January-February 2002

ECONOMIC BULLETIN

Contents

Editor's Corner

Dear readers

While some economic indicators point to improvements in the first half of FY02, there are however, other factors which are impacting growth. Exports have fallen and revenues are falling somewhat short of budget. The government is working on a strategy to broaden the tax base, minimize exemptions, increase the minimum tax limit and introduce an effective mechanism for an efficient tax administration.

The Rupee has appreciated by almost 6% in the post September period and there was an unprecedented increase in liquid foreign exchange reserves, which have crossed US$ 5 billion. This allowed State Bank of Pakistan to continue relaxing its monetary policy by reducing T-bills rates. Exporters benefited as export finance rates were reduced, and banks are slowly but surely reducing their lending rates.

Meanwhile, there was an improvement in external sector, primarily because of a fall in import bill, and an unprecedented current account surplus of $1276 million in the first half of FY02. Most remittances came through banking channels, thereby helping to reduce the current account deficit.

Exports have fallen short by 11.7% against the target of $5.05 billion set by the Trade Policy for the first half of FY02. This was due to a variety of reasons including, a slowdown in economic activity, the appreciation of the Pak Rupee which has worked against the exporters, cancellation of export orders and the imposition of War Risk Surcharge. Even though there appears to be an upward sign in the global economic growth, in all probability, Pakistan may have to revise downward its export target, as it seems unlikely to achieve $10.1 billion target set in the Trade Policy.

Positive structural changes on the external front augur well for the economy. By attaining macroeconomic stability and enforcement of fiscal and monetary discipline, Pakistan was able to successfully complete the Standby Arrangement and negotiated with the IMF for a $1.32 billion Poverty Reduction and Growth Facility.

After the September 11 events, economic sanctions were withdrawn, there was increased foreign assistance inflows and the debt restructuring agreement with the Paris Club was more accommodating than the previous two accords. For the restructured debt of $12.5 billion, Pakistan will only have to pay $7.1 billion. The write off of $1 billion of bilateral debt from the US will also reduce the external debt burden.

On the domestic front, the government was borrowing from the banking system at market determined rates of return and with the increase in rates on National Savings Scheme, the servicing burden of domestic debt rose to unsustainable levels. These rates have since been reduced, resulting in reduced interest expenditure. With large grant like facilities that Pakistan received for budgetary support, the demand for new domestic loans for deficit financing has reduced considerably, which has helped reduce the stock of domestic debt.

The resulting fiscal space would allow the government to increase development expenditures. Any increase in public investment should help the flow of investment from the private sector. In effect the debt relief and a reduced interest expenditure on domestic borrowings would provide a much needed impetus to economic growth.

The drought is continuing to affect agriculture and export through lower output of rice and cotton. In addition the water shortage has also affected output of orchards and minor crops. This would result in higher costs of primary inputs to industry, especially textiles and Pakistan's competitiveness in the international market may be affected resulting in a decline in export earnings.

Besides the build up of substantial exchange reserves, another positive development on the economic scenario is the nearly 3.0% overall growth seen in large scale manufacturing up from 2% in the first half of FY01, indicating some upsurge in demand for manufactured goods.

Despite the CBR having revised its revenue targets twice last year, revenue collections constituted 40.6% of the annual target. The shortfall was due to slowdown in economic activity, lower imports and higher refunds/rebate to exporters. On the expenditure side, the government was able to control its expenditure and these were just 43.1% of the annual budget target for the year.

Any temporary gains should however, not detract us from pursuing reforms vigorously, which are directed at reducing domestic/external debt, generating employment, alleviating poverty and improving governance.

Ayesha Mahmud

Abstract of the Bulletin

Public-Private Partnership – Pakistan's Experience

- In the changed economic environment, the state is no longer the sole provider of infrastructure, social services and other goods. The new global economy gives a greater role to a more dynamic private sector, with the public sector playing the role of a facilitator and regulator.
- In Pakistan, economic policies pursued in the past have at times been tilted towards the public sector, while at other times, the private sector has played a large part in the development process.
- There is a growing realization that it is the partnership between the two which can bring about a meaningful change in the economy.

Euro – Implications of the New Currency

- Euro became the official currency of the 12 eurozone members from January 1, 2002.
- The euro will have implications not only for EU members, but for other countries of the world also.
- Countries would be affected depending upon the trade and financial relations with the euro area, its access to international capital markets or the exchange rate policies of its authorities.

Consumer Banking in Pakistan

- Consumer banking in Pakistan is in its initial stages, with few well developed products or services for its customers.
- Problem of overstaffing, inefficiency, and large non-performing loans of the large nationalised banks has been a major drag in their efforts to introduce innovative products and services. They are however, offering same products for their large clientele.
- Some local private banks and foreign banks are marketing consumer based products and catering to the financial requirements of its customers.

Pakistan's Cement Sector

- Pakistan's cement industry suffers from excess capacity, caused by economic slowdown, expansion in capacity beyond demand, frequent price hike of essential inputs among other factors.
- Efforts are underway for substituting furnace oil with low cost fuels like natural gas and coal.
- The sector's prospects look positive, given the reconstruction efforts in Afghanistan. Locally as increased foreign assistance is channeled to development projects, domestic investment is expected to pick up.

Pakistan's Trade Patterns

- In the last decade, exports from Pakistan have diversified, as the share of manufactured goods have risen and those of primary commodities have fallen.
- However, exports continue to suffer from a narrow base, concentrated markets and low value addition.
- Imports are mainly raw material for consumer goods. The share of capital goods has fallen.
- USA in the major trading partner, followed by the EU members.

Banking and Finance

- Key monetary indicators like deposits, advances, investment, approved foreign exchange and investment in securities showed an increase at the end of February, 2002 over the corresponding period a year earlier.
- Deposits mobilised by the scheduled banks have fallen in recent years.
- Aggressive marketing by private banks have shown larger inflow of deposits in the first half of FY 02.

Agriculture

- Faced with serious drought, major crops have been adversely affected and the overall agricultural sector has suffered.
- Some rice farmers have switched to growing cotton and planting less rice which is a water intensive crop.
- Cotton exported from Pakistan is fetching a lower price than the prevailing international price.
- Sugar beet cultivation which requires less water is being encouraged.

Public-Private Partnership – Pakistan's Experience

The world is changing, and with it our ideas about the state's role in economic and social development. In an earlier era, when the world was emerging from the ravages of World War II and much of the developing world was just gaining independence, the state was accorded a central role to formulate good policies and implement them for the good of society.

Public sector plays pivotal role

Over the last century, the size and scope of government expanded enormously. The pre-World War II expansion was driven by, among other factors, the need to address the heavy toll on economic and social systems brought on by the Great Depression. The post war confidence in government bred demands for it to do more. Industrial economies expanded the welfare state, and much of the developing world embraced state dominated development strategies. The result was a tremendous expansion in the size and reach of government worldwide.

Today there is a renewed focus on the state's role, led by events in the global economy, which have fundamentally changed the environment in which the state operates. The deep transformation taking place in most countries, in order to face the challenges of globalisation, rapid technological changes and the need for improved standards of living mean new and different roles for the government — no longer as the sole provider but as a facilitator and regulator.

The changing role of govern-ment

After decades of the State dominating economic activity, there is a growing recognition that in many countries monopoly public providers of infrastructure, social services and other goods and services are unlikely to do a good job. At the same time, technological and organizational innovations have created new opportunities for competitive private providers in activities hitherto confined to the public sector.

Many governments around the world are relying increasingly on the private sector to foster growth. They are reducing their direct provision of goods and services, while becoming more active in developing market mechanisms, creating a supportive environment and providing safeguards to ensure equitable distribution.

Another positive development is that many of these governments have become aware that coping with the new global economy requires reducing the size of the public sector and giving a greater role to a more dynamic private sector.

Public-private partnership

It may be mentioned that in today's changed economic environment, it is the partnership between the public and the private sector which can exploit economic opportunities and bring benefits to a larger number of people. Both sectors should complement each other in the overall development effort. The role of government in establishing the enabling environment, and that of public and private sector, as active partners in the provision of economic services could have a lasting impact on poverty reduction and raising living standards.

