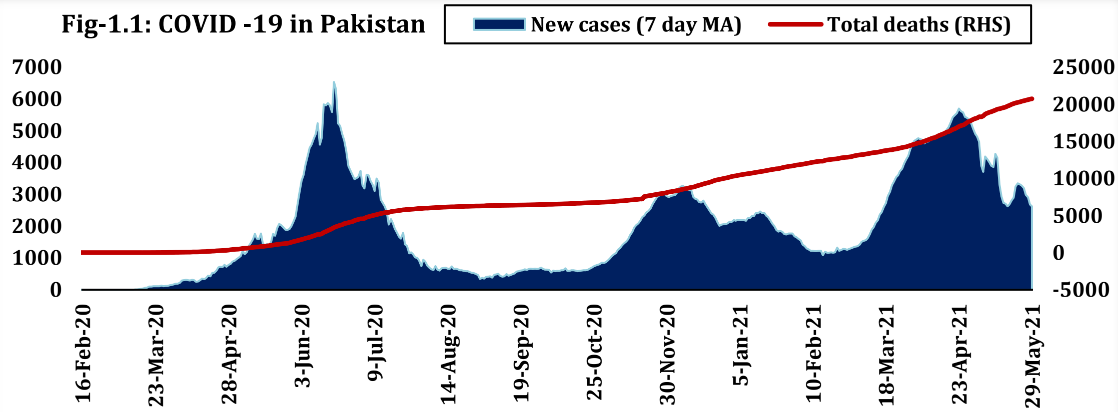
Chapter 1

Growth and Investment

Economy of Pakistan rebounded strongly in FY2021 and posted growth of 3.94 percent which is not only substantially higher than the previous two years (-0.47 and 2.08 percent in FY2020 and FY2019 respectively) but also surpassed the target (2.1 percent for FY2021). Despite strict fiscal constraints, timely and appropriate policy measures taken by the government resulted in a V-Shaped economic recovery.

Start of 2021, amid worldwide vaccination campaigns, the global economy started showing healthy signs of recovery, however, third wave of the pandemic tempered the pace of economic recovery. The pandemic which has already induced shocks like lockdowns, border closures, collapse of trade, travel bans and financial market volatility globally. Third wave in Euro Area, UK, India and many other countries further intensified these restrictions thus affecting the global supply chains. Experts started projecting difference in recovery on the basis of divergent circumstances of each country and the idiosyncrasies of its policy response. It was argued that success in the post-pandemic era will reflect a constellation of policies and capacities peculiar to each country, including national vaccination rates, integration into major economic blocks, the ability to provide fiscal and monetary stimulus and the restoration of solvency in the private sector. For Pakistani economy, this pandemic also became a severe challenge as country was already under the pressure of stabilization required to address Balance of Payments crisis emerged in FY2018. Thus, both consecutive adverse shocks; stabilization pressure owing to Balance of Payments (BoP) crisis and COVID-19 pandemic put the economy far below its potential level which resulted in a negative growth in FY2020. First wave of pandemic started in April 2020 (Fig-1), depressed majority of economic activities.

Fig-1.1: COVID -19 in Pakistan

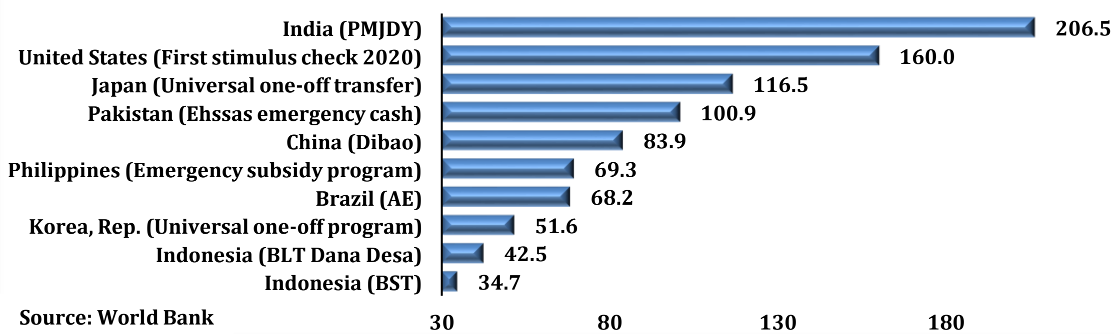


Source: https://covid.ourworldindata.org/data/owid-covid-data

Beginning of new fiscal year was better in term of containment of pandemic and economic recovery, however second wave in late October 2020 and third wave in March 2021 made government efforts more challenging for containing the pandemic and keeping the economic activities to continue.

Real GDP growth of 3.94 percent in FY2021 is V-shaped economic recovery which shows concerted efforts of government for addressing structural issues to avoid further macroeconomic imbalances. The government also took some immediately requisite measures for sustainable and robust growth along with protecting the most vulnerable segments of the society. Given fiscal constraints, the government had also to address public health issues faced because of pandemic, uplift the weaker segment of society that suffered due to lockdowns and keep the economy moving. Further unlike past, the government restricted itself in borrowing from SBP and also followed expenditure-control measures in context of the structural changes for conducting fiscal policy measures. Relief provision to vulnerable segments and growth support was government's utmost priority. However, high interest payments (July-March FY2021 Rs 2.1 trillion ($ 13.1 billion); 4.6 percent of GDP; 32 percent of Total Expenditures) restricted expenditure side from going all out with options, while the fiscal position further became weaker due to sharp decline in non-tax revenues (7.3 percent decline in July-March FY2021 compared to corresponding period last year). Still government has not made any compromise on relief provision to vulnerable segments. In FY2021, allocation for Ehsaas Programme has been increased from Rs 187 billion ($ 1.17 billion) to Rs 208 billion ($1.30 billion) to provide relief to vulnerable segments of society which was affected by pandemic in term of health and livings. Under "Ehsaas Emergency Cash Program", 14.8 million families were benefited. It was the commitment which also made the Programme globally recognized. According to World Bank report on "Social Protection and Jobs Responses to COVID-19: A Real-Time Review of Country Measures" published on May 14, 2021, Pakistan is ranked Fourth in terms of number of people covered while Third in terms of the percentage of population covered, and remained amongst those that covered over 100 million people (Fig -1.2).

