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Editor's Corner

Dear Readers,

The economic reforms pursued since the last six years have resulted in significant improvement in Pakistan's macroeconomic fundamentals. The economy grew by 8.4% in 2004-05, largely due to high growth recorded by the commodity producing sectors, exports have exceeded the year's target, a revival is witnessed in investor confidence, as foreign direct investment has risen to $1 billion, imports of capital goods and machinery, chemicals have risen, implying a pick up in investment activity, development budget has been given a significant boost, workers' remittances are higher, public debt has fallen to 59.4% of GDP, and the launch of Eurobond and the Islamic Sukuk bonds have received good response from investors in the international capital market.

There are a few areas however, where more needs to be done, although a start has been made. One such is the multifaceted issued of poverty, which continues to create problems, both for policy makers and millions of households.

Pakistan has adopted a national Poverty Reduction Strategy Programme, which is all encompassing; promoting pro-poor growth, creating opportunities for employment, improving governance, with the provincial and local governments playing a major role; investing in human capital and targeting the poor and vulnerable. By identifying several pro-poor sectors, the Fiscal Responsibility Law obliges the government of Pakistan to spend at least 4.5% of GDP on these sectors.

Pro-poor budgetary expenditures have increased in recent years; in absolute terms from Rs.167.3 billion in 2001-02 to a budgeted Rs.324 billion in FY06. As a percentage of GDP it is 4.65% for FY06; the ratio is expected to increase to 6.5% by 2009-10. This increase has been made possible mainly due to government's medium term fiscal strategy aiming to create fiscal space for higher levels of social and poverty spending.

Raising allocation for the marginalized and undertaking specific poverty targeted interventions, would to some extent contribute towards alleviating the miseries of millions of households, who have not been touched by the high economic growth rates.

As the government makes effort to sustain the high growth rate (GDP) achieved in the last two years, it also emphasizes that the benefits of economic growth reach the lowest segments of the population.

This year's budgetary allocations for sectors, which have a bearing on poverty reduction have been raised and some new programmes like the Khushal Pakistan programme with a Rs.7.5 billion budget are targeted to undertake programmes like, supply of clean drinking water, sanitation, electricity, farm to market metal roads. While the community can use the funds in the areas of their choice but this is limited to execution through government agencies. One hopes that productive use of resources would be made. In this budget, the worker's minimum wages have been raised from Rs.2500 to Rs.3000. While this is a nominal increase, and can in no way meet the rising costs of an expanding family it is still a step towards betterment.

Microfinance institutions are gradually increasing their outreach, and so far half a million families have benefited, with the numbers expected to increase to a million within a year. However, interest costs are substantially higher than for those who are better off, and targeting remains poor. Small and medium enterprises are being promoted, with the commercial banks gearing up to play an effective role. The government has established a Business Support Fund through which small business loans would be provided. One hopes that this will be on merit alone. All of these are targeted towards creating gainful employment which is perhaps one of the most significant factors, to help reduce poverty.

Studies have shown the specific roles that public investment plays in poverty alleviation. While welfare programmes and employment schemes have a direct bearing on the poor, the indirect effects arise when governments make investments in rural infrastructure, health and education all of which leads to greater employment and income earning opportunities for the poor, gives people choices regarding the kinds of lives they wish to lead.

The Federal Budget 2005-06 has enhanced development expenditure with focus on the development of infrastructure and social sectors. Effective social development programmes would enable the disadvantaged groups to benefit from the expanding opportunities that growth offers. It has been experienced that infrastructure development has the greatest impact on economic growth and poverty reduction. The measures adopted in the Budget are in the direction of achieving the ambitious targets of the Millennium Development Goals by 2015, which among others seeks to eradicate extreme poverty and hunger.

