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Editor's Corner

Dear readers

Since July 2001, the State Bank of Pakistan is pursuing an easy monetary policy. Interest rate structure has been rationalised; Discount rate reduction has been accompanied with commercial banks reducing their lending rate. Export refinance rate, which is linked with the yield on 6-month treasury bills has fallen. Simultaneously, the Government has reduced the returns on the National Saving Schemes, and the profit rates on Defence Saving Certificates have been linked to the respective maturity yields on Pakistan Investment Bonds.

The higher profit rates offered on National Saving Schemes (NSS), had attracted in its fold, a number of investors both from the government and the private sector. While they had secured a relatively safe future for themselves and their families, these high profit rates had raised the debt servicing burden of domestic debt to unsustainable levels and had begun to have distortionary implications for monetary policy in the last 2-3 years as inflationary pressures eased.

In the early 1980s, the government had started paying high nominal interest rates on NSS, while inflation was still relatively low. During this period, its impact on government interest payments was, however, dampened because borrowing through NSS was small and the bulk of this borrowing was in the form of zero coupon five or ten year certificates, the interest on which was recorded when the certificates were encashed. It was in the late 1980s and early 1990s, when interest payments on domestic debt increased manifold and the average nominal interest rates also rose. Inflation accelerated between 1990-96, and wiped out the effect of higher nominal interest rates, so that average real interest on government domestic debt fell.

In more recent years, as inflation dropped and nominal interest rates stayed high, cost of domestic borrowings jumped. Even though the returns paid on NSS have been reduced in the last three years, the average interest paid on these schemes will remain high for some years because of the time lags in the redemption of outstanding stock of such certificates.

From the government's perspective, interest rate reduction on NSS would help in lowering of interest payment on domestic borrowing and consequently reduce the growing debt burden. Unfunded debt largely comprising of instruments offered by Central Directorate of National Savings, has grown and now constitute 21% of GDP. This is largely on account of higher profit rate relative to other government debt instruments, despite the absence of risk factors.

Reduced profits on NSS could adversely affect household savings and further weaken the poor savings performance of the country. The small investor, who has been left in the lurch, may continue to persist with these schemes and get used to lower returns, given the absence of alternate secured investment avenues. With the capital market not yet fully developed, lack of knowledge on the part of investor to productively utilize their resources in the limited choices available only makes things more difficult for the small investor.

In Pakistan, problems are compounded because no mechanisms are available for protecting individuals from inadvertent reduction in their incomes. In many countries, programmes exist which allow for cash and in-kind transfers, as well as non-transfer programmes. These include child allowances, food subsidies, vouchers for various types of basic services, public employment and credit based livelihood programmes. These programmes help people cope with economic and social problems.

Pakistan too has some social protection programmes, for instance, the formal systems of pension in the public sector, social security, zakat and the food support programme. These schemes however, suffer from improper targeting, limited coverage, poor administration, and meagre allocations, which hardly provide any meaningful assistance.

The forthcoming Budget needs to focus on the well being of individuals. Need for choosing the appropriate social protection programmes that best contribute to protecting the welfare of the poor must be introduced and strengthened, so as to reach the target group. For instance, the government may like to review the pension system and give a gradual increase in real terms. One mechanism could be the introduction of a flat social pension for the oldest cohort of the elderly (e.g., those aged 75 years or more), who are not eligible for regular pensions.

Perhaps some kind of differential tax treatment may be meted out to those who use the saving schemes. If the tax authorities can bring within its ambit large numbers who evade taxes, then some relief could be provided to those who are investing in NSS.

If the government takes new initiatives and devises programmes which provide assistance to a large segment of society, it could in some small way mitigate the sufferings caused to small savers by a reduction in returns on NSS.

Ayesha Mahmud

Abstract of the Bulletin

WTO, The Agreements and their Implications for Developing Countries, with Special Reference to Pakistan

§ The World Trade Organisation set up in January 1995, deals with rules of trade between member countries.

§ The Agreements cover a wide range of activities dealing with agriculture, textiles and clothing, intellectual property and much more.

§ The Agreements have wide ranging implications for member countries.

§ With the removal of quotas under the new WTO rules, Pakistan textiles will face tough competition. Large investments are needed to upgrade the industry and move away from traditional products to value added products.

§ Anti dumping laws will be enforced, subsidies will be phased out, non-tariff barriers are to be reduced.

Pre-Budget 2003-04

§ The forthcoming Federal Budget 2003-04 is expected to reinforce the economic reform process initiated a few years back.

§ Poverty reduction, agricultural sector especially improvement of irrigation facilities, building of storage capacity is expected to receive government priority.

§ To meet WTO challenges, textiles need investment for BMR.

§ Fiscal reforms must continue, infrastructural facilities need to be upgraded and levels of investment have to be raised.

Pakistan's Automobile Industry

§ The automobile industry in Pakistan operates under franchise and technical cooperation agreement with leading international manufacturers.

§ It annually contributes around Rs.70 billion to GDP and Rs.20 billion to the national exchequer, while foreign exchange savings amount to around $500 million per annum.

§ The industry is currently engaged in manufacturing/ assembly of cars and jeeps, buses and trucks, vans and pick ups, auto rickshaws and motor cycles and tractors and bicycles.

§ Under the ongoing deletion programme, the local content in automotive vehicles at present ranges between 45-85%. The deletion programme has led to the development of a vibrant hi-tech vendor base engaged in manufacturing and supply of auto parts.

§ Currently the car industry is experiencing a boom. There has been a dramatic rise in demand and sales of locally assembled cars of popular brands like Suzuki, Honda, Toyota, Kia and Diahatsu.

Agriculture

§ Water supply situation has somewhat improved compared to earlier years, when drought affected agricultural growth.

§ During the current Rabi season, a good harvest of wheat is expected, which has brightened the prospects of enhanced exports this year.

§ For 2002-03 crop, rice production is expected at 4.228 million tonnes, exceeding both the target area and last year's production.

§ A higher production target of 10.55 million bales of cotton has been fixed for 2003-04.

§ Sugarcane crop is placed at 53 million tonnes for 2002-03 crop. The higher output is attributable to increased sown area as well as rise in per hectare yield.

Banking and Finance

§ During the week ended April 26, 2003, scheduled banks deposits, advances, investment in securities and approved foreign exchange increased over the corresponding level of last year.

§ Low rate of domestic savings in Pakistan has been one of the principal factors for rising public debt.

Market Analysis

§ The market recovered from its bearish spell in March and April, recording strong gains to reach a new record high of 2967 before short-term weakness saw it make a correction toward the end of the month. Despite the correction, the overall environment is favorable for the equity markets and the trend appears positive for the long term.

WTO, The Agreements and their Implications for Developing Countries, with Special Reference to Pakistan

The World Trade Organisation (WTO) set up on January 1, 1995 is an international body dealing with the global rules of trade between member countries. It seeks to ensure that trade flows smoothly and freely, primarily by ensuring that individuals, companies and governments know what the trade rules are around the world, settling trade disputes, administering trade agreements, assisting developing countries in trade policy issues. In other words, the body provides a framework of rules and systems within which member countries conduct trade and other commercial relations among themselves.

WTO deals with global rules of trade

The WTO has more than 130 members, accounting for over 90% of world trade. Decisions are made by the entire membership.

The Agreements

The WTO Agreements cover a wide range of activities, dealing with agriculture, textiles and clothing, banking, telecommunications, industrial standards, intellectual property and much more. These principles include individual countries commitments to lower customs tariffs, and other trade barriers, open services markets, set procedures for settling disputes, prescribe special treatment for developing countries. Member countries are obliged to notify the WTO on countries' trade policies, any changes in laws etc.

In a nutshell

The basic structure of the WTO Agreements

	Goods	Services	Intellectual property	Disputes
Basic principles	GATT	GATS	TRIPS	Dispute settlement
Additional details	Other goods agreements and annexes	Services annexes		
Market access commitments	Countries' schedules of commitments	Countries' schedules of commitments (and MFN exemptions)		

Source: *Trading into the Future World Trade Organization March 2001*

The inclusion of services in WTO agreements means that the sector now enjoys the same principles of freer and fairer trade that originally only applied to trade in goods.

