues reduced by around 3 percentage point during 2016-17 as compared with previous fiscal year, indicating some easing in government indebtedness. Encouragingly, growth in revenue outstripped the growth in public debt and accordingly debt repayments capacity improved during 2016-17. Government is committed to reduce this ratio to generally acceptable threshold of 350 percent to further improve the debt carrying capacity of the country.

6.0 Servicing of Public Debt

6.1 Comparing debt service to a country's repayment capacity yields the best indicator for analyzing whether a country is likely to face debt-servicing difficulties in a given period. During 2016-17, public debt servicing was recorded at Rs.1,893 billion against the annual budgeted estimate of Rs.1,945 billion. Public debt servicing consumed nearly 38 percent of total revenues while interest servicing consumed around 27 percent of total revenue during 2016-17 compared with 33 percent during 2012-13.

Table-4: Public Debt Servicing **(Rs. in billion)**

	2016-17			
	Budgeted	**Actual**	**Percent of Revenue**	**Percent of Current Expenditure**
Repayment of External Debt	585.2	544.3	11.0	10.5
Total External Principal Repayment (A)	**585.2**	**544.3**	**11.0**	**10.5**
Servicing of External Debt	113.0	128.2	2.6	2.5
Servicing of Domestic Debt	1,247.0	1,220.3	24.7	23.5
Total Interest Servicing (B)	**1,360.0**	**1,348.4**	**27.3**	**25.9**
Total Servicing of Public Debt (A+B)	**1,945.2**	**1,892.7**	**38.3**	**36.4**

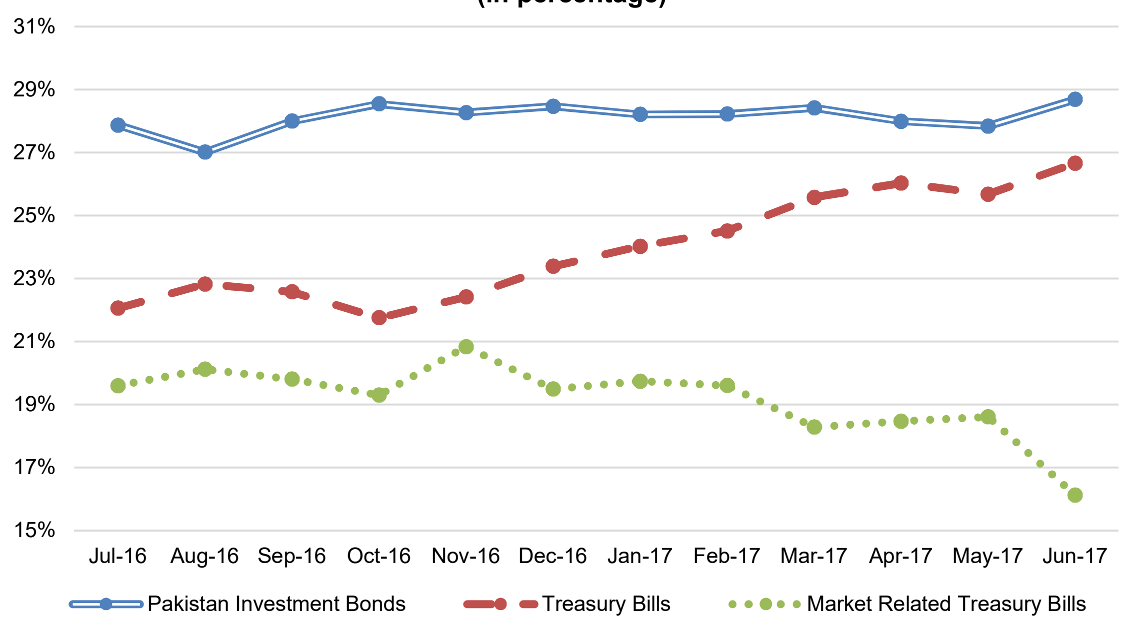
Source: Budget Wing and Debt Policy Coordination Office Staff Calculations, Ministry of Finance

6.2 Domestic interest payments constituted around 90 percent of total interest servicing which is due to increasing volume of domestic debt in overall public debt portfolio. Encouragingly, in absolute terms, domestic debt servicing remained almost at the same level of 2014-15 despite increase in domestic debt stock by around Rs.2.7 trillion during last two years owing to low domestic interest rate environment and smooth execution of MTDS. Further analysis of domestic debt servicing reveals that large portion was paid against PIBs (Rs.502 billion), followed by Treasury Bills (Rs.201 billion), Market Related Treasury Bills (Rs.151 billion), Bahbood Saving Certificates (Rs.96 billion) and Special Savings Certificates and Accounts (Rs.84 billion).

7.0 Domestic Debt

7.1 Gross domestic debt was Rs.14,855 billion while net domestic debt was Rs.13,082 billion at end June 2017. The pace of domestic debt accumulation slowed down, recording 9 percent increase in 2016-17 compared with 12 percent increase in 2015-16. This reduced momentum in domestic debt accumulation is partly attributed to utilization of government deposits held with the banking system during 2016-17. Most of the fresh mobilization was recorded in floating debt which led to increase in short term borrowing proportion to 44 percent at end June 2017 compared with 37 percent at end June 2016. However, increase in refinancing risk owing to higher proportion of short term borrowing needs to be understood with respect to the overall interest rate environment whereby banks preferred to shorten the duration of their investment portfolio. This caused the cost of domestic debt portfolio to decrease by around 90 basis points during 2016-17. The month wise share of Treasury Bills, Market Related Treasury Bills (MRTBs) and PIBs in domestic debt portfolio during 2016-17 is depicted in the table below:

Figure-4: Share of Treasury Bills, MRTBs and PIBs in Domestic Debt (in percentage)



7.2 Overall, average cost of domestic debt portfolio has reduced by around 250 basis points during last four years. The reduction in interest servicing cost was facilitated by conducive economic environment coupled with supportive monetary policy that created opportunity for the government to reduce the interest rates on its wholesales debt instruments along with aligning the rates on retail debt instruments with the wholesale market yields. It needs to be appreciated that the interest rate reduction on government domestic debt portfolio was done without any material impact on the duration of the portfolio owing to smooth execution of MTDS resulting in an additional annual savings for the government on account of interest servicing.

Table-5: Outstanding Domestic Debt - (Rs. in billion)

	2013	2014	2015	2016(P)	2017(P)	2018(P) *
Permanent Debt	**2,179.2**	**4,005.3**	**5,016.0**	**5,944.2**	**5,533.1**	**5,022.6**
Market Loans	2.9	2.9	2.8	2.8	2.8	2.8
Government Bonds	0.7	0.7	0.7	0.7	0.7	0.7
Prize Bonds	389.6	446.6	522.5	646.4	747.1	777.6
Foreign Exchange Bearer Certificates	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
Federal Investment Bonds	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
Foreign Currency Bearer Certificates	0.0	0.0	0.0	0.0	0.0	0.0
U.S. Dollar Bearer Certificates	0.0	0.0	0.1	0.1	0.1	0.1
Special U.S. Dollar Bonds	4.2	4.4	4.4	4.5	4.5	4.5
Government Bonds Issued to SLIC	0.6	0.6	0.6	0.6	0.6	0.6
Pakistan Investment Bonds (PIBs)	1,321.8	3,223.5	4,158.3	4,925.0	4,391.8	3,850.8
GOP Ijara Sukuk	459.2	326.4	326.4	363.9	385.4	385.4
Floating Debt	**5,196.2**	**4,610.9**	**4,612.6**	**5,001.8**	**6,556.6**	**7,568.6**
Treasury Bills through Auction	2,921.0	1,758.6	2,331.3	2,771.6	4,087.7	4,827.9
Rollover of Treasury Bills discounted SBP	0.5	0.5	0.5	0.5	0.5	0.5
Market Related Treasury Bills (MRTBs)	2,274.7	2,851.8	2,280.9	2,017.1	2,468.4	2,740.3
Bai Muajjal	-	-	-	212.6	-	-
Unfunded Debt	**2,146.5**	**2,303.8**	**2,570.3**	**2,680.9**	**2,765.3**	**2,784.3**
Defence Savings Certificates	271.7	284.6	300.8	308.9	325.5	326.4
Khas Deposit Certificates and Accounts	0.6	0.6	0.6	0.6	0.5	0.5
National Deposit Certificates	0.0	0.0	0.0	0.0	0.0	0.0
Savings Accounts	22.3	22.6	26.4	29.2	34.9	34.0

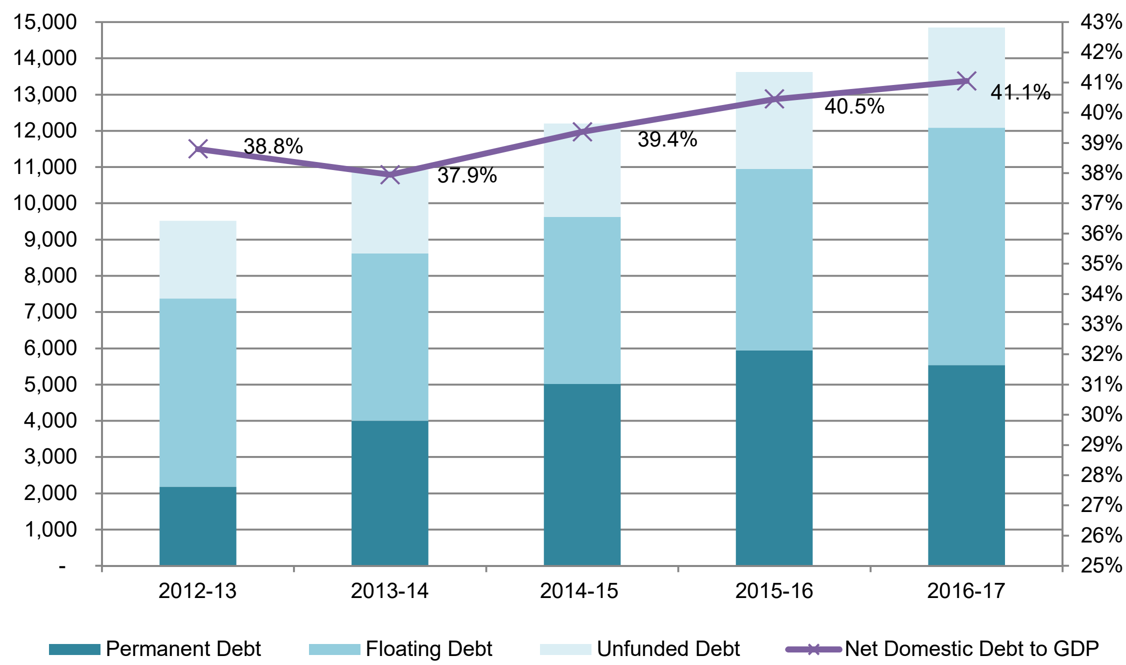
Table-5: Outstanding Domestic Debt - (Rs. in billion)

