ECONOMIC BULLETIN

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Editor's Corner

Dear Readers,

Deep regional disparities remain a persistent and troubling feature of Pakistan's economy, as over the years not only have inter-provincial economic inequalities increased but also the degree of inequality within provinces has grown. This presents a huge challenge for the government.

The Federal Budget 2012-13 has announced certain initiatives for the socio-economic uplift of Balochistan, Federally Administered Tribal Areas (FATA), Gilgit Baltistan and Azad Jammu and Kashmir. The Annual Plan 2012-13 states, 'balanced development by mainstreaming the backward and less developed areas has been recognized as an important element of the development strategy. An amount of Rs38.7 billion is proposed for accelerated development of less developed regions in Pakistan. Among the core priorities of the Rs360 billion Public Sector Development Programme for next year is, regional balance with focus on under-developed areas.

In many of the world's developing countries, there are areas which are relatively less developed and doing considerably less well than average for the country. The persistence of regional disparities within countries is a major policy concern confronting many governments in rich and poor countries alike. For instance, the western provinces of China, the Northeast of India, the southern states of Mexico, the Northeast of Brazil are a few examples of such lagging regions. Poverty rates are far higher than the national average in India's densely populated states of Bihar, Uttar Pradesh, and Orissa and the regional income gap appears to be widening, says the World Development Report 2006. While China achieved high growth rates since the reform began in the late 1970s, the growth was not fairly distributed across regions. In the early stages of the reform process, the coastal regions of the country were given preferential policy treatment which promoted their development. Regional inequalities however arose and later the government shifted its development focus to other regions. A huge sum of state funds was invested in infrastructure, energy, environment and other projects in those areas to support their development.

Pakistan too is experiencing growing and increasing regional inequality in economic growth and prosperity. The regions mentioned earlier have long been deprived of the economic and social development. A World Bank Report, titled *Pakistan: Balochistan Economic Report, May 2008*, has shown that while Balochistan offers some of the best assets for development, its economy has not done well, as it suffers from poor infrastructure, worst water crisis, weak fiscal base, high poverty, and lowest social indicators. The province's mining sector is held back by low funds and low productivity. As its gas supplies are exhausting, Pakistan is also running out of usable energy. There is lack of investment in exploration and development due to security concerns. Its coastal and marine resources remain largely untapped. Similarly FATA suffers from limited economic opportunities, poor social indicators, below average levels of literacy, and poor health conditions.

Their socio economic indicators are substantially lower than national figures. For instance, while the literacy rate for Pakistan is 58 percent, it is 41 percent for Balochistan, 17 percent for FATA and 50 percent for Gilgit Baltistan. Female enrolment rate for Balochistan in 19 percent (national 46 percent) and only 3 percent in FATA. Infant mortality is high at 87 percent for FATA (Pakistan 69 percent) and 79 percent for Gilgit Baltistan. Population per doctor is 1183 at the national level, while it is as high as 6993 for FATA, 5885 people per doctor for Azad Jammu and Kashmir. Maternal mortality is a high of 600 (per 100,000) for FATA against a national figure of 276. The number of villages electrified in Pakistan stands at 147,038, while for FATA the number is 4059.

These grim figures show that there is a pressing need to enhance investment in these areas and bring them at par with other relatively developed areas of the country. Failure to do so can have grim consequences for the economy. Chronic regional underperformance can give rise to many concerns and threaten national unity — lost economic potential, unfairness in regional opportunities, potential instability, loss of social cohesion, and adverse social consequences including higher crime and disease states the World Development Report 2006. It further states, the specific nature of the constraints to regional growth and investment performance in lagging regions needs to be identified and prioritized. Policies that provide fiscal incentives to investors are likely to fail if the main factors that adversely influence regional investment climate – quality of local institutions, skilled labour availability, proximity to key markets, functioning capital and land markets, security risks – still pose binding constraints. Public investment in infrastructure that reduces transport costs for both people and goods has often proved an effective strategy for integration.

To address regional inequalities and broad-based development, a judicious appropriation of resources is imperative. With the 7th NFC Award (2010), an agreement was reached on multiple indicators for determining distribution of resources among the provinces. It takes into consideration population, poverty or backwardness, revenue collection or generation and inverse population density. The distribution of resources taking place earlier under the narrow criteria had culminated over the years into higher regional inequality. Given the profound regional inequalities, the 7th NFC Award gave consideration to the needs of Balochistan, which had previously been receiving low development funds. There has been an increase in the federal transfer to the provinces as it has now been realized that the provinces need more funds for providing health services, educational facilities, drinking water, sanitation and under taking development work in their provinces.

Earlier the Government had announced the Balochistan Package. A number of political and economic related matters were part of the package. Initiatives for the betterment of the economic conditions in the province included among others, rationalization of the royalty formula and the gas development surcharge, setting up of new mega projects with the consent and approval of the provincial government, creation of 5000 additional jobs, the province to receive arrears of gas development surcharge of a sum of Rs120 billion payable in 12 years, and in all poverty alleviation schemes the allocation of the province should be proportional to the percentage of people living below the poverty line.

Realizing the widening gap between the conditions of the people of FATA and the rest of Pakistan, the federal government has allocated Rs17 billion in the PSDP FY2012-13, comprising of Rs10 billion for power subsidy and Rs11 billion for current spending. Similarly for the development of Azad Jammu and Kashmir, the government has allocated Rs12 billion for development and Rs16.5 billion for current expenditure. The government is also executing mega hydel power project Neelum-Jhelum in AJK. Similarly for the development of Gilgit-Baltistan, financial allocation has been enhanced alongwith other initiatives to develop the region.

Regional development policies which facilitate investment, enhance income opportunities and well being of the people living in those areas would help in addressing regional inequalities. Clarity of the factors of weak regional performance need to be identified and appropriate strategies devised and implemented if those living in poorer regions are to be empowered and the region to be developed.

Ayesha Mahmood

Federal Budget 2012-13 – An Overview

Economic Review

Pakistan has shown great resilience in the face of multiple crisis. In the last few years the country has faced significant challenges both economic and political, as a result of which key macro economic indicators still remain weak. Economic Survey 2011-12 puts real GDP growth at a modest 3.7 percent during the year, because of the ongoing energy shortages, low investment, rise in international oil prices and security concerns. While inflationary pressures have eased compared to previous year, the CPI growth rate continues to be in double digits and could rise in the year, if the government continues to borrow heavily from local banks and the State Bank of Pakistan to finance its deficit.

Economy faces several challenges

Investment which plays a crucial role in the economic growth of the country, has seen a declining trend in the last few years. It has declined from 22.1 percent of GDP in 2007-08 to 12.5 percent in 2011-12. Given the deteriorating law and order situation in the country, energy shortages, foreign direct investment inflows have declined to $812.5 million in FY12, against $1.6 billion in the preceding year. There exists large potential for foreign investors in hydel and coal based power projects, wind power, infrastructure, exploration of natural resources etc. Foreign investors will bring in investment only if the environment is conducive and safety of life and property is ensured.

Tax base continues to be narrow and there is widespread tax evasion. The ratio of tax revenue to GDP remains below 10 percent, despite efforts to boost tax collection. This prevents any significant improvement in the fiscal position. Non-Tax collection remained sluggish. Inflows into the Coalition Support Fund (these are foreign payments made to Pakistan as compensation for the expenses incurred and compensation for the use of Pakistani facilities by coalition forces operating in Afghanistan) were below target. This combined with high government spending could see the budget deficit breach the target.

Modest improvement in some areas

In the outgoing fiscal year, there was modest improvement in the performance of the commodity producing sectors, as both the agriculture and manufacturing sectors showed improved growth over the preceding year. Together with the services sector which grew by 4.0 percent and contributes 53.5 percent to the GDP, helped in the improvement of economic growth. In the services sector, the finance and insurance sub-sector showed a positive turnaround growing by 6.5 percent, against a decline of 1.4 percent in FY11. Major crops subsector (Agriculture) grew by 3.2 percent against a decline of 0.2 percent a year earlier, while livestock maintained a growth of 4 percent. The industrial sector performance improved, despite the domestic challenges, growing by 3.4 percent, compared with 0.7 percent in FY11.

In the external sector, the year recorded larger inflows of remittances and a higher trade deficit. Workers' remittances crossed $13 billion in FY12, against $11.2 billion in FY11 and $8.9 billion in FY10. There were enhanced inflows in FY12 over FY11 from USA ($2.3 bn), UK ($1.5 bn), Saudi Arabia ($3.7 bn), UAE ($2.8 bn) and some other countries. Since the launch of the Pakistan Remittances Initiative, the share of workers remittances coming through the banking channel has increased considerably. Trade deficit widened to $19.4 billion during FY12 (July-May) against $14.2 billion in the corresponding period a year earlier.

Government borrowings rise

The government's large financing needs, together with risk aversion by banks, has led to increasing diversion of credit away from the private sector, reducing funds available for investment. Bank lending to the public sector has surpassed the lending to the private sector. Government budgetary borrowing from the banking system reached a record high

Box

Pakistan Economy 2011-12 — Highlights and Targets 2012-13

The domestic economy witnessed numerous challenges in the outgoing fiscal year. The heavy monsoon rains which triggered floods caused extensive damages to crops, infrastructure and human settlements. Total damages are estimated at $3.7 billion, while rehabilitation and cost of recovery is estimated at $2.8 billion. This is in addition to damages of $10 billion to the economy during 2010 floods. The internal security hazards, the fight against extremism with its associated destruction of physical infrastructure, the displacement of thousands of people from the affected areas and the resulting rise in expenditure, and the energy crisis have all taken their toll.