Tariffs

Member countries have given their commitments to lower tariffs by 2005. These include commitments to cut and "bind" their customs duty rates on import of goods (bound rates represent commitments not to increase tariffs above the listed rates). In some cases, tariffs are being cut to zero.

Tariffs on all agricultural products are now bound. Almost all import restrictions that did not take the form of tariffs, such as quotas, have been converted to tariffs. Previously more than 30% of agricultural produce had faced quotas or import restrictions. These were converted to tariffs, which has gradually been reduced.

Agricul-ture

While the original GATT did apply to agricultural trade, it contained loopholes, like use of non-tariff measures such as import quotas, and allowing countries to subsidize. The WTO does not approve of subsidies particularly to the agricultural sector. They are usually costly, create distortions, over burden the state expenditure and increase budgetary deficits.

The WTO forum seeks to provide fairer markets for farmers. Agricultural trade which had become highly distorted, especially with the use of export subsidies and quotas is being reformed.

While the agreement allows governments to support their rural economies, it is through policies that cause less distortion to trade. Developing countries do not have to cut their subsidies or lower their tariffs as much as developed countries and they have been given more time to complete their obligations. It is being implemented over a 10 year period. Previously more than 30% of agricultural produce had faced quotas or import restrictions.

These have been replaced by tariffs. It has been agreed that developed countries would cut the tariffs by an average of 36% in equal steps over six years. Developing countries would make 24% cuts over 10 years. Least developed countries do not have to cut their tariffs.

Textiles

Textiles, like agriculture is one of the tough issues in the WTO. It is now going through a fundamental change. The system of import quotas that has dominated the trade since the early 1960s is being phased out. From 1974, the trade was governed by the Multifibre Arrangement (MFA) that established quotas limiting imports into countries whose domestic industries were facing serious damage from rapidly increasing imports.

Since 1995, the WTO's Agreement on Textiles and Clothing has taken over from the Multifibre Arrangement. By 2005, the quotas will come to an end, and importing countries will no longer be able to discriminate between exporters.

Four steps over 10 years

The schedule for freeing textiles and garments products from import quotas (and returning them to GATT rules), and how fast remaining quotas should expand.

The example is based on the commonly-used 6% annual expansion rate of the old Multifibre Arrangement. In practice, the rates used under the MFA varied from product to product.

Step	Percentage of products to be brought under GATT (including removal of any quotas)	How fast remaining quotas should open up, if 1994 rate was 6%
Step 1: 1 Jan 1995 (to 31 Dec 1997)	16% (minimum, taking 1990 imports as base)	6.96% per year
Step 2: 1 Jan 1998 (to 31 Dec 2001)	17%	8.7% per year
Step 3: 1 Jan 2002 (to 31 Dec 2004)	18%	11.05% per year
Step 4: 1 Jan 2005 Full integration into GATT (and final elimination of quotas) Agreement on Textiles and Clothing terminates.	49% (maximum)	No quotas left

Source: Trading into the Future, World Trade Organization

Services

The General Agreement on Trade in Services (GATS) is the first ever set of multilateral, legally enforceable rules covering international trade in services (GATS defines this as services supplied from one country to another e.g. international telephone calls; consumers or firms making use of a service in another country eg. tourism; a foreign company setting up subsidiaries or branches to provide services in another country; individuals travelling from their own country to supply services in another eg. consultants, fashion models).

Intellec-
tual
property

Intellectual property rights — copyrights, trademarks, patents etc have been brought into the WTO system for the fist time. It has become important in trade, and new internationally agreed trade rules gives the creators more right to prevent others from using their inventions, designs or other creations. The WTO's Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) is an attempt to protect these rights and bring them under common international rules.

Developing countries — net users of intellectual property oppose WTO coverage of this areas, while developed countries — predominant owners of intellectual property support their inclusion under WTO rules.

Anti-dumping, subsidies, safeguards, etc.

Many governments take action against dumping in order to defend their domestic industries. The WTO focuses on how governments can or cannot react to dumping — it disciplines anti-dumping actions.

Developed countries spend huge sums as subsidy on agricultural commodities. Japan was subsidizing rice, EU was subsidizing sugar and the US was subsidizing cotton. The Agriculture Agreement prohibits export subsidies on agricultural products unless the subsidies are specified in a member's list of commitments. Where they are listed, the agreement requires WTO members to cut both the amount of money they spend on export subsidies and the quantities of exports that receive subsidies.

With regard to subsidies, it disciplines the use of subsidies and it also regulates the actions countries can take to counter the effects of subsidies.

Non-tariff barriers

There are WTO agreements which deal with various other issues that could involve hindrance to trade. These include among others, technical regulations and standards, import licensing etc. Countries at times impose certain regulations which creates obstacles to the free flow of trade.

The WTO agreement tries to ensure that regulations, standards and certification procedures do not create unnecessary obstacles. The agreement encourages countries to use international standards where these are appropriate but it does not require them to change their levels of protection as a result.

On customs valuation, the WTO agreement aims for a fair, uniform and neutral system that conforms to commercial realities. Similarly on pre-shipment inspection, the obligations placed on governments which use pre-shipment inspections include non-discrimination, transparency, protection of confidential business information, the use of specific guidelines for conducting price verification among others.

Implications of the Agreements

The WTO agreements have wide ranging implications for member countries, presenting both opportunities and challenges. Some countries have to adjust their policies, create and strengthen institutions and change laws to meet the challenges in the changed economic scenario that will emerge in the year 2005.

Quotas to be removed

For the Asian developing countries, the most significant measure is the WTO's inclusion of textiles and clothing in the multilateral rules. Earlier, such trade had been governed by bilateral quota restrictions. Under the Multifibre Arrangement in force for over two decades, quotas known as "voluntary export restraints" raised prices artificially in consuming countries and penalized more efficient exporters by restricting market access. The new WTO rules state that all such quotas are to be removed between 1995-2005.

Asian developing countries account for more than 40% of global trade in textiles and 55% in clothing. Textiles and clothing are the single most important export for most of these developing countries. In countries like China, India, Bangladesh, Pakistan, these products account for a large proportion of trade.

Textiles are Pakistan's key foreign exchange driver, covering a diverse range of items from yarn, fabrics, made up textiles products to clothing.

These have been subject to bilateral quotas. Now with the Agreement on Textiles and Clothing having taken over the Multifibre Arrangement (MFA), the quotas are being gradually removed and the process will culminate with their full removal by 2004.

Textiles to face challenge

In the post 2005 scenario, the domestic textile industry will no longer enjoy the protection inherently given by the quota system and will be faced with a highly competitive and challenging market environment. Our exports will increase in categories that have the potential for greater exports but are limited by quota constraints. But at the same time, it will take away the exports that we merely got because of the quota allocated and not because of our competitiveness. Trade in textiles and clothing will be carried out on the basis of market forces.

Pakistani textile manufacturers will have to reorient themselves, develop new expertise and know-how and skills if they are to survive and become competitive in today's challenging world.

With the abolishing of quota system, Pakistani textiles would face tough competition from China, India and Bangladesh. Large investments are needed to upgrade the industry, to be in a position to move away from marketing of traditional products to value added products. Our industries need to become efficient and in doing so compete with global players in areas of comparative advantage.

While some may perceive phasing of quotas as a threat, it could in fact be a great opportunity for the industry. In the next two years, freeing of quotas should help exports get a big boost, as at times quotas in the categories like towels, bed linen, garments was fully utilised and there was still a great demand for Pakistani products.

According to the WTO estimate, with the elimination of quotas in the year 2005, the total world trade of textiles and clothing will exceed $500 billion, driven primarily by the clothing sector. Pakistan which is a player in the apparel industry will have to diversify from the present tilt towards men's wear and knitted garments towards sportswear, women garments and industrial clothing made of specialised fabrics. Introduction of computer added designing in the garment industry will aid to bring about good results. To survive in the new trading environment, would depend on how well the industry upgrades the existing technology, moves towards manufacture of products for the upper market segment and brings about innovative design development in consumer products like bedwear, apparel.

Enforcement of anti-dumping laws

In the past, developed nations have used anti-dumping laws against Pakistan's textile exports. Textile sector growth has suffered partly because of anti-dumping duty on Pakistan's bed linen. Anti-dumping restrictions are directly correlated to the spread of free trade. The more open the economy, the greater is the reliance on anti-dumping measures. The anti-dumping law would now make it possible for local manufacturers hurt by dumping to seek remedies against it.