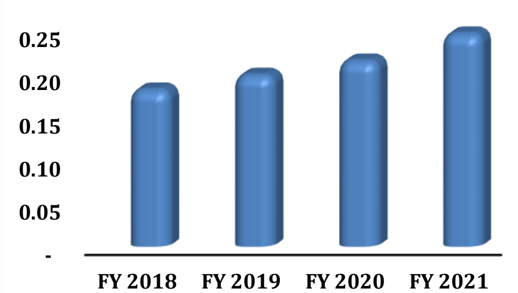
Fig - 1.2: Top 10 cash transfer programmes by actual coverage (million people)



Source: World Bank

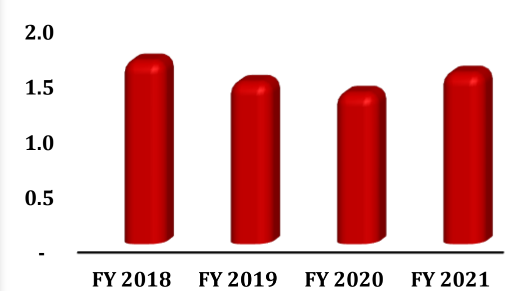
This is an indication that contrary to earlier trickle-down approach, the government followed growth-oriented policies along with protection of vulnerable segments. The government is also considering bottom-up approach for economic growth. Since COVID-19 outbreak, the government started giving special attention to the sector on which majority of daily wagers were dependent which affected livings of these people due to lockdowns and the measures are still continuing. Earlier in April 2020, the government opened the Construction sector and given special package which includes amnesty scheme for investors, tax exemptions, diaspora investment incentives and a Rs 36 billion subsidies (for 10 years) under their niche Naya Pakistan Programme. The government has extended tax amnesty till June 2021, while allowing a fixed tax regime till December 2021. Likewise, the government has also given special attention to Small & Medium Enterprises (SMEs). On 8th October 2020, Prime Minister also approved a National SME Policy Action Plan 2020 to provide much needed support to SMEs. The plan focuses on key areas including SME definition, access to finance, business development services, skills & human resource, technology, market access, infrastructure and entrepreneurship. Since start of current fiscal year, strong rebound in LSM index was also observed. In March FY2021, LSM index remained 155.6 which is 82 percent higher than 85.6 observed in April FY2020. Thus, the government appropriate and in time measures not only built business confidence but also helped in strong economic recovery earlier and more than predicted. In context of growth with protection of vulnerable segments, the mentioned government measured kept Per capita income in Pakistani rupees to continue its increasing trend. However, rebound was seen in per capita income in dollar term which reflects both stability of exchange rate and real economic growth.

Fig - 1.3 A: Per Capita Income in Million Rupees



Source: Pakistan Bureau of Statistics

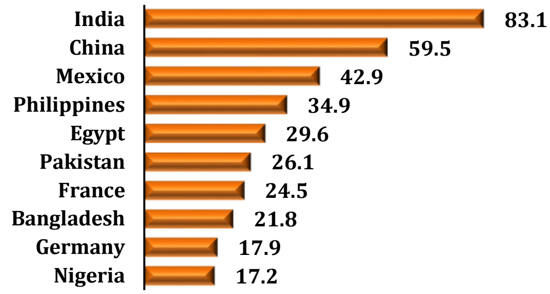
Fig - 1.3 B: Per Capita Income in Thousand Dollars



Source: Pakistan Bureau of Statistics

Although in FY2018, real GDP growth remained 5.5 percent and per Capita Income was $ 1,630. However, Gross External Financing requirements also soared to around $ 30 billion thus caused unsustainable fundamentals on Balance of Payments (BoP) side. More specifically, the total expenditures in the economy substantially exceeded the income generated by the various sectors of the economy. This resulted in a substantial current account deficit of the BoP, which was financed by running down the country's official reserves up to the point that the State Bank had no further resources to maintain the exchange rate. The incumbent government thus took difficult decisions in rationalizing exchange rate and aligned it to the market value-based exchange rate adjustments. In FY2021, external account was stabilized, economic revival started through resumption of economic activities and containment of initial domestic spread of the pandemic, even lead to an appreciation in the Pak Rupee vs. dollar. Most importantly, the growth of imports has been more in those inputs in which tariff rationalization took place which can be used as raw material which in turn helped in increase of exports. Workers' remittances, on the other hand, with government scheme of "Roshan Digital Account" proved instrumental in providing the necessary foreign reserves for current account improvement. During July-April FY2021, remittances soared to $ 24.2 billion posting a growth of 29 percent. However, from the demand side during current fiscal year, it was observed that pace of exports remained slow mainly due to ongoing restriction in its trading partners. Economic recovery was thus seen in start of current fiscal year, on the back of increase in domestic production to be used in domestic markets. On the basis of expectation, Pakistan was among the top ten remittances recipient in the world as shown in Fig -1.4. However, in calendar year 2020, Pakistan received $ 26.0 billion while from January to April in 2021, worker remittances remained $ 10.0 billion showing a growth of 35 percent compared to corresponding period last year ($ 7.4 billion). The remittances thus caused increase in domestic production for use in domestic markets to start economic recovery.

Fig - 1.4: Top 10 Remittance-Recieving Countries in 2020* ($ Billion)



Source: KNOMAD via World Bank

The improvement in the current account led to increased foreign exchange liquidity in the interbank market and was reflected in a build-up in the country's foreign exchange reserves and thus appreciation in the Pak Rupee was seen. Further, from the macro linkage of increased foreign exchange liquidity led to a buildup in Net Foreign Assets component of Money Supply (M2) as well. Earlier in FY2018, more contribution in M2 growth was observed from increase in Net Domestic Assets (NDA) mainly due to government borrowing from SBP. This made pass-through inflationary pressure in FY2019. Thus, price stability became prime concern of the incumbent government. Most importantly, demand-side inflation was controlled by prudent government expenditure policy and restricting government for borrowing from the State Bank. Further, cracking cartels, ensuring smooth supply, tax relief measures, etc along with Ramazan package for providing essential items to general public at affordable prices, helped in slowing down the pace of inflation.

The fiscal prudence and debt management resulted in making, primary balance in surplus during July-September FY2020 (0.6 percent of GDP). During Jul-Mar FY2021, it is still positive and recorded as 1.0 percent of GDP. The primary balance surplus is the necessary condition for fiscal and debt sustainability which had been met in present regime more specifically. The government also reprofiled its debt from short term to long term during last two years as a result of which refinancing risk of the debt portfolio has been reduced significantly. Most importantly, Pakistan entered the international capital market in April 2021 after a gap of over three years by successfully raising $ 2.5 billion showing confidence of international investors on Pakistan's economy.

Summarizing, FY2019 was an era of stabilization, while FY2020 was not only humanitarian crisis but economy suffered severe contraction. Recent economic growth of 3.94 percent posting quicker significant economic recovery. It can be attributed to three things. (i) The government made better management in controlling the pandemic which kept businesses going and confidence high in FY2021. (ii) Fiscal Stimulus of Rs 1.24 trillion along with monetary support given in the pandemic. Further, committed focus of the government on certain targeted sectors like housing, agriculture, industry, exports, etc. (iii) Due to vaccination, quicker than expected global recovery.