The Economic Survey 2011-12 has been released. We give below highlights of the Report: -

Growth Trends

- GDP grew by 3.7 percent, agriculture by 3.13 percent, large scale manufacturing by 1.8 percent and the services sector by 4.0 percent.
- Major crops sub-sector grew by 3.2 percent compared to a decline of 0.23 percent a year earlier. While cotton, rice and sugarcane witnessed growth in production, wheat output fell.
- Heavy floods in Sindh and Balochistan affected the minor crops such as pulses, vegetables, chillies, onions etc.
- Livestock witnessed marginally higher growth.
- Faced with energy shortages, utilization capacity remained low in the manufacturing sector. Large scale manufacturing grew by 1.1 percent during 2011-12 (July-March).

Investment and Savings

- Total investment declined from 22.1 percent of GDP in FY2008 to 12.5 percent in FY2012. Private investment contracted to 7.9 percent of GDP against a figure of 15.0 percent in the corresponding period last year. During the same period, there was a fall in t he ratio of public investment to GDP from 5.6 percent to 3.0 percent.
- Domestic savings have shown a declining trend since 2005-06, falling from 16.3 percent to 8.9 percent in 2011-12.
- Inflow of foreign direct investment stood at $666.7 million during July-April 2011-12 as against $1292.9 million in FY11.

Inflation

- Inflation as measured by changes in Consumer Price Index was 10.8 percent on average basis during July-April 2012 against 13.8 percent in FY11, with food inflation at 11.1 percent and nonfood inflation at 10.7 percent.
- The Government is focused on restricting inflation to 12 percent during 2011-12.

Fiscal and Monetary Developments

- The fiscal deficit target which was projected at 4 percent of GDP for 2011-12, was later raised to 4.7 percent.
- Revenue measures were taken during the year to meet the growing needs of flood affected people and to meet the year's revenue target.
- Pakistan's tax GDP ratio is the lowest in the region.
- The ratio can only be increased substantially if the major contributors to GDP growth not included in the tax net can be brought into the tax system.
- Large demand for government spending on subsidies (electricity subsidies), interest payments, security and flood related issues (rehabilitation and reconstruction) have put enormous strain on public finances.
- An efficient tax system is vital for raising sufficient revenues to finance essential expenditures without recourse to excessive public sector borrowing.
- Resolving the circular debt issue requires the rationalization of electricity tariff and improving the overall efficiency of the energy sector.
- The State Bank of Pakistan adopted an expansionary monetary policy during FY2011-12. Discount rate was reduced to 13.5 percent from 14 percent, and lowered again in October 2011 by 150 bps to 12 percent.
- Asset mix of the banking system shifted further toward investment, as banks continued to invest in government papers and bonds of public sector enterprises.
- Non performing loans reached Rs607 billion in December 2011 against Rs548 billion in December 2010.
- Government borrowing from the banking system for budgetary support and commodity operations has increased. This has led to sluggish growth in private sector credit, under the crowding out effect.

Balance of Payments

- During July-April 2011-12, exports are provisionally estimated at $20.47 billion and imports at $33.16 billion, resulting in a trade deficit of $12.69 billion.
- Pakistan has become the fifth largest remittances recipient developing country in 2011. Workers' remittances continued to provide strength to the current account. During July-April 2011-12, workers' remittances stood at $10.9 billion.
- Since the launch of the Pakistan Remittances Initiative, the share of workers' remittances coming through the banking channel has increased considerably from 75 percent in FY10 to 91 percent in FY12.

- Pakistan's foreign exchange reserves stood at $16.49 billion at end April 2012 compared to $17.05 billion in the corresponding period a year earlier. This was mainly due to current account deficit and repayment of $400 million to the IMF.

Energy

- During 2011-12, energy outages in Pakistan continued to be the dominant constraint in its growth.
- The estimated cost of power crisis to the economy is approximately Rs380 billion per year, around 2 percent of GDP, while the cost of subsidies given to the power sector to the exchequer in the last four years (2008-12) is around 2.5 percent of GDP.
- Liquidity crunch in the power sector has resulted in under utilization of installed capacity of upto 4000 MW.
- Oil refineries have been running below capacity; constraining the supply of oil and other fuels.
- In the gas sector, Pakistan faced severe shortages that exceeded approximately 2 billion cubic feet per day.
- To mitigate the energy crisis, the government is encouraging private parties to develop LNG projects, has decided to construct five multi-purpose water storages during the next 10-12 years and is taking measures to diversify the energy mix.
- There has been massive accumulation of circular debt.
- The number of electricity consumers has grown to 20.85 million during 2011-12 (July-March).

Public Debt

- By end March 2012, total public debt increased to Rs12,024 billion or 58.2 percent of GDP. In 2011 public debt stood at Rs10,709 billion.
- Increase in public debt results in larger allocations towards debt servicing. In 2010-11, servicing of public debt amounted to Rs852.2 billion as opposed to a budgeted amount of Rs872.9 billion. As at the end of March 2012, servicing of public debt stood at Rs719 billion against the budget amount of Rs1034.2 billion.
- Total domestic debt rose to Rs7206 billion by end March 2012 or 34.9 percent of GDP against Rs4654 billion in 2010 (31.4 percent of GDP).
- Domestic debt portfolio has undergone a transformation from a high dominance of unfunded debt to an increasing dependence on floating debt. The unfunded debt comprising of about 44.6 percent of total domestic debt in FY2002 declined to 23.9 percent by end March 2012, while the share of floating debt climbed to 54.5 percent from 31.4 percent in the comparable period.
- Pakistan's external debt and liabilities rose to $60.3 billion as of March 2012.
- As a percentage of GDP, the external debt and liabilities was down to 26.5 percent, compared to 28.5 percent in FY2011.
- The total amount of foreign economic assistance received during 2011-12 (July-March) stood at $1660 million.

Capital Market

- The Pakistan stock markets remained range bound during the first half of 2011-12 with a predominantly declining trend.
- The KSE-100 index resumed its momentum during the third quarter of FY12 due to certain measures taken.
- A total of 591 companies were listed at the Karachi Stock Exchange as of May 4, 2012 with a total listed capital of Rs1059.1 billion. During this period, aggregate market capitalisation stood at Rs3730.5 billion.
- Investment by foreign investors in the capital markets during July-March 2011-2012, showed a net outflow of $176.3 million.

Targets 2012-13

- The Annual Plan aims at GDP growth of 4.3 percent, with agriculture growing by 4.1 percent, manufacturing 4.4 percent and services by 4.6 percent.
- Major crops are targeted to grow by 3.8 percent, minor crops 4.5 percent, livestock 4.2 percent and fishery 2 percent.
- The industrial sector is expected to grow by 4.1 percent, with large scale manufacturing sector growing by 2.5 percent and small & household manufacturing by 7.5 percent.
- The construction sector is targeted to grow by 4.5 percent.
- Total investment to GDP ratio is projected at 13.1 percent, whereas national savings is projected at 11.2 percent. Provisional estimates for both indicators for 2011-12 show shortfalls against targets set for the year.
- Exports are projected to grow to $25.8 billion, while imports are projected to increase to $42.9 billion. The trade account is projected to be in deficit by $17.1 billion.
- The current account is targeted to be in deficit by $4.8 billion (1.9% of GDP) as against an estimated deficit of $4.0 billion (1.7% of GDP) a year earlier.
- Workers' remittances are targeted at $14.1 billion.
- CPI inflation is projected at 9.5 percent.
- The installed power generating capacity is planned to increase from 23,718 MW in June 2012 to 24,822 MW in June 2013.
- Energy generation is expected to grow from 124501 Gwh in FY12 to 131562 Gwh in FY13.

level of Rs932.8 billion during FY12 (July-March) states the SBP *Third Quarterly Report on the State of Pakistan Economy* for the year 2011-12. Of this amount, borrowings of Rs733.7 billion were from the commercial banks and the rest from SBP. As a consequence, the government could not adhere to its commitment of zero budgetary borrowing from SBP.

Public debt

The total public debt has risen to $12.0 trillion by the end of March 2012. The increase in public debt was led by a surge in government domestic debt that rose by Rs1.2 trillion during July-March 2012. Public debt as a percentage of GDP stood at 58.2 percent by end March 2012 compared to 60.4 percent in FY2010. Any increase in the stock of public debt leads to higher allocations for debt servicing. This in turn places a burden on limited government resources and has costs in the form of foregone public investment in other sectors of the economy.

Total outlay

The Federal Budget 2012-13 has a total outlay of Rs3203 billion compared with a revised Rs3110 billion last year, up by 3.0 percent. Last year's revised expenditure was higher by 12.4 percent or by Rs343 billion over the budgeted figure, mainly because of power sector and fertilizer subsidies. Of the total expenditure outlay for FY13, current expenditure is budgeted at Rs2612 billion marginally smaller over the revised estimates of Rs2632 billion last year. This includes a sharp reduction in subsidies of 59 percent. Development expenditure has been allocated Rs591.1 billion, 23.7 percent higher over previous year's Rs477.8 billion. Federal Public Sector Development Programme in budgeted at Rs360 billion, 18.6 percent higher over last year's revised estimates. Development expenditure outside the PSDP is budgeted at Rs154.3 billion, higher by 26.7 percent over last year's revised estimates of Rs121.7 billion. This increase reflects an allocation of Rs10 billion for Citizen Damaged Compensation Programme and Rs25 billion for other miscellaneous grants. No expenditure was incurred on both these heads last year. Subsidy to TCP for import of urea fertilizer is budgeted at Rs26 billion, while last year's revised estimates show an expenditure of nearly Rs45 billion under this head, 3.75 times higher compared to a budgeted figure of Rs12 billion. Rs60 billion has been budgeted for Benazir Income Support Programme.