Pakistan's own market has in the past proved a haven for foreign manufacturers of a wide range of imports at dumping prices or brought in through the channel of smuggling. Cheaper imports pose a serious threat to local industry, many of whom have thrived on protectionist policies. For instance, the local electronics industry faces tough days ahead, as cheaper goods have flooded the market.

Under the WTO, the importing country can take anti-dumping action to remove the injury caused to the local industry. Now Pakistan can seek recourse from WTO whenever it finds that cheaper imports is hurting its domestic industry.

Developed nations have also used anti-dumping laws against Pakistan's textile exports, hampering its exports. The European Union has imposed the anti-dumping duty on Pakistan's bed linen.

Pakistan has like some other developing countries extended variety of subsidies, protective tariffs and incentives to various sectors of the economy, particularly agriculture and industry.

Subsidies to be phased out

The WTO agreement on subsidies has given some developing countries upto 2003 to get rid of their export subsidies, while others must eliminate import substitution subsidies. In other words, one can say that subsidies are being discouraged. Subsidies in Pakistan are also being gradually eliminated. It has partially abolished subsidies on wheat. Being an agro-based economy it is not in a position to completely do away with subsidies. Gradually removing subsidies would help in cutting down on government's non-development expenditures. The step would however, pose a challenge to those sectors who have thrived on subsidies.

Non-tariff barriers to be reduced

The reduction in tariffs on trade in industrial goods combined with removal of non-tariff barriers means a reduction in protection to domestic industry on the one hand, and a greater competition in export market. Pakistan will now have to take greater care of quality control to remain competitive. Low quality of products, fetches low price in the international market. The problem of quality in Pakistan are those of technical precision, grading and standardisation. Besides quality, cost effectiveness of products can ensure competitiveness.

Lowering of trade barriers to increase trade

Lowering of trade barriers allows trade to increase, which boosts economic growth and that means more jobs. Employment would grow in companies involved in exporting. So if Pakistan can increase its trade, it will push economic growth creating employment opportunities. Unemployment is a major problem confronting large numbers. So if companies involved in exports can create jobs, it will go a long way to help fight poverty in Pakistan.

Pre-Budget 2003-04

The Federal Budget 2003-04 is expected to be announced in about two months time. Some of the structural reforms initiated in recent years appear to be slowly taking hold, laying the foundation for an acceleration of economic growth. The new government that has assumed office is committed to continue with these economic reforms. Continuity of policies should help build investor confidence, reduce uncertainties, thereby helping reinforce the economic revival process.

At the same time, government efforts will need to be directed towards maintenance of fiscal and monetary discipline, continuity with Central Board of Revenue (CBR) reforms and other regulatory reforms, restructuring of WAPDA and KESC, and privatisation. If there occurs any relaxation, it would make the achievement of the path to revival unviable.

Poverty reduction

Given the country's high and rising levels of poverty, and its low level of human development, a result of poor governance and slow economic growth, the government besides undertaking other measures had in 2001 prepared a poverty reduction strategy. The first draft of the Poverty Reduction Strategy Programme formed the basis on which the Interim Poverty Reduction Strategy Paper (I-PRSP) was based. The I-PRSP encapsulates the government's medium term programme of structural reforms, which has now been developed into a full Poverty Reduction Strategy Paper.

The I-PRSP had identified five major areas of intervention of poverty reduction in the country. These were, revival of economic growth, income generation, creation of employment opportunities, human development, strengthening of social safety net programmes to reduce vulnerability and improvement in governance.

A recent joint staff assessment of the I-PRSP identified some gaps in this strategy, which included: need for a detailed rural development strategy, a more focused human development strategy, a coherent fiscal framework, costing of programmes to achieve targets, particularly in the health and education sector. This indicates the government's commitment to the continuity of reforms envisaged in I-PRSP.

The forthcoming Budget is expected to allocate adequate financial resources for public sector interventions in the key areas identified. A monitoring framework for tracking indicators in the social sectors and anti-poverty programmes would be relevant to track progress in the achievement of the goals.

The new government would be aiming for higher sustainable growth and reducing poverty through the pursuit of a wide range of structural reforms aimed at stimulating private sector growth and improving social service delivery. During the period of the next Budget, an explicit reform agenda will be laid out in the full PRSP.

Agriculture & rural poverty

The key to attack poverty lies in rapid agricultural growth, which is the mainstay of Pakistan's economy. It has both backward and forward linkages. The former includes purchasing farm inputs such as chemicals, fertilizers and machinery, while the later includes supplying of raw materials to food and fibre processing to the non-agricultural sector.

In recent years, there has been a decline in agricultural growth rate due to unprecedented drought conditions. Agricultural incomes of the majority of people living in rural areas has declined, widening income disparities between urban and rural areas. Rural poverty is still high in Pakistan at around 32%.

Improve irrigation facilities

Among agricultural reforms, irrigation development is perhaps of vital significance. It is one of the key inputs for enhancing agricultural production and is expected to receive government priority.

For the current Budget, the government had enhanced development spending on irrigation, raising allocation from Rs.3.4 billion in the revised estimates for 2001-02 to a budgeted figure of Rs.7.1 billion in 2002-03. The forthcoming budget would probably maintain this level or raise it so that better irrigation facilities are made available to farmers to expand their cultivation especially in the dry regions. There is also a need to spend on maintenance and operation of the irrigation system, so to prevent seepage, erosion and wastage, because of which large quantities of irrigation water fails to reach the farmers' field. Efficient management of water resources is essential. We have seen that better availability of water during FY03, resulted in good harvests of kharif crops alongwith improved prospects for the rabi crops.

Build storage capacity

Many a times farmers are forced to put the entire crop in the market, in a short period after harvest because of a lack of storage capacity. This deprives them of a good price, for immediately after harvest when there is a temporary supply glut, prices tend to fall.

Constructing silos/godowns is highly labour intensive and while there has been little private sector initiative, the government can in partnership with the private sector build such godowns.

Textiles need investment

During the period of the forthcoming Budget, the implementation of WTO rules is expected to pick up, as the new era in textiles and clothing will begin in January 2005. This would require structural and operational adjustments, switching to efficient processes and production methods, conforming to international standards. Investments would be needed for BMR purposes in identified priority sector of stitching, knitting & finishing among others.

Allocations for the industrial sector are expected to be higher, especially for investments in BMR and improving production technologies of textile sector. The government could compliment the efforts of exporters by facilitating the export of finished products; devise friendly policies to assist the manufacturers to compete globally. Continue to grow contamination free cotton and modernize the present outdated machinery in view of high competition from China, India and Bangladesh.

Low investment

While some economic indicators have performed well in the recent past, a falling investment to GDP ratio is a cause for concern. The investment to GDP ratio had been hovering at around 16% since FY99, and declined in FY02 to 14%. The average ratio for the last four years is not impressive when compared to some regional countries. Low rates of investment have limited both employment generation and the growth in output. Falling rates reflect the uncertain business environment, law and order situation, inadequate infrastructure, unanticipated changes in policies. They also harm growth prospects.

Need to raise savings

The continuing low levels of savings have resulted in low investment ratios. If the economy is to grow at a higher rate of around 6%-7%, a much higher rate of investment of around 20%-22% is required. But how does one raise the investment rate, when domestic savings are low?

Perhaps the Budget 2003-04 will offer some new alternates for savings. The returns on deposits in the National Saving Schemes have been reduced, as part of government's efforts to reduce debt servicing costs. Earlier the government had also prohibited institutional investment in the NSS. The financial institutions are awash with liquidity, but there are few investment avenues. Similarly individuals who preferred to invest in NSS schemes are suddenly faced with reduced returns.

Mere rhetoric would not help but serious efforts are needed to provide the basic infrastructure for investors to come and invest in Pakistan.

Lack of infra-structure

Lack of adequate infrastructural facilities are one of the major constraints towards flow of investment to various sectors. Power supply is unreliable and rather expensive, road and rail transport are poorly maintained, telephone services and gas supplies though much better, do at times pose problems for new businesses. Investments are needed in the power sector, especially in transmission and distribution capacity, and in improving the services provided by these utilities which would help growth of private industry, and increase competitiveness of Pakistan's exporting industries.

