8 Trade and Payments

Introduction

The phenomenal growth in developing country's trade volumes started in the second half of 2010 and early 2011 in Asia have boosted economic growth. Exports from South Asia jumped more than a fifth in the last quarterly increase of 2010 and Pakistan was an active player. Commodity exporters in all regions are benefiting from strong global demand. Volatile oil prices and supply could adversely affect many developing oil importers, especially those with high GDP dependence on petroleum group. Pakistan in the past had crucial sensitivity to higher oil prices and the SBP estimated that a $10 hike in crude oil prices could cause deterioration of 0.5 percent of GDP in the current account, however, inordinate price escalation in crude oil prices was neutralized by many supporting factors, and Pakistan economy witnessed un-anticipated and unusual current account surplus of $ 748 million in the first ten months of the current fiscal year.

This was possible underpinned by phenomenal increase in remittances, robust growth in exports primarily because of positive terms of trade shock that overshadowed the strong growth in imports, and stable exchange rate. Overall external account has also exhibited improvement even when capital and financial account receipts have continued to decrease during this period.

In addition to that, the recent trends in external sector variables suggest that the implementation of macroeconomic stabilization program has supplemented the credibility of the economic policies. The narrowing of the trade deficit and robust remittances has caused a reduction of $ 5.3 billion in current account deficit during 2009-10 and further improvement continued in the first ten months of 2010-11, which allowed building-up of the country's foreign exchange reserves at around $17 billion from as low as $6.4 billion in October 2008.

Exports

Merchandise exports rose to $20.2 billion in July-April 2010-11 as against $ 15.8 billion in the comparable period of last year, thereby showing inordinate growth of 27.8 percent. The growth in exports remained broad based as almost all the groups (textile and non-textile) witnessed a high positive growth. However, the lion's share of this year's exports came from textile sector and food group contributing 61.8 percent and 18.1 percent, respectively to overall exports growth during the period under review.

Group-wise analysis of exports growth [See Table 8.1] suggests that the exports of food group on the back of fish & fish preparation, vegetables, wheat and meat & meat preparation witnessed a growth of 29.1 percent and the absolute increase of $ 794.6 million to overall exports during July-April 2010-11. Further details reveal that the overall increase in food group exports was largely a result of both higher unit value prices and substantial quantum increase, though, the impact of export prices still remained more significant.

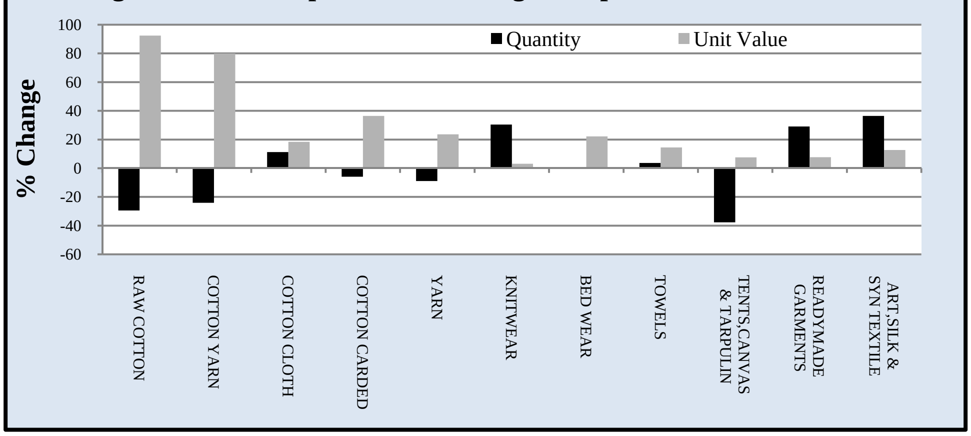
The major development has been the export of wheat to fetch $418.2 million by exploiting higher international prices and stockpile in the country. This has helped banking system to recover chunk of commodity loans to the wheat sector. This has also helped the government to save stock carrying cost on account of huge wheat stocks and now the government is only keeping strategic stocks. Furthermore, the export of fish & fish preparation and meat & meat preparation witnessed a growth of 28.6 percent and 52.9 percent, respectively. The increase in exports of fish mainly attributed to higher quantum export up by 22.9 percent compared to 4.7 percent increase in its unit value.

The meat exports escalated to $123.0 million as a result of increased demand from Saudi Arabia coupled with the higher prices of meat exports during July-April 2010-11.

On the other hand, the rice could not sustain the previous years' export growth and declined by 2.1 percent during July-April 2010-11 over the corresponding period last year mainly due to massive fall in the domestic supplies of rice as devastated floods damaged 0.876 million hectares out of 2.642 million hectares land planted in *Kharif* season. Furthermore, pest attack, disease & logging of early sown crops also contributed to the decrease in rice production. Notwithstanding falling international prices, rice remained expensive by 10.2 percent on average during July-April 2010-11 which offset the lower quantum of rice exports. Resultantly, rice export proceeds managed to reach at $ 1,775 million with 8.8 percent stake in overall export.

Textile sector benefitted from inordinate spike in prices and the textile's share in overall exports increased to 55.3 percent in July-April 2010-11 as against 53.5 in 2009-10. Textile exports have increased by $2,706 million in absolute terms. The current year's performance of textile remained broad based as both the high and low value added contributed to the overall growth in textile group mainly because of increase in unit values of all categories of textile during July-April 2010-11 over corresponding period of last year [See Fig-8.1].

Fig-8.1: Textile Export Items During Jul-Apr 2010-11



The impact of rising international prices is more pronounced in cotton based textile group among all categories of textile sector exports. Moreover, higher external demand especially from EU and US combined with improved availability of raw material inputs also played a significant role in overall increase in textile export receipts. Textile sector also benefited from the currency appreciation and increased labor cost in its competitor countries.

Export of petroleum group increased by 32.6 percent in this period (July-April 2010-11). In absolute terms petroleum group witnessed an increase of $ 267.7 million mainly on the back of higher unit prices of petroleum products (27.5 percent) and petroleum top naphta (13.5 percent). The quantum export of these two items has also increased by 8.9 percent and 8.1 percent, respectively during the period.

Exports of other manufactures grew by 8.6 percent during July-April 2010-11 and its share more or less stagnated at 16.1 percent in total exports. The sector has contributed 5.8 percent to this year overall increase in exports. The major contributors behind the positive growth of other manufacturers' include; chemicals & pharm products, leathers, sports goods and engineering goods. Major contributing factors include, improved unit values (export prices), increased demand of these categories and addition of new export destinations as part of market diversification. Owing to these factors, chemicals, leather, sports and engineering goods collectively added $353.2 million in the overall export increase. This increase in exports receipts was offset to some extent by negative growth of Jewellary (20.2 percent) and Cement (9.9 percent) during July-April 2010-11 primarily because of lower import demand of cement from Middle East, increased competition from Saudi Arabia and fall in exports to India. Resultantly, the quantity exported of cement declined by 8.7 percent and unit value witnessed a negative growth of 1.2 percent during the period.