	2013	2014	2015	2016(P)	2017(P)	2018(P) *
Mahana Amdani Account	2.0	1.9	1.8	1.8	1.7	1.7
Postal Life Insurance	67.1	67.1	67.1	67.1	45.8	45.9
Special Savings Certificates and Accounts	734.6	738.8	867.5	896.5	922.4	929.1
Regular Income Scheme	262.6	325.4	376.0	359.8	338.8	334.5
Pensioners' Benefit Account	179.9	198.4	214.1	234.7	253.4	258.4
Bahbood Savings Certificates	528.4	582.4	628.3	692.1	749.5	762.3
National Savings Bonds	0.2	0.2	0.1	0.1	0.1	0.1
G.P. Fund	73.1	80.5	85.8	88.3	88.8	87.9
Short Term Savings Certificates	4.0	1.3	1.7	1.9	3.7	3.5
Total Domestic Debt	**9,521.9**	**10,920.0**	**12,198.9**	**13,626.9**	**14,855.0**	**15,375.5**
P: Provisional						*end-September,2017

Source: Budget Wing, Finance Division and State Bank of Pakistan

The category wise domestic debt[4] along with the net domestic debt to GDP ratio is illustrated in the following graph:

Fig-5: Evolution of Domestic Debt
(LHS: Rs. in billion, RHS: percent of GDP)



[4] 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).

7(i) Auction Profile of Government Securities

7.3 The auction profile of the government securities depicts varied pattern of investment by commercial banks during 2016-17, depending on their perception of changes in interest rates, inflation, liquidity conditions and external sector developments. In this context, following points are worth noting:

- The policy rate remained unchanged throughout the 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 and amounts were not substantial. Any acceptance in these PIBs auctions may have signaled 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 current account deficit. Nonetheless, as the actual inflation consistently turned out to be lower than market expectations and accordingly some correction in the longer segment of the yield curve was observed during second half of 2016-17. Amid subdued participation, mobilization through PIBs remained less than its pre-auction targets during third and four quarters of 2016-17 as the government cautiously evaluated the emerging scenario.
- During first quarter of 2016-17, the government had to meet the higher maturity against PIBs which could not be fully refinanced through medium to long term domestic debt instruments. Therefore, the government accepted higher than the target amount in Treasury Bills auctions. The offered amount in Treasury Bills auctions was Rs.3,149 billion, which was higher than both the target and maturity. However, the government accepted Rs.1,764 billion against the target of Rs.1,450 billion keeping in view cost and risks trade-off. Similar to first quarter, the offered amounts in Treasury Bills auctions were higher than both the target and maturity during

second quarter of 2016-17, however, fresh mobilization through Treasury Bills remained within the announced target.

- During second half of 2016-17, the commercial bank's interest for PIBs somewhat recovered, however, Treasury Bills remained a preferred choice. Specifically, the offered amount in Treasury Bills was recorded at Rs.4,395 billion during third quarter of 2016-17 and the government mobilized Rs.2,964 billion against the target of Rs.2,550 billion. Government adhered to its Treasury Bills auction target during fourth quarter of 2016-17 as shortfall in PIBs auctions was covered through external finances.

The yields (6 months T-bills, 3, 5 and 10 years PIBs) and auction wise details from July 2016 to June 2017 are depicted through following graph:

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

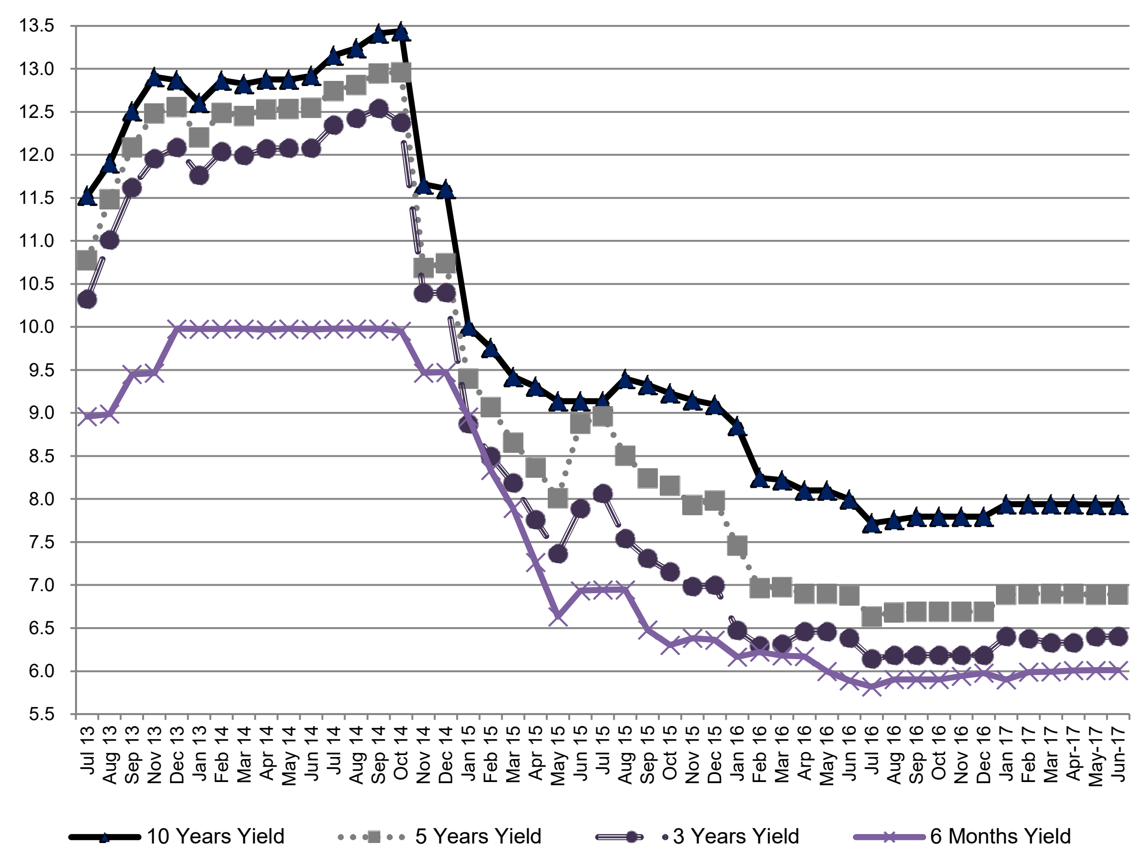
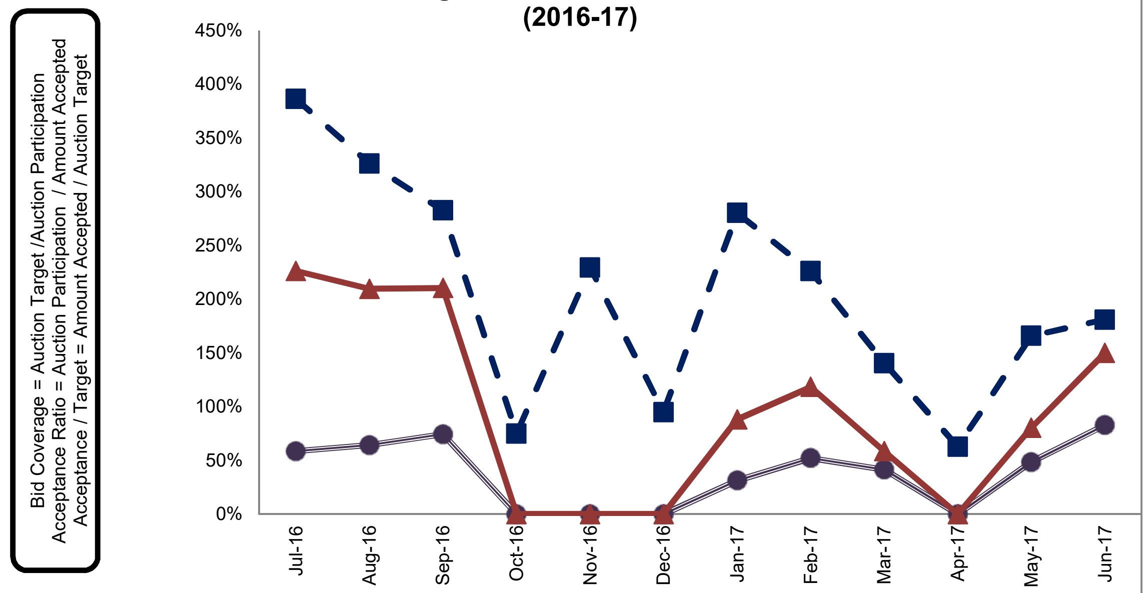
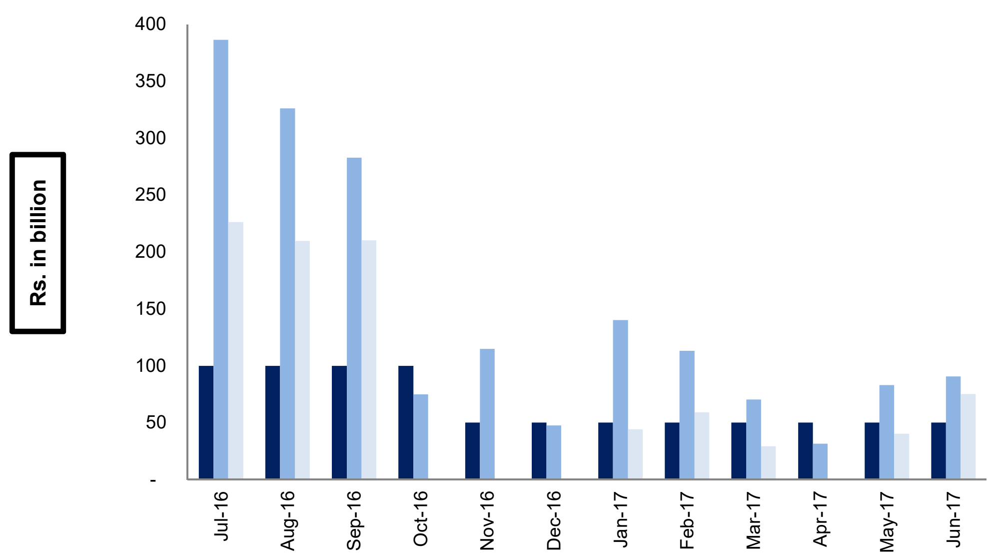