Fiscal Reforms

The Budget is expected to continue with ongoing efforts to widen the tax base and meet the fiscal deficit target. Recently the International Monetary Fund identified some categories of upper strata society of Pakistan to be specifically focused upon by the Central Board of Revenue for widening the tax base. If the CBR succeeds in netting this class of society that has so far evaded taxes it would greatly help in widening the base and raising the level of revenues.

The government has committed to prepare specific proposals for further tax policy reforms to be implemented with the 2003-04 budget, including the elimination of many of the remaining income tax and withholding exemptions.

During FY02, an estimated Rs.460.6 billion was to be collected from various taxes.Upto March 03, Rs.310.3 billion or 67.4% of the target had been collected. This is 15% higher over last year's collection during the same period. Unlike FY02, which saw tax shortfalls and frequent revisions of targets, the aggregate CBR tax collections remained on track during the first nine months of FY03.

Federal Government Tax Collection

(Rs. Bn)

	Direct Taxes	Indirect Taxes				Total Tax Collection
		Sales	Excise	Customs	Total	
1998-99	110.2	72.1	60.9	65.3	198.3	308.5
1999-00	113.0	116.7	55.8	61.7	234.2	347.1
2000-01	124.6	153.6	49.1	65.0	267.7	392.3
2001-02	142.6	166.3	46.9	48.1	261.3	403.9
2002-03*	148.5	205.7	47.5	59.0	312.1	460.6
Upto March 03	94.7	139.1	31.3	45.2	215.6	310.3
Upto March 02	96.2	113.4	31.2	29.0	173.7	269.8

* Target for whole year

Source: Central Board of Revenue

However, collection of individual taxes varied considerably against their targets.

During this period there was a sharp increase in receipts from customs (55.9%) and General Sales Tax (22.6%). Increase in the later was due to its extension to cover more domestically produced items like vegetable ghee and cooking oil, as well as increase on a number of imports. Receipts from excise duty remained more or less unchanged at last year's level, while collection from direct taxes declined marginally by 1.6%, due to lower payments by PTCL and a reduction in corporate tax rates and abolition of some withholding taxes.

It seems probable that Pakistan would achieve this year's revenue target and also the fiscal deficit target of 4.6% of GDP for FY03.

Not only has the increse in revenues to be sustained but the government also needs to focus on raising its development expenditures. These have in the past fallen short of the budget allocations. These are expected to show some increase on account of developmental plans of the newly elected federal and provincial governments.

Enhancing the professional knowledge and skills of the tax officers would improve the quality of tax assessment, so that yields from the existing sources are maximized. These and other steps should help promote fiscal discipline and correct macroeconomic imbalances.

Pakistan's Automobile Industry

The automobile industry in Pakistan can be broadly characterized into five segments; cars/ light commercial vehicles (LCVs), trucks / buses, two / three wheelers, tractors and vendor industry. The industry operates under franchise and technical cooperation agreement with leading world manufacturers. It enjoys the status of most protected industry with effective protection rate (EPR) ranging between 701% to over 5000%. It annually contributes around Rs.70 billion to GDP and provides Rs.20 billion in tax revenue to national exchequer. Foreign exchange savings amount to over $500 million, while import substitution exceeds $1 billion.

Most protected industry

Catering to the requirements of the automobile industry, there are some 25 auto engineering industries and thousands of ancillary and vendor units. The sector is presently engaged in manufacturing/assembly of cars & jeeps, trucks and buses, van and pickups, auto-rickshaws, motorcycles and scooters and tractors.

In the automotive line, Pak Suzuki, Indus Motors, Honda Atlas, Dewan Farooque Motors and Ghandhara Nissan have set up their units for manufacturing and assembly of some well known international names.

The sector provides job opportunities; car manufacturers and vendors alone employ some 200 thousand persons directly and another 300 thousand persons indirectly. The sector has attracted investment since as far back as the 1950s. Currently investments range between Rs. 10 - Rs. 20 billion.

Provides job opportunities

Investment in the automobile industry started in mid 1950s, when Kandawala Motors in collaboration with General Motors of USA commenced CKD assembly operation. The first vehicle assembled was a Bedford truck. The decade of 1960s saw a profusion of various assembly plants of well known makes being set up in the private sector. Cars assembled during that period were Ford, Prefect, Ford Cortina and Dodge.

The government took over the industry and placed it under public sector in 1972. After nationalization, the Pakistan Automobile Corporation (PACO) was established to regulate and supervise the industry. Till mid-70s, assembly plants were rolling out 4 wheel vehicles with indigenisation level not exceeding 20%. However, Bedford trucks and lorries had attained 80% indigenisation before it was closed down in 1976. By end 1970s, almost all automobile assembling in the country had ceased in the absence of any national policy on automotive sector.

Nationalisation in 1972

In the 80s, the government reactivated the automobile industry and decided to have an indigenised car manufacturing-cum-assembly plant for making cars of upto 1000cc-engine capacity. In 1983, Pakistan Automobile Corporation and Suzuki Motors of Japan joined hands to set up Pak Suzuki Motors, which introduced Suzuki brand cars with engine capacity of upto 1000cc.

Pak Suzuki Motors

Private participation came in the industry in early 90s, when two other Japanese auto makers, Toyota and Honda, also set up their plants to cater to the growing demand in the market. Presently Pak Suzuki, Indus Motors, Atlas Honda, and Dewan Farooque Motors are active in the market.

Private participation in 90s

Pakistan auto industry is mostly based on joint ventures with Japanese and other foreign car/truck makers. Pak Suzuki Motors makes Mehran/Alto 800cc cars, Ravi pick up, Bolan small van and Potohar jeeps. Indus Motors makes various models of Corolla brand (1300cc-2000cc), Hilux pick up and Hiace vans. Atlas Honda makes various models of Honda Civic and City (1300cc — 1500cc). Dewan Farooque Motors makes Santro Plus, Kia Classic (1300cc), Kia Sportage (2000cc), Kia Spectra and light commercial vehicles, Shehzore, Daihatsu has launched Cuore (850cc).

Joint ventures with Japan Korea and Italy

AUTOPARTS MANUFACTURING INDUSTRY
2001-02

Model	Local Parts Content (%)	Total Quantity (000 Nos)	Sales Amount (Rs.Mn)
CARS			
Honda (Civic)	52	6.0	1560
Suzuki (Baleno)	52	2.0	520
Toyota (Corolla)	52	8.0	2080
Suzuki (Cultus)	55	6.0	1320
Suzuki (Alto)	55	5.0	1100
Hyundai (Santro)	55	4.0	880
Kia (Spectra)	44	2.0	440
Kia (Classic)	50	2.0	450
Suzuki (Mehran)	70	12.0	2520
Total Cars		47.0	10870
TRUCKS			
Hino Pak (Hino)	52	0.4	312
Ghandhara (Nissan)	52	0.5	390
Sindh Engg.(Mazda)	52	1.0	416
Total Trucks		1.9	1118
LIGHT COMMERCIAL VEHICLES			
Suzuki (Potahar)	45	2.0	270
Suzuki (Bolan)	55	5.0	549
Hyundai (Shehzore)	38	3.0	456
Toyota (Hilux) 4x2	38	2.0	304
Suzuki (Ravi)	55	2.6	288
Total LCVs		14.6	1867
TRACTORS			
Al-Ghazi (Fiat)	86	15.0	3225
Millat (MF)	86	15.0	3225
Total Tractors		30.0	6450
MOTORCYCLES			
Atlas (Honda)	85	60.0	2550
Dawood (Yamaha)	83	25.0	10392
Suzuki	80	4.5	179
Sohrab	85	5.0	212
Saigol (Qingqi)	85	5.0	212
Total Motorcycles		99.5	41932
1. Total sales			34298
2. Federal levies on sales to OEM including sales tax and import duty 20%			6860
3. Savings in foreign exchange			17149
4. Import substitution			20579

Source: Pakistan Association of Automotive Parts & Accessories Manufacturers

Five years ago, Pakistani automakers were manufacturing only Japanese brands but now they are also making Korean and European brand.