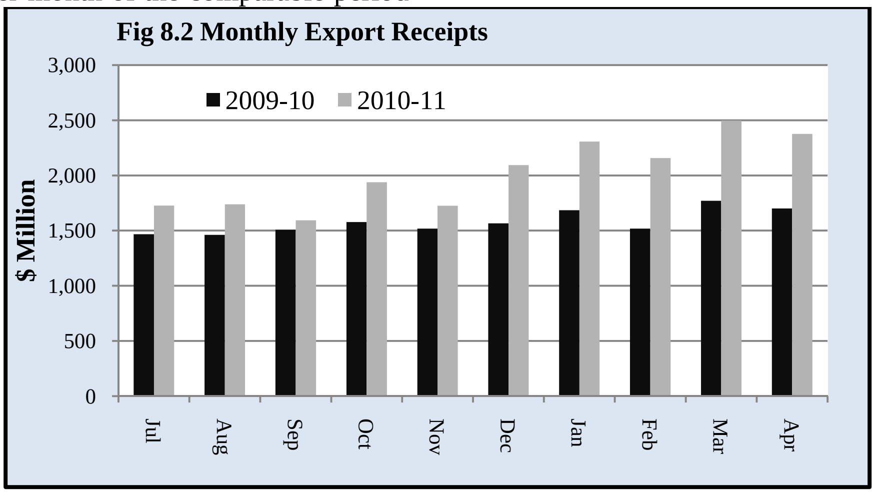
Table 8.1: Structure of Exports *($ Millions)*

Particulars	July-April		% Change	Absolute Increase/ Decrease	% Share
	2010-11*	2009-10			
A. Food Group	**3,528.4**	**2,733.8**	**29.1**	**794.6**	**17.5**
Rice	1,774.8	1,812.3	-2.1	-37.4	8.8
Fish & Fish Preparation	233.9	181.9	28.6	52.1	1.2
Fruits	246.1	214.6	14.7	31.5	1.2
Vegetables	199.0	97.7	103.6	101.3	1.0
Wheat	418.2	0.7	-	417.4	2.1
Spices	41.7	32.6	28.1	9.2	0.2
Oil Seeds, Nuts & Kernels	13.6	17.6	-22.6	-4.0	0.1
Meat & Meat Preparation	123.0	80.4	52.9	42.5	0.6
All other Food Items	477.9	295.9	61.5	182.0	2.4
B. Textile Manufactures	**11,148.6**	**8,442.7**	**32.1**	**2,705.9**	**55.3**
Raw Cotton	263.6	194.1	35.8	69.5	1.3
Cotton Yarn	1,689.7	1,238.0	36.5	451.7	8.4
Cotton Cloth	1,955.8	1,486.0	31.6	469.8	9.7
Knitwear	1,929.5	1,434.8	34.5	494.7	9.6
Bed Wear	1,739.4	1,422.5	22.3	316.9	8.6
Towels	653.5	550.7	18.7	102.8	3.2
Readymade Garments	1,435.6	1,033.5	38.9	402.1	7.1
Made-up Articles	570.1	437.3	30.4	132.8	2.8
Other Textile Materials	911.5	645.9	41.1	265.6	4.5
C. Petroleum Group	**1,089.8**	**822.1**	**32.6**	**267.7**	**5.4**
Petroleum Products	701.2	505.0	38.9	196.2	3.5
Petroleum Top Naptha	388.5	316.9	22.6	71.6	1.9
D. Other Manufactures	**3,245.8**	**2,990.0**	**8.6**	**255.8**	**16.1**
Carpets. Rugs & mats	109.6	117.0	-6.3	-7.4	0.5
Sports Goods	261.1	241.7	8.1	19.5	1.3
Leather Tanned	359.0	258.7	38.8	100.3	1.8
Leather Manufactures	447.3	377.1	18.6	70.2	2.2
Surgical G. & Med.Inst.	207.3	195.1	6.2	12.2	1.0
Chemicals & Pharma. Pro.	711.8	600.0	18.6	111.8	3.5
Engineering Goods	239.9	188.4	27.3	51.5	1.2
Jewellary	315.4	395.3	-20.2	-79.9	1.6
Cement	362.0	401.6	-9.9	-39.6	1.8
All other manufactures	232.5	215.2	8.0	17.2	1.2
E. All Other Items	**1,141.7**	**784.5**	**45.5**	**357.2**	**5.7**
Total	**20,154.2**	**15,773.2**	**27.8**	**4,381.1**	**100.0**

** Provisional* *Source: FBS*

Trend in Monthly Exports

Monthly average exports surged substantially in the period July-April 2010-11 [See Fig-8.2], however, month-wise exports started to escalate since December 2010 by showing a growth of 33.7 percent that is rising from $ 1,566 million of previous year's month to $ 2,094 million in December 2010 mainly because of impetus provided by surge in commodity prices in general and textile related items prices in particular. Exports averaged at $ 2,015 million per month during July-April 2010-11 as against average of $ 1,577 million per month of the comparable period last year.



Concentration of Exports

Notwithstanding, phenomenal increase in exports, it remained concentrated in few items like cotton manufacturers, leather and rice [Table-8.2] as these three categories accounted for 66.3 percent stake in total exports during July-March 2010-11. Out of this 66.3 percent share in total exports, the 80.0 percent consist of cotton manufactures thereby making the concentration more intense. This also reinforces the need for diversification in export goods to make it more guarded against external shocks. Furthermore, the share of cotton manufacturers during July-March 2010-11 increased by 1.2 percentage points over the corresponding period last year. The concentration of exports is changing though at a painfully slower rate as the share of other items in overall exports increased from 26.7 percent in 2005-06 to 33.7 percent in July-March 2010-11 showing that country has the potential for diversification in exports which need to be accelerated.

Table 8.2:Pakistan's Major Exports **(Percentage Share)**

Commodity	**05-06**	**06-07**	**07-08**	**08-09**	**09-10**	**July-March***	
						09-10	**10-11**
Cotton Manufacturers	59.4	59.7	51.9	52.6	50.6	51.8	53
Leather**	6.9	5.2	5.8	5.4	4.5	4.4	4.4
Rice	7.0	6.6	9.8	11.2	11.3	11.5	8.9
Sub-Total of Three Items	**73.3**	**71.5**	**67.5**	**69.2**	**66.4**	**67.7**	**66.3**
Other Items	26.7	28.5	32.5	30.8	33.6	32.3	33.7
Total	100	100	100	**100**	100	100	100

**Provisional* *Source: FBS*
*** Leather & Leather Manufactured*

Composition of Exports

The slow process of movement towards sophistication of export is evident from the share of manufactured goods in overall export which hovered around approximately three-fourth of exports for many years [Table 8.3]. However, a continuous decline in the share of manufactured goods to the overall exports is being observed since last few years as the share of manufactured goods decreased from 78 percent in 2005-06 to 70 percent in July-March 2010-11. The major reasons behind this erosion of share include lower external demand due to competitiveness problem and acute disruptions in energy supplies in the country during the period. Whereas, the share of primary commodities exports increased from 11.0 percent in 2005-06 to 18.0 percent during July-March 2010-11. The shift is in contradiction of economic transformation and raises serious question about productive capacity of the economy and de-industrialization.