It is expected that in coming years the economy will have sustainable and inclusive growth. Government is making initiatives for utilizing bottom-up approach instead of trickle-down approach. Furthermore, the government measures regarding price stability will also help in improving the living of general public.

Global Perspective

The years 2020 and 2021 are especially marked by the outbreak and evolvement of the COVID-19 pandemic. This was in the first place a humanitarian crisis. According to the Corona Virus Resource Centre of the Johns Hopkins University by the end of May 2021 nearly 167.5 million people have been infected and nearly 3.5 million corona-related deaths were registered worldwide.

Worldwide Governments took measures to protect peoples' lives, involving complete or partial lockdowns of economic activities and restrictions on movements. But these necessary measures also brought economic pains. Measured by GDP growth, the world economic growth went into a severe recession, which manifested itself in almost all countries, among which are Pakistan's main export destinations. Table - 1 shows that the world economy was estimated to have contracted with 3.3 percent in 2020. The contraction was very pronounced in the Euro Area and the UK, two of Pakistan's main export areas. The contraction in the US was slightly above the world average, whereas growth in Middle East and Central Asia also significantly declined while China witnessed a growth recession as well. These recessions resulted in a decline of the volume of world trade with 8.5 percent.

Table – 1.1: World GDP and Trade Volume Growth (%)

	2019	2020	2021	2022
World GDP growth	2.8	-3.3	6.0	4.4
United States	2.2	-3.5	6.4	3.5
Euro Area	1.3	-6.6	4.4	3.8
United Kingdom	1.4	-9.9	5.3	5.1
China	5.8	2.3	8.4	5.6
Middle East and Central Asia	1.2	-2.9	3.7	3.8
World Trade Volume	0.9	-8.5	8.4	6.5

Source: IMF World Economic Outlook, April 2021

At the same time as lockdowns were being proclaimed, governments used fiscal instruments to support peoples' incomes and together with Central Banks' Programmes were being designed to keep the economies afloat as much as possible.

Since the beginning of 2021, massive vaccination Programmes were rolled out. By the end of May 2021 around 1.7 billion doses have been administered world-wide. These developments allowed to gradually lift restrictions on human interactions and together with continuing expansionary fiscal and monetary policies, they are expected to generate V-shaped economic recoveries. World GDP growth is expected to rebound by 6 percent in 2021. All Pakistan's major export markets are expected to participate in this rebound, as well as the volume of world trade would increase.

These developments have also impacted Pakistan's economic performance, both directly and indirectly. Pakistan had to restrict human interactions in times when infections were rising both domestically and abroad. Furthermore, economic activity suffered from the economic recession in its major export countries which translated into a negative GDP growth (-0.47 percent) in FY2020. However, in FY2021, Pakistan has strongly come back on its economic front with a V-shaped recovery.

Analyzing the high frequency indicators, such as the OECD Composite Leading Indicators (CLI), it is observed that CLI in Pakistan's main trading partners like US, Euro Area, UK and China are improving which indicates better prospects for Pakistan's exports earnings in coming months. There is significant relationship between CLI in Pakistan main trading partners and Monthly Economic Indicators (MEI) of Pakistan evident from (Fig – 1.5).

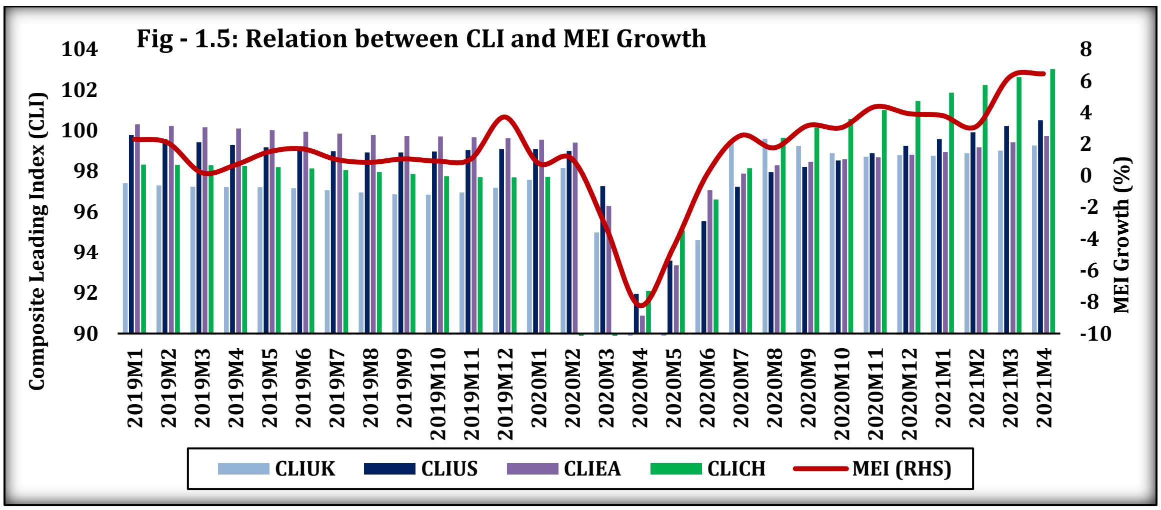
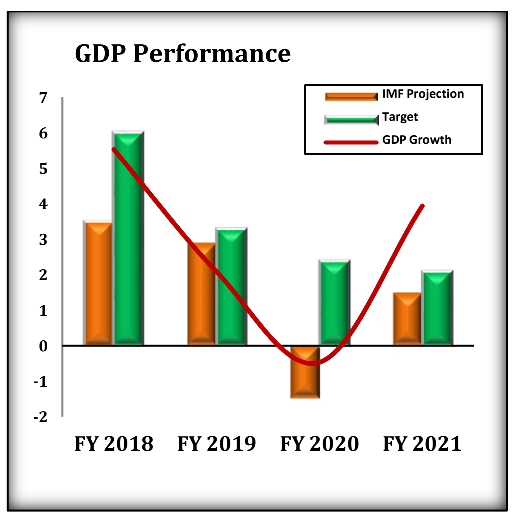


Fig - 1.5: Relation between CLI and MEI Growth

Box: From Macro imbalances to Stabilization to Economic Recovery

The growth in FY2018 (5.5 percent) could not keep momentum due to macroeconomic imbalances i.e., trade deficit in goods and services remained historically high ($ 37 billion, 12 percent of GDP) while the fiscal deficit reached Rs 2,260 billion, (7 percent of GDP). The depletion of foreign reserves and highest gross financing need constrained the government to follow stabilization policies immediately afterwards. However, the government made considerable progress in mobilizing additional financing. Further, tough decisions of following market value-based exchange rate, increasing policy rate and energy price adjustments were also made. COVID-19 worsened the stumbling economic situation. In this backdrop government announced a fiscal stimulus package of Rs1.24 trillion while the State Bank of Pakistan provided liquidity support to households and businesses



to help them through the ensuing temporary phase of economic disruption.