Ayesha Mahmud

Abstract of the Bulletin

Federal Budget 2005-06 – A Review

- § In the outgoing fiscal year, GDP grew by 8.4%, with both the agricultural and manufacturing sectors surpassing the respective targets set for the year.
- § Supported by substantial growth in credit to the private sector at low rates, large scale manufacturing grew by 15.4%.
- § Trade deficit widened as imports exceeded the year's target. Exports also grew but at a relatively slower pace.
- § Workers' remittances showed an upward trend.
- § Construction and the housing sector showed sustained growth.
- § The Federal Budget 2005-06, has a total outlay of Rs.1098 billion. Of this, 75% is the current expenditure and 25% development expenditure.
- § Development expenditure budgeted for FY06 shows an increase of 35% over revised estimates of FY05, while current expenditure is higher by 5.3%.
- § Tax collection targets were met during the year.
- § Significance of sales tax has grown over the years, contributing 58.7% of indirect taxes.
- § Tax revenue (other than CBR) more than halved the budgeted amount (Rs.74.8 billion) in FY05, primarily due to substantial fall in revenue accruing from petroleum development levy.
- § In FY-05, external resources were higher due to receipt of Rs.35.8 billion from Sukuk Bonds.
- § Bank borrowings are a major source of financing the deficit.
- § The Budget has announced specific measures for promotion of exports, raising the level of investment, agricultural sector, SMEs, the salaried class, and for the poor.

Provincial Budgets

- § Provincial governments have raised the size of their budget outlays, spending increased amount on developmental activities in their provinces.
- § The Sindh government has proposed relief in pay and pension to the provincial government employees.
- § In Balochistan, the government would not be charging any fees, except the admission fee in all state run institutions upto the intermediate level.
- § In Punjab, the budget allocates 43% of the development expenditure for infrastructure, while 35% has been earmarked for social sectors.
- § In NWFP, the budget has no new taxes.

Pakistan Millennium Development Goals

- § Pakistan is a signatory to the UN Millennium Declaration and has adopted the millennium development goals to achieve pro-poor economic growth.
- § For the full implementation of MDGs, a Poverty Reduction Strategy Paper has been prepared, and targets and indicators set for proper monitoring and evaluation.
- § The Government has also developed the Medium Term Development Framework which complements the PRSP

PTCL Privatisation

- § The government of Pakistan has sold 26% shares of PTCL to Etisalat for $2.59 billion (Rs.155.16 billion).
- § Etisalat was the highest bidder with $1.96 per share offer. The other two, China Mobile offered Rs.63.48 per share, while Sing Tel offered Rs.52.54 per share.
- § 90% of the proceeds would be used to retire debt, while 10% are meant for poverty reduction.

Market Analysis

- § Top performers during May-June 05 period were PTCL, NBP, BoP, SNGP and OGDCL.
- § The Badla/COT financing is being replaced with margin financing.

Trade Policy 2005-06 - Highlights

- § For FY06, exports are targeted at $17.0 billion.
- § Incentives given to increase exports, will focus on diversification, increased market access, reduced costs, improve quality, and provision of quality infrastrure, technical training etc.

Federal Budget 2005-06 – A Review

Back-ground to the Budget

The economy has stabilized and for the third consecutive year it has attained high growth rate. The resilience in the economy is attributable to higher than targeted growth of the three sectors, agriculture, manufacturing and services, supported by strong credit growth. Economic targets set a year earlier, have in most instances been surpassed; a low interest rate environment has spurred private sector credit growth with large scale manufacturing recording double digit growth accompanied by significant growth of consumer durables. Enhanced domestic economic activity and higher level of investment, led to a surge in imports especially of machinery, chemicals. There has been a major increase in development expenditure, while current expenditure has been contained. Fiscal deficit has come down. The Federal Budget 2005-06 has been presented against a backdrop of good macro performance.

Targets/Achievements

(%)

		2004-05		2005-06
		Target	Achievement	Target
GDP		6.6	8.4	7.0
Agriculture		4.0	7.5	4.8
Manufacturing		10.2	12.5	11.0
Large Scale		12.0	15.4	13.0
Services		6.2	7.9	6.8
Total Investment as % of GDP		18.8	16.8	18.1
National Savings as % of GDP		19.1	15.1	15.9
Inflation (CPI)		5.0	9.28	8.0
Exports	$bn	13.7	14.4	15.67
Imports	„	16.7	20.6	19.83
Trade Deficit	„	1.33	6.2	4.16
Remittances	„	4.0	4.2	4.02

Source: Pakistan Economic Survey 2004-05 Government of Pakistan

Growth picks up

GDP growth of 8.4%, the highest in South Asia, has been accompanied by a higher agricultural output, as timely rains improved water flows for irrigation purposes and also increased the availability of stored water for next season's crop. Cotton output surpassed 14 million bales, while wheat the staple diet of the people achieved a sizable crop of 21 million bales. Major crops registered a growth of 17.3%, against 1.8% last year.