Table 8.3: Composition of Exports **(% Share)**

Year	Primary Commodities	Semi-Manufactures	Manufactured Goods	Total
2005-06	11	11	78	100
2006-07	11	12	77	100
2007-08	14	11	75	100
2008-09	16	10	74	100
2009-10	18	10	72	100
July-March				
2009-10	18	11	71	100
2010-11*	18	12	70	100

*** Provisional** **Source: FBS**

Direction of Exports

Traditionally, Pakistan's exports have been concentrated in a few export destinations like USA, UK, Germany, Hong Kong, U.A.E and Afghanistan [See Table-8.4]. However, a reversal in trend has been observed since fiscal year 2005-06. The share of exports to these destinations decreased from 53.7 percent in 2005-06 to 45.0 percent in July-March 2010-11. The share of remaining countries increased to 55.0 percent during July-March 2010-11 as compared to 46.3 percent in 2005-06. The major contribution to this geographical diversification in export markets came from increased exports to regional countries mainly China and Bangladesh.

Table 8.4: Major Exports Markets ***(Percentage Share)***

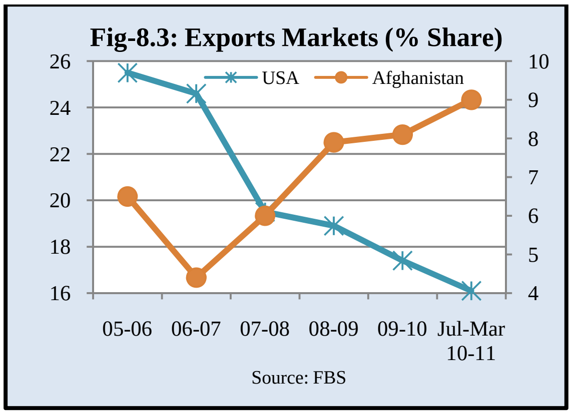
Country	05-06	06-07	07-08	08-09	09-10	July-March 09-10	July-March 10-11*
USA	25.5	24.6	19.5	18.9	17.4	17.3	16.1
UK	5.4	5.6	5.4	4.9	5.3	5.5	5.1
Germany	4.2	4.1	4.3	4.2	4.1	4.2	5.1
Honk Kong	4.1	3.9	2.7	2.1	2.2	2.1	2.3
U.A.E.	8.0	8.2	10.9	8.2	8.9	8.1	7.4
Afghanistan	6.5	4.4	6.0	7.9	8.1	8.3	9.0
Sub-Total	**53.7**	**50.8**	**48.8**	**46.2**	**46.0**	**45.5**	**45.0**
Other Countries	46.3	49.2	51.2	53.8	54.0	54.5	55.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

**Provisional* *Source: FBS*

USA continues to be the most favourite export destination with 16.1 percent share in overall exports when its share in overall exports is exhibiting continuous fall since 2005-06 mainly due to weakening economic activity in the US amidst global financial crisis. On the other hand, Afghanistan is emerging as an important export market for Pakistan as its share is persistently rising during the period under review [Fig- 8.3].

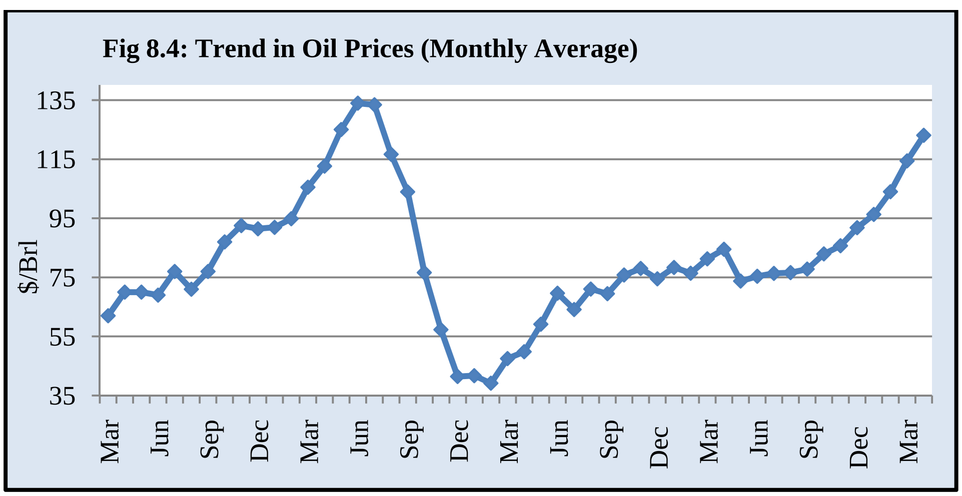
Imports

Merchandise imports increased to $ 32.3 billion in July-April 2010-11 as against $ 28.1 billion in the comparable period of last year, thereby showing an increase of 14.7 percent. The overall import bill is higher by $ 4.1 billion, reflecting the impact of higher global crude oil and commodity prices. With the exception of machinery group, the higher import bill is contributed by food group ($ 1,528 million), petroleum group ($ 678.3 million), consumer durables ($ 247 million), raw material group ($ 1,039 million), telecom ($ 245 million) and on other items group ($ 951 million). The price and quantity effects worked in the same direction; however price effect remained stronger than quantity effect. The imports excluding petroleum group grew by 17.3 percent and excluding petroleum and food grew by 11.2 percent. This implies dominant role of food imports on import growth.



Further analysis indicates that food group imports accounting for 13.4 percent of total imports, showed a massive growth rate of 54.9 percent during July-April 2010-11. Within food group import, the major contribution came from sugar, edible oil and pulses [See Table-8.5]. The domestic shortfall in sugar production necessitates import of 1.1 million tons of sugar resulting in growth of 262.9 percent during July-April 2010-11 and country has to incur expenditure of $681.4 million during the period. The import bill of edible oil increased by 57.4 percent and has added $ 605.6 million to this year's import bill. Palm oil imports surged in quantity, value and per unit value terms as they increased by 16.1 percent, 53.7 percent and 32.3 percent, respectively. The higher import bill of palm oil is culmination of higher international price, higher domestic demand and reduction in import duty on palm oil during the period, thereby in absolute terms palm oil import bill increased by $558.6 million in July-April 2010-11.