A vibrant private sector can contribute significantly to job creation and increased government revenues. As the private sector expands in the sectors that were traditionally handled by the public sector, the government will have more resources available to finance critically needed public goods, such as basic education, health services and social safety nets.

When we are talking about how governments can contribute to establishing the right environment for private sector led growth, the following points may be mentioned: -

- governments must promote appropriate policies;
- introduce appropriate legal and regulatory framework;
- promote access of the poor.

It is only when the poor have access to the benefits of development in a country, can growth be sustainable and there is progress all round.

- Governments could create investment opportunities for the private sector, mainly by privatizing public enterprises that can be more efficiently run by the private sector. Many public sector corporations represent a drain on government coffers and by privatizing such corporations in a responsible and prudent manner would clearly bring fiscal benefits to governments, allowing them to fund socially relevant, pro-poor programs.

Experience worldwide has shown that besides a stable macroeconomic framework and an efficient institutional environment, private sector led growth many a times faces constraints, which include, a cumbersome tax administration, an inefficient judicial system, scarce skilled labour and poor information flow. Removing these constraints is key to forming stronger partnerships with the private sector.

Public Private Initiatives in Pakistan

Economic policies pursued in Pakistan have had a chequered past. At times it has been the public sector which has provided the goods, while at other times, the private sector has played a large part in the development process.

For instance, in the industrial area, the government played an important positive role by establishing Pakistan Industrial Development Corporation and Pakistan Industrial Credit & Investment Corporation in the 1950s. By providing the critically needed capital, the industrialisation process was initiated. Later the public sector withdrew in favour of the private sector.

Public investment in the 70s

The private sector led growth in industry and the economy through much of the 1960s and 1980s, while the public sector dominated in the 1970s. During the 1970s the manufacturing sector saw a rise in public investment, which was directed largely at the heavy industries of steel, cement, fertilizers and chemicals. While the large scale manufacturing sector performed sluggishly during the period, there was a diversion of private investment to small scale enterprises. Most of the growth and expansion that took place during the 1970s stemmed from small scale industry.

New era of the 90s

The 1990s ushered in a new era for the private sector, with more emphasis on deregulation, privatisation and liberalisation. Fiscal incentives introduced were meant to encourage the flow of private investment, which had been reduced since nationalisation.

Private sector in oil & gas

Private sector has now been involved in areas, which were hitherto the exclusive terrain of the public sector. For instance, in the oil & gas sector, the government is redefining its role and disinvesting its interests in existing ventures. Privatisation of fuel sector entities viz Sui Northern Gas Pipeline Ltd, Sui Southern Gas Pipeline Ltd and Oil & Gas Development Corporation, Pakistan Telecommunications etc is underway.

Changes in the financial sector

Similarly the financial sector has seen an interplay of public/private sectors. The 1950s and 60s saw banks being established and operated by the private sector. Due to malpractices that crept in the banking sector, the Bank Nationalisation Ordinance was promulgated in 1974. Of the four largest banks in Pakistan then, only one was state controlled, while the other three were owned by industrial families. 14 banks were nationalised, of which 13 were merged into five.

Twenty years down the road, two of the banks have been privatised and two of the remaining three are scheduled to be returned to the private sector and more private banks have since been established.

It is generally acknowledged that the process of building partnership between the public and private sector is rendered difficult by the general climate of mistrust and lack of confidence that prevails between the two parties. At times the private sector is seen as being motivated primarily by profit maximization considerations in conflict with the objective of increasing say the outreach of health services to essentially poor un-served populations at relatively low cost. On the other hand, the private sector sees the government as being restricted by bureaucratic red tape which tends to slowdown decisions and retard innovation.

Public-private participation in social sector

Despite good economic growth, Pakistan with its centrally planned, government run delivery systems and history of under-investment in social services, rates below countries with comparable economies in the areas of education, fertility, nutrition and health. Pakistan has now embarked on a national Social Action Program that encourages individual communities to improve social services themselves, with the ultimate aim of bringing the country’s social indicators into line with its high level of economic achievement.

Pakistan is committed to increase national investment in the social services and to promote the idea of smaller, healthier, better educated families. Under the plan, Pakistan will decentralize the delivery of social services; enter into annual agreements with private service providers.

Perhaps the most innovative feature of Pakistan's Social Action Program is its emphasis on participatory development. Through non-governmental organizations and other private institutions, it encourages local people to initiate projects to improve social services within their own community.

Private health sector

In Pakistan, the private health sector is large, as in most developing countries. It is a thriving sector with private spending accounting for almost 70% of all health expenditures. This sector is dominated by private clinics managed by general practitioners (almost 25% in the private sector, the remaining 75% in government facilities). The private sector provides more extensive health services than the public sector, non-governmental organizations (NGOs) are playing a more important role in the population planning and preventive health areas.

There are examples of NGOs providing state of the art curative health facilities setup and operated by trusts and foundations, usually on government land provided at low cost and with customs duty exemptions on machinery and income tax exemptions. Two such large initiatives are the Al-Shifa Trust Hospital in Islamabad and Shaukat Khanum Cancer Hospital in Lahore. In addition, there are 104 hospitals operated by NGOs. NGOs are also playing a more important role in the population planning and preventive health areas.

Mention may be made of the success of public private partnership between the Frontier Medical College (FMC) in Abbottabad and the District Headquarters Hospital in Manshera in the province of NWFP. The private sector partner is the Frontier Medical College, located in Abbottabad, while the partnership of FMC is legally with the government of NWFP, which owns the District Headquarters Hospital in Manshera, the effective partner. The strength of the public sector partner consists primarily of its ability to make available at least a minimum package of medical services to all, including the poor, at relatively low cost.

Partnership in the education sector

In the education sector, it is both the public and private sector which contribute. Even though the public school network is extensive, it cannot meet the demands placed on it. Private schools offer a quality of service which ranges from a level marginally higher than government schools to that comparable to the best available abroad.

There are primary education programs initiated by the USAID, which was later extended by the World Bank, whose objectives are to increase access, equity and efficiency particularly in the more backward areas of the province of Balochistan. Nearly 300 home based schools were established in the coastal district of Balochistan and have been successful in improving access to girls.

The Orangi Pilot Project has established home based schools in Orangi, a squatter settlement in Karachi. There are many instances where education in the country is provided by both public and private sector.

Conclusion

It is not for the public sector alone to do the task, or for that matter the private sector, it is only through an interface of both. The public sector is required to provide the enabling environment through its economic policies and also by investing in the development of the infrastructure. Given such policies and the necessary incentives, it is the private sector which will take up the challenge and perform its due role. One cannot work in isolation of the other. It is their partnership which can bring about a meaningful change in the overall economy and meet today's challenges arising out of a changed economic scenario.

EURO — Implications of the New Currency

Euro arrives

Three years after its birth as a currency — a financial instrument used by banks and traders, but not by ordinary citizens, the Euro became a tangible reality shared by 300 million inhabitants of the 12 eurozone countries from January 1, 2002.

The event marked the final step in European economic and monetary union, a process begun in 1990, as a way to revitalize economic integration and as a further step in the achievement of even closer union in Europe. It reflects a remarkable achievement given the number of countries involved, the size of their economies and population. It also clearly demonstrated the ability of the member countries to meet the Maastricht Treaty stipulated criteria.

The introduction of the Euro has created a huge common currency area, with a weight in world economy that is rivaled only by the US. For the Euro area itself, the new common currency has done away with exchange rate uncertainty and the disruptive impact of exchange rate realignments on intra-European trade.

The euro will have implications not only for the EU member states, but also for other countries in the world. Countries would be affected in different ways, the extent would vary from case to case, depending on factors like the intensity of a country's trade and financial relations with the euro area, its access to international capital markets or the exchange rate policy of its authorities.

Perhaps one of the major routes through which the introduction of the euro will affect economic conditions, would be via these countries international trade relations with the euro area. The introduction of the new currency is expected to bring efficiency gains, for having to deal with only one currency will reduce the cost of converting one currency to another and eliminating exchange rates between European countries, eliminates the risks of unforeseen exchange rate revaluations or devaluations. Before the euro, it was difficult for a European customer to know whether a shirt that he was buying was cheaper in Deutsche mark or the Italian lira. Now with a single currency the pricing has become transparent.