Main assemb-lers

A significant transformation is taking place in the local auto industry, where new entrants in the market have increased competition of cars and LCVs segment of the market. Pak Suzuki, Atlas Honda and Indus Motors - the three main assemblers - have been dominating the cars and light commercial vehicle market, with Pak Suzuki enjoying the position of market leader in small cars, and Indus Motors and Atlas Honda competing for bigger car segment. However, recent entry of Dewan Farooque Motors, Daihatsu, Hyundai Motors and Raja Group of Industries has made the domestic market more competitive.

According to the Pakistan Association of Automotive Parts and Accessories Manufacturers Suzuki has attained maximum deletion level ranging between 42%-60%. Toyota has achieved 18%-30% maximum localization, while Honda has attained deletion level ranging between 28%-30%.

Besides passenger cars, the auto manufacturers are also engaged in the manufacturing-cum-assembly of buses, trucks, coasters, tractors, LCVs and motorcycles. The leading manufacturers of heavy vehicles include, Ghandhara Nissan, Sindh Engineering, Hino Pak, Kohinoor Motors, Millat Tractors, Al-Ghazi Tractors and Allied Motors.

Ongoing deletion process

The indigenisation process in the automobile industry is progressing satisfactorily. Each category of vehicle has attained different levels of deletion. Under the ongoing deletion programme, car industry has so far achieved 50%-70% indigenisation followed by tractors (48%-83%), motorcycles (77%-83%), light commercial vehicles (38%-63%) and buses (45%-47%). Overall the local content in automotive vehicles now ranges between 45%-85%. The deletion programme has led to the development of a vibrant Hi-tech vendor base in the country.

Vendor industry

There are over 800 vendors in the organized as well as unorganized sector engaged in the manufacturing and supply of auto parts to local Original Equipment Manufacturers (OEMs). These vendors are supplying a variety of auto parts to Pak Suzuki, Atlas Honda, Indus Motors, Allied Motors, Millat Tractors and also to motorcycle assemblers.

The auto parts being locally manufactured in the organised sector include pistons, engine valves, gasket, camshaft, shock absorbers, steering mechanism, gears of all types, radiators, cylinder heads, wheel hubs, brake drums, bumpers, fly wheels, automotive pumps, instrument panels, blinkers, light, doors and door locks.

In addition some small units in the unorganized sector, which fabricate smaller parts without brand name like ignition control system, micro touch buttons, built in alarm system, light and door operating system, dash board, door handles, warning lights and horns also command a big market. They are producing quality products imitating foreign makes, which are much cheaper than those produced or imported under brand names.

At present the vendor industry is meeting 85% of local demand for spare parts reaching a peak high deletion of 80% of the tractor industry and a low of 35% for cars. An estimated $25 million worth of spare parts are exported annually. It provides jobs to 500 thousand persons, both skilled and unskilled, in the organised and unorganized sectors.

Low demand for local assembled cars

The growth in the automobile sector remained sluggish till the 1990s, due to host of reasons. These included, flawed regulatory framework and shortsighted policies, paucity of working capital, etc.

Smuggling of fully conditioned cars and auto parts and import of reconditioned and second hand cars had dramatically decreased the demand for locally assembled cars, thereby adversely affecting local manufacturers. As a result the installed capacity of major components of automobile sector remained underutilized.

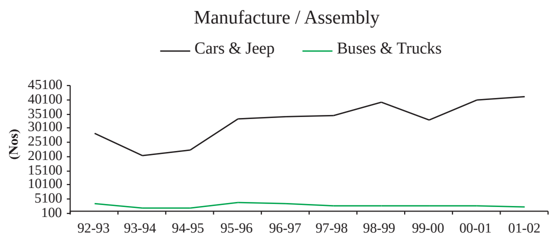
Assemblers	Installed Capacity 000 units/annum
Cars	120
Buses	2
Trucks	13
LCVs	28
Motor Cycles/Scooters	340
Tractors	33

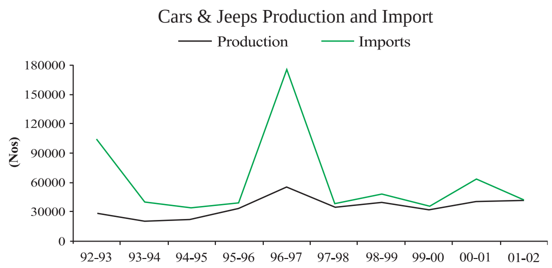
Boom in car industry

After remaining stagnant for more than a decade, the growth in auto industry jumped 20% in FY02, attributable to significant rise in demand for new cars. The growth continues. According to the latest available data for March, demand for cars has jumped by 50%, resulting in production of a record number of cars (41800 units) in the first nine months of FY03.

Not only has capacity utilization of car industry improved, but major market players had to add new capacity to meet the rising demand. It is expected that car manufacturing may cross the level of 50,000 units in FY03. As a result of increase in demand, car sales have also doubled.

Various factors have contributed to the surge in demand for cars and subsequent increase in production and sales. These include among others, increased inflow of home remittances after the 9/11 events, increased liquidity in the market in the absence of profitable investment schemes, decline in interest rates and easy availability of loans for purchase of cars at competitive rates.





Car financing by banks/ leasing companies

The consumer financing facility offered by commercial banks and leasing companies has significantly enhanced sales. During the current year, car sales are up by 50%, tractors by 18%, LCVs by 58%, buses and trucks by 65% and motorcycles and bikes by 30%. At present over 40% of all new car sales are being financed by major banks and leasing companies.

Problems facing the industry

The performance of the car manufacturers does not represent the performance of the entire auto industry. Though, among other auto components, production of trucks grew by a record 139%, LCVs by 47%, buses by 92%, motor cycles by 60% and tractors by 9% in the first half of FY03 the market conditions for medium and heavy transport have deteriorated.

The capital and operational costs of commercial vehicles have increased, while revenues have not grown commensurately. Consequently manufacturing of medium and heavy transport equipment has become an unprofitable business. At the same time increase in import of CBU buses in recent years has also adversely impacted local manufacturing activities. As present the capacity utilization of trucks and buses is less than 15%.

The auto manufacturers also complain that reduction in import duty on auto parts has resulted in cheap imports, making local fabricated auto parts uncompetitive. Due to low production volume, prices of local components have increased. High input cost is adversely affecting local assemblers and vendors.

Currently CKD import under deletion programmes and general commercial imports attract the same tariff levels, which has seriously damaged growth of the vendor industry, affecting overall performance of automobile sector.

Conclusion

Improved capacity utilisation

Automobile has become an attractive sector for foreign investment in Pakistan. At present the entire auto sector is experiencing increase in sales ranging from 30% to 58% in different categories. Significant growth in demand, particularly that of cars, has resulted in increase in production, besides addition in existing production capacity by leading auto makers. Despite this increase, capacity utilization is still around 40%

The market for cars is expected to grow by about 10% annually. The demand for passenger and commercial vehicles is expected to reach 270 thousand units by 2005 against the existing production capacity of 120 thousand units. More sophisticated hi-technology would be required in the local vendor industry to enable Pakistani car manufacturers to enter foreign market.

Elimina-ting import needs

If given proper consideration, the vendor industry has the potential to fabricate all automotive components locally, thereby eliminating the need for import. At present the industry is not technically viable to meet entire demand from local parts and vendors are also serving as assemblers of imported components.

Both the private sector as well as government need to make all out efforts to create a conducive environment for the robust growth of automobile industry. Greater efforts are required to develop vendor industry, where all parts and components are manufactured locally. It could result in foreign exchange savings of more then $500 million annually.

Since the majority of the basic spare parts are still being imported, the vendor industry has not been able to provide a strong support to the engineering sector. At the sametime, Pakistan's vending industry is running strickly on self-financing basis. It is deprived of credit facilities from banks, as a result the vendors have been unable to induct latest technology, which needs heavy financing.

Low level of indeginisa-tion

Currently levels of indeginisation, though improved, are still very low, particularly, in passenger cars segment. Entry of new players coupled with increase in local content is likely to give requisite boost to domestic component industry.

Local auto manufacturers are of the opinion that the government should undertake measures for the expansion of automobile market and the growth of the industry. They suggest various steps that are needed to protect local vendor industry. These include, imposition of regulatory duty on commercial imports of auto parts, complete ban on import of reconditioned cars and its strict enforcement on all categories and imposition of heavy penalties on smuggling.