Import of petroleum group grew by 8.4 percent during July-April 2010-11 mainly reflecting the impact of spike in international oil prices as per unit values of petroleum crude increased by 23.6 percent. In addition to that, quantity import of crude oil also increased by 10.6 percent during July-April 2010-11. The increase in petroleum import bill is evident from international monthly average prices of oil which surged from $ 76 per barrel in July 2010 to $ 123 per barrel in April 2011 thereby showing an escalation of 61.2 percent during the period [See Fig-8.4]. The impact of this phenomenal increase in international oil prices will be more visible in the coming months in import bill of petroleum group as there is a time lag of around three months. The quantity is also started to increase beyond February 2011.



The import of consumer durables added $ 247 million to overall import bill of July-April 2010-11. The huge injection of money in the rural areas mainly because of inordinate rise in prices of cotton and sugarcane led to higher domestic demand to import road motor vehicle which increased to $ 1,080 million in July-April 2010-11 as compared to $951 million in the comparable period of last year, thereby showing growth of 13.6 percent. Relatively small group electric machinery and appliances also added $ 118 million during July-April 2010-11 against the corresponding period of last year.

Import of raw material group surged by 15.7 percent and accounting for 23.7 percent of total imports during the period of July-April 2010-11. Within raw material imports, raw cotton with 2.6 percent stake in overall imports and 11.1 percent share in raw material group increased in absolute terms by $ 354 million mainly due to shortages in domestic production of raw cotton owing to unprecedented flood. Lower domestic supplies were compensated by increasing the import of raw cotton (8.4 percent) combined with rising import price of cotton as evident from increased unit value (58.3 percent) of raw cotton during the current fiscal year 2010-11. Other items like synthetic fibre, synthetic & artificial silk yarn and plastic material on absolute terms collectively added $616 million to the import bill of July-April 2010-11. The prominent decline witnessed in the imports of fertilizer manufactured due to higher domestic production as quantity of fertilizer import declined by 52 percent during July-April 2010-11 over the corresponding period last year.

Telecom imports grew by 40.8 percent during the first ten months of the current fiscal year 2010-11 and in absolute term the import in telecom sector witnessed an increase of $245 million. Most of the increase in overall telecom imports has been contributed by mobile phone imports which grew by 75.5 percent and added $188 million during July-April 2010-11 from the corresponding period last year. This increase may be the result of increasing demand for mobile phone as higher purchasing power in increasing nominal income in rural areas.

Machinery group import decreased to $3,480 million during first ten months of the current fiscal year 2010-11 as against $4,028 million in the corresponding period last year. Among the different items of machinery group, only textile machinery and office machinery imports witnessed positive growth. Buoyancy in textile sector resulted in massive growth of 78.4 percent in textile machinery imports. Furthermore, the 13.6 percent decline in machinery group imports is a reflection of weaker economic activity in the country.

Table 8.5: Structure of Imports **($ Million)**

Particulars	July-April		% Change	Absolute Increase	Share
	2009-10	2010-11*			
A. Food Group	**2,784.7**	**4,312.5**	**54.9**	**1,527.8**	**13.4**
Milk & milk food	67.8	129.4	91.0	61.6	0.4
Wheat Unmilled	35.4	5.2	-85.4	-30.3	0.0
Dry fruits	67.8	73.5	8.5	5.7	0.2
Tea	227.8	288.3	26.6	60.5	0.9
Spices	61.0	91.1	49.5	30.2	0.3
Edible Oil (Soyabean & Palm Oil)	1,054.7	1,660.3	57.4	605.6	5.1
Sugar	187.7	681.4	262.9	493.6	2.1
Pulses	209.4	342.6	63.6	133.1	1.1
All Other Food Items	873.1	1,040.7	19.2	167.7	3.2
B. Machinery Group	**4,028.0**	**3,479.6**	**-13.6**	**-548.4**	**10.8**
Power Gen. Machines	1,253.5	858.9	-31.5	-394.7	2.7
Office Machines	186.0	194.1	4.3	8.1	0.6
Textile Machinery	223.0	397.8	78.4	174.8	1.2
Const. & Mining Mach.	142.0	98.9	-30.4	-43.2	0.3
Aircraft Ships and Boats	709.0	601.4	-15.2	-107.7	1.9
Agri. Machinery	179.6	77.7	-56.7	-101.9	0.2
Other Machinery	1,334.8	1,250.9	-6.3	-83.8	3.9
C. Petroleum Group	**8,087.6**	**8,765.9**	**8.4**	**678.3**	**27.2**

Particulars	July-April		% Change	Absolute Increase	Share
	2009-10	2010-11*			
Petroleum Products	5,274.4	4,918.3	-6.8	-356.1	15.2
Petroleum Crude	2,813.3	3,847.6	36.8	1,034.4	11.9
D. Consumer Durables	**1,500.5**	**1,747.8**	**16.5**	**247.3**	**5.4**
Elect. Mach. & App.	549.9	667.6	21.4	117.7	2.1
Road Motor Veh.	950.5	1,080.2	13.6	129.7	3.3
E. Raw Materials	**6,605.7**	**7,645.1**	**15.7**	**1,039.4**	**23.7**
Raw Cotton	493.4	846.9	71.7	353.5	2.6
Synthetic fibre	290.4	464.2	59.8	173.7	1.4
Silk yarn (Synth & Arti)	287.5	444.7	54.7	157.1	1.4
Fertilizer Manufactured	731.6	439.6	-39.9	-292.0	1.4
Insecticides	120.4	122.3	1.6	1.9	0.4
Plastic material	978.0	1,263.3	29.2	285.4	3.9
Iron & steel and Scrap	383.4	405.9	5.9	22.5	1.3
Iron & steel	1,017.9	993.0	-2.4	-24.9	3.1
Other Chemical Products	2,303.0	2,665.3	15.7	362.3	8.3
F. Telecom	**599.1**	**843.8**	**40.8**	**244.7**	**2.6**
G. Others	**4,516.9**	**5,468.3**	**21.1**	**951.4**	**16.9**
Total	**28,122.4**	**32,262.9**	**14.7**	**4,140.5**	**100.0**
Excluding Petroleum Group	20,034.8	23,497.0	17.3	3,462.3	72.8
Excluding Petroleum & Food Groups	17,250.1	19,184.5	11.2	1,934.4	59.5

** Provisional* *Source: FBS*

The rise in overall import bill of the country is the result of increase in international oil and commodity prices. The import bill increased by 2,467 million in the first ten months of the current fiscal year only because of surge in import price of major items i.e. petroleum products, petroleum crude, palm oil, raw cotton, Iron & steel and sugar. Moreover, Pakistan's overall import growth during July-April 2010-11 would have been 6.0 percent and not 14.7 percent if only the unit values of items listed in Table 8.6 remained equal to it's last year level.