During FY2021, the government continued to support agriculture and industrial sectors. Government has formulated short-, medium- and long-term strategies to achieve inclusive sustainable economic growth and social prosperity:

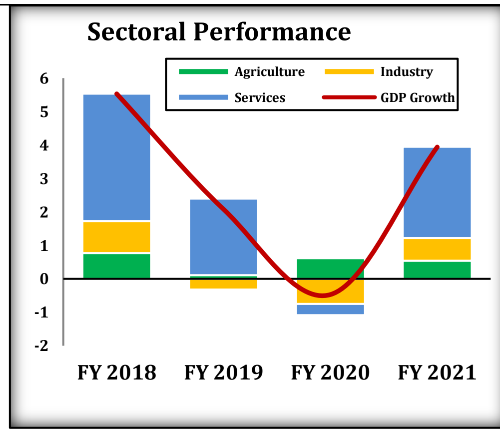
- The government has launched flagship Ehsaas Programme in which total allocation was increased to Rs 208 billion in FY2021 from Rs 187 billion in FY2020.
- Prime Minister approved "Rabi Package" of Rs 5.4 billion and subsidy disbursement in Kharif season 2021 through Provinces on sharing basis (75:25) to reduce the input cost for the farmers. Minimum Support Price of wheat has been increased to Rs 1,800 per 40 kg from Rs 1,400 per 40 kg to encourage wheat cultivation.
- Government allocated Rs 36 billion for payment of mark-up subsidy for financing for the construction and purchase of new houses over a period of 10 years.
- Relief Package for Small & Medium Industries.
- Government slashed Federal Excise Duty (FED) on cement from Rs 2/kg to Rs 1.5/kg w.e.f 1st July, 2020.
- Export Finance Scheme (EFS) Rate is maintained at 3.0 percent and Long-Term Finance Facility (LTFF) has reduced from 6.0 to 5.0 percent in FY2021. Per project LTFF limit has been enhanced to Rs 5 billion from 2.5 billion.
- The total subsidies under credit to exporters outstanding under both schemes (EFS and LTFF) is approximately Rs 660 billion.

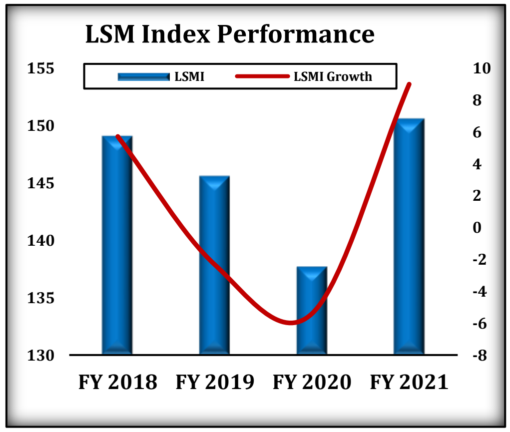
Regardless of strict fiscal constraints, the government followed timely and appropriate policy measures. Thus, better management and fiscal stimulus kept businesses going and confidence high in FY2021. V-Shaped economic recovery despite stabilization pursuit.

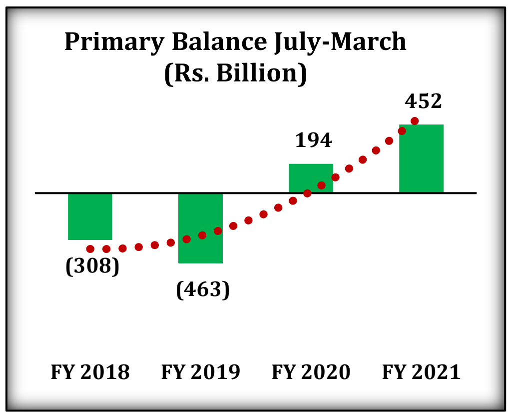
The industrial sector showed a robust growth evident from LSM index while performance of important crops caused an overall improvement in the agriculture sector as well. Buoyancy in the commodity-producing sector, in turn, trickled down to the services sector, with significant improvement in wholesale and retail trade.

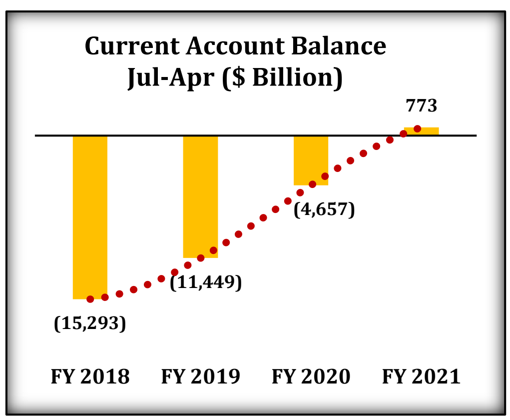
Fiscal performance remained prudent due to austerity measures supported by controlling the non interest expenditures. Thus, expenditure under defense as well as running of civil govt were declined which caused Primary Balance Surplus (Rs 452 billons; 1.0 % of GDP) during July–March FY 2021

Significant improvement in Current Account Balance ($773 million) during July–April FY 2021 helped in maintaining foreign reserve above threshold level, due to which stable exchange rate persists.