Manu-facturing shows improve-ment

Supported by substantial growth in credit to the private sector, at low rates of interest, large scale manufacturing grew by 15.4%. The auto and electronics sub-sector benefited from the availability of consumer credit. Substantial amount was invested in BMR of textiles sub-sector and for its higher value addition. This resulted in increased production and textile exports rose to nearly $10 billion. The sustained growth in the construction and housing sector pushed the growth of cement, paints and varnishes, glass sheets, wood etc.

Funda-mentals improve

On the external front, the trade deficit widened to an estimated $6.2 billion, as imports ($20.6 billion) exceeded the year's target ($16.7 billion) during the fiscal year 2004-05 and more than offset the increase in exports. Workers' remittances showed an upward trend. The current account balance showed a deficit, as against surplus a year earlier, due mainly to widening of trade deficit and higher net outflows under services account. Foreign exchange position remained comfortable and net foreign private investment crossed $1 billion.

Challen-ges

While the economy has attained high growth, it continues to face several challenges. Social indicators are not favourable and require massive intervention to bring improvement; poverty continues to affect millions of households; investment activity has picked up but there is a need for an improved investment climate; economic governance has to be improved so that the benefits of growth reach the target of poverty reduction and price increases of items of daily consumption need to be checked.

The Federal Budget 2005-06 takes forward the initiatives adopted in FY00, when the government adopted an economic framework, which seeks to reduce the social disparities and thereby poverty, have sustainable growth in the economy, continue with the structural reforms, which in other words is the second phase of reforms aimed at strengthening institutional capacity and improving economic governance.

Revenue Receipts to Grow

Non-tax receipts increase

Revised estimates of revenue receipts for 2004-05, show an increase of nearly 10 percent over the budgeted amount. While tax collection by the Central Board of Revenue (CBR) is estimated to rise by Rs.10 billion (1.7%), non-tax receipts show a substantial jump of 76%. A disaggregation of non-tax receipts shows that income from dividends, interest (public sector enterprises & others) and defence were the major contributors towards the higher accruals. Under receipts from defence services, Rs.58 billion accrued from miscellaneous sub-head. Dividends represent the return on federal governments investment in the share capital of financial institutions and commercial enterprises. Substantial increase was recorded from investment in the shares of OGDC and PTCL.

Income from dividends / interest rises

For fiscal 2005-06, non-tax revenue is budgeted at Rs.194.8 billion, nearly 22% lower over preceding year's revised figures, as receipts from defence services are expected to fall.

CBR has exceeded the tax revenue target by Rs.10 billion. Direct taxes as per revised estimates have risen by 13% to an estimated Rs.182.7 billion, compared to a year earlier. Major portion of the collection originates from the corporate sector. Within the corporate sector, the public sector companies, are the major contributors whose income tax rates have been brought down to 35% and for banking companies it has been progressively reduced from 47% to 38%. Similarly rates of tax on private limited companies is proposed to be reduced to 37% for the tax year 2006.

Large tax collected from corporate sector

Capital value tax rose to Rs.4 billion, against last year's revised figure of Rs.2.3 billion (it was budgeted at Rs.650 million). Leviable on imported motor vehicles at the import stage, the higher figure implies large imports of automobiles.

Indirect taxes comprising of sales tax, central excise duties and customs duties, are estimated to have exceeded the year's target. For FY06 these are budgeted at Rs.474.6 billion.

The significance of sales tax has grown over the years, presently contributing 58.7% of indirect taxes or 40.5% of tax revenue. The tax base has gradually broadened, including both domestic manufacturers and retailers, as well as importers, wholesalers, dealers and specified services @15%.