Fig-7: PIBs Auction Ratios (2016-17)



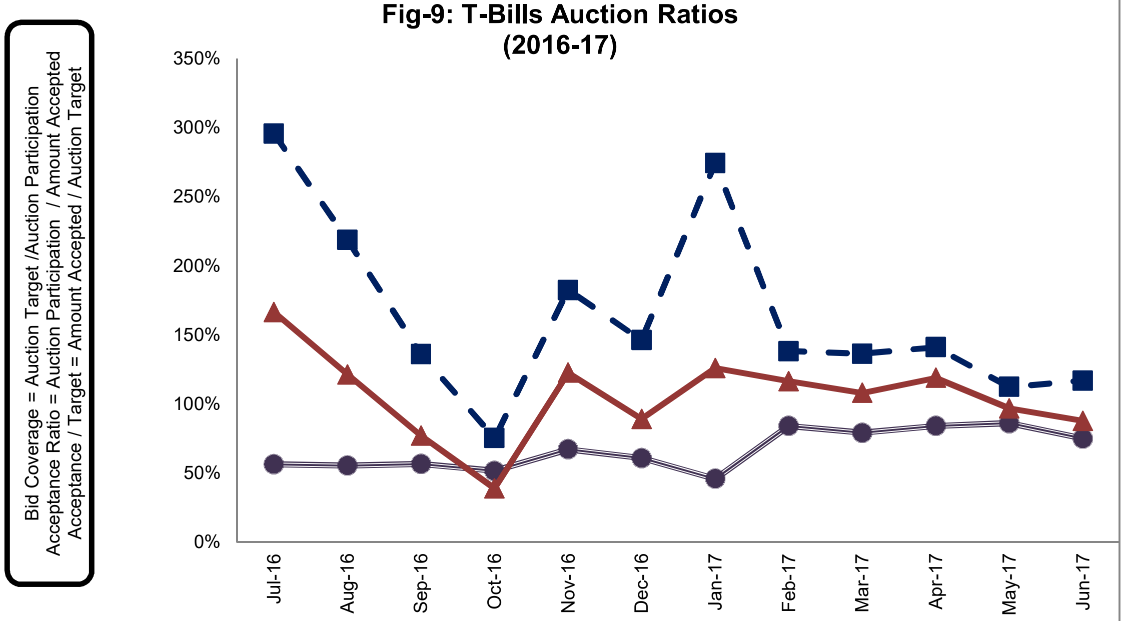
	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17
Bid Coverage	386%	326%	283%	75%	229%	95%	280%	226%	141%	63%	166%	181%
Acceptance Ratio	59%	64%	74%	0%	0%	0%	31%	52%	42%	0%	48%	83%
Acceptance/ Target	226%	210%	210%	0%	0%	0%	88%	118%	58%	0%	80%	150%

Fig-8: PIBs Auction Profile (2016-17)



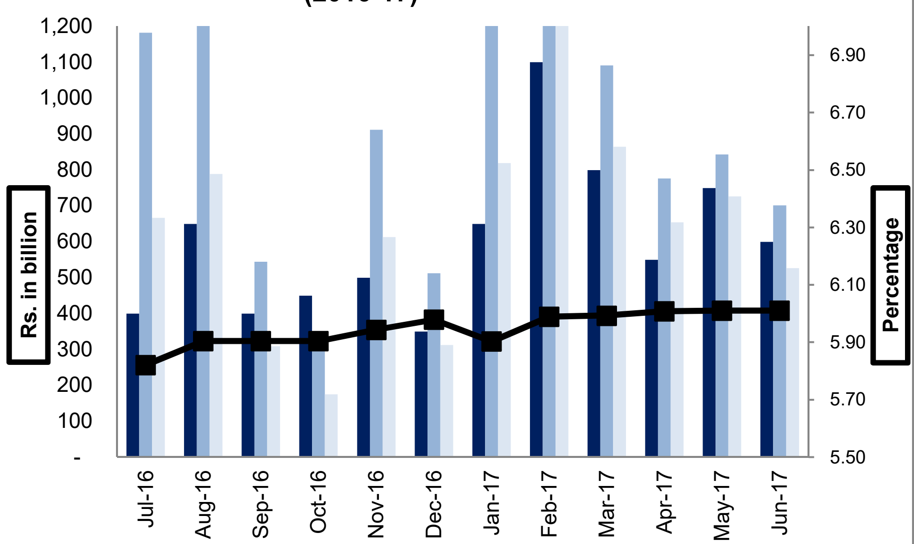
	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17
Auction Target (Rs. in billion)	100	100	100	100	50	50	50	50	50	50	50	50
Auction Participation (Rs. in billion)	386	326	283	75	115	48	140	113	70	31	83	91
Amount Accepted (Rs. in billion)	226	210	210	-	-	-	44	59	29	-	40	75

Fig-9: T-Bills Auction Ratios (2016-17)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17
Bid Coverage	296%	219%	136%	75%	182%	146%	274%	138%	136%	141%	112%	117%
Acceptance Ratio	56%	55%	57%	52%	67%	61%	46%	84%	79%	84%	86%	75%
Acceptance/ Target	167%	121%	77%	39%	123%	89%	126%	116%	108%	119%	97%	88%

Fig-10: T-Bills Auction Profile (2016-17)



	Jul-16	Aug-16	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17
Auction Target (Rs. in billion)	400	650	400	450	500	350	650	1,100	800	550	750	600
Auction Participation (Rs. in billion)	1,183	1,422	545	339	912	512	1,783	1,521	1,091	776	843	702
Amount Accepted (Rs. in billion)	666	789	309	175	613	312	819	1,281	865	654	726	527
6 month T-Bill Yield (%)	5.82	5.90	5.90	5.90	5.94	5.98	5.90	5.99	5.99	6.01	6.01	6.01

7(ii) Secondary Market Activities of Government Securities

7.4 The secondary market trading volumes of the government securities witnessed considerable increase during 2016-17, as government securities worth Rs.14,779 billion were traded on outright basis, reflecting a growth of 31 percent year on year (Ref:Table-6). This translates into an average daily trading volume of Rs.60 billion in 2016-17 compared with Rs.45 billion in 2015-16. In 2016-17, the secondary market trading grew faster than the growth in primary issuances, which can be seen in increased turnover of 1.64 times.

Table-6: Secondary Market Outright Trading Volume

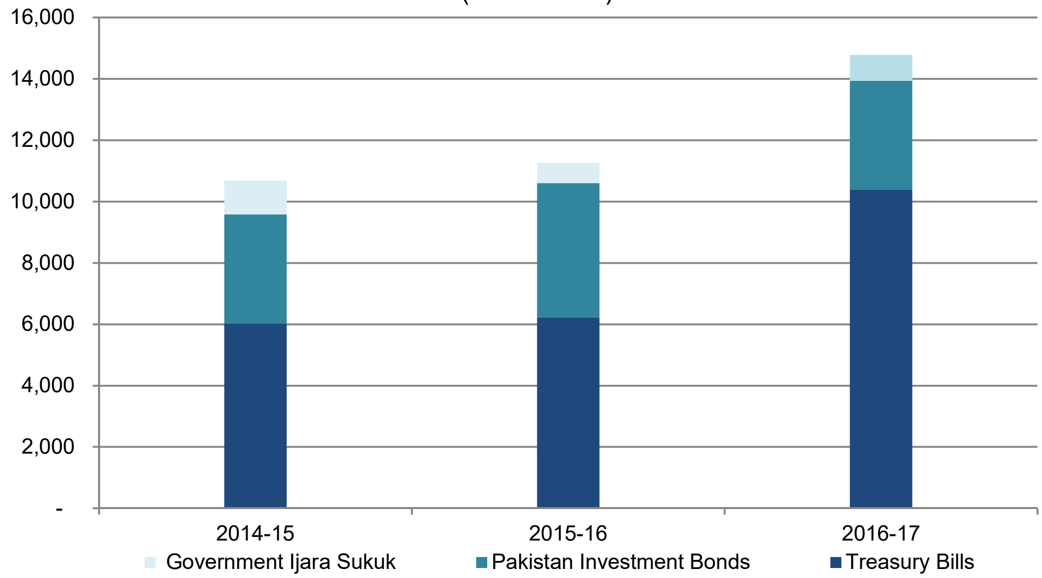
(Rs. in billion)			
Security	**2014-15**	**2015-16**	**2016-17**
Treasury Bill - 3 Months	1,550	1,369	4,954
Treasury Bill - 6 Months	2,156	2,142	3,069
Treasury Bill - 12 Months	2,325	2,720	2,361
Pakistan Investment Bonds - 3 Years	1,751	2,387	1,480
Pakistan Investment Bonds - 5 Years	742	959	1,193
Pakistan Investment Bonds - 10 Years	1,014	1,018	853
Pakistan Investment Bonds - 15 Years	6	3	4
Pakistan Investment Bonds - 20 Years	34	10	19
Sukuk	1,110	653	846
Total	10,689	11,261	14,779
Daily Average volume	43.3	44.9	60.3
End Period Stock	6,955	8,199	8,991
Turnover Ratio (times)	1.54	1.37	1.64

Source: State Bank of Pakistan

7.5 The surge in secondary market trading of government securities was mainly driven by Treasury Bills, as shown in figure 11, the share of Treasury Bills in overall secondary market trading volume increased to 70 percent in 2016-17 from 55 percent in 2015-16. The increase in share of Treasury Bills (i.e. the decline in share of PIBs) in overall market trading volume is primarily owed to the buy-and-hold behavior of the long term investors amidst greater issuances of Treasury Bills than

PIBs by the Government of Pakistan in 2016-17 and increased interest of market participants in Treasury Bills in anticipation of bottoming-out of interest rates.