PAAPAM has also demanded that commercial importers are misusing the window for overseas Pakistanis, which is directly hitting local industry and so it should be discontinued. The window provides the opportunity to overseas Pakistanis to import auto vehicles and parts under baggage and transfers of residence scheme.

Manufacture /Assembly of Automobiles

Year	Cars (000 Nos)	Jeeps (Nos)	LCVs (Nos)	Trucks (Nos)	Buses (Nos)	Motor Cycles (000 Nos)	Tractors (000 Nos)	Bicycles (000 Nos)
1992-93	27	1324	11478	222	1177	96	17	589
1993-94	19	816	5128	1394	427	64	15	564
1994-95	21	1310	5154	703	312	61	17	473
1995-96	31	2274	6834	3030	438	122	16	545
1996-97	33	792	9817	2916	362	117	10	432
1997-98	34	657	9886	1850	425	97	14	452
1998-99	39	622	8079	1131	1220	93	27	504
1999-00	32	380	6656	977	1508	95	35	534
2000-01	40	459	6965	952	1337	118	32	570
2001-02	41	570	8491	1141	1099	133	24	553
2002-03*	26	165	5537	822	802	85	11	313

* (July - December)

Agriculture

Outlook brightens

The severity of the drought which had affected agricultural growth over the past two years; the sector declined by 0.6%, has somewhat subsided. The water supply situation has improved during the current Rabi season, compared to the Kharif season when water shortages were affecting the crops. Then 6.4% less than the normal supplies was available. This was an improvement compared with a 22% shortfall in FY01 and 29% shortage in FY02. On the whole, the water situation this year appears slightly better. This will have a positive impact on agriculture performance. Production of major crops – wheat, rice and sugarcane – have already exceeded their respective targets and are well above the previous season's crop. Though cotton production has declined, agriculture growth is estimated at around 3%, surpassing the target of 2.7% set for the year.

Wheat

Target revised upward

The government had fixed the area and production targets for the 2002-03 crop at 8.03 million hectares and 19.75 million tonnes respectively. A latest report reveals that growers have brought 8.07 million hectares under the current Rabi crop, which is almost close to the targeted area as well as last season's acreage. Country wide heavy rains in mid-February have brightened the prospects for a good harvest. Growers are now expecting a bumper harvest.

The official production target has already been revised upward to 20.6 million tonnes, as growers in Punjab expect to produce a crop of 16.5 million tonnes against the targeted 15.64 million tonnes. Punjab produces 80% of the total crop. Better weed control and improved fertilizer usage by growers in the province helped increase area and production. In Sindh, wheat production is expected to reach 20.8 million tonnes, up 13.2% over last year.

Procure-ment starts

Wheat procurement drive which started mid April in Punjab is progressing well, while it has yet to start in Sindh. The Ministry of Food, Agriculture & Livestock has fixed a procurement target of 5.3 million tonnes, with Punjab procuring 3.5 million tonnes, Sindh 0.5 million tonnes, Balochistan 0.1 million tonnes and Pakistan Agricultural Storage & Services Corporation (Passco) 1.2 million tonnes. The government will procure the crop at Rs.300 per 40 kgs. The Punjab Food Department has established 276 procurement centers. The government is yet to start wheat purchases.

In Sindh, wheat procurement season commenced early April. The Sindh Food Department which is setting up procurement centres in wheat growing areas, has so far set up 53 centres. But it is yet to start purchasing wheat from the farmers. There are concerns among the farmers of some wheat growing districts in Sindh, over the delay in the purchase of the new crop by the government. The federal government has directed the provincial governments to double the number of procurement centres, so to facilitate the farmers and ensure reasonable price for their produce.

Higher exports expected

Wheat exports are expected to continue this year in view of the bumper crop. The government has allowed Passco to export 0.3 million tonnes from the previous crop. Some 0.7 million tonnes of wheat are expected to be exported this year slightly higher over last year. Exports are mainly to countries in the Middle East, Africa and to some European and south Asian countries. Wheat exports from Pakistan commenced in 2001 as the crop output improved. Export to Iraq which was 0.1 million tonnes last year have fallen after the war. However, efforts are being made to reach a deal with Bangladesh for the supply of 0.1 million tonnes. About 0.125 million tonnes of wheat is scheduled to be shipped to East Africa, Philippines, Vietnam and the Middle East during April-June.

Rice

Area / production targets surpassed

For the 2002-03 crop, the targets for production and area have been fixed at 4 million tonnes and 2.114 million hectares respectively.

However, growers have reportedly brought larger area under this season's crop, which has been sown at over 2.201 million hectares; exceeding the targeted area by 4.1%, but still 0.4% less than the previous season. As a result of an increase in area, its production is placed at 4.228 million tonnes, exceeding the targeted area by 5.7% and 8.9% higher over the previous season's crop. The increase is mainly attributable to a rise in per hectare yield. Sindh known for growing irri-6 and irri-9 varieties has successfully produced basmati variety on experimental basis. It now expects to cultivate 0.200 million tonnes of super quality basmati.

Meanwhile, the Ministry of Food has recommended increase in prices of paddy for the 2003-04 crop, to enable farmers to meet their per hectare input cost. The input cost of paddy has gone up substantially due to a rise in the prices of fertilizer, pesticides and herbicides. Higher domestic prices and declining stocks, amid growing domestic demand, have dampened rice exports. At present 0.60-0.62 million tonnes of rice is available. About 1.23 million tonnes of rice has so far been exported, while another 0.3 million tonnes would be exported shortly. However, traders expect exports to reach 1.7 million tonnes by end season.

Cotton

Higher targets for 2003-04

For the 2003-04 crop, the Federal Committee on Agriculture (FCA) has fixed higher targets both for area and production. The production target for the new crop has been fixed at 10.55 million tonnes, 4.5% more over the previous season. It will be sown over an area of 2.86 million hectares larger by 5%. Efforts would be made next year to promote cotton cultivation in the province of Balochistan and NWFP. Sowing of the new crop is in progress in Sanghar and Nawabshah districts of lower Sindh, while it has completed in Mirpurkhas, Tharparkar and Badin districts. The sowing area for the new crop is expected to be higher in Punjab, while in Sindh it has been fixed at 0.541 million hectares. For Sindh production target has been fixed at 2.4 million bales and for Punjab 8 million bales.

Production declines

Last season, due to water shortage the area under the crop fell by 5.2% against the target of 2.9 million hectares and by 11.8% over the preceding year's crop. Despite a decline in area sown, production is estimated at 10.13 million bales, 0.6% above the target but 4.5% less than the crop of 10.6 million bales produced a year earlier. Increased usage of urea fertilizer and improved quality seeds helped improve per hectare yield by 8.3% to 626 kgs.

Pakistan Cotton Ginners Association estimates cotton production during the season, based on arrivals at the ginneries at 9.67 million bales, 4.3% less than the previous season. Punjab and Sindh recorded declines of 3.9% and 4.3% respectively. Of the total arrivals, the textile mills have purchased 8.8 million bales, while private exporters have lifted 0.14 million bales, leaving an unsold stock of 0.7 million bales.

Sugarcane

Bumper harvest

Growers have reportedly reaped a bumper 2002-03 crop. The size of the crop is currently placed at 53 million tonnes, 15.2% above the target and 10% higher over the preceding season's crop of 48.04 million tonnes. This is largely attributable to increased area sown, as well as rise in per hectare yield. While area was targeted at 0.991 million hectares, growers brought 1.096 million hectares under cultivation, 10.6% higher over the target and 9.6% more than the previous season. Per hectare yield increased by 0.5% to 48.36 tonnes from 48.1 tonnes.

Crushing operation has reportedly ended. The Pakistan Sugar Mills Association has estimated output at 3.66 million tonnes, an increase of 12.6% over the previous crushing season when about 3.25 million tonnes of sugar was produced. This season's output leaves stocks at 4.23 million tonnes, including a carryover of 0.637 million tonnes. After catering to local needs, an exportable surplus of 0.938 million tonnes would be available. The government has initially allowed export of 0.300 million tonnes through the Trading Corporation of Pakistan. The Corporation has also lifted 0.100 million tonnes of sugar under interim arrangements, which would still leave 0.500 million in stocks.