Subsidies surge

In FY2011-12 revised current expenditure is placed at Rs2631.9 billion, 13.7 percent higher over the budgeted figure of Rs2314.8 billion. All sub-heads showed increases. Interest payment, subsidies, and defence consume 71 percent of the current expenditure. During the year subsidies surged three fold rising to Rs512.3 billion compared with a budgeted figure of Rs166.4 billion, primarily because of enhanced subsidy to WAPDA/PEPCO and KESC. Rs18.7 billion subsidy was given to PASSCO, of which Rs10.4 billion was given for paddy operation, a figure which had not been budgeted for. TCP was given Rs17 billion for sugar operation against a budgeted amount of Rs4 billion.

Subsidies

(Rs Bn)

	2010-11 Revised	2010-12 Budget	2011-12 Revised	2012-13 Budget
Subsidy to WAPDA/PEPCO	295.8	122.7	419.0	134.9
Inter disco tariff differential	238.8	50.0	412.0	120.0
Subsidy to KESC	47.3	24.6	45.2	50.3
Pick up tariff differential	46.0	24.0	45.0	50.0
Subsidy to TCP	17.1	4.0	18.2	10.0
Sugar operation	4.0*	4.0	16.9	-
Subsidy to PASSCO	2.9	4.1	18.7	5.1
Wheat operation	0.6	-	4.2	1.1
Paddy operation	2.0	-	10.4	-

** Import of Sugar* *Source: Budget in Brief 2012-13*

Higher domestic interest payments

Interest payments were higher at Rs843.8 billion compared with the budgeted figure of Rs791 billion. Interest on domestic debt has risen by Rs57.2 billion during the period, while interest on foreign debt showed a decline of Rs4.3 billion. For FY13, interest payments are budgeted at Rs925.8 billion, with interest on domestic dept rising by Rs73.6 billion.

Interest Payments

(Rs Bn)

	2010-11 Revised	2010-12 Budget	2011-12 Revised	2012-13 Budget
Interest Payment	728.0	791.0	843.8	925.8
Interest on Domestic Debt	653.6	714.7	771.9	845.6
Interest on Foreign Debt	74.4	76.3	71.9	80.2

Source: Budget in Brief 2011-12 & 2012-13

Expenditure on public sector development programmes are less than the interest payments on public debt. This gives government less fiscal space to support economic growth and invest in the social sectors.

PSDP

Meanwhile the size of the Public Sector Development Programe for FY2012-13 has been budgeted at Rs873 billion, Federal PSDP is Rs360 billion and Rs513 billion has been allocated to the provinces. Of the Federal PSDP, Rs80.4 billion has been allocated for two corporations; WAPDA (Rs29.7 bn) and National Highway Authority (Rs50.7 bn). The Annual Plan 2012-13, gives a broad sectoral allocation of PSDP, as shown below:-

PSDP—Broad Sectoral Allocations

(Rs Bn)

	2011-12	2012-13
Water	37	48
Energy	55	65
Railways	15	23
Roads	50	57
Education	19	20
Health & Population	22	24
Others	102	123
Total	300	360

Source: Annual Plan 2012-13

Revenue Receipts

Revised estimates for 2011-12 show that gross revenue receipts at Rs2536.7 billion were short of the budgeted figure by 7.2 percent. This is attributable to lower tax and non-tax revenue collection during the year. Revised tax revenue figures show that while direct taxes were higher by Rs1.4 billion over the budgeted figure, indirect taxes were lower by Rs51 billion, primarily because of lower

Revenue Receipts

(Rs Bn)

	2011-12 Budget	2011-12 Revised	2012-13 Budget
A. Tax Revenue*	**2074.2**	**2024.6**	**2503.6**
Direct Taxes	**743.6**	**745.0**	**932.0**
Income	718.6	730.0	914.0
Workers' Welfare Fund	25.0	15.0	18.0
Indirect Taxes	**1330.6**	**1279.6**	**1571.6**
Customs	206.4	215.0	247.5
Sales Tax	836.7	852.0	1076.5
Federal Excise	165.6	140.0	125.0
Petroleum Levy	120.0	69.0	120.0
ICT Taxes	1.8	3.5	2.5
Airport Tax	0.07	0.07	0.07
B. Non-Tax Revenue	**658.0**	**512.2**	**730.3**
Income from Property & Enterprises	**197.5**	**93.7**	**178.8**
Profits Pak Telecom Authority	75.0	-	79.0
Interest (Provinces)	15.6	12.9	15.4
Interest (PSEs & Others)	42.5	22.2	19.7
Dividends	64.4	58.7	64.6
Receipts from Civil Admn & Other Functions	**321.4**	**249.0**	**354.2**
General Administration	0.8	0.8	0.9
SBP Profit	200.0	200.0	200.0
Defence Services	118.7	45.7	150.6
Law & Order	0.9	1.0	1.1
Community Services	0.5	0.7	0.7
Social Services	0.4	0.8	0.9
Miscellaneous Receipts	**139.1**	**169.4**	**197.4**
Economic Services	2.4	2.4	2.5
Passport & Citizenship Fees	13.7	11.7	14.8
Gas Development Surcharge	24.9	24.0	30.9
Discount Retained on Local Crude Oil	25.1	22.0	22.5
Royalty on Oil	15.2	22.8	22.0
Royalty on Gas	32.8	35.2	36.1
Windfall Levy against Crude Oil	-	5.1	5.3
Gas Infrastructure Dev. Cess	-	8.0	30.0
Petroleum Levy on LPG	-	0.4	1.0
Others	24.9	37.7	32.2
Total Revenue Receipts (A+B)	**2732.2**	**2536.8**	**3233.9**
* Out of which FBR	1952.3	1952.0	2381.0

Source: Budget in Brief 2012-13

collection from petroleum levy (Rs69 billion against a target of Rs120 billion) and federal excise duty (FED). Last year FED was withdrawn on certain items, 1 percent special excise duty was eliminated and a major portion of services was brought in the purview of provincial sales tax instead of FED. This year the government plans to further eliminate FED on additional 10 items.

Tax revenue target raised

For FY2012-13, the Government is targeting domestic tax revenue generation of Rs2,503.6 billion up 24.0 percent over last year, to raise tax GDP ratio. While no new tax has been imposed, a 25 percent increase in direct taxes and 23 percent increase in indirect taxes is envisaged. This would require improving the administrative and collection measures and bringing those outside the tax net in its ambit. The imposition of 1 percent withholding tax on traders/distributors would help in enhancing documentation of the economy. Tax collection is expected to grow, as efforts are made to increase tax payer documentation, improved tax administration, simplying the tax system and keeping a close watch on Afghan transit trade.

Collection to increase

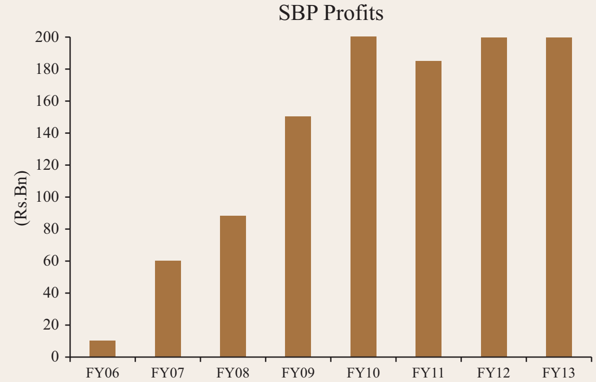
Of the total tax collection budgeted for FY2012-13, direct taxes would generate Rs932 billion, higher by 25 percent over last year. Indirect tax collection would net in Rs1.57 trillion, where sales tax is estimated to increase 26 percent over the year to Rs1.07 trillion. Collection against FED and customs is projected at Rs372.5 billion, an increase of 5 percent over the year. FED on cement was reduced by Rs250 per metric ton in FY12, while this year it would be reduced by Rs100. Customs duty on stationery items has been abolished, while it has been reduced on pharmaceutical products.Customs duty in FY13 are budgeted to be higher by Rs32.5 billion, while FED is expected to be lower by Rs15 billion.

The government has budgeted non-tax receipts at Rs730.3 billion during FY2012-13, higher by 43 percent from a revised estimate of Rs512.2 billion in FY12. Last year's revised estimates show a decline of 22 percent over the budgeted figure, attributable to a fall in receipts from income from property and enterprise and receipts from civil administration and other functions. Under the former head, profits of Pakistan Telecommunication Authority were expected at Rs75.0 billion to be earned through auction of 3-G licenses. However, these licenses could not be auctioned due to recession in the market. However, the auction is expected to take place in the current fiscal year (FY13). Interest receipts from Public Sector Enterprises and others declined by Rs20.3 billion. Receipts from defence services were short of the budgeted figure of Rs118.7 billion by 61.5 percent. Last year's miscellaneous receipts were higher by 21.8 percent, because of higher gas infrastructure development cess, royalty on natural gas/ crude oil and levy against crude oil. Total development surcharges and royalties are budgeted for Rs147.8 billion, against preceding years revised estimates of Rs117.5 billion.

Non-tax receipts

For FY2012-13, receipts from civil administration and other functions are earmarked at Rs354.2 billion, up 42 percent over the year. Under this head the primary contributor remains profits from State Bank of Pakistan which are estimated at Rs200 billion.

SBP Profits



In addition, revenue of Rs150 billion is expected under the Defence Services, and Rs79 billion as profit from Pakistan Telecommunication Authority through auction of 3G licenses. Dividends are expected to be slightly higher at Rs64.6 billion, against last year's revised estimates of Rs58.7 billion on account of higher dividends budgeted for Pakistan Petroleum Limited, Oil & Gas Development Corporation, Saindak Metal Limited, National Shipping Corporation etc.