Fig-11: Share of Government Securities in Overall Trading Volume
(Rs in billion)



7.6 The secondary market trading of Government Ijara Sukuk (GIS) increased slightly, as compared to previous years on the back of fresh issuance of new 3-year Fixed Rental Rate GIS in 2016-17. However, the share of GIS in overall secondary market trading of government securities is still very low, which reflect scarcity of the Shariah compliant instruments in the market.

Repo Market:

7.7 During 2016-17, trading volumes in the repo market increased to Rs.19,609 billion, showing a growth of 45.6 percent (Ref:Table-7). Encouragingly, the rise in repo trade is accompanied with a significant growth in outright trading; reflecting that the banks have accessed the secondary market for both short-term liquidity management as well as for satisfying long-term trading appetite. Overall, the share of repo market in the government securities' secondary market increased by 3 percentage points to 57 percent in 2016-17. As expected, the activity in the repo market was largely concentrated in overnight tenure, which constituted around 88 percent of the repo market volume, indicating banks utilization of repo market for short-term liquidity management.

Table-7: Government Security based Transactions

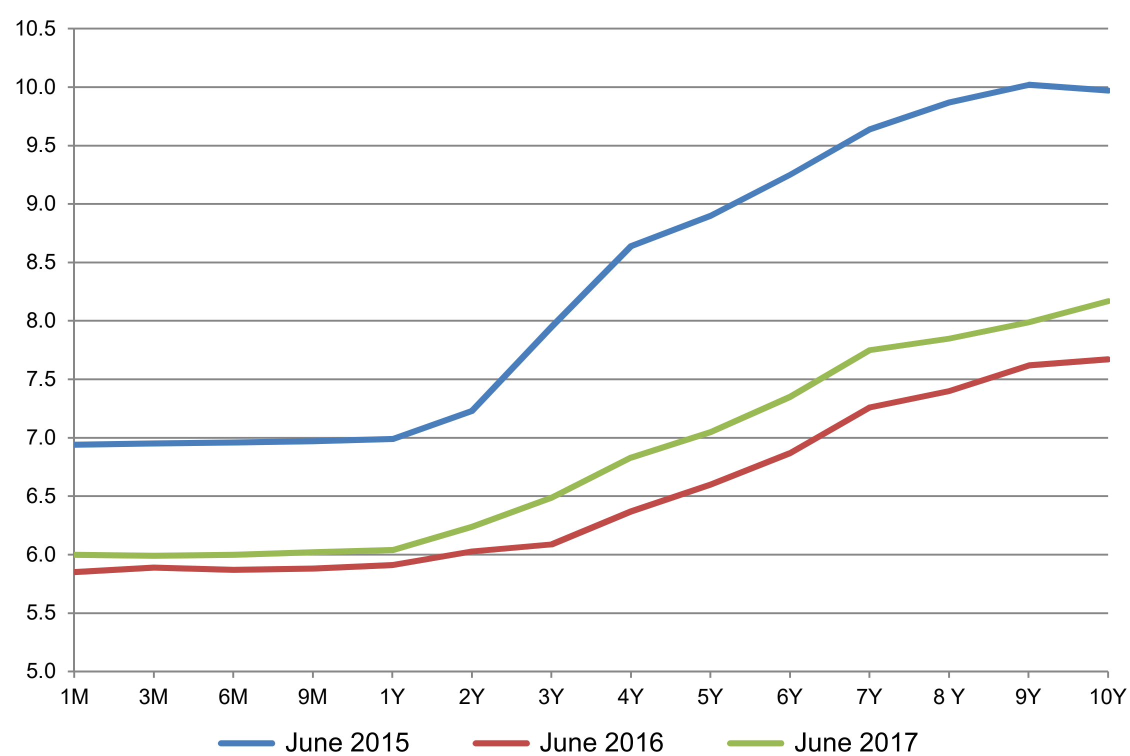
Type	Volume (Rs. in billion)			Percentage Share (%)		
	2014-15	2015-16	2016-17	2014-15	2015-16	2016-17
Repo	14,146	13,469	19,609	57	54	57
Outright	10,690	11,261	14,779	43	46	43
Total	**24,836**	**24,730**	**34,388**	**100**	**100**	**100**

Source: State Bank of Pakistan

Yield Curve Trend:

7.8 With the State Bank of Pakistan maintaining status quo on the policy rate in 2016-17, yield curve for the government securities remained largely unchanged for tenors up to 1 year. However, the yield curve steepened a bit for longer tenors (3-10 years). This shows that market perceives that the interest rates have bottomed out.

Fig-12: Secondary Market Yield Curve (in percentage)



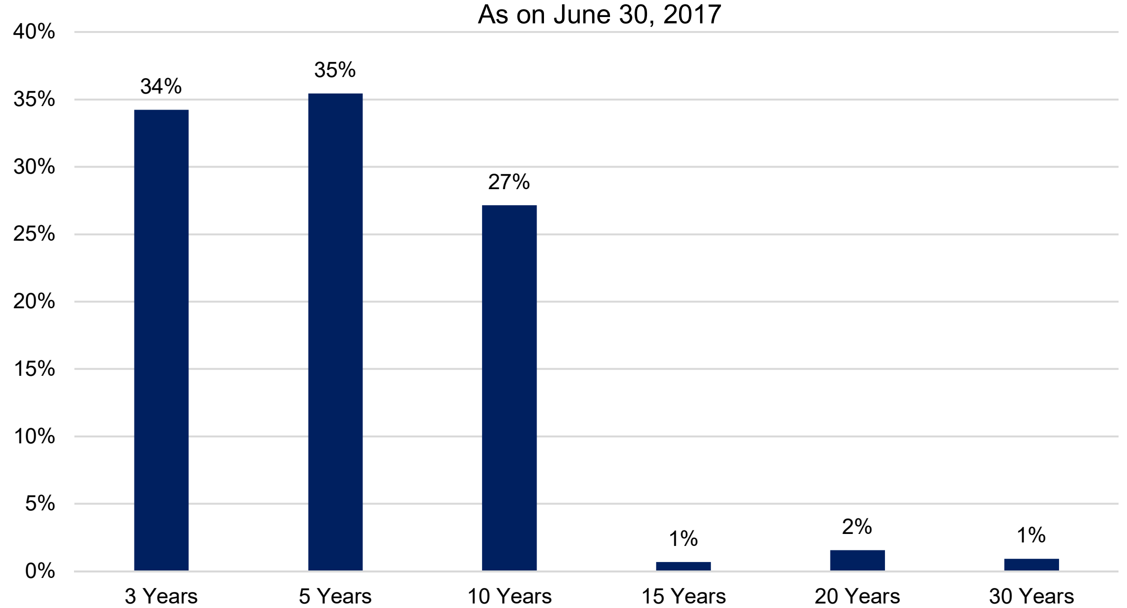
7(iii) Development in Domestic Debt During 2016-17

The following sections highlight the developments in the various components of domestic debt during 2016-17:

I. Permanent Debt

7.9 The amount of permanent debt in total domestic stood at Rs.5,533 billion at end June 2017, representing a decrease of Rs.411 billion during the year. This decrease was driven by PIBs maturity amounting to Rs.1,427 billion which was repaid during the first quarter of 2016-17 while fresh mobilization from PIBs was around Rs.894 billion during the year i.e. Government issued Rs.523 billion with a maturity of three years, Rs.239 billion with a maturity of five years and Rs.132 billion with a maturity of ten years during 2016-17 through PIBs auctions. Share of permanent debt decreased to 37 percent of total domestic debt at end June 2017 compared with 44 percent at end June 2016 while it was only 23 percent at end June 2013. Encouragingly, medium to long term domestic debt portfolio increased from Rs.1,781 billion to Rs.4,777 billion or by around 2.7 times during last four years in-line with objectives of Medium Term Debt Management Strategy of Pakistan. The maturity wise composition of PIBs portfolio at end June 2017 is depicted through graph below:

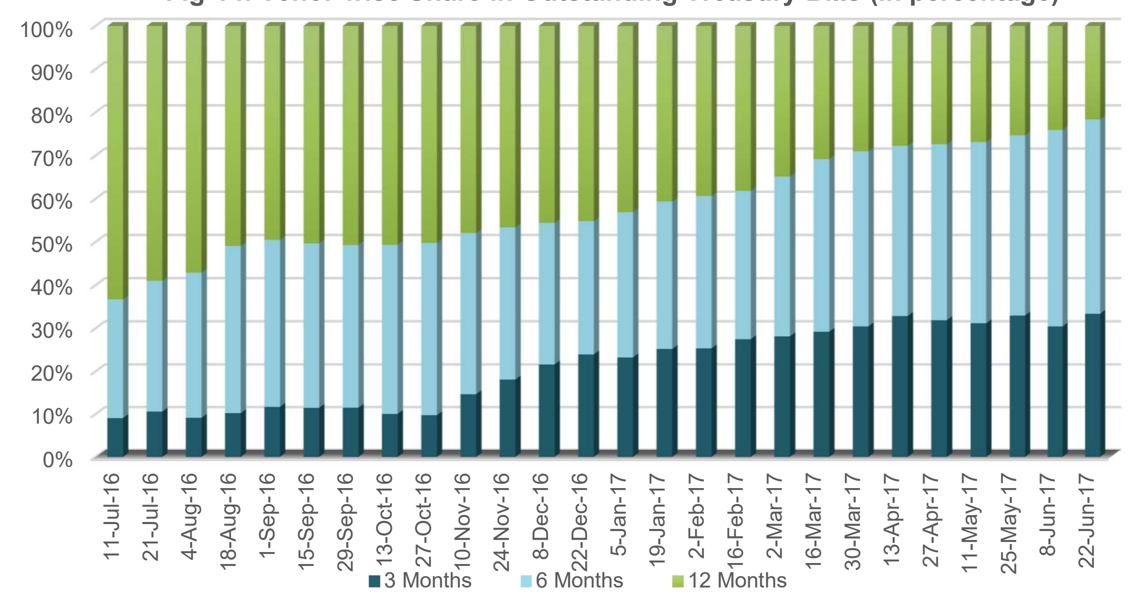
Fig-13: Maturity Wise Percentage Share in PIBs Portfolio
As on June 30, 2017