Macroeconomic stability effects, arising both from the elimination of intra-EU exchange rates and from greater discipline in monetary and fiscal policies will give a substantial growth impetus to the countries of the EU. This means an increase in demand for goods and services and hence increase in exports from its trading partners.

As a result, the EU demand for imports from non-EU countries will also be boosted. This will however, depend on the share of the EU as a market for a third country's exports. Market access has been made easier with a single system.

Implications for Pakistan

European Union is the second largest market for Pakistan's exports after the US. In 2000-01, Pakistan's trade with the 12 member eurozone is estimated at around $2.9 billion; where exports are estimated at $1.75 billion and imports at $1.17 billion. Of these 12 euro-members, Pakistan's trade is concentrated with Germany, France, the Netherlands and Italy.

Trading partners of the European Union like Pakistan would gain from a single currency depending on whether the gains from reduced transaction cost, the elimination of exchange rate instability and greater price transparency because of the direct comparability of prices/wages will increase competition across Europe, outweighs the losses of cost of introducing the new currency and possible macroeconomic adjustment costs.

Earlier in January, the European Union had removed 15% tariffs from exports from Pakistan, which should help enlarge exports from the country and directly have a favourable impact on the balance of payments and on forex reserves. The removal of duties was provided to Pakistani exporters under the Generalised System of Preference.

The EU has also increased quotas by 15% on value added goods from Pakistan. Of the total textile exports from Pakistan, 40% is contributed by yarn and fabrics and the remaining is from value added products. Removal of quotas should help provide exporters room to enhance exports.

If these countries show better performance, their demand for goods and services will rise and Pakistan is in a position to take advantage of increasing its trade with the eurozone members. Unlike the US whose market is homogenized, in the euro area are countries like France and Germany whose markets differ to that of say for instance Spain or Portugal. Pakistan can easily tailor its exports to take advantage of these different markets.

Traders — both exporters and importers have a preference for a currency which can easily be bought and sold on financial markets, with low transaction costs, and/or for a currency with a high degree of acceptability for other transactions.

Euro and world trade

The European Commission in a paper *"The Implications of the introduction of the Euro for non-EU countries, July 1998"* has talked about the future use of the euro as an international currency in world trade. In 1995, 24.8% of world exports were expressed in the four main EU currencies participating in the euro area (DM 13.2%, FRF 5.5%, NG 2.8% and ITL 3.3%). By adding some of the remaining EU currencies of the eurozone will raise this figure by a few more percentage points. However, intra-eurozone trade becomes domestic trade after the euro's introduction, and one cannot say that the above ratio will rise purely as a result of the mechanical effect of replacing the existing national currencies by the euro.

The creation of a single currency will bring a reduction of transaction costs and the elimination of exchange rate risk, within the euro area, which together with other elements linked to the creation of EMU, will lead to increased competitiveness of euro area countries. In some cases, trade between the countries of the euro area will replace certain import flows from outside the EU. Also in non-EU countries, some imports from non-euro area countries may be replaced by imports from within the euro area as a result of this higher degree of competitiveness. Over time, this will probably also lead to an increase of the share of the euro in international trade.

In the decade of the 1960s, 70s and early 1980s, the US dollar was the only vehicle currency, while the German mark emerged as a second vehicle currency during the 1980s. The US dollar continues to serve as a global vehicle currency, while the role of the German mark is largely limited to trade between the currencies of EU. (A vehicle currency performs the same function on the foreign exchange market as money on the goods market: instead of exchanging currency *x* directly into currency *y*, currency *x* is exchanged into currency *z*, which is then exchanged into currency *y*). This type of operation is preferred by foreign exchange operators if the sum of the transaction costs of the two transactions through the vehicle currency is lower than the transaction costs of the direct exchange.

Euro as a vehicle currency on foreign exchange markets

The future role of the euro as a vehicle currency will depend on the size of the transaction costs associated with exchanging the euro. The large size of the euro market will likely result in a lower transaction cost and should therefore increase the euro's potential as a vehicle currency as compared to that of the existing national currencies. The euro's potential role as a vehicle currency is expected to be developed gradually.

Euro in private portfolio holdings

With the introduction of the euro, a large single currency financial market has been created. The market is expected to grow and develop, given the large size of the euro area, the elimination of the exchange rate risk between participating countries and the existence of a single monetary policy.

While the combined equity markets of the EU members is relatively small compared to the US market, it is nevertheless expected to grow as investors who had been earlier limited by currency risk to invest in equities in their home markets will now with a single euro denominated market be able to seek investment opportunities across the euro zone.

The new currency is expected to enlarge the euro denominated government securities market. International portfolios will also see some diversification. Statistics show that between 1981 and 1995 European currencies share of the world private portfolio increased from 13% to 37%, while the dollar's share fell from 67% to approximately 40%.

Euro as a reserve currency

The share of the US dollar in official currency reserves declined from 76.1% in 1973 to 63.7% in 1996. During these years the share of the four main EU currencies, pound sterling, Deutsche mark, French franc and Dutch guilder increased from 14.3% to 25.7%, in official reserve holdings. The fact that the euro area is no longer a zone of currency turbulence is already a strong contribution to greater stability in the international monetary system. Given the economic potential of Europe, the euro can develop into a major international reserve currency.

The currency composition of central banks reserve holdings depends on:

- the country's exchange rate arrangement,
- the direction and currency composition of its trade flows and
- the currency denomination of its debt

As mentioned above, the role of the euro as an exchange rate anchor for non-EU countries is expected to gradually increase over time. Also its importance as a reserve asset will gradually increase. As developing countries trade flows with the euro area grows, and also the denomination of these trade flows will increasingly be based on the euro, this may be an incentive for augmenting the share of the euro in their international currency reserves.

As Europe has a large share in total world trade, euros will be needed to pay for the imports and central banks of various countries will be maintaining a certain portion of their reserves in euro.

In Pakistan, the State Bank of Pakistan has to purchase some European currencies to make payments. By maintaining euro as reserve currency, there will be some reduction in the cost of maintaining various currencies as euro will be used for making multi country trade related payment.

Box	*Summary of Main Events* *1*
1951	The six founders — Belgium, France, Germany, Italy, Luxembourg, the Netherlands create the European Coal & Steel Community.
1957	European Economic Community (EEC) created.
1970	Werner report recommends methodology for economic and monetary union and the creation of a single currency.
1972	EEC members agree for launching of monetary union.
1973	Denmark, Ireland and Britain join the EEC.
1979	Creation of the European monetary system and exchange rate mechanism.
1981	Greece joins.
1985	EU Commission President Jacques Delors launches the single market program to remove all remaining obstacles to internal trade by 1993 and setting in motion a process leading to the drafting of the Maastricht Treaty on European Union.
1986	Spain and Portugal join the EEC.
1990	West and East Germany are unified.
1990	Stage one of the single currency process begins in July.
1993	Maastricht treaty on European Union takes effect.
1994	Stage two of EMU begins on January 1, leading to the creation of the European Monetary Institute.
1998	Eleven of the 15 EU countries qualify to participate in the eurozone on the basis of five key criteria requiring convergence and control of interest rates, inflation, public deficits & debt, and the exchange rate; as well as general performance in terms of such maters as integration of market and unit labour costs. The 11 countries are: *Austria, Belgium, Finland, France, Germany, Ireland, Luxembourg, Italy, the Netherlands, Portugal and Spain*. Britain, Greece and Sweden are not included.
1999	Euro becomes the official currency in the eleven participating countries.
2000	Greece becomes the 12th member of the eurozone on January 1.
2001	On December 31 at midnight, euro notes and coins are introduced in the 12 eurozone countres.
2002 Feb 28	The legal tender status of national banks and coins is canceled. This marks the end of the dual circulation period which started on January 1, 2001.

Consumer Banking in Pakistan

Increased competition amongst banks

The banking and financial services sector in Pakistan comprises of the commercial banks and the non-banking financial institutions including Development Financial Institutions (DFIs), Leasing Companies, Modarabas and Investment Banks. They are controlled and regulated by the State Bank of Pakistan. Beginning 1990, the government has introduced various reforms in the financial services sector and enhanced the level of autonomy enjoyed by the central bank. As the number of banks operating in Pakistan increased, competition amongst 42 commercial banks (24 domestic and 18 foreign) has also increased.