Table 8.6: Additional Import Bill as a Result of the Change in Import Prices (July-April 2010-11*) **($ Million)**

Commodity	Actual Imports	Imports at Last Year's Prices	Additional Bill
Palm Oil	1,599.5	1,208.7	390.9
Petroleum Products	4,918.3	4,200.1	718.2
Petroleum Crude	3,847.6	3,112.2	735.4
Iron & Steel	993.0	787.7	205.3
Raw Cotton	846.9	534.9	312.0
Sugar	681.4	576.2	105.2
Total	**12,886.7**	**10,419.8**	**2,466.9**

**Estimated*

Trend in Monthly Imports

Month-wise imports averaged at $3,226 million during July-April 2010-11 and remained higher than the average import of $2,812 million in the same period last year. During first ten months of fiscal year 2010-11 the highest growth of 29 percent has been witnessed during the month of December 2010 [See Fig-8.5] reflecting absolute addition of $377 million and $102 by petroleum products and sugar imports, respectively. The major contributors behind the increase in imports in April 2011 remained petroleum crude and palm oil.

Composition of Imports

The import structure in terms of its composition exhibits that majority of Pakistan's imports consists of raw material for consumer goods [Table-8.7]. More recently, the share of import for consumer goods increased to 16 percent in July-March 2010-11 from 13 percent last year. However, the share of capital goods declined from 28 percent in July-March 2009-10 to 25 percent in July-March 2010-11.

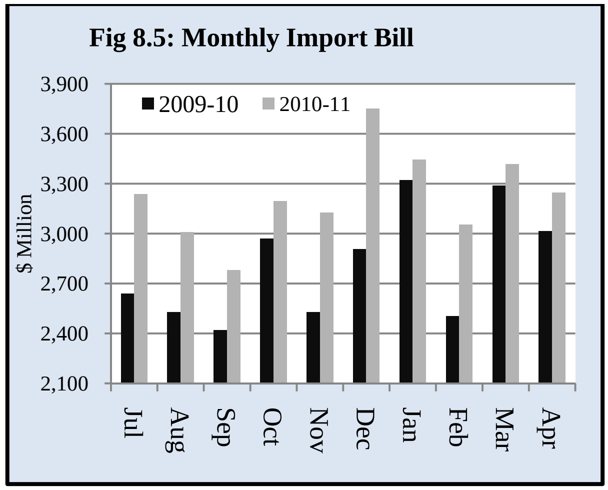


Table 8.7: Composition of Imports **(% Share)**

Year	Capital Goods	Raw Material for		Consumer Goods	Total
		Capital Goods	Consumer Goods		
2004-05	36	8	46	10	100
2005-06	37	7	45	11	100
2006-07	36	7	47	10	100
2007-08	29	8	53	10	100
2008-09	29	9	49	13	100
2009-10	28	7	52	13	100
July-March*					
2009-10	28	7	52	13	100
2010-11	25	7	52	16	100

** Provisional* *Source: FBS*

Direction of Imports

Pakistan's imports are concentrated in few markets and chunk of imports originates from UAE, Saudi Arabia, Kuwait, Malaysia, Japan, Germany, USA and U.K. These markets account for approximately 50 percent share in overall imports of the country [Table-8.8]. Further analysis suggests that within these import origins, the highest share came from UAE, followed by Saudi Arabia and Kuwait during July-March 2010-11.

Table 8.8: Major Sources of Imports **(Percentage Share)**

Country	00-01	01-02	02-03	03-04	04-05	05-06	06-07	07-08	08-09	09-10	July-March	
											09-10	10-11*
U.S.A.	5.3	6.7	6.0	8.5	7.6	5.8	7.5	6.1	5.4	4.6	4.8	4.3
U.K.	3.2	3.4	2.9	2.8	2.6	2.8	2.3	1.9	2.6	1.7	1.7	1.6
Germany	3.5	4.3	4.6	3.9	4.4	4.7	3.9	3.2	3.8	3.4	3.7	2.3
Japan	5.3	5.0	6.6	6.0	7.0	5.6	5.7	4.6	3.6	4.4	4.4	4.1
Malaysia	3.9	4.4	4.6	3.9	2.6	3.0	3.1	3.9	4.6	5.0	5.1	5.7
Kuwait	8.9	7.1	6.6	6.4	4.6	6.2	5.7	7.5	6.6	6.9	6.0	6.8
Saudi Arabia	11.7	11.6	10.7	11.4	12.0	11.2	11.4	13.4	12.3	9.7	10.4	11.7
U.A.E.	14.5	13.1	12.4	11.0	8.3	11.9	9.1	8.5	9.1	14.5	14.7	13.3
Sub-Total	**56.3**	**55.6**	**54.4**	**53.9**	**49.1**	**51.2**	**48.7**	**49.1**	**48.0**	**50.2**	**50.8**	**49.8**
Other Countries	43.7	44.4	45.6	46.1	50.9	48.8	51.3	50.9	52.0	49.8	49.2	50.2
Total	100	100	100	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

**Provisional* *Source: FBS*

Terms of Trade

The process of improvement in terms of trade that started in 2008-09 and approximately maintained its position in 2009-10, further strengthened in July-March 2010-11. The terms of trade witnessed an improvement of 5.7 percent to 59.1 percent during July-March 2010-11 against 55.9 percent increase witnessed in term of trade indices in the same period of last year [See Table-8.9]. This improvement in terms of trade mainly led by increase in unit value index of exports that outstripped the increase in unit value index of imports as earlier grew by 23.5 and former witnessed a growth of 16.8 percent during July-March 2010-11, thereby strengthening current account position of the country. The main driver for this improvement is unit value indices of manufacturers which increased by 55 percent.

Trade Balance

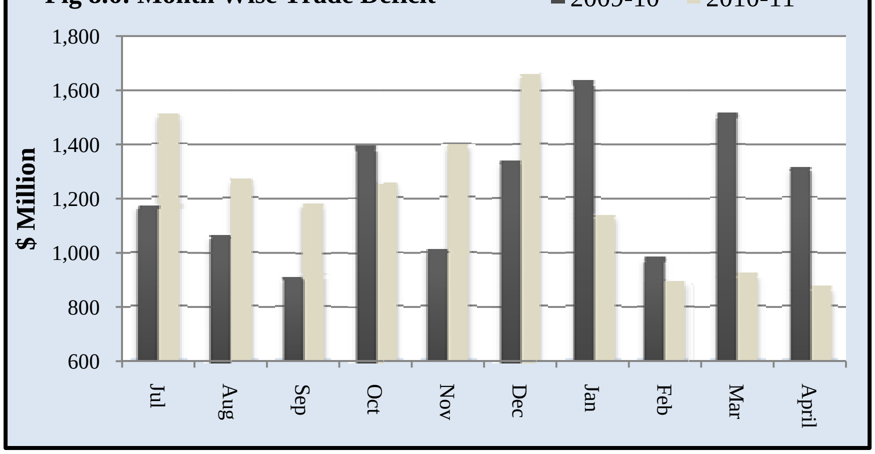
Merchandise trade deficit improved by $ 240 million to $ 12,109 million during July-April 2010-11 as compared to $12,349 million in the same period last year, thereby showing an improvement of 1.9 percent. The month of November 2010 witnessed most severe worsening in trade deficit when compared to previous year's same period position. This deterioration in trade deficit mainly owed to increase in flood related import expenditure during November and December 2010. However, since January 2011, the trade deficit is improving against the corresponding months of last year [See Fig-8.6] mainly due to buoyancy in monthly exports growth combined with slowdown in import bill during the period under review. More recently, the trade deficit has witnessed an improvement of 33.8 percent in April 2011 against the same month last year.