Banking and Finance

Key Monetary Indicators

(Rs. Bn)

	April 26, 2003	January 25, 2003	April 27, 2002
Scheduled Banks' Deposits	1639.5	15881.1	1392.6
Scheduled Banks' Advances	924.4	929.7	882.7
Scheduled Banks Investment in Securities & Shares	691.3	638.6	390.8
Notes in Circulation	519.8	513.4	450.8
Approved Foreign Exchange (incl. balances held outside Pakistan in approved foreign exchange)	546.7	493.9	237.7

Source: State Bank of Pakistan

Deposits continue to grow

Scheduled banks deposits grew 17.7% to Rs.1639.5 billion in the week ended April 26, 2003 against last year's corresponding figure of Rs.1392.6 billion. Compared to three months earlier figure of Rs.1588.1 billion, the current week's figure is higher by 3.2%.

Advances rise over last year

Scheduled banks advances grew over last year's corresponding figure, but was smaller over the figure recorded three months earlier. At Rs.924.4 billion it was larger by 4.7% over last year's corresponding figure of Rs.882.7 billion, but was smaller by 0.57% over the figure of Rs.929.7 billion recorded three months earlier.

Investment in securities maintains the upward trend

Scheduled banks investment in central government securities and shares continued to grow and in the week ended April 26, 2003 the figure rose to Rs.691.3 billion. This was nearly 77% larger over the corresponding figure of last year and 8.3% higher over the investments recorded three months earlier.

Notes in circulation rises

Notes in circulation rose by 15.3% to Rs.519.8 billion in the week ended April 26, 2003 against last year's corresponding figure of Rs.450.8 billion. Compared to the figure recorded at end January it was 1.2% larger.

Approved foreign exchange rises substantially

Pakistan's approved foreign exchange including balances held outside Pakistan, rose to Rs.546.7 billion at end April, more than doubling over last year's corresponding figure and a gain of 10.7% over the level recorded three months earlier.

Low Savings behind rise in public debt

The state of underdevelopment in Pakistan requires large investment which however, is constrained by limited financial resources. Pakistan's low domestic savings rate of 14.7% and low levels of tax collection at 14% of GDP are not sufficient to finance a high GDP growth rate. Comparing across neighbouring countries, Pakistan's savings rate is low in the region. India enjoys a rate of 23.8%, Bhutan 27.7%, Bangladesh 21.9%, Sri Lanka 18%.

Pakistan's lackluster savings performance can be explained among other factors by the insatiable urge for consumption, residents paying higher taxes in one form or the other with little left to save, rising public expenditure not accompanied by a commensurate growth in revenues etc.

As Pakistan cannot save enough to finance investment, it has to rely on borrowings both local and foreign. This reliance has led to large fiscal deficits and growing public debt burden. Additionally, the problem has deteriorated because resources have not been productively utilized. If government borrowings had been used to finance public development spending, the burden would have been lower as it would have contributed to higher GDP and government revenue growth.

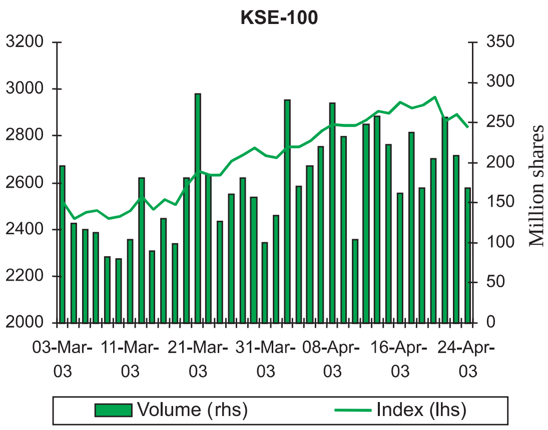
Besides low savings, structural weaknesses in public finance, deteriorating financial health of public sector enterprises, rising non-interest external current account deficits, decline in capital inflows during the 1990s were among some of the principal factors resulting in rising public debt.

In early 2000, the Government had set up a Debt Reduction and Management Committee to suggest an efficient debt management system. Among other recommendations, it spelt out the need to reduce the debt servicing cost by lowering the cost of domestic debt. Interest rates on domestic debt have been lowered significantly since July 2001 by pursuing easier monetary stance.

Market Analysis

Market Outlook

March was a very good month for the market as the KSE-100 Index gained 317 points (13%) during the month to close at 2716. After the large slide in January and early February, share levels had become very attractive and as confidence returned, buying began in March. Average daily trading volume was 141m shares. The index continued to rise for most of April, and at the end of the third week had reached a record high of 2967, up 252 points from the start of the month. The peak was short-lived however as heavy profit taking saw an immediate correction in the ensuing days.



The fundamentals going forward remain strong for the market. The correction at the end of April was a result of short-term market forces and not borne out by fundamentals. Driving the market is a healthy economic growth rate (expected at 4.5% this year), strong foreign exchange reserves and stable exchange rate, low interest rates, and the influx of liquidity in the form of foreign remittances.

Dividend yields on the blue chips are superior to yields on money market instruments, which in some cases are offering negative returns in real terms. Furthermore, dividends have a tax advantage over interest income, increasing over interest income, increasing the after-tax spread between yields of equity and money market investments (see table).

Yields on Selected Equity and Money Market Instruments
(As of 24/4/03)

(%)

Company	Yield	After-tax yield*
Hub Power Company	10.3	9.3
Unilever	11.8	10.6
P.T.C.L.	12.5	11.3
Sui Northern Gas Ltd	8.7	7.9
Sui South Gas Company	11.9	10.7
Engro Chemical	7.8	7.0
Fauji Fertilizer	11.4	10.3
Pakistan State Oil	7.4	6.7
Shell Pakistan	5.8	5.2
3-year PIB	3.2	2.1
5-year PIB	3.5	2.3
PLS bank deposit rate	3.5	2.3

** Dividends taxed at 10% for individuals (rate for corporations is lower at 5%). Interest income taxed at 35%.*

One point of concern is the recently proposed cap on equity investments by banks to 20% of their capital base. The idea behind this draft prudential regulation is that equity investing is not a core function of banks, so they should limit their activities in this area. However application of this rule would require many banks to sell off a portion of their equity investment. The proposal is not about to take effect in the near future however, as the SBP will consult with banks before making any changes to the prudential regulation final. The rule also won't apply to Islamic banks such as Faysal Bank and Meezan Bank.

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

Investment Potential of Pakistan

Low levels of investment

Investment is a key driving force for GDP growth, and declining investment levels point to low GDP growth rates. In the early 1990s, while private investment rose, public investment stagnated. Later years were characterized by a lack of continuity in economic policy and political uncertainty. Fiscal deficits rose and further constrained public finances. The burden fell on public investment, which fell from 9% of GDP in 1993 to 4.9% in 1998 because of inadequate resource mobilisation efforts. In the next three years total investment fell from 17.1% in 1998 to 13.8% in 2002.

To stimulate investment in the economy, which has continued to be low over the past decade, the government is making all out endeavours. It is focusing on reducing the cost of doing business, rationalizing the regulatory framework, maintaining continuity of economic policies among others.

Pakistan Investment Guide

More recently the Experts Advisory Cell, Ministry of Industries and Production has prepared a useful document "*Pakistan Investment Guide – 2003*", which would benefit investors in identifying the potential sectors for investment, the type of infrastructure available the different policies being pursued, existing procedures for establishing business etc.

Potential sectors identified

The first chapter identifies the potential sectors for investment. Engineering (especially automobiles), textiles, energy, fertilizer, petrochemicals & chemicals, mining, pharmaceuticals, fisheries, poultry, leather, tea cultivation and processing, software, and tourism sector have been identified among others, where prospects exist both for local and foreign investors. Going through this chapter one learns about the structure of each category of industry, alongwith various incentives that the government is offering. While the chapter provides useful insights, it lacks an objective assessment of the risks involved, and does not respond to the oft-repeated questions: "Why Pakistan? What advantages does it offer over the other locations in the region?". Moreover, the concerns with respect to the environment should also have been addressed.

Infra-structural facilities available

The chapter on Enabling Environment discusses the availability of infrastructural facilities — roads, railways, ports, telecommunications, utilities, industrial estates, the facilities available on investment in Export Processing Zones. The legal and regulatory supporting institutions that have been set up, and the financial infrastructure developed to assist growth of industries.