Previously all the large five banks were state-owned, but now two (Muslim Commercial Bank and Allied Bank Limited) have been privatized, while National Bank of Pakistan, Habib Bank and United Bank, control more than 50% of the entire banking sector's deposits and advances.

In recent years, the banking sector in general, has shown good progress. Five large banks alongwith small local and foreign banks dominate the banking sector. Inspite of a large branch distribution network and customer base, retail banking is in the initial stages with few value added services for customers, as main focus continues on mobilization of deposits. In Pakistan, currently the products of retail banking are restricted to commercial and personal loans, credit cards and ATMs.

With the privatisation program that began in 1991, banks are facing increasing competition. The banks (particularly privatized, small and foreign) are incorporating innovative approaches to their traditional commercial banking functions. They are moving away from their conventional products of saving and current accounts and are trying to establish niche markets such as in credit cards, travelers cheques, ATMs, house and vehicle loans and repo transactions.

Pakistani banks (particularly the 3NCBs) are still focusing on conventional lending – and much of that is sector-specific, unlike those in the developed countries, whose exposures include real estate and stock market. These banks are engaged predominantly in corporate lending, and in various forms of concessional lending to the trade sector, financing machinery etc. They are the main sources of short and medium term credit for domestic investment.

Emphasis on consumer banking

The three Nationalised Commercial Banks (NCBs) in the public sector are in the process of major restructuring. The problem of overstaffing, inefficiency and large non-performing loans (NPLs) in these banks, has been a major impediment in efforts to introduce innovative products and services. The privatized Muslim Commercial Bank, some domestic private banks (particularly Askari Commercial Bank, Bank Al-Falah and Union Bank) and foreign banks (Citibank and Standard Chartered Bank in particular), despite tough competition with NCBs, have shown substantial progress over the past five years. They are providing better customer services. The foreign banks, in particular, are playing a significant role by incorporating new technologies and providing better quality services.

In the post nuclear period, when people's confidence was at a low ebb because of freezing of foreign currency accounts, some banks introduced lucrative schemes to attract money converted into rupees. These schemes proved successful. Such schemes were however, phased out by December 1999. With the loss of dollar deposits, after the freezing of foreign currency accounts in May 1998, and given the general economic environment, some foreign banks downsized their operations, while some large foreign banks re-positioned their business.

Foreign banks in the lead

Foreign banks in recent years are offering more consumer-oriented packages, which were not available in the past. They are now offering facilities, such as the payment of utility bills, payment of the account holder's children school fees, credit card bills, personal loans, mortgaged and car financing amongst various other schemes. To diversify their lending portfolio these banks have dipped deeper into the domestic market, by entering into alliances with local banks and firms.

Consumer banking originated in the US and Europe in the 1930s and 1940s. Initially large regional and local banks issued proprietary cards and home loans to retail customers. Large US and European banks expanded their consumer banking operations in Asia Pacific in the early 1980s. In early 1990s India, South Asia and Middle East became the focus of consumer banking.

Citibank pioneered the development of consumer banking in Pakistan and in 1993 became the first foreign bank to offer a comprehensive programme for automobile loans and individual mortgages. Today it is offering a wide range of schemes to individuals and small consumers. These include tele-banking, credit cards, auto and home loans and business finance.

ABN Amro, the first foreign bank to enter Pakistan markets in 1948, has over the last 4 years, significantly enhanced its profits in Pakistan, and is now comfortably ranked amongst the top 3 foreign banks in the domestic market. The Bank structured innovative products for clients seeking diverse modes of finance in a highly competitive banking environment. It offers a large range of commercial, retail and investment banking products

The Standard Chartered, competes with Citibank and ABN Amro in the marketing of consumer banking products. It also offers various products to small individual customer. All the three banks have a wide network of ATMs and are providing quality services to a growing consumer base. Their auto loans, home loans and business finance schemes are very much popular. These foreign banks have now entered into utility bills payment business, enabling their clients to pay their utility bills in a more congenial environment.

Private banks competi-ting

Among the privatized banks, Muslim Commercial Bank is catering to the financial requirements of its customers. It is marketing some consumer-based products like credit cards, funds transfer facility via its large ATM network, and providing various savings schemes. It recently launched Pyara Ghar – a housing finance scheme and Car Cash, an auto loan scheme. Askari Commercial Bank amongst the private banks, is aggressively marketing some consumer products like credit cards, phone banking services, car leasing and a growing ATM network facilities.

Among the NCBs, the National Bank of Pakistan is providing various services like, ATMs, Travellers Cheques, payment orders, collection of utility bills, faster transfer of remittances to its 8.5 million clients. With the strength of a large customer base, it is in an advantageous position to cultivate and expand this relationship.

National Bank developing retail banking

The Bank has embarked upon a program to build the infrastructure, and tailor it to meet the requirements of its growing clientele. A new full-fledged Commercial & Retail Banking Group has been set up at the Head Office, where professionals have been hired to develop this function of the Bank. They have devised a new strategy and will soon be coming up as a retail bank in the fraternity of local banks. The new group will be fully IT supported.

Process of delayering begun at the Bank is a shot in the arm, as now the turnaround time will be minimized. Studies are in progress for the lunching of various consumer products such as auto financing, house financing, personal loans, etc. In the past, National Bank issued Master and Visa Cards. Due to lack of infrastructure and related facilities it had to close it. Decisions are being taken prudently, so new products that come to the market are on a sustainable basis.

Schemes offered by UBL

United Bank Limited is also offering products for its customers. It was among the few who had launched a credit card schemes in the sixties. It recently entered into consumer banking in the UAE, with two schemes offering attractive incentives. Tez Raftaar remit and gain, is to promote remittances through the banking channel. The bank's second scheme Personal Loan Assistant (Plan) offers loans against salary. As an incentive, the bank is processing the loan without any fee and is charging reduced interest rates on the loan.

HBL offers schemes

Habib Bank is also providing ATM facility but on a limited scale. Lately it has launched auto loans and house finance facilities to enhance consumer base.

In the field of consumer banking, car leasing has been a success. A House Refinance Window has also been set up at the State Bank of Pakistan. The banks have also been allowed to float TFCs to match housing assets with liabilities.

Consumer banking is so far restricted to major cities like Karachi, Lahore and Islamabad. The consumer banking is tailored to offer a wide array of financial services and facilities to individuals. By raising current purchasing power of the consumers, it increases the demand for goods and services and spurs industrial production. It would also help in documentation of the economy.

Factors constrain-ing growth

Growth of consumer banking is however, constrained by a number of factors. It involves high risk, which local banks are reluctant to take; there is absence of credit culture and the legal framework/regulations are not favourable for lending. Current downward trend in interest rates, opening up of new business avenues, emphasis on housing, small and medium enterprises and micro finance, increased competition and improving economic indicators are likely to help in future consumer banking growth.

Pakistan's Cement Sector

Cement industry consists of 23 plants with an annual production capacity of 16-17 million tonnes. The industry is broadly divided into two distinct geographical regions, north zone and the south zone. The 14 units operating in the north zone have a rated capacity of 12.4 million tons for cement and 11.8 million tons for clinker. The 9 units in the south zone have smaller rated capacities of 4.6 million tons and 4.4 million tons respectively.

Demand – Supply Position

Falling demand

Cement is a basic commodity whose demand is driven by economic activity - infrastructural construction, housing, commercial plazas and is also closely linked to agricultural growth and manufacturing output. Any increase in agricultural growth raises the income level of farmers, who have resources to spend for development purposes.