Fiscal Measures – Highlights
Some of the measures adopted in the Federal Budget 2012-13

Income Tax

- To provide relief to low income earners, basic exemption limit has been raised for salaried individuals to Rs400,000. The existing rate slabs are proposed to be reduced from 17 to 5.
- Exemption limit for income tax for business individuals and Association of Persons is also being enhanced to Rs400,000.
- In the case of business community the rate of minimum tax is proposed to be reduced to 0.5 percent from 1 percent on gross turnover.
- Advance tax @0.2 percent is levied on cash withdrawal from banks if it exceeds Rs25,000. This amount has been raised to Rs50,000.
- Capital Gain Tax (CGT) is being levied on the sale of property if it is disposed off within two years of its acquisition.
- To promote investment in securities and insurance sectors, the limit of investment eligible for tax credit is being enhanced from 15 percent to 20 percent of the taxable income. The existing limit of investment of Rs500,000 in securities or insurance premium is also being increased to Rs1,000,000. The retention period of securities is also being reduced from three to one year.
- To recognize and incentivize compliant taxpayers, it is proposed to introduce a Taxpayer Honour Card scheme for all taxpayers who have filed tax returns and paid due taxes for the last 5 fiscal years. The holders of the card will be entitled to various privileges and benefits.
- It is proposed that profit on intra-group debt be exempted from withholding tax.
- It is proposed that the exemption to Workers Profit Participation Fund be granted in the Income Tax Ordinance 2001.
- It is proposed that dividend received by banks from money market funds and income funds are to be taxed progressively over a period of two years. For tax year 2013 @25 percent and for tax year 2014 and onwards @35 percent.
- In order to incentivize the taxpayers opting out of Presumptive Tax Regime (PTR) a lower rate of tax is being offered to commercial importers, exporters and suppliers if they opt out of PTR.
- To ensure documentation of the economy and to bring traders/distributors on tax roll, it is proposed that the manufacturers shall be made withholding agents to collect 1 percent tax against the sale made to traders and distributors. However, the tax so collected shall be adjustable against their income.
- It is proposed to levy and collect CVT on transactions of immovable properties in Islamabad with identical structure adopted by the provinces.
- The value of vehicles is proposed to be enhanced from Rs1.5 million to Rs2.5 million for the purpose of depreciation allowance.
- The rate of initial depreciation on new buildings is 50 percent which results in converting the accounting income to tax loss. The rate of initial depreciation is being reduced to 25 percent.
- The exemption granted to profit and gains to the Venture Capital Company and Venture Capital Fund till 2014 is proposed to be extended for 10 years i.e. upto 2024.

Customs Duty

- The maximum general tariff slab has been reduced from 35 percent to 30 percent. This will reduce the number of duty slabs from 8 to 7.
- Customs duty on raw materials and components for printing and stationery sector has been reduced.
- Customs duty on 88 pharmaceutical raw materials and other input goods has been further reduced from 10 percent to 5 percent.
- Customs duty on self-copy papers and self-adhesive papers has been reduced from 25 percent and 20 percent to 10 percent.
- Three major Notifications (SRO 565, 567 and 575) provide exemptions and concessions on import of plant and machinery for setting up of industries and import of raw materials for a large number of domestic industries. These are being cleansed of anomalies and are being simplified.
- In order to promote indigenous industry, some industrial raw materials are being included in the concessionary regime.
- Customs duty on scrap of rubber/shredded tyres has been reduced from 20 percent to 10 percent to encourage its use as a substitute fuel for the cement industry.
- WCO has made 5-yearly changes in HS nomenclature for commodity classification and has issued HS-2012 version. Pakistan Customs Tariff classification structure is being aligned with the WCO nomenclature.
- Introduction of 12 Digit Subheadings in Customs Tariff to fulfill the requirement of full automation of import processing through the Customs computerized system (WeBOC) and statistical purposes.
- In order to encourage import of hybrid electric vehicles (HEVs) at affordable prices the rate of duty and taxes presently applicable to HEVs and their batteries are being reduced by 25 percent.
- A number of legislative measures have been taken.

Sales Tax/Federal Excise Duty

- Reduction in the higher rates of Sales Tax from 22 percent and 19.5 percent to 16 percent.
- Reduction in Federal Excise Duty on cement from Rs500/PMT to Rs400/PMT.
- Elimination of excise duty on 10 items with the objective to further phasing out of Federal Excise regime.
- Streamlining the sales tax regime by substituting zero-rating on certain items with a view to stop illegal refunds.
- Exemption of federal excise duty on livestock insurance.
- Revision in the upward limit of price tiers of cigarettes to enhance the federal excise duty on locally produced cigarettes.
- Increase in the rate of sales tax on steel sector.
- Shifting of cotton seed oil from exemption to zero-rating regime enforced through amendment in Schedules to the Sales Tax Act, 1990.
- Federal Excise Duty on foreign travel to be revised.
- A number of simplification measures adopted.

Source: Federal Budget Documents 2012-13

The miscellaneous receipts of Rs197 billion is a 16 percent growth over preceding year's receipts of Rs169.4 billion. During FY13, it is expected that Rs30.0 billion would accrue from gas infrastructure development cess, Rs36 billion from royalty on natural gas, while a 28.6 percent increase is projected from gas development surcharge.

The provincial share in revenue receipts from the divisible pool taxes is governed by the 7th NFC Award. This takes into consideration multiple indicators; population, poverty or backwardness, revenue collection or generation and inverse population density; with a weight assigned to each indicator. The resources for the provincial governments are to be distributed on the basis of the percentage specified against each. In FY2011-12, provincial share in revenue receipts at Rs1208.6 billion were marginally higher over the year's budgeted figure.

Provincial Share in Revenue Receipts

(Rs Bn)

	Divisible Taxes		Straight Transfers		GST on Services**		Total	
	2011-12 Revised	2012-13 Budget	2011-12 Revised	2012-13 Budget	2011-12 Revised	2012-13 Budget	2011-12 Revised	2012-13 Budget
Punjab	540.5	662.5	8.8	7.3	36.6	40.5	585.9	710.3
Sindh	256.5	314.4	55.1	59.2	1.9	-	313.5	373.6
Khyber Pakhtunkhwa*	171.1	209.7	17.5	22.1	8.9	10.0	197.5	241.8
Balochistan	95.0	116.4	13.1	12.8	3.6	4.1	111.7	133.3
Total	1063.1	1303.0	94.5	101.4	51.0	54.5	1208.6	1458.9

* One percent of the net proceeds of divisible taxes shall be assigned to Khyber Pakhtunkhwa to meet the expenses on war on terror.
** Provisional

Revised estimates of net capital receipts of the Federal government are placed at Rs525.5 billion in FY2011-12, nearly 33 percent higher over the budgeted figure. This is attributable to higher receipts from Ijara Sukuk Bonds and Treasury Bills. Receipts from Saving Schemes were short of the target of Rs149.2 billion by Rs51.6 billion, as receipts from Behbood Saving Certificates were lower by Rs10.3 billion over the budgeted figure of Rs62.0 billion for FY12.

Capital Receipts

(Rs Bn)

	2011-12 Budget	2011-12 Revised	2012-13 Budget
Receipts	464.2	549.6	541.1
Recoveries of Loans and Advances	51.6	57.0	54.0
Permanents Debt	129.3	175.4	143.8
Ijara Sukuk Bonds	80.0	125.5	90.0
Floating Debt	119.1	209.2	155.6
Prize Bonds	37.0	49.2	45.6
Treasury Bills	82.1	160.0	110.0
Public Account	164.2	108.0	187.6
Saving Schemes	149.2	97.6	178.2
Disbursements	68.5	24.1	63.3
Net Capital Receipts	395.7	525.5	477.8

Source: Budget in Brief 2012-13

To finance its expenditure, the government had budgeted external resources at Rs413.9 billion for FY12. However, revised estimates for the year place them at Rs226.2 billion, short of the target by 45.3 percent. Disaggregated figures for external resources show a substantial decline in non-food commodity aid and other aid. For FY13 external financing has been budgeted at Rs386.9 billion.

External Resources

(Rs Bn)

	2011-12 Budget	2011-12 Revised	2012-13 Budget
Project Aid	76.8	184.5	165.8
Commodity Aid (Non-Food)	127.0	10.1	44.4
Tokyo Pledges	17.6	5.0	1.0
Kerry Lugar	34.2	20.4	8.2
Other Aid	158.4	6.2	93.0
Privatization	70.4	0.0	74.4
Total External Resources	413.9	226.2	386.9

Source: Explanatory Memorandum on Federal Receipts 2012-13

Last year as external resources fell sharply over the budgeted amount and revenue receipts could not meet the targets for the year the government's recourse to bank borrowings rose significantly. As against a budgeted amount of Rs303.5 billion, borrowings were three times higher at Rs939.2 billion. For FY13 bank borrowings have been budgeted at Rs483.8 billion.