II. Floating Debt

7.10 Floating debt recorded an increase of Rs.1,555 billion during 2016-17 and stood at Rs.6,557 billion at end June 2017. The increase in floating debt was higher than the overall change in domestic debt as the government retired long-term debt during the year. Net mobilization through Treasury Bills and MRTBs stood at Rs.1,316 billion and Rs.451 billion respectively, while the government retired maturing Sukuk (Bai-Muajjal) of Rs.213 billion. Within Treasury Bills, the market participation was mainly concentrated in 3 and 6-months during 2016-17 as depicted in the graph below:

Fig-14: Tenor-wise Share in Outstanding Treasury Bills (in percentage)



III. Unfunded Debt

7.11 The return offered on National Savings Schemes (NSS) instruments remained relatively lower than previous year which led to decrease in pace of net mobilization of Rs.84 billion during 2016-17 from unfunded debt compared with Rs.111 billion during preceding fiscal year. Most of the incremental mobilization came from Bahbood Savings Certificates (Rs.57 billion) and Special Savings Certificates and Accounts (Rs.26 billion). The share of unfunded debt in the government's domestic debt stood at Rs.2,765 billion or 19 percent at end June 2017. The rates on NSS were revised three times during 2016-17 to align them with the market rates.

7.12 Over a period of time, the 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.

7.13 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-8: Causative Factors in Change in Stock of Domestic Debt (Rs. in billion)

	Stock	Stock	Receipts	Repayments	Net Investment
	2015-16	2016-17	(in 2016-17)		
Permanent Debt	**5,944.2**	**5,533.1**	**1,113.9**	**1,525.0**	**(411.1)**
Market Loan	2.8	2.8	-	-	-
Government Bonds	0.7	0.7	-	-	-
Prize Bonds	646.4	747.1	148.9	48.2	100.7
Foreign Exchange Bearer Certificates	0.1	0.1	-	-	-
Bearer National Fund Bonds	0.0	0.0	-	-	-
Federal Investment Bonds	0.0	0.0	-	-	-
Special National Fund Bonds	0.0	0.0	-	-	-
Foreign Currency Bearer Certificates	0.0	0.0	-	-	-
U.S. Dollar Bearer Certificates	0.1	0.1	-	-	-
Special U.S. Dollar Bonds	4.5	4.5	-	-	-

Table-8: Causative Factors in Change in Stock of Domestic Debt (Rs. in billion)

	Stock	Stock	Receipts	Repayments	Net Investment
	2015-16	2016-17	(in 2016-17)		
Government Bonds Issued to SLIC	0.6	0.6	-	-	-
Pakistan Investment Bonds (PIBs)	4,925.0	4,391.8	894.0	1,427.3	(533.3)
GOP Ijara Sukuk	363.9	385.4	71.0	49.5	21.5
Floating Debt	**5,001.8**	**6,556.6**	**13,986.7**	**12,431.9**	**1,554.8**
Treasury Bills through Auction	2,771.6	4,087.7	7,735.4	6,419.3	1,316.1
Rollover of Treasury Bills discounted SBP	0.5	0.5	-	-	-
Treasury Bills purchased by SBP (MRTBs)	2,017.1	2,468.4	6,251.3	5,800.0	451.3
Bai Muajjal	212.6	-	-	212.6	(212.6)
Unfunded Debt	**2,680.9**	**2,765.3**	**894.5**	**810.2**	**84.3**
Defence Savings Certificates	308.9	325.5	48.3	31.7	16.6
Khas Deposit Certificates and Accounts	0.6	0.5	-	0.1	(0.1)
National Deposit Certificates	0.0	0.0	0.0	0.0	(0.0)
Savings Accounts	29.2	34.9	238.3	232.6	5.7
Mahana Amdani Account	1.8	1.7	0.0	0.1	(0.1)
Postal Life Insurance	67.1	45.8	-	21.3	(21.3)
Special Savings Certificates and Accounts	896.5	922.4	308.9	283.0	25.9
Regular Income Scheme	359.8	338.8	57.9	78.9	(21.0)
Pensioners' Benefit Account	234.7	253.4	47.5	28.8	18.7
Bahbood Savings Certificates	692.1	749.5	151.4	93.9	57.4
National Savings Bonds	0.1	0.1	-	-	-
G. P. Fund	88.3	88.8	33.0	32.5	0.6
Short Term Savings Certificates	1.9	3.7	9.2	7.4	1.8
Total Domestic Debt	**13,626.9**	**14,855.0**	**15,995.1**	**14,767.1**	**1,228.0**

Source: Budget Wing, Finance Division

8.0 External Debt and Liabilities

8.1 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 owed to the International Monetary Fund.

8.2 External public debt is primarily 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, provides stability to exchange rate vis-à-vis other currencies and help in achieving accelerated economic growth.

8.3 EDL stock stood at US$ 83 billion at end June 2017 out of which external public debt was US$ 62.5 billion. EDL increased by US$ 9 billion out of which external public debt contributed US$ 4.8 billion during 2016-17 compared with increase of US$ 6.8 billion recorded in external public debt stock during 2015-16. Despite higher gross external disbursements during 2016-17, the growth in external public debt stock contained to 8 percent compared with 13 percent during preceding fiscal year owing to higher external debt servicing coupled with revaluation gains registered on account of appreciation of US Dollar against other international currencies.

8.4 Encouragingly, within external public debt, the largest component is the multilateral and bilateral debt, constituting around 85 percent. 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 development loans are, thus, simultaneously adding to the debt repayment capacity of the country.

Table-9: Pakistan External Debt and Liabilities

	2013	2014	2015	2016(P)	2017(P)	2018(P)*
	(US Dollar in billion)					
PUBLIC EXTERNAL DEBT						
1. Public Debt (i+ii+iii)**	**48.1**	**51.3**	**50.9**	**57.7**	**62.5**	**63.4**
i). Medium and Long Term(>1 year)	**43.5**	**47.7**	**45.8**	**50.0**	**55.5**	**56.2**
Paris Club	13.5	13.6	11.7	12.7	12.0	12.1
Multilateral	24.2	25.8	24.3	26.4	27.6	27.9
Other Bilateral	2.9	3.4	3.9	4.4	5.8	6.3
Euro Bonds/Saindak Bonds	1.6	3.6	4.6	4.6	4.8	4.8
Military Debt	0.1	0.0	-	-	-	-
Commercial Loans/Credits	-	0.2	0.3	0.9	4.8	4.6
Local Currency Bonds**	0.0	0.0	0.0	0.0	-	-

Table-9: Pakistan External Debt and Liabilities

	2013	2014	2015	2016(P)	2017(P)	2018(P)*
	(US Dollar in billion)					
Saudi Fund for Development	0.2	0.1	0.1	0.1	0.0	0.0
SAFE China Deposits	1.0	1.0	1.0	1.0	0.5	0.5
NBP/BOC Deposits	-	-	-	-	-	-
ii). Short Term (<1 year)	**0.3**	**0.7**	**1.0**	**1.7**	**0.9**	**1.0**
Commercial Loans/Credits	-	0.2	-	0.6	-	0.3
Multilateral	0.3	0.4	1.0	1.1	0.8	0.7
Local Currency Securities**	0.0	0.1	0.0	0.0	0.1	0.0
iii). IMF	**4.4**	**3.0**	**4.1**	**6.0**	**6.1**	**6.2**
of which Central Government	1.5	0.7	0.1	-	-	-
Monetary Authorities	2.9	2.4	4.1	6.0	6.1	6.2
PUBLICLY GUARANTEED DEBT						
2) Publicly Guaranteed Debt	**0.6**	**0.5**	**1.0**	**1.3**	**1.2**	**1.4**
i). Medium and Long Term(>1 year)	0.6	0.5	1.0	1.3	1.2	1.4
Paris Club	-	-	-	-	-	-
Multilateral	0.0	0.0	0.0	0.0	0.0	0.0
Other Bilateral	0.6	0.5	1.0	1.3	1.2	1.2
Commercial Loans/Credits	-	-	-	-	-	0.2
Saindak Bonds	-	-	-	-	-	-
ii). Short Term (<1 year)	-	-	-	-	-	-
NON PUBLIC DEBT						
3. Private Sector Debt	**3.1**	**3.1**	**3.0**	**4.1**	**6.4**	**6.7**
4. Public Sector Enterprises (PSEs Debt)	**1.2**	**1.5**	**1.5**	**1.5**	**1.5**	**1.6**
5. Banks	**1.6**	**2.0**	**2.3**	**2.7**	**4.5**	**5.0**
Borrowing	0.7	1.1	1.3	1.6	3.3	3.8
Nonresident Deposits (LCY & FCY)	0.8	0.9	1.0	1.1	1.2	1.2
6. Debt liabilities to direct investors - intercompany debt	**3.1**	**3.4**	**2.7**	**3.0**	**3.2**	**3.3**
Total External Debt (1 through 6)	**57.8**	**62.0**	**61.5**	**70.3**	**79.4**	**81.4**
FOREIGN EXCHANGE LIABILITIES						
7. Foreign Exchange Liabilities	3.1	3.3	3.7	3.6	3.6	3.6
Total External Debt & Liabilities (1 through 7)	**60.9**	**65.3**	**65.2**	**73.9**	**83.0**	**85.1**

P: Provisional *end-September, 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

8.5 During 2016-17, against external commitments of US$ 11,206 million, gross external disbursements were recorded at US$ 10,465 million while US$ 5,127 million were repaid. The details of gross external inflows from main creditors during 2016-17 are as follows:

- Disbursements from multilateral and bilateral development partners amounting to US$ 5,095 million were mainly for the financing of various public projects primarily in the areas of education, energy, infrastructure development, social spending and public sector management;

- Pakistan mobilized US$ 1,000 million through issuance of international Sukuk; and
- Remaining funds were mobilized from commercial banks aimed at diversifying avenues for future funding needs.