Table 8.9: Unit Value Indices and Terms of Trade (Base year 1990-91 = 100)

Year	Unit Value Indices		Terms of Trade
	Exports	Imports	
2006-07	310.03	495.33	62.59
2007-08	350.4	632.3	55.42
2008-09	450.4	790.82	56.95
2009-10	478.07	839.6	56.94
July-March*			
2009-10	463.35	828.31	55.94
2010-11	572.01	967.44	59.13

** Provisional* *Source: FBS*

Fig 8.6: Month Wise Trade Deficit



Balance of Payments

Current Account Balance

Pakistan has long suffered a current account deficit which is regarded is as an important indicator to gauge the pressures on a country's external sector. Large and persistent current account deficit may threaten the viability of the external account. The sustainability of the current account deficit depends, not only on the composition of the deficit, but also the way it is financed.

During July-April 2010-11, the current account deficit turned to surplus of $748 million from deficit of $3,456 million in the comparable period of last year [See Table-8.10]. This year's improvement in current account is broad based as improvement witnessed across the board in all sub-components including balance of goods, services and income account while buoyancy in current transfers helped current account to turn it into surplus in the form of higher export growth, strong and sustained inflows of workers' remittances, logistic support related receipts and grants received for flood relief. In the backdrop of improvement in all sub groups, the current account absorbed commodity and oil price shock of high intensity without impacting exchange rate or foreign exchange reserves.

Unlike the current account, the financial account surplus deteriorated and reached to $412 million during July-April 2010-11 as compared to $3,533 million in the corresponding period last year. Notwithstanding, lower surplus in the capital and financial account, the overall external balance of the country witnessed a surplus of $ 1,210 million during July-April 2010-11. This development in overall external account balance mainly came from improvement in the current account balance and also complemented by surplus in the capital and financial account.

Within the current account, deficit in trade account contracted by 10.8 percent during July-April 2010-11 over the last year which remained at $8,285 million. Encouragingly, the improvement in trade account was mainly driven by fall in imports during last year but this year's improvement was predominantly the result of robust growth of 27 percent in exports during this period. The improvement in the trade account was supplemented by improvements in current transfers, services and income accounts. In particular, current transfers recorded growth of 23.9 percent during July-April 2010-11 and stood at $ 12,846 million. The improvement in the current transfers is mainly owes to remarkable rise in the workers' remittances and other private transfers.

Decline in services account deficit by 28.2 percent during July-April 2010-11 was the result of 24.7 percent growth in services exports that outpaced 6.6 percent growth in services imports. Robust growth in services exports came from logistic support receipts ($743 million), transportation ($1,188 million), travel ($289 million) and other business services ($573 million). Due to increased receipts under logistic support, the share of government services exports increased by 5.3 percentage points during July-April 2010-11 and its share in overall services exports was 45.3 percent. On the other hand, import of services grew by 6.6 percent during July-April 2010-11. The major contribution to this increase in import services came from expenditure on transportation group which in absolute term added $ 331 million to the import bill during July-April 2010-11 as compared with the corresponding period last year. Income account deficit declined by 6.7 percent during July-April 2010-11 over the same period last year mainly due to lower investment and interest outflows.

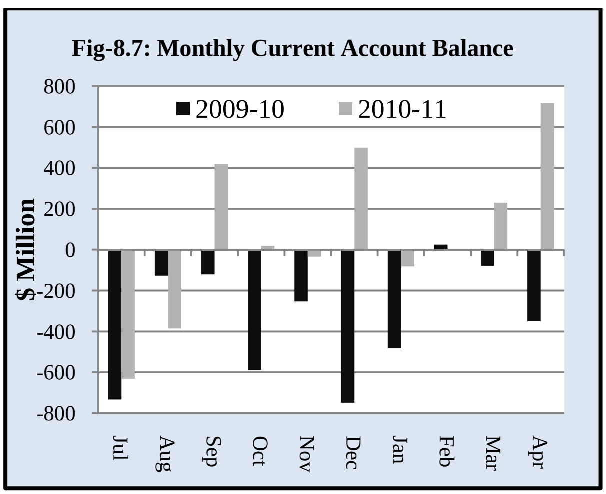
Table 8.10: Summary Balance of Payments **($ Million)**

Items	July-June		July-April	
	2008-09	2009-10	2009-10	2010-11*
Current Account Balance	-9,261	-3,946	-3,456	748
Trade balance	-12,627	-11,536	-9,292	-8,285
Goods: Exports	19,121	19,673	16,167	20,526
Goods: Imports	31,747	31,209	25,459	28,811
Services Balance	-3,381	-1,690	-1,937	-1,392
Services: Credit	4,106	5,229	3,740	4,662
Services: Debit	7,487	6,919	5,677	6,054
Income Account Balance	-4,407	-3,282	-2,594	-2,421
Income: Credit	874	561	469	562
Income: Debit	5,281	3,843	3,063	2,983

Items	July-June		July-April	
	2008-09	2009-10	2009-10	2010-11*
Current Transfers Net	11,154	12,562	10,367	12,846
Of which:				
Workers remittances	7,811	8,906	7,307	9,046
Capital & Financial Account	6,087	5,272	3,687	498
Capital Account,	455	175	154	86
Financial Account	5,632	5,097	3,533	412
1. Foreign Investment	2,622	2,010	1,605	1,491
FDI (Net)	3,695	2,075	1,653	1,193
FPI	-1,073	-65	-48	298
2. Foreign Long Term Loans	1,897	2,210	1,472	333
Disbursements	4,753	4,085	3,020	1,964
Amortization	2,856	1,875	1,548	1,631
Net Errors and Omissions	118	-60	499	-36
Overall Balance	-3,056	1,266	730	1,210
Reserves and Related Items	3,056	-1,266	-730	-1,210
Reserve Assets	-635	-4,063	-2,159	-1,010
Use of Fund Credit and Loans	3,691	2,174	1,106	-200
Exceptional Financing	0	623	323	0