Bank Borrowings (Rs Bn)

	Budget	Revised
2008-09	149.0	146.0
2009-10	144.10	89.10
2010-11	166.54	452.22
2011-12	303.52	939.20
2012-13	483.8	-

The Medium Term Budgetary Statement forecasts macroeconomic indicators for 2012-15, which are given below:-

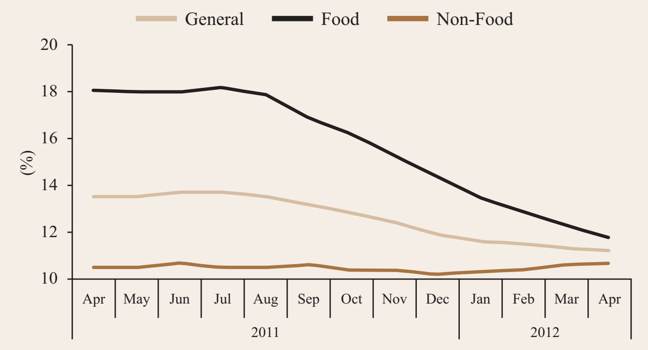
Medium Term Budgetary Statement

	Budget	Forecast	
	2012-13	2013-14	2014-15
Real GDP Growth (%)	4.3	4.8	5.3
Inflation (%)	9.5	8.5	8.0
(as percentage of GDP unless otherwise indicated)			
Total Revenue	14.3	14.0	14.0
Tax Revenue	11.1	11.6	11.7
FBR Tax Revenue	10.1	10.7	10.9
Non Tax Revenue	3.2	2.4	2.3
Total Expenditure	19.0	18.2	17.7
Current Expenditure	14.5	13.8	13.1
Development Expenditure	4.4	4.4	4.6
Fiscal Balance	-4.7	-4.2	-3.7
Revenue Balance	-0.3	0.2	0.9
Total Public Debt	56.5	53.2	50.6
GDP at market prices (Rs. in billion)	23,655	27,002	30,759

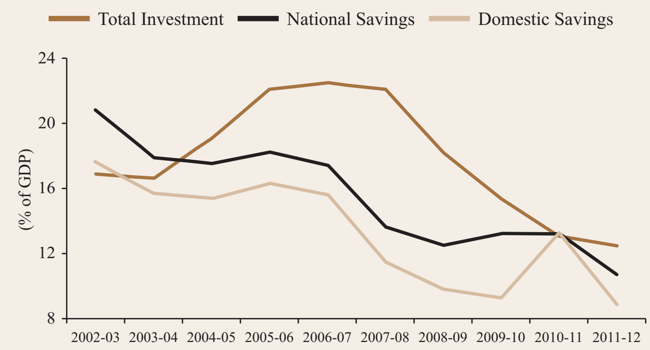
Source: Budget in Brief 2012-13

Economy at a Glance

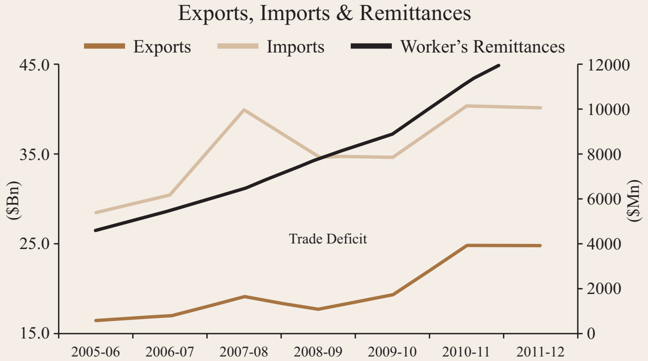
Trends in Inflation – CPI



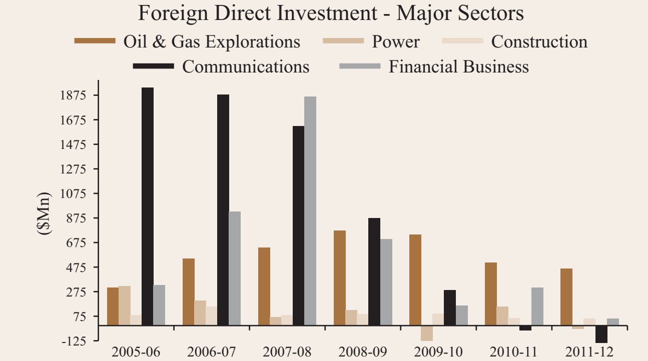
Savings and Investment



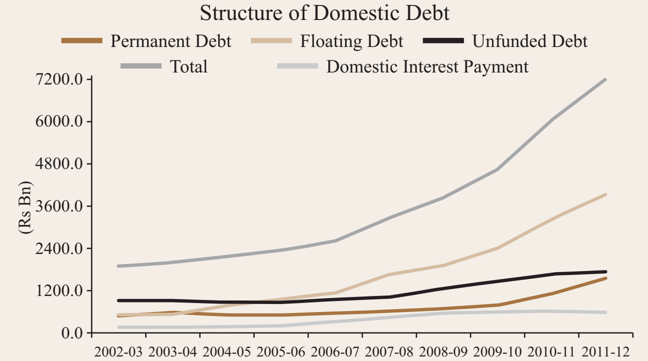
Exports, Imports & Remittances



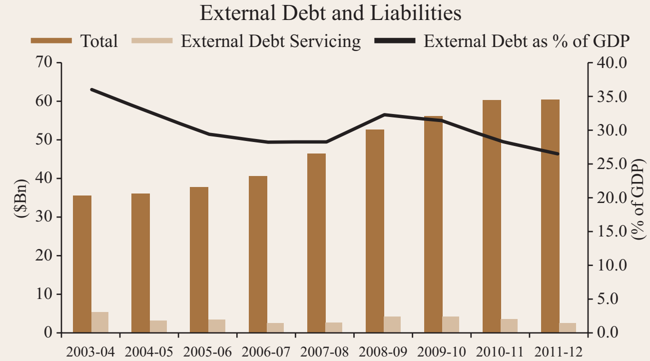
Foreign Direct Investment - Major Sectors



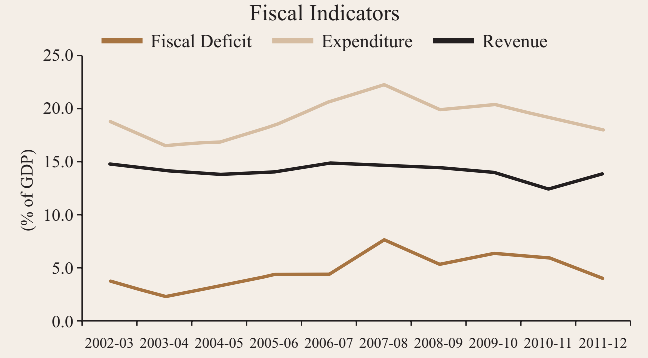
Structure of Domestic Debt



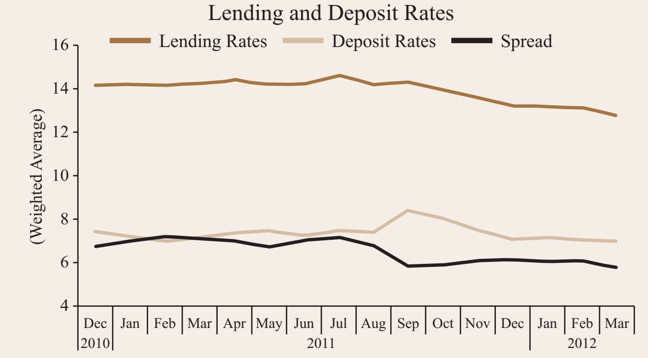
External Debt and Liabilities



Fiscal Indicators



Lending and Deposit Rates



Sectoral Implications of the Federal Budget 2012-13

Budget Report: FY 2012-13, prepared by Taurus Securities Ltd, a subsidiary of National Bank of Pakistan gives the sectoral implications of the Federal Budget. We give below excerpts from the said report.

Capital Market

Capital markets are vital for the economic development of a country. The changes made through the Finance (Amendment) ordinance, 2012 may be incorporated into the Statue through the Finance Bill to give poise to the investors and help develop the capital markets.

To promote the capital markets, exemption on the profit and gains of a Venture Capital Company and Fund is being extended up to the year 2024.

On the other hand, there are measures that are positive for the equity and money markets such as:

Measures

- To promote investment in securities and insurance, the limit of investment as a proportion of taxable income is being increased from 15% to 20% and from Rs 500,000 to Rs 1 million, whichever is lower. The required retention period of shares is being reduced from 3 years to 2 years.
- Transfer of funds between retirement funds will be exempt from tax to encourage a competitive market. Furthermore, retirement funds would also be exempt from withholding tax provisions on Capital Gains Tax.
- Dividends received by banks from money market and income funds will be taxed progressively over a period of two years as normal business income. Dividends will be taxed at 25% in tax year 2013 and at 35% from tax year 2014 onwards to eliminate tax arbitrage.

Impact Neutral to Positive

We feel that the budget would have a "*Neutral to Positive*" impact on the capital markets due to the budget being populist-based.

Oil & Gas

Measures

- Revenue in the shape of petroleum levy targeted at Rs120 billion against a revised FY12 estimate of Rs69 billion.

Impact Neutral

We expect Neutral impact of the above developments on the overall oil and gas sector. Since E&P sector is regulated under the petroleum policies, as expected, no specific measures are part of this announced budget. While in the case of oil marketing companies, though the government implements levies and GST through budget, however ex-refinery prices and OMC margins determination are the responsibility of Oil and Gas Regulatory Authority.

Apropos of the above, a further non-budget revision may be anticipated by the government for the regulated products that may involve an improvement of margins for the OMCs, thus, the profitability of the sector may improve.

Electricity

Measures

- Power sector subsidies reduced by 60% to Rs 185.28bn for FY13, as opposed to revised allocation of Rs464 billion during FY12.
- Inter disco tariff differential has been allocated at Rs120 billion against revised allocation of Rs464 billion during FY12.
- Allocation of Rs50.3 billion, as subsidy to KESC against revised allocation of Rs45.23 billion.

Impact Neutral

As circular debt continued to plague the power sector, budgetary measures taken show tightening of screws on WAPDA and KESC. With over Rs500 billion circular debt the government has taken some steps to bring an end to this menace. The problem arises due to tariff differential as determined by NEPRA for different distribution companies. However, no amount has been allocated to pick up interest payment for TFC against Rs55.7 billion allocated during FY12. No allocation has been made for adjustment of additional surcharge against GST despite the fact that Rs10 billion was allocated during FY12.