Statement Showing Rated Capacity & Cement Despatches
From July 2001 to June 2002

North Zone

Sr. No.	*Name of Unit*	*Rated Capacities (in 000)*		*Total Despatches*	*Average Despatches*	*% of Capacity*
		Clinker	*Cement*			
1.	Askari Cement (Wah)	900	945	375.70	46.96	59.63
2.	Askari Cement (Nzp)	600	630	234.40	29.30	55.81
3.	Bestway Cement	990	1039	405.77	50.72	58.55
4.	Cherat Cement Co	750	787	313.10	39.14	59.64
5.	Dandot Cement Ltd	480	504	207.22	25.90	61.67
6.	DG Khan Cement	1650	1733	692.40	86.55	59.94
7.	Fauji Cement Co	900	945	369.55	46.19	58.66
8.	Fecto Cement	600	630	253.80	31.72	60.13
9.	Gharibwal Cement	540	567	223.31	27.91	59.08
10.	Kohat Cement Co	540	567	229.60	28.70	60.73
11.	Lucky Cement Ltd	1200	1260	489.40	61.17	58.26
12.	Maple Leaf Cement	1461	1534	611.83	76.48	59.82
13.	Mustehkum Cement	630	662	-	-	-
14.	Pioneer Cement Ltd	600	630	243.35	30.42	57.94
	Sub Total	**11841**	**12433**	**4649.43**	**581.16**	**59.24**
	South Zone					
15.	AC Rohri Cement	230	242	-	-	-
16.	Attock Cement Pak	720	756	315.88	39.49	62.68
17.	Dadabhoy Cement	450	473	241.49	30.19	76.66
18.	Essa Cement Ltd	450	473	217.34	27.17	69.00
19.	Javedan Cement	600	630	189.86	23.73	45.21
20.	Pakland Cement	480	504	240.58	30.07	71.60
21.	Pakistan Slag Cement	150	158	21.32	2.67	20.30
22.	Thatta Cement	300	315	109.80	13.73	52.29
23.	Zeal Pak Cement	1008	1058	116.20	14.53	16.47
	Sub Total	**4388**	**4607**	**1452.46**	**181.58**	**47.29**
	Grand Total	**16229**	**17040**	**6101.77**	**762.74**	**55.88**
	Despatches from July 00 to January 01			**6827.81**		
	Difference			**(726.04)**		
	Growth %			**(10.63)**		

Source: *Pakistan Cement Manufacturers Association*

Public spending on infrastructure has been badly affected by the government of Pakistan's fiscal crunch, while private sector demand for office space and housing has also floundered, particularly in the commercial capital Karachi. Around 60-70% of the demand for cement originates from the housing sector.

Already in slump, the sector was further hit by the situation emerging after the event of September 11, and the prospect for a turnaround in the construction sector did not happen.

Excess capacity

As against an installed capacity of 17.04 million tons, the operational capacity is slightly less at 16.2 million tons because of the closure of Associated Cement and Mustehkum Cement. As total demand in the country for cement is around 10 million tons, it gives an average capacity utilisation of nearly 62%. Despite the excess supply, additional capacities in the cement sector are in the pipeline. Saadi Cement with a capacity of 1800 tons per day is expected to be operational soon. Additional capacity is also expected from Pakland and AWT is also in the process of capacity expansion.

Large idle capacity has been caused by economic slowdown, expansion in capacity beyond demand potential, heavy taxation and frequent price hikes of furnace oil and electricity.

Cement demand has been affected by the changes in the development budgets, which have been slashed year after year. As such the demand for cement in public sector projects has considerably reduced. With the general slowdown in economic activity, private sector investment has also remained sluggish, resulting in a double squeeze on the cement sector.

Demand to rise

However, there has been a change and the government is undertaking large infrastructural projects which will increase the demand for cement. These projects, include among others, Gomal/Mirani dams, Greater Thal Canal, Right Bank Outfall Drainage project, Quetta Greater Water Supply Scheme, Gawadar Coastal Highway, Karachi Northern Bypass and the Gawadar port. It will take 5-10 years but it will directly or indirectly stimulate demand for cement.

Cost of Production

Taxation

The cement industry pays substantial taxes. Prior to July 00, the industry was paying a fixed central excise duty at Rs.1400/ton on its output, plus a 15% GST. In FY00-01 budget, the government lowered CED by Rs.400 to Rs.1000 per ton, reducing overall effective taxation.

According to estimates, taxes on cement in Pakistan are upto 300 percent higher than other neighbouring countries.

Furnace oil/ electricity prices

Cement units in Pakistan presently rely on furnace oil as fuel, which alone constitutes around 35% of the total cost of production. Cost of fuel had risen to Rs.14350/tonne in 2000 compared to Rs.10000/tonne in 1999. Power tariff, which also constitutes about 30% of the cost of production have also been subject to frequent upward revisions and the increase has been much higher during the last five years. These charges have risen from Rs.1.38/kwh in 1990 to Rs.2.89/kwh in 1996 and further to Rs.4.29/kwh in 2000. With fuel and electricity prices having risen, gross margins of most cement producers are under pressure.

Efforts are underway for substituting furnace oil with low cost fuels like natural gas and coal. The second quarterly report for 2001-02 of the State Bank of Pakistan on the State of Pakistan's Economy cites some factors, which inhibit the cement units from using natural gas. These are:-

- existing gas reserves do not allow the country to burn them at a mass level.
- frequent load shedding during winters causes discontinuity in production process.
- rising gas prices inhibits switching over to gas.

Existing plants like Maple Leaf, Gharibwal and Dandot were using gas, but were facing problems during the peak season. As it was proving unviable they are shifting to coal.

Major cement manufacturing countries are using coal as a kiln-fuel. Pakistan has large reserves of coal, estimated at around 180 million tons and when processed and blended with imported one can produce required heating content.

Use of coal as kiln fuel

By switching to coal, the cost of production of cement is expected to come down, which would subsequently lower the price of cement per bag, which in turn is likely to increase domestic demand. Using coal would lead to a savings of about $69 million foreign exchange annually used on the import of furnace oil. Lower prices would also make exports feasible.

While Pioneer Cement has been the first plant to completely switch over to coal. Units like Lucky, Cherat and DG Khan are planning to switch over to coal. They are already consuming coal at 30-40% of the total energy requirement with the balance being met by furnace oil. The benefits would be reduced cost of energy resulting in lower production costs. Taurus Securities Ltd, says " the investments for coal conversion have ranged from Rs.250-Rs.300 million. The benefit of using coal instead of furnace oil comes to Rs.400-500/ton.

Cartel Formation

The cement industry has been operating as an informal cartel since October 98, which keeps cement prices firm through regulated production. The cartel allocates each manufacturer a sales quota. The quota is expressed as a percent of rated capacity with the percentage being equal to the ratio of total cement demand to total installed capacity. Early October 2000, this arrangement collapsed due to several reasons, the primary factor behind the breakdown of the cartel was sales tax exemption given to some units, thereby allowing an advantage to a few. Secondly, the cost differential between plants who use oil fired kilns and those cement manufactures who use natural gas to fire their kilns resulted in cost advantage for some units leading to a price war.

As a result, the price of cement declined from Rs.230-Rs240/bag in September 00 to Rs.175-Rs.180/ bag in November 00. When cement prices were falling, the price of furnace oil after having peaked in mid November 00, followed a gradual declining trend. Cement prices also stabilized at Rs.185/bag. The cartel came back into force in late February 01 and currently holds strong. Manufactures agreed to raise the price of cement to Rs.235-Rs.240/ bag.

Prospects of the Sector

While cement demand remained flat last year, there are positive triggers both domestically and foreign which should help revive demand in 2002. Government infrastructure spending is expected to pick up, as increased foreign assistance is channeled to development projects. Moreover, with improving prospects of multilateral sponsored development activity in Afghanistan, interest is likely to return to the sector.

A part of the financial assistance received by Afghanistan would be spent on reconstruction, which would raise the demand for cement. Invest Capital Securities Ltd in a recent study expects 15% of the aid received or $675 million to be spent on cement in the next five years. Pakistan cement manufactures are expected to gain a foothold in the Afghan cement market with around one-third of the total share (0.7-1.0 million tons).

Conservative estimates however, put cement demand in Afghanistan at 1 million tons, with Pakistan's share at about 35-40%. Pakistan is already sending cement to border cities. Of Pakistan's share, 40% would be contributed by Cherat.

The units situated in the north zone are expected to benefit because of their close proximity to cities of Kabul, Jalalabad and adjoining areas, while Lucky and DG Khan are catering to the Kandhar market. While export opportunities are there, much depends on how soon the conditions return to normal in Afghanistan. Another opportunity for the sector is the switch to coal from furnace oil, which would reduce the fuel expenses. The sector needs to see its costs for only then can it become cost efficient.