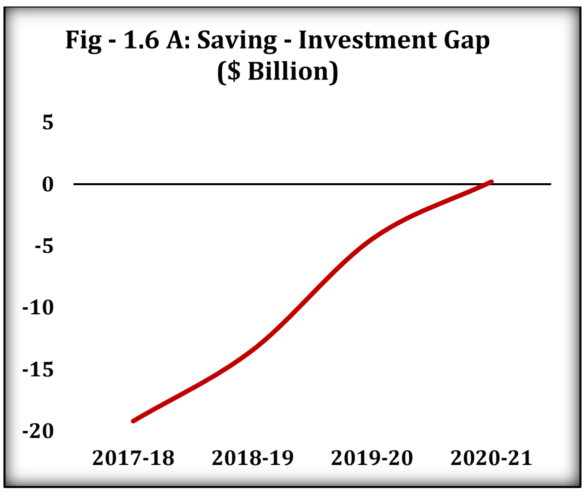


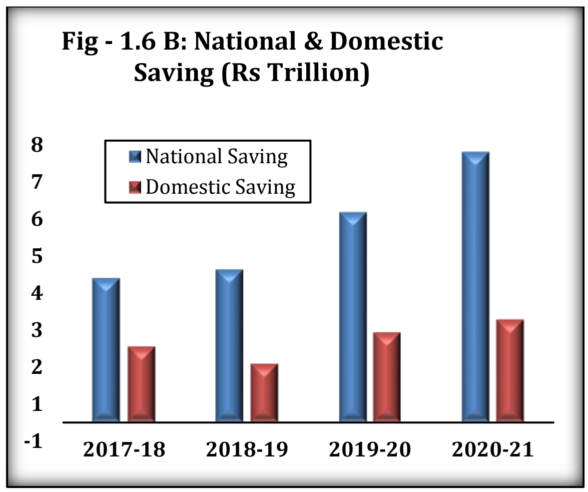




Pakistan Economic Performance FY2021

Effective policy measures taken by the government to contain the virus along with fiscal stimulus and monetary measures by the State Bank of Pakistan in FY2020 helped to kickstart the economy in the pandemic when severe economic depression was prevailing around the globe. Further, relief provision to vulnerable segments through Ehsaas Cash Emergency Programme helped in increase in domestic production for domestic use when exports were not performing well due to worldwide lockdown. Significant growth in remittances helped in stabilizing Pakistan's external account. In second half of current fiscal year, with global recovery, exports also started playing the role in improving current account balance. For July-April FY2021, current account remained in surplus $ 773 million ($ 4.7 billion deficit last year) (Fig – 1.6 A) implying a significant improvement in Saving-Investment Gap which in turn helped in building foreign exchange reserves. Thus, the exchange rate not only remained stable but nine percent appreciation in the Pak Rupee was observed in April 30, 2021 (1$ = Rs 153.45) compared to June 30, 2020 (1$ = Rs 168.06). Further improvement in Saving – Investment gap translated into improvement in National and Domestic Saving (Fig–1.6 B).

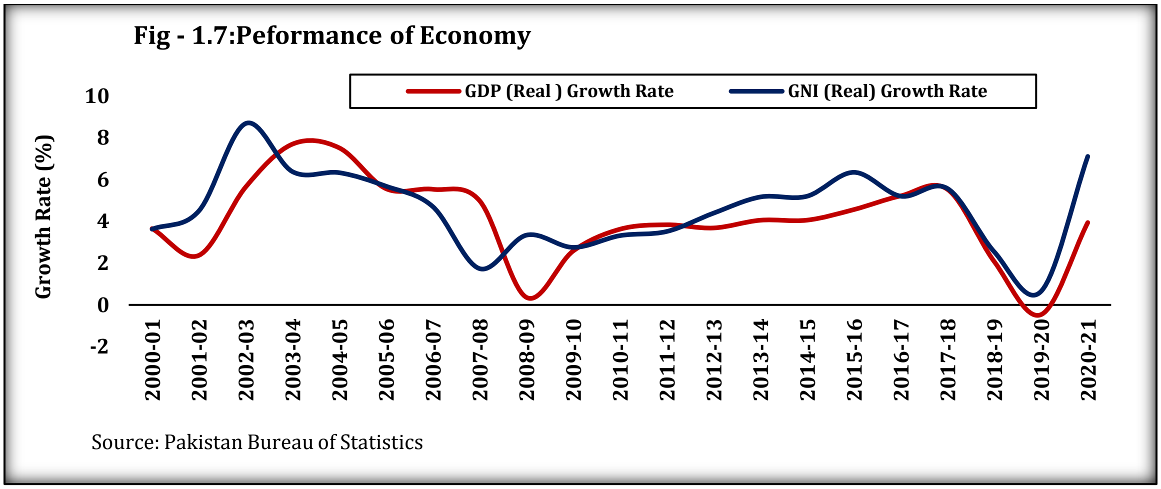




The government is also making efforts for effective mobilization of national savings that will allow higher levels of investment in future.

Aggregate Demand Analysis

For aggregate demand analysis, Nominal GDP (MP) i.e., GDP(MP) at current prices is used. For FY2021, GDP at current market prices stands at Rs 47,709 billion showing a growth of 14.8 percent over last year (Rs 41,556 billion). In dollar term, it remained $ 299 billion higher than GDP observed in FY 2019 ($ 263 billion) due to stabilization. Gross National Income (GNI) is also used for measuring and tracking a nation's wealth which is calculated by adding Net Factor Income from abroad (NFI) to GDP (MP). In FY2021, Real GNI (GNI at basic prices of 2005-06) posted a growth of 7.1 percent, it is the highest since FY2004 (Fig – 1.7).



For FY2021, there was 17 percent growth in GNI at current prices as NFI posted growth of 39 percent on account of 28 percent growth in Workers Remittances as per National Accounts.

In Pakistan, due to non-availability of National Accounts on Expenditures approach, Private Consumption is estimated on residual basis. Thus, Private Consumption has significantly large share in GDP. This large share implies that Pakistan's economy is consumption driven economy like other developing economies. Better consumer confidence can influence increase in domestic production by increasing demand for durables.

Table 1.2: Composition of Aggregate Demand

	FY2019	FY2020	FY2021	FY2019	FY2020	FY2021	FY2019	FY2020	FY2021
	As percent of GDP (MP)			Growth Rates (%)			Point Contribution		
Private Consumption	82.8	79.3	80.7	11.1	4.4	16.8	9.1	3.7	13.4
Public Consumption	11.7	12.8	12.4	9.9	19.3	11.4	1.2	2.3	1.4
Total Consumption [C]	**94.5**	**92.1**	**93.1**	**10.9**	**6.3**	**16.1**	**10.3**	**6.0**	**14.8**
Gross Fixed Investment	14.0	13.7	13.6	(1.9)	6.7	13.8	(0.3)	0.9	1.9
Private Investment	10.5	10.6	9.8	9.2	10.3	6.6	1.0	1.1	0.7
Public Investment	3.5	3.2	3.8	(24.4)	(3.7)	38.1	(1.3)	(0.1)	1.2
Changes in Stock	1.6	1.6	1.6	10.0	9.1	14.8	0.2	0.1	0.2
Total Investment [I]	**15.6**	**15.3**	**15.2**	**(0.8)**	**7.0**	**13.9**	**(0.1)**	**1.1**	**2.1**
Exports (Goods & Services) [X]	10.1	10	9.9	23.7	8.5	13.6	2.1	0.9	1.4
Imports (Goods & Services) [M]	20.3	17.4	18.2	11.0	(6.0)	20.1	2.2	(1.2)	3.5
Net Exports [X-M]	**-10.2**	**-7.4**	**-8.3**	**0.8**	**(20.4)**	**28.9**	**(0.1)**	**2.1**	**(2.1)**
Aggregate Demand [C + I + X]	**120.3**	**117.4**	**118.2**	**10.2**	**6.6**	**15.6**	**12.2**	**7.9**	**18.3**
Domestic Demand [C + I]	**110.2**	**107.4**	**108.3**	**9.1**	**6.4**	**15.8**	**10.1**	**7.0**	**16.9**
GDP (MP)	**100**	**100**	**100**	**10.0**	**9.1**	**14.8**	**10.0**	**9.1**	**14.8**

Source: Pakistan Bureau of Statistics

From Table–1.2, it can be seen that in FY2019, increase in borrowing costs and depreciation of Pakistani Rupee has not alter the Private Consumption patterns except in FY2020, where its growth was recorded 4.4 percent while its share in GDP was 79.3 percent. In FY2021, growth in Private Consumption remained 16.8 percent significantly contributing in GDP growth on account of higher growth in workers remittances and cash transfer to low segment of society through Ehsaas Cash Emergency Programme.