Chemicals

Measures

- Reduction in GST to 16% from 17%
- GIDC increased by PKR 103 per MMBTU

Demand for urea is price inelastic hence increase in price will result in negligible change in off takes.

Keep gas prices constant will keep margins stable.

Impact Neutral

As per expectations gas cess (GIDC) was increased to the tune of Rs103 MMBTU. This will increase cost of urea by Rs135 per bag. Earlier the government announced its decision to import 100,000 tons of urea, with further imports 200,000 tons the expected in the third quarter. The government was contemplating importing urea from Iran in exchange of wheat and rice, however the deal did not materialize. We believe total urea available in the market at the end of May is around one million tons. We believe urea off take will decline by 1 percent year-on-year due to higher off takes during December and January. We forecast total urea off takes to be 5.859 million tons.

Higher inventories of urea will not bode well for most companies in particular FFC which has a higher inventory level. The company also decided to reduce prices by Rs145 in order to kick off its urea sales. We believe the government will make further urea imports as there is sufficient quantity available in the market.

FFBL should benefit from producing more of DAP than from its urea sales. We currently are estimating DAP primary margins to be around $240 per ton for CY12.

Cement

Measures

- The allocation for Annual Development Plan for FY13 has been set at Rs873 billion, experiencing a significant rise of 19% year-on-year over the last fiscal year. The federal component PSDP has been increased to Rs 360 billion (rising by 18.4% rise from Rs303 billion during FY12).
- Federal Excise Duty has been reduced by Rs100 per tons to Rs400 per ton applicable in FY13, declining by 20% year-on-year over Rs500 per ton during FY12.
- Duty on scrap rubber and shredded tyres has been reduced to 10% over 20% during FY12 (relief of 50% year-on-year).
- Rs38.5 billion have been allocated for construction of small and medium sized dams, canals and improvement of existing irrigation system.
- Sales tax has been kept at 16%, same as in FY12.

Impact Positive

Similar to previous years there has been a substantial increase in the total size of the annual development plan allocations. The PSDP allocation for FY12 has been kept at Rs228.4 billion out of which 75.5 percent have been disbursed. The next fiscal year i.e. FY13 being the election year we expect the same level of disbursements as the government will try to keep a high pace for development projects.

The federal excise duty (FED) has been reduced Rs100 per ton to Rs400 per ton for FY13, against a reduction of Rs200 per ton during FY12. This reduction in FED translates into expected Rs5 per bag relief by the manufacturers in order to augment total dispatches during FY13. As the major manufacturers move towards energy provision through Tyre Derived Fuel (TDF), the move of cutting down the duty on shredded tyres and rubber scrap has given a much needed stimulus to the cement industry which is currently burdened by high energy costs. The allocation of Rs38.5 billion for the construction of small and medium sized dams, canals and improvement of existing irrigation, and continuing work on the Neelum-Jehlum hydel power project is expected to keep the momentum of the industry during FY13.

Commercial Banks

Measures

- Tax rate on dividends from money market and income funds raised from 10% to 25% in FY13 and to 35% in FY14.
- WHT limit increased from Rs.25,000 to Rs.50,000 on cash withdrawals.

Impact Neutral

Upon cash withdrawals of Rs25,000 or above, a withholding tax of 0.2 percent was being charged. The limit has now been increased to Rs.50,000. Banks will not be affected by this move, as we feel these taxes were not seriously affecting the amount of transactions customers did in a day.

Banks' dividend income from money markets and income funds will be taxed at 25 percent previously at 10 percent. This rate will be increased to 35 percent in FY14. These funds were invested mostly in T-Bills and so by investing in these funds banks were giving a tax of only 10 percent as opposed to 35 percent, they would have paid by investing directly in those T-Bills (Interest income from T-Bills were going into the top line for banks and were being considered as normal business income, therefore they were taxed at the corporate tax rate).

In case banks do not shift their investments in money market and income funds to other funds that still have a 10 percent applicable tax rate, then their bottom lines will be affected by 0.04 percent (HBL) -3.6 percent (ABL).

In case banks' decide to shift their investments in money market and income funds to holding T-Bills themselves, the effect on their earnings will be the same as above, only slightly less because they won't have to pay management fees to asset management companies. If banks' do move away from investing in these funds, then they (the open-ended MM and income funds) could see a substantial outflow of funds under management. This negative effect will be greatest for the small funds that are relying on their management companies' related Bank's investment in them.

We, however, feel that banks will continue to invest in these funds as they (the banks) will pay the same rate of tax whether they invest here (in MM and Income funds) or there (directly in T-Bills), and that they would like to pay the management fees for the diversity these funds bring. Also, avoidance of higher taxes isn't incentive enough to move into a different asset class (like shifting to equity funds), due to the vast differences in risk. Moreover, Equity funds almost always have higher management fees.

We feel that the budget is also positive in the sense that contrary to fears, higher tax rate on income from government securities and overall hike in corporate tax rate was not implemented.

Fixed Line Telecommunication

Measures

- Status quo maintained.

Impact Neutral

Once again FED has been abolished on different items. Consumers of telecom products will continue to pay 19.5 percent FED on telecom services. Please note telecom services had a FED of 19.5 percent on them, and not sales tax. As a result, the measure of reduction in sales tax will not affect them.

The government is expecting to raise Rs79 billion from auction of the 3G licence this year. For budget FY11 it had estimated Rs50 billion and for FY12 it had estimated Rs75 billion. We once again doubt that the Government will be able to raise such a high amount, and feel that Rs50 billion is a much more realistic target. Also, we feel that there are chances the auction will not take place again this year.

Automobiles

Measures

- Status quo has been maintained in terms of CKDs, CBUs and used cars.
- Duty on auto and tractor parts have been reduced by 5% to 30% as per the FY13 budget

Impact Neutral to Positive

With decreasing value of the rupee, the 5 percent decrease in duty on auto parts has provided much needed relief to the auto assemblers and consumers. With increasing prices of automobiles the decrease in the duty has provided a cost advantage to the auto assemblers which is expected to be passed on to the consumers in the shape of a price decrease in the cost of vehicles. The auto industry as a whole will be able to benefit from the decrease in duty. The tractor industry will not benefit much from this change as 90 percent of the parts used in tractors are locally made.

Oil Refineries

Measures

- FED on base lube oils and lubricating oils abolished.

Impact Positive

In the current budget, the turnover tax has been reduced from 1 percent to 0.5 percent; however, this will not affect refineries because the applicable rate on them was already 0.5 percent. Moreover, PRL was the only refinery that was getting affected by turnover tax.

Moreover, FED on base lube oils and lubricating oils has been abolished, which will reduce prices of these products. (Base lube oils will get cheaper by Rs7 per liter and lubricating oils will get cheaper by ten percent). We expect demand from consumers to increase slightly which will benefit refineries.

(Contributed by Taurus Securities Ltd,
a subsidiary of National Bank of Pakistan)

Provincial Budgets 2012-13

Highlights

Sindh

- The Sindh provincial government estimates total expenditure for 2012-13 at Rs578 billion.
- Revenue receipts for the year are estimated at Rs570.82 billion, showing a deficit of Rs7.16 billion.
- Development budget is estimated at Rs231 billion.
- This includes Rs181 billion of provincial Annual Development Programme, Rs35.65 billion of foreign project assistance and Rs14.51 billion for other grants.
- The current revenue expenditure is estimated at Rs315.3 billion, and capital expenditure at Rs31.5 billion.
- Receipts from the federal divisible pool have been estimated at Rs314.36 billion, Rs59.25 billion under straight transfers, and province's own receipts, including sales tax on services are estimated at Rs96.63 billion.
- Nearly 70 percent of ADP allocation has been made for completion of on-going projects. This will help complete 700 schemes during 2012-13.
- Some of the major initiatives for the next financial year, include, agriculture credit line for small farmers at 7 percent interest subsidy through Sindh Bank, provision of assistance to farmers for purchase of 15000 tractors, microfinance for enterprise development, through Sindh Technical Education and Vocational Training Authority and Sindh Bank at a total cost of Rs2 billion; establishment of multi-organ transplant center at Sindh Institute of Urology and Transplantation (SUIT), Karachi.
- Rs13.585 billion has been earmarked in the ADP for development of Thar coal.
- Under the Wasela-e-Haq Programme 34,000 families in low income bracket would be provided Rs300,000 interest free loans.
- Quota of women for recruitment in government jobs has been enhanced to 25 percent from the existing 5 percent.
- The Sindh government aims at reviving Karachi Circular Railway, which will be completed by the end of 2016 and will be operational in 2017.
- Allocation for the Sindh police has been increased to strengthen the law enforcement institution.
- The education sector receives an allocation of Rs111.96 billion.
- To strengthen health services, Rs49.52 billion has been allocated for the sector.
- Rs1 billion has been provided for village electrification and Rs1.5 billion for provision of sui gas to towns and villages across the province.