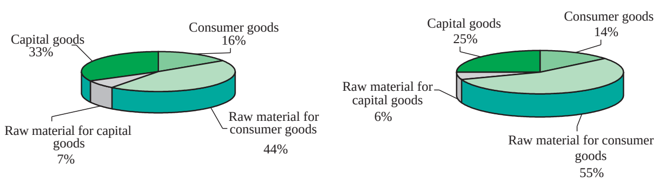
Pakistan's Trade Pattern

Pakistan trade pattern, both in terms of items exported/imported and country/region has shown some change in the last decade. However, exports receipts continue to be vulnerable on account of the narrow base, concentrated markets and low value addition.

More than half the imports are accounted by raw material for consumer goods. Share of raw material for capital goods has stagnated at around 5%, whereas capital goods (in total imports) is showing a declining trend falling to 25% in FY01 from nearly 33% in FY91. Poor investment climate in the country has been responsible for a decline in imports of capital goods and industrial raw material.

Economic Classification of Imports (share in %)

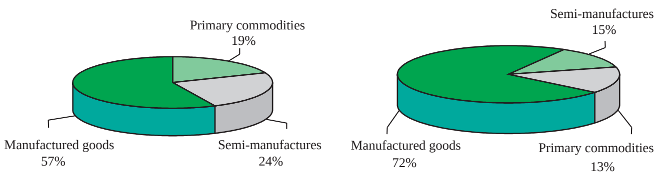
1990-91 **2000-01**



Meanwhile, economic classification of exports reveals a substantial increase in the export of manufactured goods, which have risen from 57% in FY91 to 72.4% in FY01. Semi-manufactured goods which constituted 23.6% of total exports in FY91, have come down to 15% in FY01. Similarly the share of primary commodities has also come down from 18.7% to 12.6% in the same period.

Economic Classification of Exports (share in %)

1990-91 **2000-01**



Over the years, Pakistan's export receipts have been vulnerable on account of narrow base. As cotton & textile manufacturing account for the major share of the revenue, any adverse changes to the cotton crop domestically has a bearing on trade.

Textile products which account for about 63% of total revenues, has seen a qualitative change in favour of high value added items. Value added items, now account for 55% of total cotton and textile manufactures. More specifically, marked improvements were recorded in towels, synthetic textiles, readymade garments and bedwear last year.

Rice continues to be the second highest foreign exchange earner after textiles. Last year there was some fall in its export earnings despite an increase in volume, for the share of basmati came down, resulting in a substantial loss of foreign exchange. Falling international prices of rice, quality concerns and lack of proper marketing were also responsible for the decline.

Export of non-traditional items, like carpets and rugs, petroleum products, cutlery, footwear, manufactured onyx items have shown an increase.

Major Exports

(% Share)

	2000-01	*1990-91*
Cotton & Textile Manufactures	64.4	56.4
Raw Cotton	1.5	6.9
Textile Manufactures	62.9	30.12
Cotton yarn & thread	11.7	19.3
Cotton fabrics	11.2	11.0
Hosiery (Knitwear)	9.9	5.4
Readymade garments	9.0	8.0
Synthetic textiles	6.0	5.6
Rice	5.7	5.7
Leather & manufactures	7.2	4.5
Carpets & Rugs	3.1	3.6
Fish & fish preparations	1.5	1.9
Sports goods	2.9	2.2
Surgical instruments	1.3	1.4

Source: State Bank of Pakistan

The pattern of imports shows continued high imports of petroleum, its products, machinery, especially textile & electrical machinery, plastic material, medicinal products and fertilizer. There has been a decline in the import of fertilizer, on account of an increase in domestic production of DAP following the commissioning of Fauji Jordan's fertilizer plant.

The share of machinery group in total imports has come down in the last decade. However, there has been a steady increase in the import of textile machinery, in the last five years a reflection of the continued BMR drive that has been going on. Other machinery imports has also increased on account of incentives given to private investment in the power generation sector.

Major Imports

(% Share)

	2000-01	*1990-91*
Tea	1.9	2.2
Edible Oil	3.0	5.3
Sugar	3.7	2.1
Petroleum & products	31.3	22.1
Machinery	15.3	20.5
Fertilizer	1.6	3.5
Plastic material	3.3	-
Medicinal products	2.2	2.6
Iron & steel	2.6	3.4
Transport equipment	4.0	6.7

Source: State Bank of Pakistan

In terms of export markets,USA continues to dominate, followed by UK, Hongkong,Germany and the UAE. The share of the US in total exports has increased over the last decade from 10.8% in FY 91 to 24.4% in FY 01. Exports to the EU countries have decreased over the years. The table below shows falls in the share of exports to France, Italy, UK, and Germany among others.

Noteable increase has been recorded in exports to the UAE, which mainly imports rice, cotton, fabrics, cloth, yarn, poultry products, and vegetables among other items from Pakistan. There has also been some rise in exports to Kuwait from a negligible amount in 1990-91 when because of the Gulf crisis there was an embargo on trade with Kuwait and Iraq.

Exports to Japan have fallen reflecting the economic slowdown in the country and the fact that their textile manufactures moved to lower wage countries in south east Asia.

Pakistan is making efforts to diversify into new export markets of Eastern Europe, which includes the central Asian States of Kazakhstan, Uzbekistan, and Russian Federation among others. Exports to Afghanistan have risen in FY91 from a share of a mere 0.05% to 1.5% in FY 01.

As far as imports are concerned, UAE, Saudi Arabia and Kuwait account for 33% of the total imports, which are mainly petroleum crude and products. Edible oil is mainly imported from Malaysia and today it accounts for 4% of the imports. There has been some diversification as the share of other Asian countries has increased.

Direction of Trade

(% Share)

	2000-01		*1990-91*	
	Exports	*Imports*	*Exports*	*Imports*
Canada	2.0	0.8	1.7	-
USA	24.4	5.3	10.8	11.8
France	2.9	1.4	3.8	3.0
Italy	2.5	1.7	3.7	3.5
UK	6.3	3.3	7.3	5.0
Germany	5.4	3.6	8.5	7.3
Netherlands	2.5	1.6	2.0	-
Japan	2.1	5.4	8.3	13.0
Hongkong	5.5	0.6	6.0	-
Singapore	0.5	3.0	2.2	3.2
China	3.3	4.9	1.0	5.1
South Korea	3.0	3.3	NA	-
Malaysia	0.6	4.0	0.5	4.0
Iran	0.3	3.5	1.6	2.4
Kuwait	0.5	9.0	-	0.7
UAE	6.8	4.0	3.3	-
Saudi Arabia	3.0	11.7	3.6	6.3

Source: State Bank of Pakistan

Banking and Finance

Key Monetary Indicators

(Rs. Bn)

	Feb 21, 2002	Feb 23, 2001
Scheduled Banks Deposits	1366.0	1210.9
Scheduled Banks Advances	906.2	856.0
Scheduled Banks Investment in Securities & Shares	362.8	257.0
Notes in Circulation	473.6	402.4
Approved Foreign Exchange (Incl. Balances held outside Pakistan in approved foreign exchange)	227.3	62.8

Source: State Bank of Pakistan

Rise in bank deposits

In the month ended February 21, 2002 scheduled banks deposits rose by 12.8% to Rs.1366.0 billion over a year earlier figure of Rs.1210.9 billion.

Increase in advances

Scheduled banks advances showed an increase of 5.9% rising to Rs.906.2 billion over preceding year's corresponding figure of Rs.856.0 billion.

Investment in securities increase

Scheduled banks investment in central government securities, treasury bills and other approved securities rose by 41% to Rs.362.8 billion at end February 2002 over a year earlier figure of Rs.257 billion.

The State Bank of Pakistan signalled that the stance on monetary policy would not be eased further and kept the cut offs on T-bills unchanged.

The State Bank had started easing its monetary policy since the start of the fiscal year 2001-02 in July to inflate the sagging economy. Between July 2001-January 2002, the discount rate has been lowered by 5% from 14% to 9%. Meanwhile, the weighted average yield on six-month T-bills has fallen by 6.2%.

Notes in circulation rises

Notes in circulation stood at Rs.473.6 billion at end February 2002, a 17.7% rise over previous year's corresponding figure of Rs.402.4 billion.

Approved foreign exchange shows gains

Pakistan's approved foreign exchange (incl. balances held outside Pakistan in approved foreign exchange) has shown a three and a half-fold increase to Rs.227.3 billion on February 21, 2002, against preceding year's corresponding figure of Rs.62.8 billion.