Likewise, growth in the Public Consumption increased in both FY2020 and FY2021 because of COVID-19 related expenditures which started in FY2020 and remained continue in FY2021. However, in FY2021, growth in the Public Consumption remained 11.4 percent lower than 19.3 percent recorded last year mainly due to squeezing unnecessary expenditures as well as decrease in interest payments.

Investment in Pakistan is constrained by many factors like low saving rate, less saving and investment opportunities, lack of financial literacy and access to capital and much of the savings are parked in real estate and abroad. The government is taking measures to increase both savings and investment to augment the employment generating ability of the economy as well as raise resource availability for investment. In this regards Kamyab Jawan Scheme, Rozgar scheme, National SME Policy Action Plan 2020, Export Finance Schemes and Construction Package are some notable measures taken by the government which will accelerate investment in coming years as well.

Gross Fixed Capital Formation (GFCF) posted a growth of 13.8 percent in FY2021 and remained 13.6 percent of GDP. Private and Public including General Government being two components of GFCF posted a growth of 6.6 percent and 38.1 percent respectively. For Private GFCF, 6.6 percent additional investment was observed, however, spare capacity was already available due to lockdown and slow economic activities happened in FY2020. Further, significant growth in Public including General Government GFCF supplemented in acceleration in economic activities for V-Shaped recovery.

During FY2021, a significant increase in Private GFCF was seen in Agriculture (17 percent) on account of increase in imported agriculture machinery and increase in value of stock in the livestock sub-sector. The other sectors in Private GFCF which posted growth were Small Scale including Slaughtering (21 percent), Wholesale and Retail Trade (16 percent), Housing Services (12 percent) and Other Private Service (12 percent). However, Private GFCF in Mining and Quarrying declined by 16 percent due to conservative reporting of expenditure by companies. The other significant decrease in Private GFCF was observed in Electricity Generation & Distribution and Gas Distribution which declined by 67 percent because of lower expenditure reported by K-Electric and Independent Power Producers (IPPs). Due to decrease in imported construction machinery, Private GFCF in construction industry also declined by 24 percent compared to last year. Private GFCF in Transport & Communication industry also posted a decline of 16 percent due to lower expenditure on this account by mobile phone companies.

In context of 38.1 percent growth in Public including General Government sector, it is mentionable that Public Sector GFCF during FY2021 was estimated at Rs 435.2 billion against Rs 314.8 billion during last year. The major industries with positive changes were Electricity Generation & Distribution and Gas Distribution showing 8 percent growth (Rs 246.6 vs. 228.8 billion due to WAPDA and companies being more proactive), Manufacturing (Rs 32.3 vs. 8.6 billion mainly owing to Pak Arab Refinery), Construction with 18 percent growth (Rs 4.9 vs. 4.2 billion due to Capital Development Authority and Lahore Development Authority taking up bigger infrastructure projects) and Transport & Communication with 230 percent growth (Rs 126.4 vs. 38.4 billion due to increase spending on Port Qasim Authority, Pakistan Civil Aviation Authority, National Highway Authority and National Logistics Cell) whereas those with negative changes are Mining & Quarrying posting decline of 34 percent (Rs 16.6 vs. 25.1 billion due to Oil and Gas Development Company Limited not being able to increase its operations) and Finance & Insurance with decline of 15 percent (Rs 8.1 vs. 9.4 billion due to Nationalized Banks). It is also mentionable that estimates of GFCF in the General Government sector were based on budgetary data of federal, provincial and districts governments. The budgeted data is used in the first year which is subject to changes on the basis of actual and reconciled expenditure by various tiers of government in subsequent year. Thus, overall provisional GFCF in general government services increased by 38.1 percent on account of GFCF related expenditure for the Federal Government posted growth of 16 percent, while Provincial Governments posted growth of 47 percent with Punjab (51 percent, increased from Rs 146.1 to 221.0 billion), Sindh (73 percent, increased from Rs 131.8 to 227.6 billion), Khyber Pakhtunkhwa (28 percent, increased from Rs 143.9 to 183.8 billion) and Balochistan (36 percent, increased from Rs 106.2 to 144.5 billion). Moreover, expenditure on GFCF incurred by District Governments also increased by 84.1 percent. Specifically, provisional GFCF by Tehsil Municipal Administration (TMAs) has been estimated at Rs 111.2 billion during FY2021 compared to Rs 49.4 billion, last year posting growth of almost 125 percent.

In aggregate demand, historically contribution of Net Exports usually remained negative. For FY2021, in National Accounts, Exports of Goods and Services posted a growth of 13.6 percent while Imports of Goods and Services posted growth of 20.1 percent. However, in FY2021, higher imports of capital and raw materials helped in growth of exports and domestic economic recovery.

Contemporary global trade relies heavily on the formation of global values chains and successful countries have liberalized their imports to be able to become part of these chains. Pakistan has traditionally followed a high import tariff regime, consequently has not been able to integrate with the global as well as regional value chains and therefore could not achieve its true export potential. In 2019, National Tariff Policy was announced by the Government having an important pillar of reducing input tariffs for local and exporting industries. Under this policy during FY2021, Additional Customs Duties were eliminated on 1622 tariff lines, Customs duty was rationalized on 131 tariff lines, regulatory duty was reduced on hot rolled coil in iron and steel industry and more regulatory duties were removed under the Prime Minister's anti-smuggling drive. These reforms intended to improve availability of raw materials at a cheaper cost so that final produced goods can be produced at competitive rates and hence are better able to compete in international market for exports.

As a result of this policy, during July-April FY2021, under the reformed tariff, import of raw materials registered 23-24 percent growth which has helped up lift Pakistan's exports. Some examples of the imported products that showed increase in quantity and value include cotton, iron & steel, chemicals, rubber, copper, plastics, jute, machinery, tools, tanning & dying extracts, aluminum and others. Over the year a strong correlation has been observed between increase in imports, LSM and economic growth, therefore the National Tariff Policy has been one of the key drivers of the economic growth for the current fiscal year. Further, for product diversification in the export basket, the government has taken steps to facilitate the private sector. One apparent result is that value added exports have risen including clothing, home textiles and apparel, prepared food stuffs, chemicals, surgical instruments, manufactured goods, iron and steel, oil seeds, machinery, tractors, rubber, paper and paperboard, glassware, wood articles, jewelry, ceramics and others. On the other hand, raw or intermediate exports have fallen e.g., cotton yarn, raw leather etc. This is an indication that export oriented sectors are performing decent activity and hence showing good numbers. Further government is also taking measures in exploring more destinations for exports base. Based on available data, it has been found that during July–March FY2021, significant growth in exports has been observed in Australia (26 percent), Russia (27 percent), Denmark (25 percent), Netherlands (12 percent), Belgium (5 percent) and Portugal (4 percent).