Punjab

- The Punjab provincial government has presented a Rs782.85 billion budget for FY2012-13.
- The size of the Annual Development Programme is proposed at Rs250 billion. Nearly 35 percent of the total ADP allocation has been made available for ongoing schemes, while 65 percent would be for new schemes.
- Current expenditure is proposed at Rs532.8 billion.
- To finance the budget outlay, Rs650.74 billion would accrue through federal transfers, Rs95 billion through provincial tax revenues and Rs35 billion through provincial non-tax receipts.
- The Punjab ADP emphasizes development of social sector with major focus on health, women empowerment, infrastructure development, district development, South Punjab Development Programme, agriculture & livestock sector.
- Rs4 billion has been allocated for the Chief Minister's laptop scheme for students. Around 125,000 laptops will be distributed amongst the students.
- Rs2 billion has been allocated for green tractor scheme for rural youth.
- Rs1 billion has been earmarked for solar tubewells/renewable energy and same amount has been allocated for solar panels.
- The government announced an increase in pay and pension of its employees by 20 percent.
- The government has decided to set up a Punjab revenue authority to collect general sales tax on services (provincial).
- The budget proposes Rs34 billion for implementing pro-poor schemes.
- A sum of Rs10 billion has been allocated for tackling the energy crisis.
- The government is to set up coal fired power stations of upto 500 MW at six locations to give uninterrupted power supply to the industries located in the Industrial Estates.
- The provincial government has announced a 5 percent pay cut in the salary of the Punjab cabinet.
- The government will import 1200 new buses during the next year.
- Less developed areas receive substantial amounts.
- New jobs will be created to benefit the youth of the province and decrease the level of unemployment.

Khyber-Pakhtunkhwa

- The provincial government has presented a Rs303 billion budget for fiscal 2012-13.
- It has earmarked Rs97.4 billion for Annual Development Programme, which includes foreign assistance of Rs23.2 billion. There are 940 projects in the ADP, of which 667 are ongoing and 273 are new. Of the total foreign assistance, the grant portion comprises Rs19.56 billion, whereas loan component is Rs3.69 billion.
- Rs183 billion will be raised through federal tax assignments, and the province will get Rs22.01 billion for its losses because of the war on terror. It will also receive Rs22 billion as straight transfers, Rs9.886 billion as its share from general sales tax on services whereas the province's own receipts are estimated at Rs7.812 billion. Regarding receipts from hydel sector, it would receive Rs6 billion as net hydel profit and Rs25 billion as arrears of net hydel profit.
- Current expenditure outlay is estimated at Rs191.6 billion, while current capital expenditure is budgeted at Rs13.94 billion.
- Of total current expenditure, 43.7 percent is to be transferred to district governments and 23 percent has been allocated for general public service.
- The salary budget of the province is increasing.
- Allocation for health has been increased to Rs10.3 billion.
- Pro-poor welfare schemes/special initiatives will be continued during 2012-13 with an allocation of Rs5.742 billion. These include Pakhtunkhwa Hunermand Rozgar Scheme, Riwaiti Hunermand Scheme, Benazir Health Support Programme, establishment of IT parks, Rokhana Pakhtunkhwa public-private partnership scheme, scholarship scheme for promotion of girls education etc.
- The provincial government focuses on the education sector. An amount of Rs12.18 billion has been allocated.
- Women development has also been emphasised.
- For promotion of tourism Rs685 million has been allocated.
- The existing coverage of clean drinking water and sanitation facilities would be extended in the province. The sector has been allocated Rs3.2 billion.
- The province's water sector receives Rs2.86 billion which will be used for timely completion of ongoing projects.
- Law & order receives higher allocation of Rs23.36 billion.
- Rs1.73 billion allocated for vocational education.

Balochistan

- The provincial government of Balochistan has presented a Rs179.93 billion budget for FY2012-13, against an outlay of Rs164.57 billion last year.
- The current expenditure is budgeted at Rs144.11 billion, while Rs35.81 billion has been allocated for the annual development programme.
- Receipts of the province from the federal as well as it own sources have been gradually growing. For 2012-13, total federal and provincial receipts are budgeted at Rs153.48 billion, which includes Rs114.2 billion from federal divisible pool taxes, Rs16.86 billion as straight transfers, Rs12 billion as grants on services and provincial own receipts of Rs5.21 billion, tax receipts of Rs1.38 billion.
- The provincial tax receipts mainly include urban immovable property tax, land revenue and registration, taxes on professions, trades and callings and capital gain tax.
- Provincial non-tax receipts are budgeted at Rs3.82 billion.
- Pay, allowances, pension and debt servicing are the major heads of current expenditure.
- The provincial government has announced a 20 percent increase in salaries and pension of government employees.
- 6530 new jobs would be created.
- The provincial budget allocates Rs24.5 billion to the education sector, including Rs2 billion from the development budget. The government plans to build 150 new schools.
- Rs9.9 billion will be spent on law & order.
- Solar home electricity system which is aimed at energy conservation receives Rs888 million.
- Rs800 million will be spent completing the Pasni Fish Harbour, a project funded by the government of Japan.
- The provincial government has decided to raise the minimum wage in the province from Rs7000 per month to Rs9000.
- The budget plans to recruit upto 15,000 young people into the provincial government.
- The government will subsidize electricity for agriculture tubewells in the province.
- The government earmarked Rs5.2 billion for agriculture sector and Rs6.71 billion for rural development.

(This was prepared from newspaper reports)

Market Analysis

Market Review – May-June 2012

The market during the period was bearish with strong volumes. Overall, the KSE-100 Index during May to June, 2012 shed 188 points or 1.4 percent to close at 13,801 on average daily turnover of 139.11m shares.

May

The market had a positive start in the month as foreign buying interest was a key factor to the KSE-100 Index surging by 627 points in the first 7 days to close at 14,617 on May 7.

Unfortunately, the positive momentum could not be sustained for the remainder of the month. The KSE-100 Index plunged by 831 point from May 7 to the end of the month to close at 13,786 on May 31. The main reasons for the slide during this period were:

- The falling commodity prices, particularly oil prices,
- Pre-budget jitters and
- Uncertainty over the re-opening of the NATO supply line.

June

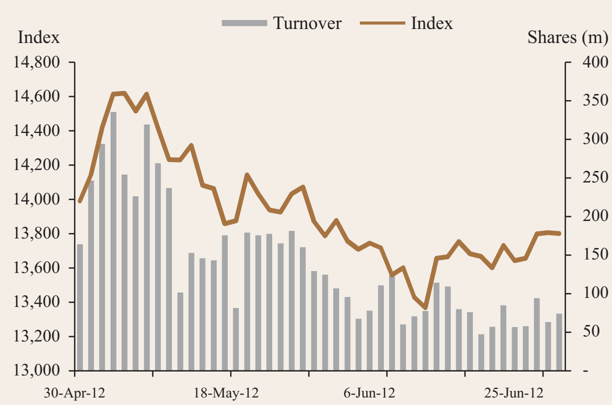
The market had a poor start but staged a recovery in the final two weeks of the month. The volumes were mainly on the downside. During June, the KSE-100 Index gained only 14 points to end the month at 13,801.

During the first two weeks of June, the market continued its slump that began in early May. The KSE-100 Index shed 417 points to close at 13,368 on June 13. The key drivers for this slump were foreign outflow from the market and fears that the SBP would raise the policy rate in the upcoming policy statement on June 8.

The market staged a modest recovery during the final two weeks of June despite the disqualification of Yousuf Raza Gilani as Prime Minister by the Supreme Court on the back of hopes in improvement in Pak-US ties and selective buying interest in banking, cement and chemical stocks. In addition, the SBP decision not to raise the policy rate gave support to the bourses. In a major development, the KSE notified a decision to transfer current benchmark KSE-100 index to a free-float based index (w.e.f Oct. 1) from current market cap-based methodology in order to limit the impact of low liquid stocks.

The market breathed a sigh of relief as a Presidential Ordinance was promulgated to give cover for decisions and actions (such as the FY13 Budget and the CGT relief package included in the budget) taken by Yousuf Raza Gilani from April 26 to June 19. The KSE-100 Index surged by 432 points from June 13 to the end of the month to close at 13,801 on June 29.

KSE-100 Index (May-June 2012)



Regional valuation

The Pakistan market PE at 5.80x is trading at a 50.2 percent discount to the regional average of 11.65x. Based on dividend yield, Pakistan is the most attractive at 7.83 percent as compared to the regional average of 2.94 percent, followed by Taiwan (4.51 percent) and Thailand (3.83 percent).

Regional Valuation Comparison

Country	12m F PEx	12m F Dividend Yield (%)
China	10.33	2.22
Hong Kong	10.70	3.31
India	11.16	1.83
Indonesia	12.14	2.74
Malaysia	13.48	3.43
Pakistan	5.80	7.83
Philippines	13.85	2.23
Singapore	11.33	3.76
South Korea	8.45	1.54
Taiwan	13.92	4.51
Thailand	11.10	3.83

Source: Thomson One Analytics, Date: June 14, 2012

Looking ahead

With another earnings season starting, the focus will return to results and payout of the major companies. However, political developments will likely dominate investor sentiments as many events are happening on the political front such as the NRO implementation case which may lead to the disqualification of another Prime Minister, challenge to the new contempt of court law in the Supreme Court and continued speculation regarding the timing of the next general elections. Macroeconomic performance will also be important in determining the future direction of the market as the situation remains precarious, especially on the fiscal front.

(Contributed by Taurus Securities Ltd, a subsidiary of National Bank of Pakistan)

Book/Report Reviews

Electoral Malpractices during the 2008 Elections in Pakistan
Iffat Humayun Khan
Oxford University Press

This book is a study of Pakistan's elections and the malpractices which beset them. It has provided a detailed account of electoral malpractices beginning from the 1950s when elections were held in the provinces. How elections are manipulated to get the desired results, is the central theme of the book which traces the history of these electoral frauds, with special emphasis on the 2008 elections. The book attempts to address a number of issues like; causes of electoral malpractices, why do authoritarian regimes indulge in electoral malpractices, how these malpractices are capable of undermining the future of democracy in Pakistan etc. It seeks to explain what actually electoral malpractices are — the various techniques of rigging employed, the adverse impact of electoral malpractices on the Pakistani society, judiciary and the parliament, and contains certain guidelines to ensure creditable electoral practices for the future.