Deposit Mobilization

Deposits of Banks (Flows) (Rs. Bn)

	1998	1999	2000	First Half 01	First Half 02
Nationalised Commercial banks	58.22	43.02	38.854	(-)10.1	38.9
Privatised banks	13.48	22.333	7.012	5.1	2.2
Specialised banks	(-)2.73	4.157	1.014	(-)2.6	2.0
Private banks	16.26	3.068	33.314	23.6	26.5
Foreign banks	(-)8.48	(-)29.887	4.307	8.7	1.3
All banks	76.75	42.691	84.501	24.8	70.9

Source: State Bank of Pakistan

Deposits mobilized by the banks have fallen considerably after 1997, as deposits to GDP ratio fell from 42.4% in 1997 to 38.5% in 2000. Foreign banks have been the most affected as a result of foreign currency account freeze. They witnessed an erosion of nearly Rs.30 billion in 1999. However, they have since been able to successfully turn it around to show a deposit build-up.

Deposits mobilised by the nationalised commercial banks (NCBs) dropped, after closure of their successful Rupee deposit schemes linked through lottery prizes. Despite this, they still maintain a large share of the market. Aggressive marketing by private domestic banks in mobilizing more deposits is clearly reflected in their growth going up from only 1.9% in 1999 to 21.7% in 2000.

More recent statistics show that deposits of the banking sector grew by Rs.70.9 billion in the first half of FY02 against Rs.24.8 billion in the same period last year. The increase can be attributable to money being remitted through banking channels, and the low premium between kerb and interbank rate was also an inducement to use the official channels.

The money coming in through Hajj Sponsorship Scheme, helped replenish the deposit base, especially of the NCBs. Their large branch network and focus on rupee banking and for the fact that they are considered safer with explicit government guarantee saw an increase in deposits.

Agriculture

Pakistan has suffered from severe drought from 1998 until mid-2001. Drought has turned million of hectares of cultivable land in the southern provinces of Sindh and Balochistan into parched wasteland, forcing thousands of people to relocate. The resulting decline in agricultural production has had a significant impact on Pakistan's economy. Last season's severe drought, adversely affected agricultural growth, which went into negative 2.5% against the targeted growth of 3.9% and previous year's positive 6.1%. Major crops like rice, wheat and sugarcane not only missed their respective targets but were lower over preceding year's output. The sector, still reeling from three years of drought, faces another severe water shortage this season, as prospects for good, and above normal rainfalls are bleak.

Water shortage during March

The period from October to December last year had been drier than usual. The winter rainy period from January to March, when most of northern and catchment areas get rainfall and snowfall, received 10-20% below normal rains. The overall shortage of irrigation water is projected at around 60%. With water levels at Mangla and Tarbela dams the main sources of water for irrigation and hydroelectric power already below normal, the sector faces severe drought.

During the last monsoon, although Tarbela reached its full capacity, Mangla remained about six metres below capacity. Latest reports reveal water at Tarbela Dam, the largest reservoir, has already reached dead levels. The Punjab Irrigation Department fears massive water shortage during March would severely affect supply of canal water for irrigation purposes.

Wheat

Drought affecting wheat output

Below than normal rainfalls and extremely dry weather this season further intensified shortage of irrigation water and drought conditions in Punjab and Sindh, taking a heavy toll on the standing wheat crop during the current rabi season. While the growers have managed to bring 0.8% larger area under the crop its fate hangs on the availability of irrigation water during crop germination and grain formation stage.

Punjab contributes nearly 80% to the total wheat production, while the rest is shared by Sindh(13%), NWFP and Balochistan(7%). Punjab is currently facing 73% irrigation water shortage. while Sindh fears, the water situation has worsened since January due to persistent dry weather. If present conditions prevail, growers fear 50% shortfall in production this season.

While it is early to predict about the size of this season's crop, given the irrigation water shortage, production could fall short by between 1-2 million tonnes against the target of 20 million tonnes.

Sufficient stocks available

To meet domestic demand estimated at 20 million tonnes, the country has an estimated 5.7 million tonnes in stock which should help cover any shortfall. The government also plans to export one million tonnes of wheat this season against 0.7 million tonnes exported last season. It is however, facing some difficulty in fetching a good price.

Global trade expand-ing

Global wheat trade in 2001-02 is projected at 107.6 million tones. Lower production in the United States, EU and South Asia will be more than offset by larger crops in Australia, Argentina and Eastern Europe. Though importing less, Brazil will likely remain the world's largest wheat importer, with Iran a close second due to continued drought.

Some major wheat exporters faced with lower wheat production, have seen a fall in shipments. Losses in wheat sales from major exporters are expected to be more than compensated by shipments from a number of smaller exporters, including India and Pakistan.

Rice

Rice product-ion lower

Estimates of 2001-02 crop released by the Ministry of Agriculture reveals lower plantation of rice, which has been cultivated at over 2 million tonnes, down nearly 16% against the previous season's crop and 4.8% below the sowing target for this season. Lower than normal snowfall and persistent shortage of irrigation water has adversely affected rice production, inducing farmers to plant less of high yielding rice varieties.

Production estimates have also been scaled down on account of irrigation water shortage. It is now being placed at 3.74 million tonnes, 11% less than the revised production target of 4.2 million tonnes and 22% lower than the previous season's crop.

Despite the reduced size of this season's crop, there is an exportable surplus of 1.44 million tonnes, for annual domestic consumption is estimated at 2.3 million tonnes. During the first eight months of the current year, rice exports have reportedly declined by 26.5%, attributable to shortage of Irri-6 and basmati in the local market and appreciation of Pak rupee.

Export market under pressure

The rice export business has been affected by; war risk premium and the depressed prices prevailing in the world market. India and Thailand are offering cheap rice making it difficult for Pakistani exporters to compete. The situation for Pakistani exporters is likely to deteriorate further as Vietnam enters in the export market in the next two months.

Presently Indian government is providing huge subsidy to its rice exporters. India and Thailand are selling rice at a price $15 cheaper than Pakistan. India is quoting a price of $130-132 per tonne for Irri-6 variety compared to Pakistan's $150-152 per tonne. Burma and Thailand are charging $124 per tonne for the same variety.

While global rice production for 2001-02 is projected to be slightly 1% lower at 392.2 million tonnes (milled basis), over a year earlier, global consumption is projected at a record 403.7 million tonnes, reducing global stock projected at 126 million tonnes by 8%. Global rice trade for 2002 is projected at 22.5 million tonnes (milled basis), 1.7 million tonnes below a year earlier.

The decline in global trade is primarily due to weaker imports from Nigeria, the Philippines, Cote d'Ivoire, North Korea and the United States. Among the major exporters, Thailand, Pakistan and China are projected to export less rice in 2002, while India, Vietnam and the United States are projected to expand exports.

Cotton

Uncertainty still persist about the 2001-02 crop size due to severe irrigation water shortage and the discovery of a new virus Bura Cotton. Reported attack of white fly, spotted and American bollworms in Punjab and jassid in Sindh has affected the crop. However any large-scale damage has not been reported so far.

Larger area under cotton plantation

Growers have brought larger area under the current crop, sown at over 3.1 million hectares, about 7% above last season's crop and 19% higher than the targeted area. Increase in sown area has been reported in Punjab, whereas in Sindh it has remained unchanged, and declined in Balochistan.

The size of the crop varies from 9.1-10.5 million bales. The Pakistan Cotton Ginners Association has reported arrival of 9.62 million bales of phutti by end February, 2.2% less than the 9.84 million bales reported in the corresponding period last year and 8.4% below the anticipated production of 10.5 million bales for the whole season. Sindh severely hit by drought has shown significant progress, where phutti arrival of 2.26 million bales is close to the estimated production of 2.3 million bales. However, Punjab with reported arrival of 7.4 million bales, is facing a shortfall of 8.6% against the anticipated production of 8.1 million bales.

Surplus cotton available

Increase in cotton output last season has created a surplus in the local market in the absence of foreign buyers and a drop in consumption by the textile mills, putting downward pressure on prices. The ginners are faced with rising unsold stocks of over 1.7 million bales. The textile mills have reportedly lifted nearly 7.7 million bales, while the Trading Corporation of Pakistan has contracted 0.32 million bales, of which only 0.15 million bales have so far been delivered by the ginners. Private exporters have purchased 60.2 thousand bales, while 0.75 million bales have also been imported.