Initiating business

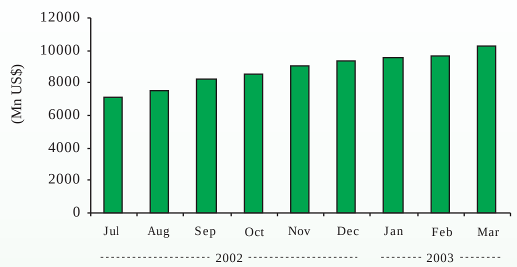
The different methods of doing business, the various requirements that have to be fulfilled for registration of a company, the documents needed for registration have been separately given for private/public companies, and foreign companies. The section also provides information on the costs of doing business, such as on various taxes and tariffs; the cost of utilities, industrial loans, and construction; and for a basket of other services..

The Guide informs its readers the procedures for obtaining a business visa. The various policies that the government has issued from time to time with regard to Textiles, Engineering, Tourism, Minerals, Engineering, Fertilizer, Investment, Trade have been given separately as Annexures.

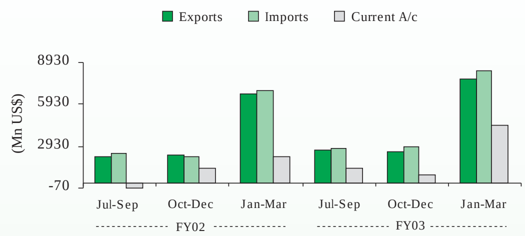
This guide is available from Experts Advisory Cell, Ministry of Industries, Islamabad, or on their website: www.eac.gov.pk.

Economic Performance at a Glance

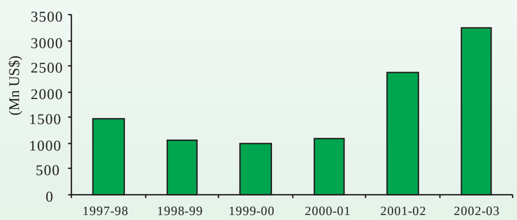
Foreign Exchange Reserves



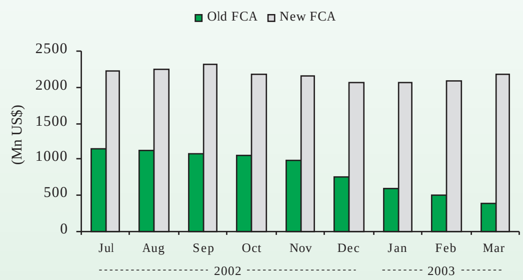
Balance of Payments



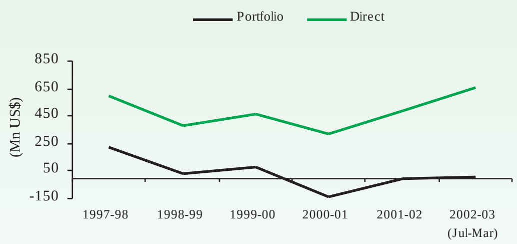
Home Remittances



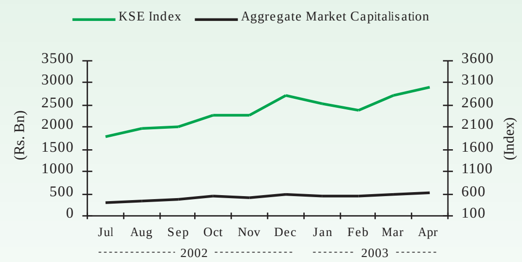
Foreign Currency Accounts



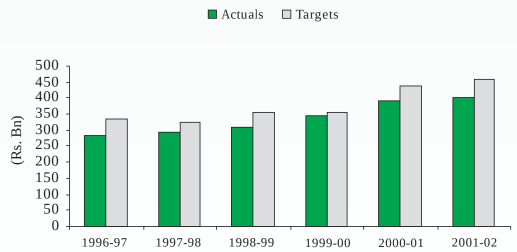
Inflow of Foreign Private Investment



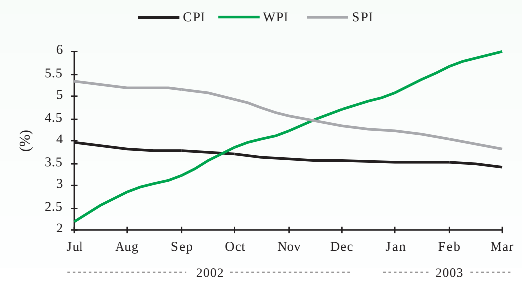
Capital Market Indicators



Federal Government Tax Collection/Targets



Price Indicators



Key Economic Indicators

Economy Size & Growth		1998-99	1999-00	2000-01	2001-02P
GNP - Market Prices	Rs bn	2912.8	3102.3	3365.4	3752.5
GDP - Market Prices	Rs bn	2938.4	3147.2	3416.3	3726.6
Per Capita Income	Market Prices Rs	21899	22811	24198	26413
	Market Prices US $	438	441	414	427
Growth					
GDP	%	4.18	3.91	2.45	3.61
Agriculture	%	1.95	6.09	-2.64	1.39
Manufacturing	%	3.73	1.53	7.58	4.39
Services	%	4.99	4.79	4.79	5.09
Rate of Inflation	%				
Consumer Price Index		5.7	3.6	4.4	3.5
GDP Deflator		5.5	2.8	5.6	4.6
Balance of Payments	$ mn				
Exports (f.o.b.)		7528	8190	8933	9133
Imports (f.o.b.)		9613	9602	10202	9493
Trade Balance		-2085	-1412	-1269	-360
Services Account (Net)		-2618	-2794	-3142	-2620
Private Transfers (Net)		2274	3063	3898	4255
Current Account Balance		-2429	-1143	-513	1275
Fiscal Balance	% of GDP				
Total Revenue (Net)		15.9	17.1	16.0	17.1
Total Expenditure		22.0	23.6	21.3	23.7
Overall Deficit		6.1	6.6	5.3	6.6
Domestic & Foreign Debt					
Domestic Debt	Rs bn	1375.9	1559.9	1712.5	1695.5
As % GDP		46.8	49.6	50.1	46.0
Total External Debt	$ bn	31.3	32.3	32.1	33.4
Total Debt Servicing	Rs bn	343.1	353.9	340.3	412.5
As % GDP		104.2	105.4	113.2	102.0
Investment & Savings	% of GNP				
Gross Investment		15.6	16.2	16.2	13.8
Fixed Investment		14.0	14.6	14.5	12.2
National Savings		11.8	14.3	15.3	13.8
Domestic Savings	% of GDP	12.9	15.8	16.9	13.8
Foreign Investment	$ mn	403.3	543.4	182.0	474.6
Portfolio		27.3	73.5	-140.4	-10.0
Direct		376.0	469.9	322.4	484.7
Monetary Aggregates	%				
M1		33.9	14.9	3.0	14.9
M2		6.2	9.4	8.9	14.8
Interest Rates (Weighted Average)	%				
Deposits*		7.96	6.62	6.58	4.60
Advances		14.8	13.52	13.61	13.19
Gold & Foreign Exchange Reserves	$ mn	2922	2766	3810	6997
Exchange Rate++	Rs./$				
Official Rate		51.6	52.16	64.4	60.05
Open Market Rate		54.4	54.82	66.7	60.20

P Provisional
* PLS & Interest bearing
++ End-June Buying Rate

Source: Annual Report 2001-02
State Bank of Pakistan

NBP Performance at a Glance

(Rs. Bn)

Items	1998	1999	2000	2001	2002
Net Fund Base Income	8.9	10.4	8.8	12.4	12.8
Non Fund Base Income	2.7	4.0	4.0	4.5	4.8
Administrative Expenses	6.2	7.9	8.0	8.6	9.1
Pre-Tax Profit	2.14	0.52	1.03	3.02	6.04
After-Tax Profit	0.53	0.03	0.46	1.15	2.25
Total Assets	325.1	350.4	371.6	415.1	432.8
Deposits	273.4	294.8	316.5	349.6	362.9
Advances	109.5	122.6	140.3	170.3	140.5
Investments	103.0	91.5	72.6	71.8	143.5
Shareholders' Equity	10.0	10.4	11.4	12.0	14.3
Number of Branches	1434	1431	1428	1245	1204
Number of Employees	15785	15541	15351	15163	12195