Federal Government Revenue Receipts

	2004-05		2005-06
	Budgeted	Revised	Budgeted
Total Revenue Receipts	796.3	875.3	927.4
Tax Revenue CBR	580.0	590.0	690.0
Direct Taxes	181.9	182.7	215.4
Taxes on Income	174.4	175.4	205.9
Other Taxes	7.5	7.3	9.5
Indirect Taxes	398.1	407.3	474.6
Customs	103.2	113.9	121.2
Sales Tax	249.2	239.0	294.0
Federal Excise	45.7	54.4	59.4
Tax Revenue (other than CBR)	74.8	36.3	42.6
Petroleum development levy	47.5	10.9	15.9
Surcharge on natural gas	15.0	14.7	16.6
Others	12.3	10.7	10.1
Total Tax Revenue	654.8	626.3	732.6
Non Tax Revenue	141.5	249.0	194.8
Interest	54.0	61.1	51.1
Dividends	34.8	57.5	53.0
Receipts from civil administration	15.3	74.0	33.0
Others	37.4	56.4	57.7

Source: Annual Budget Statement 2005-06 Government of Pakistan

Despite this, revised estimates for 2004-05 show that sales tax collection declined by 4% against the year's target of Rs.249 billion. This could partly be explained by lower collection from cigarettes, cement and sugar. For the former, it was due to withdrawal of tax which proved beneficial for the cigarette distributors. For the cement sector, while their taxable sales have risen and also the retail price of cement, the tax receipts have shrunk. A similar situation prevails for the sugar industry.

Sales tax collection falls

Sales tax collection from imports improved because of a pick up in imports in FY05, especially of petroleum and products and machinery. For FY06, sales tax collection is budgeted to be higher by 23% at Rs.294 billion.

The share of customs duty collection to total indirect taxes has been reduced to 28%, as a consequence of tariff reforms implemented by successive governments since 1990-91. These are levied at import stage and charged on dutiable imports.

Gross collections from customs duty are estimated to have risen by 8.7% over the year's target, but after adjustment for refund/rebates, the revised figures show a growth of 10.4%.

Custom duties rise

Higher accruals have been recorded from machinery, chemicals, vehicles and plastic resins etc. 'Other items' category showed a 19% jump over the budgeted figure. A rise in customs duty is attributable to higher trade transactions, improvement in the customs business processes and efficiency gains.

During the year there have been revisions in the duty structure within the existing slabs, with reduced duty for capital goods and smuggling prone items. For FY06, gross customs duty is budgeted at Rs.142.47 billion.

CED rises

Central excise duty is levied on domestic production of selected commodities like cement, cigarettes, natural gas etc. In the outgoing FY05, central excised duty (CED) showed an increase of 19%, unlike past years when collection was declining. Central excise duty has declined over the years due to withdrawal of additional commodities from CED net and bringing them within the ambit of GST. In the last Budget, excise duty was withdrawn from paints and varnishes and syrups and squashes. The number of items subject to CED has been reduced and only those items will in future be subject to this tax whose consumption is required to be regulated eg cigarettes, beverages, cement.

Revised estimates of federal excise collection place it higher at Rs.54.4 billion, attributable to substantial accruals from cigarettes & tobacco and cement. These together contribute 63.8% of the total collections. For FY06, federal excise collection is budgeted at Rs.59.4 billion.

CBR Tax Collection
Target & Revised

(Rs. bn)

	2000-01		2001-02		2002-03		2003-04		2004-05		2005-06
	Target	Revised	Target	Revised	Target	Revised	Target	Revised	Target	Revised	Target
Gross Revenue Receipts	594.6	557.9	643.8	632.8	674.9	701.6	728.4	760.9	796.3	875.3	927.4
Tax Revenue	435.7	406.5	457.7	414.2	460.6	458.9	510.0	510.0	580.0	590.0	690.0
Direct Taxes	137.5	133.9	149.8	146.5	148.4	145.0	161.1	161.5	181.9	182.7	215.4
Indirect Taxes	298.2	272.6	307.9	267.7	312.2	313.9	348.9	348.5	398.1	407.3	474.6
Customs	73.0	64.6	69.6	50.5	56.05	69.6	78.1	86.6	103.2	113.9	121.2
Federal Excise	53.4	52.2	53.1	47.1	50.0	46.5	47.7	43.5	45.7	54.4	59.4
Sales Tax	172.6	155.8	185.2	170.1	205.7	197.8	223.1	218.4	249.2	239.0	294.0
Surcharges	38.0	33.0	47.0	53.9	60.5	66.9	61.1	64.4	65.3	27.1	32.5
Non-Tax Revenue	120.9	118.4	139.1	164.7	153.8	175.8	157.2	180.8	141.5	249.0	194.7

Source: - Federal Budget in Brief, Various Issues Government of Pakistan

Revenue other than CBR

Revised estimates for FY05 show a major reduction in tax revenue (other than CBR). These have more than halved the budgeted amount, primarily due to a substantial fall (77%) in revenue accruals from petroleum development levy. Before the deregulation of prices of petroleum products, development surcharge was quite substantial (Rs.46 billion in FY05).