Some other significant measures of the government in context of increasing exports are:

- Announcement and implementation of the National Tariff Policy.
- Development on the trade facilitation efforts including implementation of WTO Agreement on Trade Facilitation, launching of National Single Window, operationalization of TIR carnet for seamless transport etc. The objective of the TIR Convention is to facilitate international transit through a simplified Customs transit procedure and an international guarantee system.
- Keeping a close liaison with businessmen and resolving their issues
- The trade and investment officers abroad have been actively engaging with importers to facilitate Pakistan's exports.
- Anti-smuggling crack down, tariff rationalization and rehabilitation efforts of people living in the western border areas of Pakistan.
- Launching of the first ever E-Commerce Policy which has recently helped Pakistan to become part of the Amazon suppliers list

E-commerce growth in Pakistan has been rapid in the last few years especially during the pandemic. Recently, Pakistan has been added by Amazon to its seller's list which essentially means that local Pakistani sellers can now list and use Amazon's platform to sell globally. Thus, Pakistan has now joined the international market which will enhance investment and produce employment opportunities.

Preferential trade agreements with Uzbekistan and Kazakhstan along with the negotiation of agreements on transit trade with Afghanistan are underway to facilitate physical access to those markets. It is also mentionable that enforcement of the China Pakistan FTA, Retention of the EU-GSP plus status and economic recovery in Pakistan's main trading partners will significantly increase value-added exports in coming years as well.

Sectoral Growth Analysis – Production Side

Pakistan's economy is now on course towards strong and sustained recovery mainly due to utilization of unused capacities present due to the pandemic which resulted in lockdown and depressed demand and adequate government policies to support growth.

On the basis of rebound in almost all sectors, provisional GDP growth rate is estimated at 3.9 percent on account of 2.8 percent growth in Agriculture, 3.6 in Industrial sector and 4.4 percent growth in Services sector during FY 2021. Sectoral Point contribution is given below (Table-1.3):

Table 1.3: Sectoral Point Contribution at Constant Prices 2005-06

	FY2019	FY2020	FY2021	FY2019	FY2020	FY2021	FY2019	FY2020	FY2021
	As percent of GDP (MP)			Growth Rates (%)			Point Contribution		
A. Agriculture	18.7	19.4	19.2	0.6	3.3	2.8	0.1	0.6	0.5
B. Industry	19.9	19.2	19.1	(1.6)	(3.8)	3.6	(0.3)	(0.7)	0.7
Commodity Producing Sector (A+B)	**38.6**	**38.6**	**38.3**	**(0.5)**	**(0.3)**	**3.2**	**(0.2)**	**(0.1)**	**1.2**
C. Services Sector	61.4	61.4	61.7	3.8	(0.6)	4.4	2.3	(0.4)	2.7
GDP (GVA)	**100**	**100**	**100**	**2.1**	**(0.5)**	**3.9**	**2.1**	**(0.5)**	**3.9**

Source: Pakistan Bureau of Statistics

Agricultural Sector: The agriculture sector posted growth of overall 2.8 percent mainly due to 2.5 percent growth in Crops and 3.1 percent growth in Livestock. The growth in crops were recorded on account of 4.7 percent growth in Important Crops and 1.4 percent growth in Other Crops.

Better performance of Agriculture is attributed to better weather and improved production system spurred by the Prime Minister's Agriculture Package and increase in minimum support prices of wheat and sugarcane.

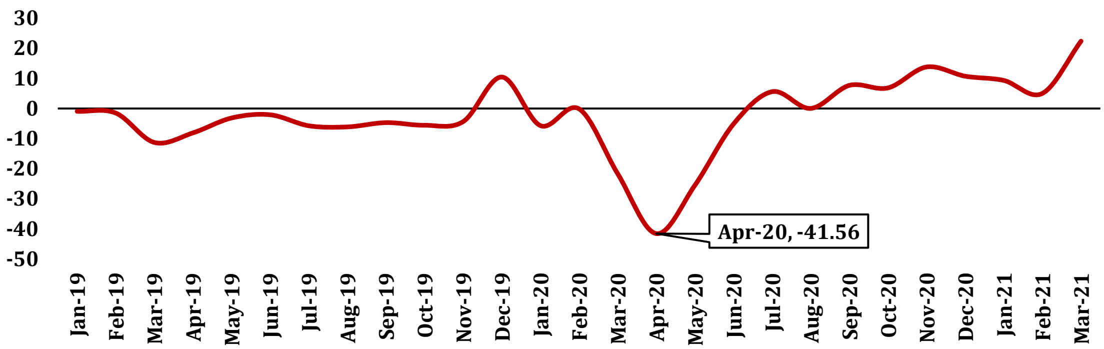
Important Crops has share of 70.2 percent share in Crops Value Addition. In which, historically highest wheat production of 27.3 million tones was reported thus, posting growth of 8.1 percent (25.1 million tonnes last year). Likewise, Rice, Sugarcane and Maize also posted significant growth of 13.6, 22.0 and 7.4 percent respectively. Rice production increased to 8.4 million tonnes from 7.4 million tonnes while production of Sugarcane remained 81.0 million tonnes (66.4 million tonnes, last year) and that of Maize increased from 7.9 million tonnes to 8.5 million tonnes. The production of cotton decreased to 7.1 million bales (9.1 million bales last year) posting a decline of 22.8 percent mainly due to decrease in area sown (2.1 million hectares in FY2021) which is almost 17.4 percent less than last year (2.5 million hectares). One reason was Locust attack while area cultivation under sugarcane has been increased to 1.2 million hectare (1.0 million hectares last year) showing growth of 12.1 percent. This implies that farmers are switching towards sugarcane production. The decline in cotton crop also reduced value added in Cotton Ginning by 15.6 percent. With present performance of important crops, share of wheat in GDP is 1.8 percent and that of rice is 0.7 percent while share of sugarcane, cotton and maize stood at 0.6 percent each in GDP.

Other crops posted growth of 1.4 percent mainly due to 4.2 percent growth in vegetables, 2.0 percent growth in fruits and 5.5 percent growth in production of fodder having share 8.9, 9.3 and 6.7 percent respectively in crops. There was 14 percent decline in pulses which has 1.4 percent share in Crops. Thus, Crops Sector posted a growth of 2.5 percent.