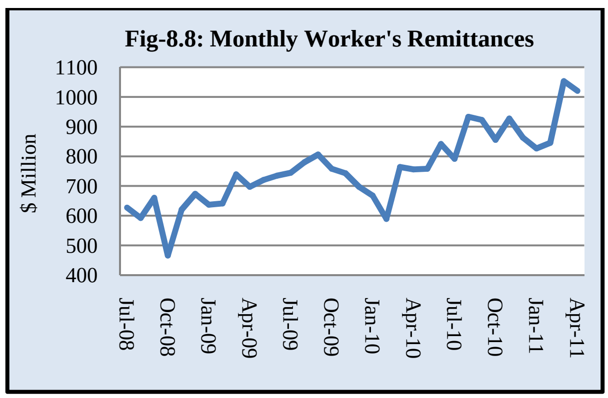
**: Provisional* *Source: SBP*

Quarter-wise analysis of current account balance suggests that with the exception of first quarter July-September 2010-11, current account witnessed surplus during second and third quarters. Furthermore, current account surplus ($716 million) during the month of April 2011 remained 95.0 percent of surplus witnessed during July-April 2010-11.



Workers' Remittances

Remittances for the first time in the history of Pakistan crossed the one billion dollar mark in a single month during March 2011 and remained over the one billion for second consecutive month in April 2011[Fig-8.8] which has boosted optimism about workers' remittances to cross the $11 billion this year. Pakistan Remittance Initiative (PRI) has removed many irritants and incentivizes routing of remittances through former channel.



Workers' remittances totaled $9.1 billion in July-April 2010-11 as against $7.3 billion in the comparable period last year depicting an increase of 23.8 percent [See Table-8.11]. This implies that worker remittances have increased by $ 1.8 billion in July-April 2010-11 which contributed by that amount in improvement of the current account balance. The recent upsurge in remittances can be attributed to the government's efforts for transformation of remittances from informal to formal channels. In addition to that increased support to flood affected relatives also contributed this improvement in remittances.

Analysis of country-wise data (July-April 2010-11) shows that remittance inflows from EU, Saudi Arabia, UK and UAE recorded strong growth of 38.3 percent, 36.7 percent, 34.9 percent and 25.7 percent, respectively. UAE has captured the position of largest source of remittances by accounting for 23.1 percent stake in overall remittances during July-April 2010-11 [Table-8.12]. Moreover, UAE has also taken over USA as a largest source of remittances flows to Pakistan mainly on back of increased remittances inflows from Dubai and Abu Dhabi. Other major contributors to remittance increase remained Saudi Arabia with 23.1 percent share followed by USA (18.6 percent) and UK (11 percent).

Table 8.11: Workers' Remittances **($ Million)**

Monthly Cash Inflow *	2009-10	2010-11	% Change
July 10	744.9	791.2	6.2
August	780.5	933.1	19.5
September	806.1	922.1	14.4
October	758.3	855.1	12.8
November	742.8	926.9	24.8
December	697.6	863.1	23.7
January	667.9	826.6	23.8
February	589.0	845.3	43.5
March	763.7	1,052.9	37.9
April 11	755.8	1,030.4	36.3
July-April	7,306.6	9,046.6	23.8
Monthly average	730.7	904.7	23.8

** Including FEBCs and FCBCs* *Source: SBP*

Moreover higher inflows of remittances from UAE and UK seem to be the result of bilateral arrangements of commercial banks with foreign entities under Pakistan Remittance Initiatives (PRI). Furthermore, initiatives under PRI such as recently introduced Xpress money, Interbank Fund Transfer (IBFT) Facility and individual efforts by some commercial banks in Dubai have also helped to improve the remittance flows to Pakistan. On the other hand increase in remittances from Saudi Arabia was the result of higher demand of Pakistani workers in the kingdom.

Table 8.12 Country/Region Wise Cash Workers' Remittances **($ Million)**

Country / Region	July-April	July-April*	% Change	% Share
	2009-10	2010-11		
USA	1,461.8	1,677.9	14.8	18.6
UK	734.6	990.9	34.9	11.0
Saudi Arabia	1,525.9	2,085.8	36.7	23.06
UAE	1,663.2	2,091.3	25.7	23.12
Dubai	690.0	961.3	39.3	10.6
Abu Dhabi	925.7	1,074.0	16.0	11.9
Other GCC Countries	1,033.0	1,063.5	3.0	11.8
EU Countries	210.2	290.8	38.3	3.2
Others Countries	481.8	552.2	14.6	6.1
Total	7,306.6	9,046.6	23.8	100.0

** Provisional* *Source: SBP*

Financial Account

Net inflows in the financial account declined to $412 million in July-April 2010-11as against $3,533 million during the same period last year. The massive decline in inflows is unevenly contributed by debt creating and non-debt creating inflows. The massive fall in disbursement of loans is witnessed. The inflow of disbursements of long term loans stood at $1964 million in July-April 2010-11 as compared to $3020 million in the comparable period of last year. Amortization payments witnessed some upsurge and resultantly net inflow of loans stood at $333 million as against $1472 million in the comparable period of last year. On the other hand non-debt creating inflows registered negative growth of 7.1 percent by declining to $1491 million from $1605 million. Portfolio investment provided a cushion against worsening of financial account and recorded inflow of $298 million as against outflow of $48 million. FDI component registered much of the decline in non-debt creating inflows.

Foreign Direct Investment

Foreign direct investment (FDI) declined by 28.7 percent during July-April 2010-11 as a result of fall in equity capital and reinvested earnings. The decline in FDI in Pakistan mainly led by the domestic factors such as deteriorated law & order situation, energy crises, circular debt issues and weak economic activity.

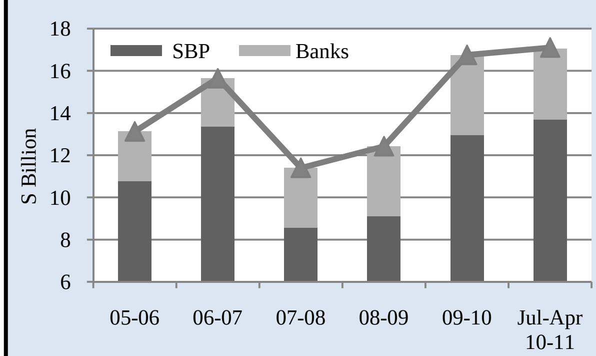
Sector-wise data shows that a large part of fall in overall FDI during July-April 2010-11 was driven by decline in investment inflows in communication, petroleum refining, paper & pulp and chemicals as their share in overall FDI decreased by 13.8 percentage points, 5.2 percentage points, 2.9 percentage points and 2.0 percentage points, respectively. The fall of FDI in communication sector was mainly led by telecommunication where contraction of 75.4 percent was recorded. Apart from impact of negative reinvested earnings on account of companys' losses or lower profits, lower equity investment is due to stiff competition and market saturation in the telecom sector. Lower foreign investment in petroleum refining sectors is largely attributed to deteriorating law & order situation and circular debt issue which constrained business operations. On the other hand, financial business recorded year-on-year increase of 24.3 percent growth and its share in overall FDI increased by 5.7 percentage points.