Surcharge on natural gas fetched Rs.14.7 billion, slightly lower against the target of Rs.15 billion. The difference between the sale price for consumers and the prescribed price for the gas companies is the margin available to the government as surcharge. These resources are subsequently transferred to the provinces according to the production of gas in a province.

Capital receipts

Net capital receipts showed a decline of 63.3 percent over the budgeted figure of Rs.64.4 billion.

The disaggregated figures of capital receipts reveal that the decline was primarily due to a sharp reduction in the permanent debt of the government (budgeted at Rs.44.1 billion, revised figure Rs.4.7 billion) and receipts from prize bonds (revised figures Rs.7 billion against the budgeted figure of Rs.27.5 billion). This was accompanied by larger disbursement — on account of government investments loans, advances and others, which rose to an estimated Rs.51.27 billion against the budgeted Rs.11.6 billion.

Capital Receipts

(Rs.bn)

	2004-05		2005-06
	Budget	Revised	Budget
Receipts	103.2	76.4	86.7
Recovery of Investment	0	3.0	0
Recovery of Loans	28.5	60.1	31.3
Permanent Debt	44.1	4.7	18.7
Floating Debt	30.1	12.0	20.0
Public Account	0.46	(-)3.4	16.6
Disbursement	38.7	52.7	36.1
Net Capital Receipts	64.4	23.7	50.6

Source: - Annual Budget Statement 2005-06

External resources exceed target

To meet its capital and development expenditure, the government obtains external loans and grants. While the fiscal year 2004-05 budgeted external assistance for Rs.156.3 billion, these were 26.4 percent higher at Rs.197.6 billion. This increase was due to the receipt of Rs.35.8 billion from Sukuk Bonds. The first sovereign Islamic Sukuk issue was offered early this year and against a total subscription of $1.2 billion, the government accepted $600 million.

Project aid contracted by the federal and provincial governments declined by 17.5% to a revised estimate of Rs.46.5 billion in FY05, while commodity aid (non-food) was higher at Rs.78.6 billion against the budgeted figure of Rs.54.6 billion. For FY06, external resources are set at Rs.212.3 billion.

Budget size

The Budget for FY06, has a total outlay of Rs.1098.5 billion, where current expenditure accounts for 75 percent and development expenditure 25 percent. In the outgoing fiscal year, revised development expenditure met the year's budgeted figure, while current expenditure had to be revised upwards by 12%, due among others, to higher foreign loan repayments, servicing of domestic debt, larger transfer payments, substantial increase of expenditure under general economic, commercial and labour affairs etc.

Current expenditure raised

For FY06, current expenditure has been raised by 5.3% from Rs.784.7 billion to Rs.826.5 billion, as servicing of domestic debt rises to Rs.190.2 billion against Rs.180.0 billion a year earlier and foreign loan repayments increase by 20.4% and servicing of foreign debt by 13.4%.

The size of the defence budget has been contained as the government allocates more resources for development. Constituting 19.7% of the total outlay for FY06, its allocation has been raised to Rs.223.5 billion against Rs.216.2 billion in FY05.

PSDP larger

Public sector development programme is budgeted at Rs.272 billion, 34.7% higher over Rs.202 billion in FY05. Ongoing developmental activities have been given a significant boost. Last fiscal year, unlike previous years, the development programme was implemented in full. Infrastructure development, (including water sector, communication) is to receive 34% of the development budget, while the social sector has been allocated 27%. In the later category, one-fourth of the resources will go towards the special programmes undertaken by the government. Emphasis is on human development, including education, health and poverty reduction measures.