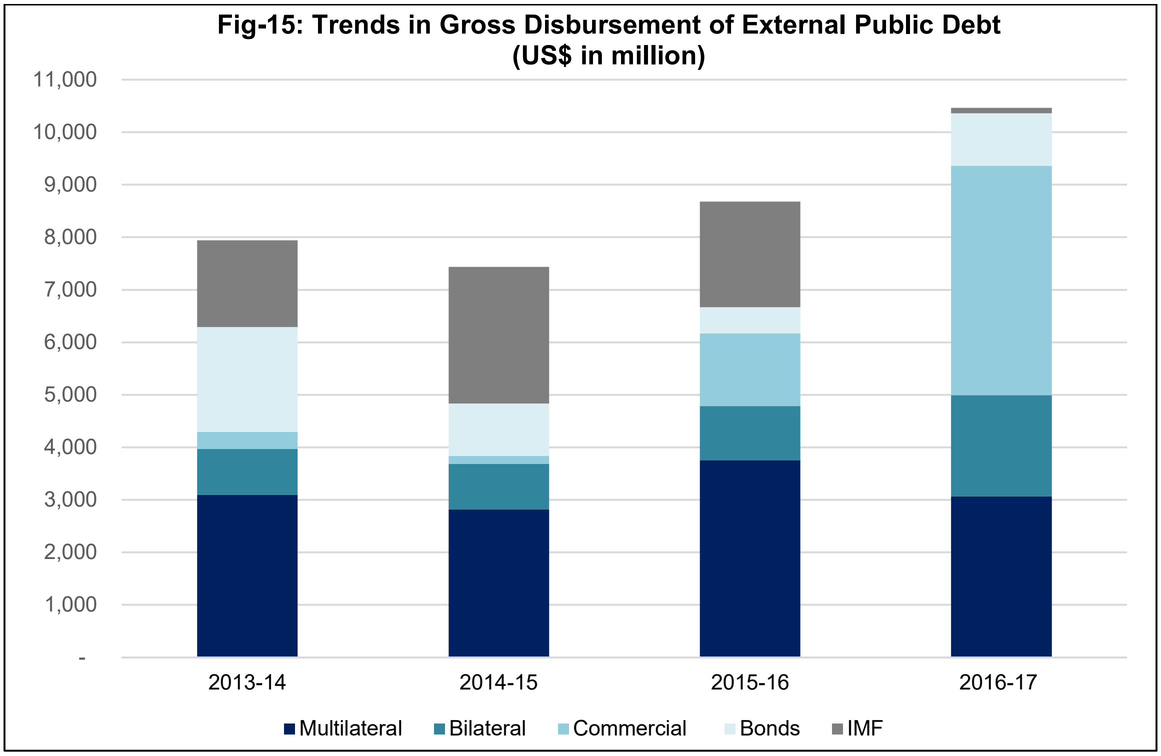
The creditor wise disbursements are presented in the table below:

Table-10: Creditor Wise Disbursements Details (2016-17)

Financing source	Donor	Disbursements (US$ in million)
Multilateral	Asian Development Bank	1,495
	International Development Association	665
	Islamic Development Bank	618
	International Bank for Reconstruction and Development	239
	International Monetary Fund	102
	Others	49
Multilateral Total		**3,167**
Bilateral	China	1,655
	France	119
	Saudi Arabia	69
	Japan	53
	Others	32
Bilateral Total		**1,928**
Eurobonds/Sukuk	**Pakistan International Sukuk**	**1,000**
Commercial banks	China Development Bank	1,700
	SCB (London)	700
	Suisse AG,UBL,ABL	650
	Noor Bank	445
	ICBC-China	300
	Bank of China	300
	Citibank	275
Commercial banks		**4,370**
Grand total		**10,465**

Source: Economic Affairs Division

The trends in gross disbursement of external loans from 2014 are shown in the graph below:



8(i) External Public Debt Servicing

8.6 External public debt servicing went up by 48 percent to settle at US$ 6,440 million during 2016-17 compared with US$ 4,340 million during the preceding fiscal year. The higher repayments against multilateral loans, Eurobonds, Paris Club Countries and commercial loans mainly led to this increase. In addition, the government repaid Safe China Deposits amounting US$ 500 million.

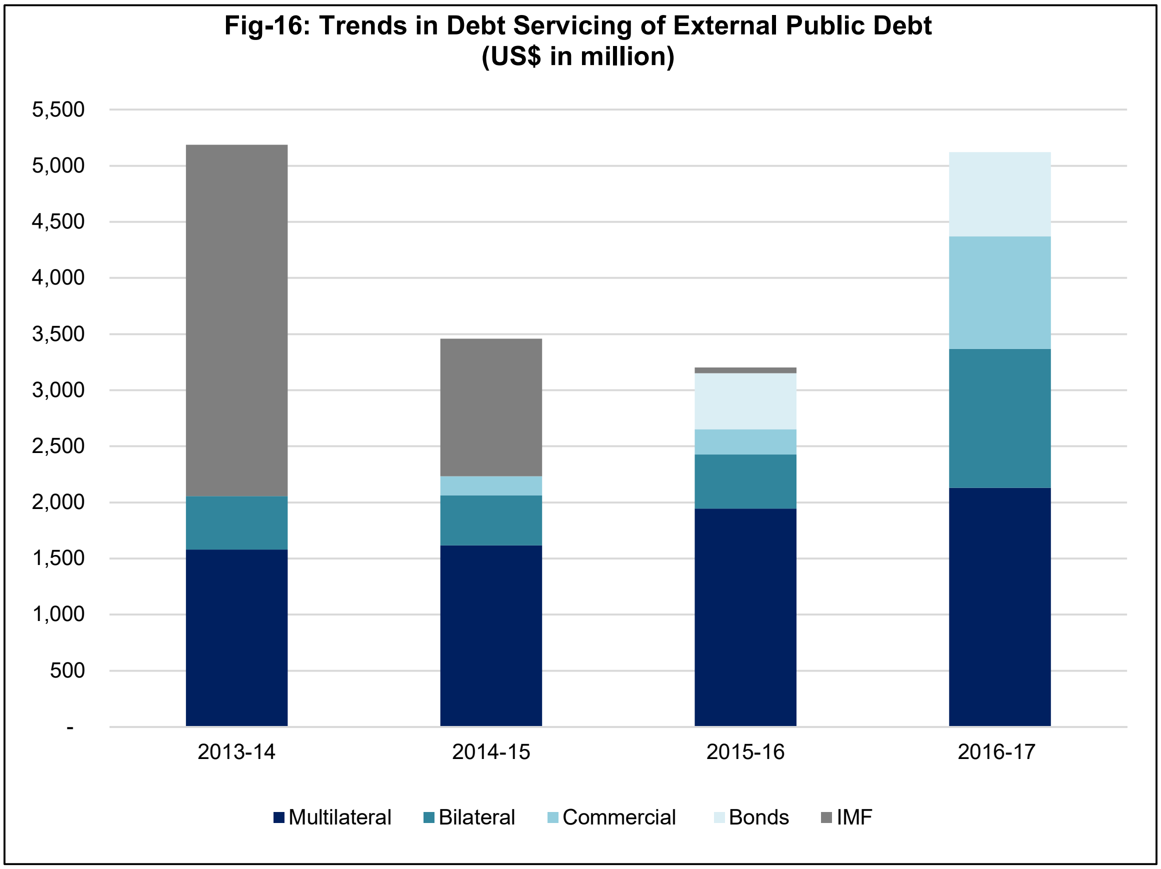
Table-11: External Public Debt Servicing

Years	Principal	Interest	Amount Rolled Over	Total
(US Dollar in million)				
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	5,126.7	1,313.2	500.0	6,939.9
2017-18*	1,349.1	291.1	-	1,640.2

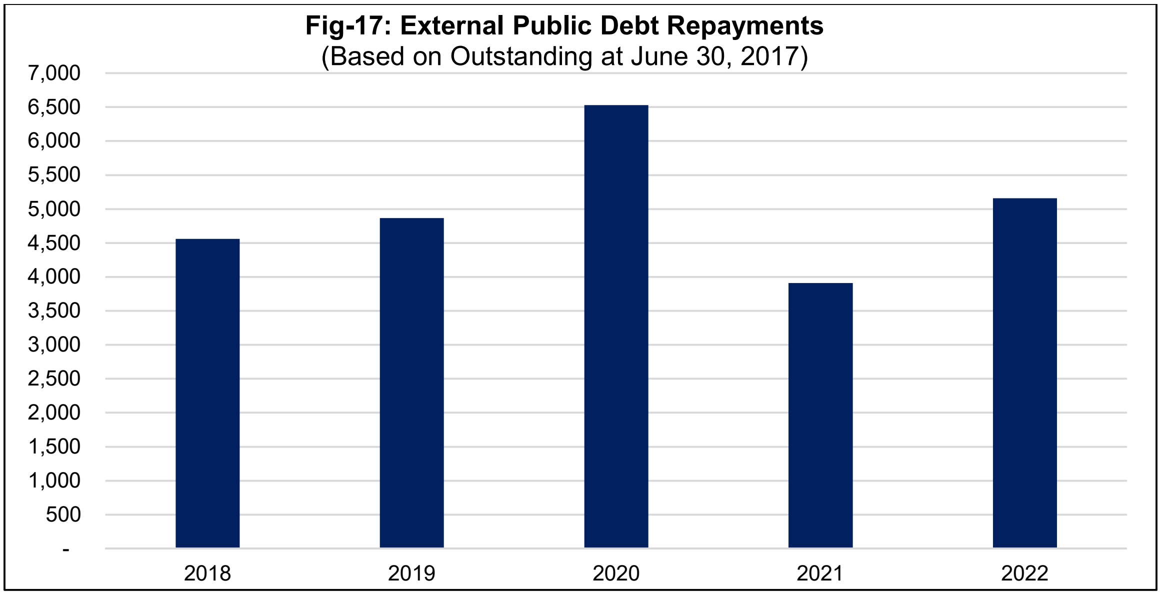
*July-September, 2017

Source: Source: State Bank of Pakistan, Economic Affairs Division and Debt Policy Coordination Office , Ministry of Finance

The trends in external debt servicing from 2014 are shown in the graph below:



8.7 A country can achieve external debt sustainability if it can meet its current and future external debt service obligations, without debt rescheduling or the accumulation of arrears and without compromising growth. External public debt repayment obligations for Pakistan are not more than an average of US$ 5 billion per annum until 2022. Keeping in view the track record of the country, this amount of repayments should not raise any concern as Pakistan has successfully met higher repayment obligations even with much lower volume of foreign exchange reserves. Furthermore, external inflows are expected to be sufficient to meet repayment obligations. Government is cognizant of the developing trends in balance of payment and has taken several remedial measures to keep the current account deficit within manageable limit. The projected external public debt repayments based on outstanding at June 30, 2017 is presented through the graph below:



8 (ii) Performance of Pakistan Eurobonds

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

8.9 Pakistan's Eurobonds have traded well since issuance and levels have remained relatively stable since the start of 2015. The Pakistan 16s, 17s, 19s, 24s and recently the 36s have broadly traded at a premium. As illustrated by these levels and Pakistan's issuance of international bonds and Sukuk since 2014 after a gap of 7 years, markets are accessible with investor appetite there for emerging market credit like Pakistan. The most recent issuance in December 2017 was a record issuance whereby Pakistan raised a landmark US$ 2.5 billion through a 5-year Sukuk and 10-year conventional bond with the latter being issued at 6.875 percent, the lowest rate for a Pakistan 10-year Reg S/144A bond.