The first chapter defines electoral malpractices, how it operates under different types of regimes, causes of electoral malpractices, who are the key manipulators and the various techniques of electoral malpractices.

Chapter 2 provides insights into the origins of electoral malpractices in Pakistan — provincial elections in the 1950s, malpractices during the Ayub regime, during the 1965 presidential election, in the general elections of 1970s, in the 1977 general elections, and under the Zia regime, and so on.

Electoral malpractices during the 2008 elections in Pakistan have been discussed in detail. These encompass, system rigging, pre-poll malpractices, polling day irregularities and post-poll machinations. A chapter is devoted to each aspect. At the end, the author states, 'It can safely be stated that the propensity for manipulation, in all elections throughout Pakistan's history, whether conducted by the military or by civilians, has been strong, hence the political actors become the manipulators of elections. There is a need for sincerity, selflessness, equity, and justice in Pakistan, particularly in those who seek political office.'

Pakistan Energy Outlook 2010-11 to 2025-26
Petroleum Institute of Pakistan

The energy sector in Pakistan is facing serious crisis, which has negatively impacted the social and economic development of the country. While energy demand has increased significantly, supply has failed to match this growth due to policy failures. The growing problems in the energy sector is due to an unrealistic power tariff, high inefficiencies, low payment, recovery among others. Nonpayment of electricity subsidies by the government, default on payments by energy consumers, and build up of payables and receivables within the energy sector has led to the emergence of circular debt.

The Report gives the country's energy needs based on two scenarios. It has identified a set of recommendations 'Blueprints', which if implemented could allow the energy sector in Pakistan to grow and become the engine for the social and economic development of the country. The other scenario is the 'Scramble' approach, a short term approach with limited energy focus, low efficiencies and constrained energy supply.

Under the scramble scenario, Pakistan will face a rapidly growing natural gas deficit, imports of oil products will grow in the absence of new natural gas supplies; share in hydel power in the energy mix will grow gradually due to slow development of new hydro projects; and the power sector in the absence of reforms will continue to face problems leading to growing power outages.

Pakistan Economy – Key Economic Indicators

	Unit	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Output and Prices								
GNP Size (MP)	Rs.bn	6634	7773	8831	10452	13070	15403	18847
GDP Size (FC)	Rs.bn	6123	7158	8235	9921	12110	14066	17107
Income Per Capita	$	724	823	905	1022	1017	1068	1122
Real Growth	(%)							
GNP		8.7	5.6	6.7	3.7	4.0	5.1	2.8
GDP		9.0	5.8	6.8	3.7	1.7	3.8	2.4
Agriculture		6.5	6.3	4.1	1.0	4.0	0.6	1.2
Manufacturing		15.5	8.7	8.3	4.8	-3.6	5.5	3.0
Services Sector		8.5	6.5	7.0	6.0	1.7	2.9	4.1
Prices	(%)							
Consumer Price Inflation		9.3	7.9	7.8	12.0	20.8	11.7	13.9
Wholesale Price Inflation		6.8	10.1	6.9	16.4	18.2	12.6	23.3
Food Inflation CPI		12.5	6.9	10.3	17.6	23.7	12.5	18.0
Non Food Inflation CPI		7.1	8.6	6.0	7.9	18.4	11.1	10.6
Core Inflation†		7.2	7.5	5.9	8.4	17.6	11.0	9.7
GDP Deflator		7.0	10.5	7.7	16.2	20.0	11.9	18.8
Gold Tezabi (Karachi)	Rs./10 grams	8216	10317	12619	16695	22195	29587	37658
Petrol Super	Rs/Ltr	40.74	55.12	56.00	57.83	67.68	67.56	75.70
Kerosene Oil	Rs/Ltr	29.11	36.19	39.09	43.44	66.79	72.65	84.89
Wheat Flour (Avg. Quality)	Rs/Kg	13.28	13.06	13.64	18.07	25.64	28.77	29.56
Savings and Investment	% GDP							
National Savings		17.5	18.2	17.4	13.6	12.5	13.1	13.6
Domestic Savings		15.4	16.3	15.6	11.5	9.8	9.3	9.3
Gross Fixed Investment		17.5	20.5	20.9	20.5	16.6	13.8	11.8
Public Sector		4.3	4.8	5.5	5.4	4.3	3.6	3.3
Private Sector		13.1	15.7	15.4	15.0	12.3	10.2	8.5
Public Finance								
Revenue Receipts (Fed Govt)	% GDP	13.8	14.2	14.9	13.7	13.2	13.8	11.7
Tax Revenue	% GDP	8.9	9.4	9.7	9.9	9.8	10.0	8.9
Total Expenditure	% GDP	17.2	18.5	19.1	18.7	16.5	17.4	14.8
Fiscal Deficit	% GDP	3.3	4.3	4.3	7.6	5.3	6.3	4.0
FBR Tax Collection (Fed Govt)	Rs.bn	590.4	713.5	847.2	1007.2	1161.2	1328.6	1558.0
Direct Taxes	% share	31.0	31.5	39.4	38.4	38.2	39.8	38.7
Indirect Taxes	% share	69.0	68.5	60.6	61.6	61.8	60.2	61.3
Internal Debt Outstanding	Rs.bn	2158	2337	2610	3275	3861	4654	6017
Funded Debt	% Internal Debt	59.8	62.3	64.0	68.8	67.1	68.7	72.5
Unfunded Debt	% Internal Debt	40.1	37.7	36.0	31.2	32.9	31.3	27.5
Monetary Sector								
Growth of Monetary Assets M2	%	19.3	15.2	19.3	15.3	9.6	12.5	16.0
Currency in Circulation	Rs.bn	665.9	740.4	840.2	982.3	1152.2	1295.4	1501.4

† *non-food non-energy*

	Unit	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Credit to Private Sector	Rs.bn	1712	2114	2480	2890	2907	3020	3141
Credit to Public Sector	Rs.bn	752	834	927	1510	2034	2441	3020
Borrowings for Budgetary Support	Rs.bn	647	708	810	1365	1681	2011	2602
Resident Foreign Currency Deposits	Rs.bn	180	196	207	263	280	345	368
Demand Deposits / Money Ratio	%	32.1	31.9	65.0	65.5	62.4	62.2	60.5
Capital Market (KSE)								
Listed Capital	Rs.bn	439	496	631	706	782	910	920[†]
Market Capitalisation	Rs.bn	2068	2801	4019	3778	2121	2732	3217
Listed Companies at KSE	Nos	659	658	658	652	651	652	638[†]
Banking Sector								
Scheduled Banks Deposits[a]	Rs.bn	2428	2817	3373	3812	4138	4693	5489
Scheduled Banks Advances[b]	Rs.bn	1694	2071	2376	2816	3080	3174	3311
Non-Performing Loans All Banks	Rs.bn	177	173	214	314	432	548	579
Lending and Deposit Rates	weighted average							
Deposits	% per annum	1.37	1.96	2.60	4.13	4.44	4.29	4.53
Advances	% per annum	8.81	10.61	11.55	12.49	14.25	13.63	13.46
Open Market Operation	weighted average							
SBP 3-Day Repo[1]	% per annum	9.00	9.00	9.50	12.00	14.00	12.50	14.0
Treasury Bills Yield - 6 Months	% per annum	7.96	8.49	8.90	11.47	14.01	12.59	11.92
KIBOR - 6 Months (Offer)	% per annum	8.46	9.36	10.4	10.5	14.2	12.4	13.4
Pakistan Investment Bonds - 5 yrs	weighted average	7.50	9.65	10.0	10.80	14.33	12.56	14.03
Interbank Call Rates (Overnight)	%	6.10	8.80	8.90	9.90	11.35	11.0	12.41
SBP Export Finance Rate	%	6.50	7.50	6.50	6.50	6.50	8.00	10.0
External Sector								
Exports	$ bn	14.39	16.45	17.00	19.05	17.69	19.29	24.81
Imports	$ bn	20.59	28.58	30.54	39.97	34.82	34.71	40.41
Balance of Trade	$ bn	6.18	12.01	13.40	20.20	16.92	15.18	15.27
Current Account Balance	$ mn	1534	4990	6878	13874	9261	3946	268
Workers' Remittances	$ mn	4168	4600	5494	6451	7811	8906	11201
Foreign Investment in Pakistan	$ mn	1677	3872	6960	5454	3209	2739	1999
Direct	$ mn	1525	3521	5140	5410	3720	2151	1635
Portfolio	$ mn	153	351	1820	44.3	-510	588	365
Debts								
External Debt and Liabilities	$ bn	35.8	37.6	40.5	46.2	52.3	57.4	61.8
Domestic Debt Outstanding	Rs.bn	2158	2337	2610	3275	3861	4654	6017
Internal Debt as % of GDP	%	33.5	30.7	30.1	32.0	30.3	31.4	33.3
National Saving Schemes	Rs.bn	940	936	1004	1094	1361	1585	1820
Total Reserves	$ mn	13338	14354	18890	13436	13971	17921	20941
Gold	$ mn	917	1268	1344	1926	1935	2575	3117
Liquid Fx Reserves	$ mn	12421	13086	17546	11510	12036	15346	17824
Exchange Rate (Average for year)	Rs/US$	59.3576	59.8566	60.6342	62.5465	78.4983	83.8017	85.5017

[†] *July-March* [a] *excludes deposits of scheduled banks* [b] *excludes advances to scheduled banks*
[1] *SBP 3 day repo rate was renamed as SBP reverse repo rate wef August 17, 2009*

Source: Pakistan Economic Survey 2010-11
Annual Report 2010-11, State Bank of Pakistan