Livestock having 60 percent share in agriculture is very important in determining the overall outcome. Within Livestock Poultry and Poultry Products posted growth of 12.8 percent. Likewise, other components of livestock also have shown positive growth, however, due to 8.9 percent increase in intermediate consumption, growth in livestock remained 3.1 percent in FY2021. The other components of agriculture, forestry and fishing posted growth of 1.4 and 0.7 percent respectively.

Industrial Sector: Industrial sector performance is more dependent on Large-Scale Manufacturing (LSM) as it holds 51 percent share in Industry whereas LSM is reflected by Quantum Index of Manufacturing (QIM) data. Since July 2020, QIM was posting significant year on year (YoY) growth (Fig – 1.8). Thus, its growth is built on momentum by capacity utilization, monetary incentives in the form of low interest rate and other facilitations.

Fig - 1.8: LSM YoY Growth (%)



Source: Pakistan Bureau of Statistics

In March and April last year, the international and domestic spread of the COVID-19 virus had depressed industrial activity, thus QIM index declined MoM by 32.7 percent in March 2020 while in April 2020, it reached to lowest level of 85.6 showing a YoY decline of 41.6 percent.

In National Accounts, growth of QIM has registered a 9.3 percent growth for FY2021 on the standard methodology of Pakistan Bureau of Statistics (PBS). Major contributors to this growth are Textile (5.9 percent), Food Beverage & Tobacco (11.7 percent), Petroleum products (12.7 percent), Pharmaceuticals (12.6 percent), Chemicals (11.7 percent), Non-Metallic Mineral Products (24.3 percent), Automobiles (23.4 percent) and Fertilizer (5.7 percent).

In case of Small Scale, the government has provided Rs 6.9 billion to support the SMEs. Further, Prime Minister approved National SME Policy Action Plan 2020 to provide much needed support to SMEs. The plan focuses on access to finance, business development services, skills & human resource, technology, market access, infrastructure and entrepreneurship. These efforts made Small Scale sector to grow by 8.3 percent during FY2021. Slaughtering also posted growth of 3.9 percent.

Thus, growth in Manufacturing was recorded 8.7 percent on account of growth in LSM, SMEs and Slaughtering. The other sector which has shown significant growth was Construction, which recorded a growth of 8.3 percent due to increase in general government spending (36 percent). Further the contribution of this sector is derived from investment of different construction activities.

Mining and Quarrying posted a decline of 6.5 percent due to decline in production of gas and crude oil by 4.7 and 6.7 percent respectively. Likewise, Electricity and Gas sub sector shown a negative growth of 23 percent, mainly due to decline in subsidy and increase in intermediate consumption of WAPDA and Independent Power Producers (IPPs).

Services Sector: In FY2021, share of Services sector in GDP reached to 62 percent and posted a growth of 4.4 percent. Sub-sectors of Services with respective shares in Services and GDP are given below:

Table 1.4: Components of Services

	Share in Services	Share in GDP
1. Wholesale & Retail Trade	30.5	18.82
2. Transport, Storage & Communication	19.7	12.18
3. Finance & Insurance	6.0	3.72
4. Housing Services (Ownership of Dwellings)	11.3	6.97
5. General Government Services	13.3	8.21
6. Other Private Services	19.1	11.77

Source: Pakistan Bureau of Statistics

Wholesale & Retail Trade is dependent on the output of agriculture, manufacturing and imports. The growth in trade value added relating to agriculture, manufacturing and imports stands at 3.8, 8.2 and 16.1 percent respectively. Based on these, the growth of Wholesale & Retail Trade was recorded at 8.4 percent for FY2021.

In Transport, Storage and Communication, Railways, Water Transport, Air Transport and Pipeline Transport constitute 11 percent share in it. In FY2021, there was almost 24 percent decline as the value recorded at Rs 116.9 billion (Rs 152.8 billion last year) mainly due to lockdown and restriction on travel. Likewise, Communication which includes Postal system including courier services and telecommunication activities having approximately 16 percent share in Transport, Storage and Communication posted a decline of 21.4 percent. However, Road Transport which has 74 percent share posted a growth of 8.4 percent while Storage which has 3 percent share posted 8.7 percent growth during FY2021. Due to these factors, Transport, Storage and Communication posted a decline of 0.6 percent.

During FY2021, Finance and insurance sector showed an overall increase of 7.8 percent due to increase in deposits, loans and insurance. Last Year, in March 2020, Quarter on Quarter (QoQ) growth of Assets was 0.7 percent while in Dec 2020, the YoY growth remained 14.2 percent.

Regarding, Housing Services (Ownership of Dwellings), its data is survey based. Thus, keeping the past trend, constant growth rate of almost 4.0 percent was estimated while the provisional growth in General Government Services based on budgeted data stands at 2.2 percent. Regarding Other Private Services, it includes diverse economic activities scattered over many industries. However, it can be categorized into Computer Related Activities, Professional, Scientific and Technical Activities, Education, Health, Recreation, Cultural & Sports Activities and Miscellaneous whereas Professional, Scientific and Technical Activities has almost 61 percent share in Other Private Services. For FY2021, growth in Professional, Scientific and Technical Activities remained 5.6 percent while due to lockdown measures and closing of recreational places, hotels, etc. a negative growth of 21 percent was observed in Recreation, Cultural and Sports Activities (its share is 0.05 percent in Other Private Services). Thus, provisional growth of Other Private Services for FY2021 remained 4.6 percent.

Way Forward

The Economy has fairly recovered from a dip of last year due to COVID-19 situation. The economic recovery cannot be completely attributed to the holdup of economic activities, the government timely and appropriate policies especially fiscal stimulus also helped in containing the pandemic and recovering economic activities. Further, monetary and financial measures by SBP accelerated the speed of recovery.

The government will continue to take the necessary measures for achieving a higher, sustainable and inclusive growth rate. Thus, increased size of PSDP, better containment of pandemic along with roll-out of vaccination and continuation of Ehsaas Programme will keep momentum of the economic growth. Some other initiatives like new health and nutrition programme (Ehsaas Nashonuma) have been rolled out in timely manner and the expansion of the shock-oriented safety net (Ehsaas Tahafuz) is planned to be extended to other parts of the country in next phase. Additional resources have been allocated for the 'National Poverty Graduation Initiative'. Likewise, another programme "Koye Bhooka Na Soye" also been designed to uplift low segment of society which will in turn bring prosperity to the society. Furthermore, Agriculture and Industrial Packages will not only bring growth in respective sectors but also give boost to the Wholesale and Retail Trade sub-sectors and others sectors in services. Likewise, Special lending schemes for housing, SMEs and agriculture will help financial sector growth. Moreover, reopening of economies and government measures to expand trade will help in strengthening external sector of the economy as well.