8.10 The order book for Pakistan's sovereign papers was over US$ 8 billion. However, the government decided to pick up only US$ 2.5 billion in order to ensure low final yields on the Sukuks and Eurobonds. Such oversubscription and overwhelming response of global investors is an evidence of the trust and confidence of international capital markets in the economic policies of the government and the impressive economic turnaround story of Pakistan. The orders were placed by numerous blue chip institutional international investors from all across the globe. About 44 percent of the orders were placed by investors from Europe, 24 percent from Asia, 20 percent from North America, 8 percent Middle East and 12 percent from other regions.

Table-12: Secondary Trading Levels:

Bond	Ratings			Maturity	Size	Coupon (%)	Price	Yield (%)
	Moody's	S&P	Fitch		($ in million)		(Bid / Ask)	
EM Sovereign Bonds								
Pakistan	B3	B	B	Apr-19	1,000	7.250	103.5 / 103.9	4.3
Pakistan (Sukuk)	B3	B	B	Dec-19	1,000	6.750	103.6 / 103.9	4.7
Pakistan (Sukuk)	B3	-	B	Oct-21	1,000	5.500	100.8 / 101.1	5.2
Pakistan	B3	B	B	Apr-24	1,000	8.250	110.0 / 110.4	6.2
Pakistan	B3	-	B	Sep-25	500	8.250	110.8 / 111.4	6.4
Pakistan	B3	B	B	Mar-36	300	7.875	103.4 / 104.1	7.5
Pakistan (Sukuk)	B3	B	--	Dec-22	1,000	5.625	99.8 / 100.1	5.65
Pakistan	B3	B	-	Dec-27	1,500	6.875	99.4 / 99.9	6.97

Source: Bloomberg, December 13, 2017

8 (iii) - Currency Movements and Revaluation Impact

8.11 In Pakistan, external loans are contracted in various currencies, however, 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 source of fluctuation in the stock of public external debt over a period of time in contrast to actual inflows.

8.12 During 2016-17, appreciation of US Dollar against other major currencies resulted in decrease in foreign currency component of public debt mainly from Japanese

Yen which depreciated around 9 percent against US dollar during the year. Pakistan Rupee remained largely stable against US Dollar lending stability to the external public debt in Pak Rupee terms. However, the gains on account of revaluation during 2016-17 was somewhat reversed during the first quarter of 2017-18, as slight depreciation of Pak Rupee against US Dollar coupled with depreciation of US Dollar against other international currencies resulted in increase in the external public debt.

8.13 Pakistan's loss on foreign currency debt is mitigated by the concessional terms (low servicing costs and extended maturities) associated with its external loans as the cost of adverse currency movements and existing external debt rates is still lower than the cost of domestic debt. Accordingly, the Government's policy is to increase the share of external debt in public debt portfolio as envisaged in MTDS.

8 (iv) - External Debt Sustainability

8.14 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-13: External Debt Sustainability Indicators

(In percent)	2013	2014	2015	2016	2017
ED/FEE (times)	1.0	1.0	1.0	1.1	1.2
ED/FER (times)	4.4	3.6	2.7	2.5	2.9
ED/GDP (Percentage)	20.8	21.0	18.8	20.7	20.6
ED Servicing/FEE (Percentage)	11.1	11.7	8.5	8.5	12.4

FEE: Foreign Exchange Earnings; ED: External Public Debt; FER: Foreign Exchange Reserves
Source: Debt Policy Coordination Office, Ministry of Finance
Note: The above ratios are calculated based on US Dollar amounts.

8.15 External public debt to GDP ratio decreased to 20.6 percent at the end of 2016-17 from 20.7 percent at the end of 2015-16 while it was 20.8 percent at the end of

2012-13, indicating relative reduction in external debt burden of the country. The slight reduction in external debt burden during 2016-17 was mainly supported by higher repayments and translational gain on account of appreciation of US Dollar against other international currencies.

8.16 ED to FEE ratio increased marginally and settled at 1.2 times during 2016-17 compared with 1.1 times during preceding fiscal year. Similarly, ED Servicing to FEE ratio increased to 12.4 percent in 2016-17 from 8.5 percent in 2015-16 while it was 11.1 percent in 2012-13. The lower growth in FEE during 2016-17 led to increase in these ratio which can be mainly attributed to:

- Stagnation in exports largely due to global economic conditions, low commodity prices and bottlenecks in the energy and infrastructure sectors of the economy; and
- Workers' remittances remained marginally lower than preceding fiscal year due to adverse economic conditions in the Middle East, stringent USA regulations and impact of Brexit.

8.17 External debt in relation to foreign exchange reserves reflects the consolidation of foreign exchange reserves and general improvement in country's repayment capacity. This ratio started improving since 2012-13 from 4.4 times towards 2.9 times at the end of 2016-17. While, moderate decline in foreign exchange reserves on account of increase in current account deficit during 2016-17 led to a slight decline in this ratio during 2016-17. It is important to note that increase in current account deficit was mainly due to increase in imports of machinery, industrial raw material and petroleum products. These imports are enhancing productive capacity of the economy for higher output and exports in future.

9.0 Progress on Medium Term Debt Management Strategy (2015/16 - 2018/19)

9.1 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 FRDL

Act, 2005. 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 keeping in view cost risks tradeoff while remaining within the indicative ranges as specified under MTDS.

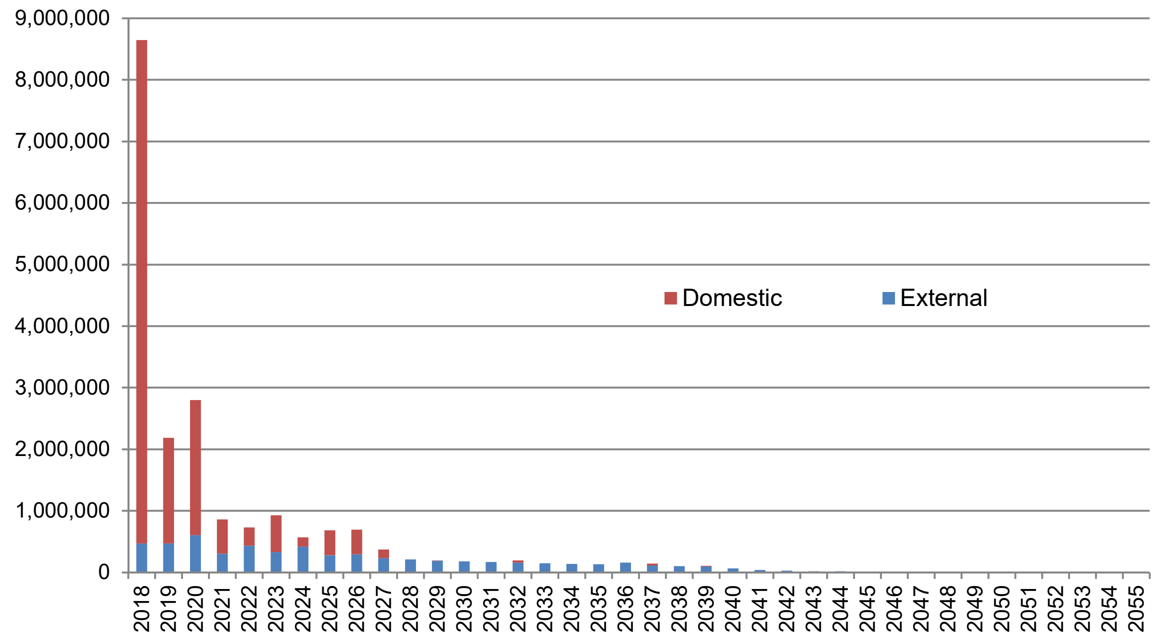
Table-14: Public Debt Cost and Risk Indicators*

Risk Indicators		Indicative Ranges (MTDS 2015/16 - 2018/19)	External Debt		Domestic Debt		Public Debt	
			2013	2017	2013	2017	2013	2017
Refinancing Risk	Average Time to Maturity (ATM) - Years	1.5 (minimum) and 2.5 - DD 3.0 (minimum) and 4.5 - PD	10.1	8.4	1.8	2.0	4.5	3.8
	Debt Maturing in 1 Year (% of total)	50% and 65% (maximum) - DD 35% and 50% (maximum) - PD	8.9	8.0	64.2	55.6	46.0	42.1
Interest Rate Risk	Average Time to Re-Fixing (ATR) - Years	1.5 (minimum) and 2.5 - DD 3.0 (minimum) and 4.5 - PD	9.2	7.5	1.8	2.0	4.2	3.5
	Debt Re-Fixing in 1 year (% of total)	50% and 65% (maximum) - DD 40% and 55% (maximum) - PD	22.2	26.0	67.2	56.4	52.4	47.8
	Fixed Rate Debt (% of total)	**	83.4	77.7	39.6	54.6	54.0	61.2
Foreign Currency Risk (FX)	Foreign Currency Debt (% of total debt)	20% (minimum) and 35%					32.9	28.4
	Short Term FX Debt (% of reserves)	**					68.5	27.7