The entry of Trading Corporation of Pakistan in the cotton market has brought some stability to prices. In the local market, prices have improved from Rs. 1250 to Rs. 1600 per maund. The Trading Corporation of Pakistan has been given a procurement target of 1 million bales at Rs. 1855 per maund. However, export process is slow and so far only 58 thousand bales have been exported. Cotton exported from Pakistan is fetching 38 cents per lb, while prevailing international prices are 43 cents, making exports unattractive. Pakistan is facing tough competition from Egypt and China, who have surplus cotton.

Competitive prices

The United States Department of Agriculture (USDA) latest cotton forecasts for 2001-02 indicate record world output with world consumption slightly below the previous year. With world production expected to increase by more than 5 million bales in 2001-02, stocks are expected to equal 48% of total consumption in 2001-02.

US cotton prices are the most competitive in the world. US exports are projected to reach close to 2.2 million tonnes in 2001-02, 48% more than last season, boosting the US export market share from 26% to 35% of the world total. Historically low prices will reduce production and stimulate consumption in 2002-03.

Sugarcane

Drought affects sugarcane

Pakistan is amongst the major cane producing countries of the world. It ranks fifth in cane acreage and production and almost 15th in sugar production. Sugarcane is grown on an area of more or less one million hectares. Of the total area cultivated, Punjab has a share of 62%, Sindh 26% and NWFP 16%. The national average cane yield at 47 tonnes is far below the existing potential. In respect of cane yield, Sindh is the leading province followed by NWFP and Punjab.

According to a latest report for the 2001-02 crop, growers have sown sugarcane at over 1.04 million hectares, 8.3% higher than the previous season's acreage and nearly 21% larger than the targeted 0.860 million hectares. Production at 49.0 million tonnes has exceeded the target by 28.6% and is 12.4% more than last season's. It is however, feared that current water shortage may adversely affect sowing of the new crop, and Punjab may see 10% decrease in area sown in canal irrigated areas

Sugar beet cultivation

Meanwhile, the government has planned to enhance sugar production by promoting sugarbeet cultivation as it requires less water for irrigation and is suitable for cultivation given the prevailing dry weather condition Being low delta crop it takes 4 to 5 months to grow and mature. Moreover, the average recovery of sugarbeet is much higher than that of sugarcane. If beetroot is farmed alongside sugarcane in September, it will provide a bumper harvest and ensure increased sugar production in the country.

With sugar-beet crop, the mills processing can continue in the months of April, May and June. If the experiment with the sowing of sugar-beet in Sindh proves successful and economically feasible then the big sugar mills would also bring about amendments in their plants to process sugar-beet for the production of sugar.

Key Indicators of Developing Asian Countries

	Population Mn 2000	Population in poverty [a] % 1999	Adult Literacy Rate [c] % 1999		Persons Per Physician 1999	Per Capita GNP US$ 1999	International reserves to import ratio Months 2000	Total External Debt $mn 1999	Total External Debt / GNP % 1999	Foreign direct Investment $ Mn 1999	Fiscal Balance % of GDP 2000
			Female	Male							
Afghanistan	22.7	-	20	50	7144[d]	-	-	-	-	-	-
Bangladesh	130.2	44.7	43	59	4102[e]	370	2.2	17.5	37.1	178.6	6.2
India	1002.1	26.1	44	68	1916[e]	440	7.9	94.4	21.3	2168.6	0.2
Indonesia	210.5	23.4	81	91	6195[f]	600	9.2	150.1	113.3	(-)2745.0	(-)1.2
Malaysia	23.3	8.1b	83	91	1465	3390	4.6	45.9	62.5	1552.9	(-)5.8
Nepal	22.9	42.0	28	62	25001	220	0.3	2.9	57.6	4.4	(-)6.5
Pakistan	137.5	32.2	32	57	1544	470	2.6	34.3	58.3	530.0	(-)6.5
Philippines	78.4	40.0	95	95	9689[g]	1050	5.9	52.0	64.8	573.0	(-)4.2
Thailand	62.4	12.9	93	97	3670[f]	2010	7.0	96.3	79.9	6213.0	2.2
Srilanka	19.4	26.7	89	94	3132[e]	820	2.0	9.5	60.3	177.1	(-)9.9

Source: Key Indicators 2001, Asian Development Bank

[a] Propotion of the population falling below the poverty line (in each country) to total population
[a] Refers to percentage of poor households.
[c] Adult literacy rate refers to population of 15 years old and over.
[d] Refers to 1993
[e] Refers to 1998
[f] Refers to 1997
[g] Refers to 1995

Key Economic Indicators

Economy Size & Growth		1997-98	1998-99	1999-00	2000-01P
GNP - Market Prices	Rs bn	2653.3	2912.8	3138.1	3411.3
GDP - Market Prices	Rs bn	2677.7	2938.4	3182.8	3472.1
Per Capita Income	Market Prices Rs	20415	21899	23073	24528
	Market Prices US $	473	438	446	429
Growth					
GDP	%	3.50	4.18	3.89	2.55
Agriculture	%	4.52	1.95	6.14	-2.49
Manufacturing	%	6.93	4.07	1.42	7.05
Services	%	1.64	4.99	4.79	4.38
Rate of Inflation	%				
Consumer Price Index		7.8	5.7	3.6	4.4
GDP Deflator		7.7	6.0	3.1	5.4
Balance of Payments	$ mn				
Exports (f.o.b.)		8434	7528	8190	8925
Imports (f.o.b.)		10301	9613	9602	10195
Trade Balance		-1867	-2085	-1412	-1269
Services Account (Net)		-3264	-2618	-2794	-3137
Private Transfers (Net)		3210	2274	3063	3898
Current Account Balance		-1701	-1856	-217	331
Fiscal Balance	% of GDP				
Total Revenue (Net)		16.0	15.9	17.0	16.3
Total Expenditure		23.7	22.0	23.4	21.7
Overall Deficit		7.7	6.1	6.4	5.3
Domestic & Foreign Debt					
Domestic Debt	Rs bn	1176.2	1375.9	1559.9	1708.5
As % GDP		43.9	46.8	49.0	49.2
Total External Debt[a]	$ bn	32.1	32.9	34.3	34.7
As % GDP		51.7	56.1	55.8	58.4
External Debt Servicing	$ bn	4.67	2.66	2.98	3.33
Investment & Savings	% of GNP				
Gross Investment		17.9	15.7	15.8	14.9
Fixed Investment		15.2	14.1	14.2	13.3
National Savings		14.8	11.8	13.9	12.9
Domestic Savings	% of GNP	16.0	12.9	15.4	14.5
Foreign Investment	$ mn	822.6	499.6	543.4	182.0
Portfolio		221.3	27.3	73.5	-140.4
Direct		601.3	472.3	469.9	322.4
Monetary Aggregates	%				
M1		8.3	33.9	14.9	3.1
M2		14.5	6.2	9.4	8.9
Interest Rates (Weighted Average)	%				
Deposits*		8.38	7.96	6.62	6.58
Advances		15.64	14.80	13.52	13.61
Gold & Foreign Exchange Reserves	$ mn	1737	2371	2150	2666
Exchange Rate+	Rs./$				
Official Rate		46.23	51.60	52.16	64.40
Open Market Rate		54.20	54.40	54.82	66.70

P Provisional
a Excludes foreign exchange liabilities
* PLS & Interest bearing
+ End-June Buying Rate

Source: Annual Report 2000-01, State Bank of Pakistan

NBP Performance at a Glance

(Rs. Bn)

Items	1996	1997	1998	1999	2000
Income	28.2	34.2	34.5	35.3	33.7
Expenditure	29.5	33.2	32.4	34.8	32.7
Pre-Tax Profit/(Loss)	(1.26)	0.995	2.14	0.52	1.03
Total Assets	274.1	310.6	325.9	350.4	370.7
Deposits	235.9	254.9	273.4	294.8	316.5
Advances	85.9	105.6	109.5	122.6	140.3
Investments	108.2	109.5	102.9	91.5	80.4
Number of Branches	1555	1445	1434	1431	1428
Number of Employees	23730	18096	15785	15541	15351