Foreign Exchange Reserves

The rising trend in Pakistan's foreign exchange reserves continued unabated since 2008-09 [Fig-8.9] and reached to $17.1 billion by end-April 2011. Out of $17.1 billion, reserves held by SBP stood at $13.7 billion and by banks stood at $3.4 billion.

During July-April 2010-11, the improvement in the reserve position was due to inflows of $451 million from the IMF under the Emergency Natural Disaster Assistance (ENDA) and $743 million received under coalition support fund (CSF), thereby increasing the SBP reserves. SBP reserve position was also helped by lower outflows due to shifting of oil payments to inter-bank market. Inflows in the scheduled bank also improved on account of healthy remittances and exports growth.

Fig 8.9: Gross Foreign Exchange Reserves



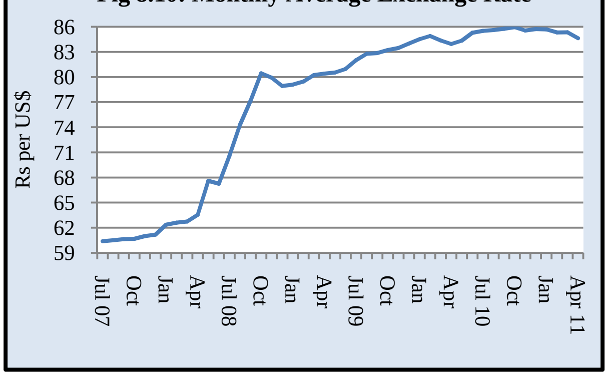
Furthermore, the improvement in reserves can also be attributed to account valuation impact and benefited from lower current account financing requirement.

Exchange Rate

The continued build up in foreign exchange reserves, a surplus in the current account balance and a sufficient inflow of remittances through official banking channels have strengthened Pak rupee vis-à-vis the US dollar both in the inter-bank and open market. Exchange rate averaged Rs. 83.7 in fiscal year 2009-10 and Rs. 85.3 to a dollar in June 2010. During July-April 2010-11, the Pakistan's rupee against US dollar depreciated by 2.2 percent against the 6.6 percent depreciation in same period last year. This comparative stability in rupee mainly owes to improvement in country's overall external account surplus position during the period.

Month wise analysis suggests that the major contribution to 2.2 percent depreciation during July-April 2010-11 came from initial months of the year when rupee came under pressure due to mismatch in inflows and outflows as oil marketing companies had made payments for the import of crude oil.

Fig 8.10: Monthly Average Exchange Rate



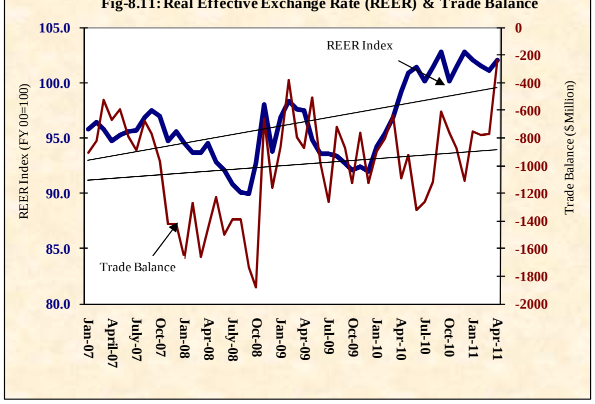
Real Effective Exchange Rate

Real Effective Exchange Rate (REER) is an extension of Nominal Effective Exchange Rate (NEER) index, which along with the exchange rates of the trading partner countries also takes in to account the CPI inflation of the respective countries. REER is mostly indicative of the long term equilibrium exchange rate and the competitiveness of a country and therefore has assumed greater importance within external sector macroeconomic indicators. Conceptually, the REER, defined as a weighted average of nominal exchange rates adjusted for relative price differential between the domestic and foreign countries.

Nominal exchange rate remained relatively stable and rupee depreciated by 4.8 percent vis-a-vis US dollar during 2009-10 as compared to 15.7 percent depreciation recorded in the previous year. Pak Rupee exchange rate with other currencies is determined through cross rates based on the movement of the US Dollar against these currencies in the foreign exchange markets. Pak rupee appreciated 5.2 percent against the pound and 10.1 percent against euro. Japanese yen appreciated against the US dollar in the international market thus, consequently rupee depreciated against the yen by 12 percent during the year. Despite depreciation against the dollar and the yen, Pakistan's currency appreciated by 10.2 percent in real terms during 2009-10 against 0.3 percent depreciation recorded in the previous year.

More importantly the trend in July-April 2010-11 is not very much encouraging because most international currencies have bounced back against US dollar. Resultantly, as rupee depreciated against US dollar by just 0.27 percent, its depreciation against other currencies is massive. Rupee depreciated by 10.9 percent vis-à-vis Euro followed by pound sterling (5.7 percent) and Japanese yen (7.0 percent). Overall NEER depreciated by 6.1 percent, however, the REER appreciated by With SBP no more intervening in the forex market to support oil payments, the exchange rate of the country has become more representative of demand and supply conditions in the forex market. This is likely to be helpful in resolving external account imbalances in the future as exchange rate flexibility provides an adjustment mechanism that can reduce excesses in the external accounts.

Fig-8.11: Real Effective Exchange Rate (REER) & Trade Balance



Historically, there is a strong correlation between REER depreciation and trade balance improvement [See Fig-8.11]. The correlation is not working since Feb-2010 and correlation is reversed. Export growth remained buoyant since January 2010 and terms of trade is supporting Pakistan. The persistent real appreciation of rupee is mainly driven by weaker dollar and the trend will converge to original relationship in months to come. This is evident from Figure 8.11 that in March and April 2011 the REER index and trade balance are converging to their original relationship. Imports on the other hand grew by 19.4 percent in this period which implies persistent appreciation is fueling demand for imports as theory suggests. The export patterns are not truly reflecting trade patterns, however, normalization of commodity prices export will lose momentum.

Another explanation of why rising inflation differential is not reflecting in REER appreciation and this in turn is not translated into trade patterns is redundancy of composition of REER index. REER depend on number of factors such as selection of countries in the trade basket, trade weights allotted to these countries and choice of the base year etc. Even small differences in the selection of these variables can lead to considerable variation in the end results. The REER index base need to be revised to incorporate current trade dynamics.