* As per modalities of MTDS (2015/16 - 2018/19)
**Not Applicable
PD: Public Debt, DD: Domestic Debt
Source: Debt Policy Coordination Office, Ministry of Finance

9.2 Encouragingly, all public debt risk indicators remain within the targets set under MTDS at end June 2017. The refinancing risk of the domestic debt was reduced at the end of 2016-17 as domestic debt maturing in one year reduced to 55.6 percent compared with 64.2 percent at the end of 2012-13. This improvement has contributed towards improvement in average time to maturity of domestic debt to 2 years at the end of 2016-17 as compared with 1.8 years at the end of 2012-13. However, average time to maturity of external debt decreased to 8.4 years at the end of 2016-17 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 four years. The redemption profile of domestic and external debt as at end June 2017 is shown in the graph below:

Fig-18: Redemption Profile of Public Debt at end June 2017 (Rs. in million)



9.3 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. However, it is important to note that MTDS emphasizes tradeoff between cost and risk indicators. Therefore, there remains need to evaluate both cost and risk indicators in conjunction rather in isolation. Accordingly, following positive developments are worth noting:

- The average cost of total gross public debt was reduced by over 150 basis points during past couple of years owing to smooth execution of the MTDS and yet the indicators have witnessed improvement over the medium term;
- Encouragingly, the medium to long term domestic debt portfolio increased from Rs.1.78 trillion to almost Rs.4.80 trillion or by around 2.7 times during last four years in-line with objectives of Medium Term Debt

Management Strategy of Pakistan; and

- Interest cost over the last two years have remained broadly constant despite increase in the absolute quantum of public debt. Accordingly, the government interest expenditure as percentage of revenue reduced to 27 percent of total revenue during 2016-17 as compared with 33 percent during 2012-13. It is therefore evident that not only the cost of debt portfolio has reduced but the risk indicators have also improved tremendously over the medium term as compared to 2013, a win-win situation.

9.4 Exposure to interest rate risk reduced as percentage of debt re-fixing in one year decreased to 47.8 percent at the end of 2016-17 as compared with 52.4 percent at the end of 2012-13. Average time to re-fixing decreased to 3.5 years at the end of 2016-17 as compared with 4.2 years at the end of 2012-13. Fixed rate debt as a percentage of total debt increased to 61.2 percent at the end of 2016-17 as compared with 54 percent at the end of 2012-13 indicating reduced exposure to interest rate changes.

9.5 Around 28.4 percent[5] of total public debt stock was denominated in foreign currency exposing public debt portfolio to exchange rate risk. Currency wise composition of public debt portfolio is depicted through table below:

Table-15: Currency Wise Public Debt[(a)] (in US$)

Currencies	**Percentage**
Pak Rupee	71.6
US Dollar	13.3
Special Drawing Right	8.7
Japanese Yen	4.3
Euro	2.1
Total	**100.0**

[(a)]As per modalities of MTDS

[5] As per modalities of MTDS

9.6 The improvement in foreign exchange stability and repayment capacity is evident from the fact that share of external loans maturing within one year was around 27.7 percent of official liquid reserves at the end of 2016-17 as compared with around 68.5 percent at the end of 2012-13.

10.0 Guarantees

10.1 Contingent liabilities can be distinguished from the liabilities as these are conditional in nature and do not represent the present obligations of the government. Accordingly, contingent liabilities are not recognized as liabilities regardless of the likelihood of the occurrence (or nonoccurrence) of the uncertain future event. Contingent liabilities of Pakistan are guarantees issued to Public Sector Enterprises (PSEs). The sovereign guarantee is normally extended to improve financial viability of projects or activities undertaken by the government entities with significant social and economic benefits. It allows public sector companies to borrow money at lower costs or on more favorable terms and in some cases allows to fulfill the requirement where sovereign guarantee is a precondition for concessional loans from bilateral/multilateral agencies to sub-sovereign borrowers.

10.2 During 2016-17, the government issued fresh/rollover guarantees aggregating to Rs.599 billion while outstanding stock of government guarantees as at end June, 2017 amounted to Rs.937 billion. The share of rupee guarantees increased during past few years and accounted for 91 percent of the total guarantees stock as at end June 2017.

Table-16: Guarantees Outstanding as on June 30, 2017 (Rs. in billion)

Outstanding guarantees extended to PSEs	**936.9**
-Domestic Currency	850.5
-Foreign Currency	86.4
Memo:	
Foreign Currency (US$ in million)	824.0

Source: Debt Policy Coordination Office, Ministry of Finance

Table-17: Entity Wise New Guarantees Issued (2016-17) - (Rs. in billion)	
Name of Organization	**Amount**
WAPDA	203
PHPL	166
SNGPL	55
ZTBL	54
PIA	44
SSGC	40
NTDC	28
NHA	9
Total	**599**
In percent of GDP	**1.9**

Source: Debt Policy Coordination Office, Ministry of Finance

10.3 Guarantees issued against commodity operations are secured against the underlying commodity which are essentially self-liquidating on short term basis and thus should not create a long term liability for the government. The quantum of these guarantees depends on the supply-demand gap of various commodities, their price stabilization objectives, volume procured, and domestic and international prices. The guarantees were issued against the commodity financing operations undertaken by TCP, PASSCO and provincial governments. As on 30th June 2017, the outstanding stock against commodity operations was Rs.750 billion.

10.4 During first quarter of 2017-18, the government issued fresh/rollover guarantees aggregating to Rs.60 billion while outstanding stock of government guarantees at end September, 2017 amounted to Rs.999 billion.

Table-18: Guarantees Outstanding as on September 30, 2017 (Rs. in billion)	
Outstanding guarantees extended to PSEs	**998.7**
-Domestic Currency	918.0
-Foreign Currency	80.7
Memo:	
Foreign Currency (US$ in million)	765.6

Source: Debt Policy Coordination Office, Ministry of Finance

11.0 Report on Compliance with FRDL Act 2005

11.1 The FRDL Act, 2005 requires that the federal government take measures to reduce total public debt and maintain it within prudent limits thereof. Government has made amendments in FRDL Act to provide better operational guidance for fiscal policy making and safeguard debt sustainability over the medium term by imposing certain limits on the federal government budget deficit and public debt to GDP ratio. The following sections identifies the various limits prescribed by the FRDL Act and reports on progress thereof.

(1) limiting of Federal fiscal deficit excluding foreign grants to four percent of gross domestic product during the three years, beginning from the financial year 2017-18 and maintaining it at a maximum of three and a half percent of the gross domestic product thereafter;

The above clause related to limiting the federal fiscal deficit (excluding grants) to four percent is effective from 2017-18.

(2) ensuring that within a period of two financial years, beginning from the financial year 2016-17, the total public debt shall be reduced to sixty percent of the estimated gross domestic product;

The above provision related to reducing the total public debt to GDP to 60 percent is effective from 2017-18. Government remains committed to reduce public debt to GDP ratio to 60 percent by 2017-18 as envisaged through amended FRDL Act. Accordingly, gross public debt witnessed reduction and settled at 67.2 percent of GDP while total government debt stood at 61.6 percent of GDP as at end June, 2017.

(3) ensuring that within a period of five financial years, beginning from the financial year 2018-19 total public debt shall be reduced by 0.5 percent every year and from 2023-24 and going upto financial year 2032-33 a reduction of 0.75 percent every year to reduce the total public debt to fifty percent of the estimated gross domestic product and thereafter maintaining it to fifty percent or less of the estimated gross domestic product; and";

The debt reduction path in terms of GDP has been envisaged after 2017-18 to reduce the public debt to GDP ratio to 50 percent by 2032-33 and thereafter maintaining it at or below that level.

(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."

During 2016-17, the government issued new guarantees including rollovers amounted to Rs.599 billion or 1.9 percent of GDP.

12.0 Conclusion

12.1 Over the past four years, the government has reduced economic vulnerabilities and implemented various growth-supporting structural reforms under home-grown economic program. Macroeconomic resilience was strengthened as growth rate increased, fiscal deficit reduced and foreign currency reserves shored-up. Structural reforms also mitigated long-standing energy sector constraints while efforts were directed to strengthen social safety nets. Government continued to strengthen the stability of the financial sector and enabled recovery of credit to the private sector. In parallel, the government reinforced effective public financial management and tax administration, reduced tax concessions and exemptions and untargeted energy subsidies and began implementing strategies to improve the business climate. These efforts are reflected in growth momentum witnessed in the economy for 4th consecutive year in a row with real GDP growing at 5.3 percent in 2016-17 which remains highest in ten years.

12.2 Pakistan was facing grave economic problems in 2013 as a result of decade long inadequate economic policies. Present government after assuming office demonstrated meticulous strategic depth to balance the current budgetary requirements of the country, while concurrently putting in place structural reforms to bridge the country's output gap. In early 2013, economy was burdened with perilous fundamentals from large fiscal deficit, rising debt burden, unfavorable balance of payments, low foreign exchange reserves, poor growth in tax revenues with shrinking tax-base, swelling current expenditures, energy sector crises, flight of capital, weakening exchange rate and perilously declining investors' confidence.

12.3 There was consensus among financial experts and economists at the time that given the inherent situation, Pakistan would require significant external resources or would fail to meet its foreign obligations beyond February/June 2014. Keeping in view of the alarming situation, immediate remedial measures were taken to stabilize a collapsing economy and avoid default, through ensuring fiscal discipline, increasing the tax revenues, reduction in un-targeted subsidies, building foreign exchange reserves, restructuring of Public Sector Enterprises (PSEs), and reducing the fiscal deficit, while ensuring that public debt was brought to sustainable level without compromising development spending.

12.4 Government is committed to accomplish objectives outlined in FRDL Act, 2005. Going forward, the prime objectives of public debt management remain: (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 maximum available concessional external financing to enhance potential output of the economy 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. Thus, implementing structural reforms that boost potential growth remain key to ensure public debt sustainability.