Broad Sectoral Distribution
of PSDP

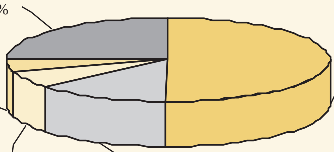
(Rs. bn)

Infrastructure	92.3
Social Sectors	73.1
Other Sectors	38.6
Federal	204.0
Provincial	68.0
Total	272.0

PSDP for FY06 reflects the objectives of the Medium Term Development Framework. As Pakistan is also a signatory to the Millennium Development Goals, this year's development budget moves towards the development of regions and various social groups, development of human capital and reducing poverty.

The total available internal resources of a sum of Rs.768.0 billion budgeted for fiscal 2005-06, falls short of the expenditure requirements of Rs.1098.5 billion. This shortfall of Rs.330.5 billion, would be met through external resources, privatization proceeds and bank borrowings.

Public Sector Development Programme
2005-06



Of the total external resources, 37.4% would come from commodity aid utilized for commercial imports of commodities — these are generally industrial raw materials, equipment & spares, chemicals, fertilizers etc. Other aid, generally by way of balance of payment support is expected to increase by 12.6%, as Rs.30.5 billion is budgeted to come from global bonds and a similar amount from the Islamic Development Bank.

Financing through privatization proceeds are budgeted to double to Rs.20.0 billion, from revised estimates of Rs.10 billion in the last fiscal year, as some public entities are privatised. Bank borrowings of Rs.98.0 billion would cover the remaining shortfall.

Financing the Deficit

(%)

		2004-05		2005-06
		Budget	Revised	Budget
Deficit	Rs.bn	213.1	246.0	295.0
Non-Bank Borrowing		35.1	5.4	18.8
Net External Resources		36.7	57.7	41.2
Bank Borrowings		21.2	32.8	33.2
Privatization Proceeds		7.0	4.1	6.8

Source: - State of the Economy Annual Review, June 2005 Social Policy & Development Centre

The budget deficit for 2004-05 is estimated at 3.2%, which is expected to increase to 3.8% in the forthcoming fiscal year. Development expenditure has been raised by 35%, while current expenditures will increase by 18%.

The financing of the deficit is shown in the above table. Dependence on external resources has increased and revised estimates for FY05, show that more than half of the deficit was financed from these resources. In FY06, its share is expected to come down to 41%. Bank borrowings are another major source of financing the deficit.

Implications of the Federal Budget

The Federal Budget has far reaching implications for the various sectors of the economy. We shall focus on some of the areas.

Exporters

With increased competition in the international market in the post quota regime, Pakistani exporters would have to gear up by adopting quality standardization, state of art technology, diversified products among others to gain an edge. They require support from the government in the form of reduced duties/taxes paid and lower production costs to remain competitive.

Sales tax refund process

One of the major irritants, the exporters had been complaining about was the sales tax refund process. It was a long standing demand of the exporters to rid them of this obstacle, for a lot of their time was wasted on getting the sale tax refunds. This issue has been addressed in this year's Budget.

The entire chain of textile and articles of textile, leather and articles thereof, carpets, surgical and sports goods have been zero rated. All the raw materials and inputs, including those consumed in these industries will be zero rated. This measure will improve the cash flow problems of exporters, which should subsequently increase their competitiveness in the world market.

Import and supply of inputs/raw materials used in the manufacturing of plant and machinery which is chargeable to sales tax at rate of zero percent, shall be zero-rated for the purpose of levy of sales tax.

Investment

Investment is the key to sustain the high growth rates achieved during the last two successive years. Investment as a proportion of GDP has not shown any significant increase, hovering at around 17 percent, despite the wide ranging structural reforms introduced, specific measures undertaken to revive investment and the access to a developed financial system.

Factors affecting invest-ment

There are a number of impediments facing the government, which have constrained investment levels rising in the economy. The Medium Term Development Framework 2005-10, states, 'the cost of doing business remains high due to bureaucratic hurdles and red tapism , resulting in higher transaction costs, high utility prices, multiplicity of taxes and their high rates. The legal and regulatory infrastructure also needs improvement.

In the outgoing FY2004-05, the interest rate environment remained relatively investment friendly and the year witnessed enhanced credit growth to the private sector; private sector credit rose by Rs.362 billion. Inflow of foreign investment picked up, which until recently was low. Investment climate has to be further improved to bring about any meaningful amelioration in the levels.

The current year's PSDP focuses on the development of infrastructure. The improvement in infrastructure by the public sector would crowd in the private sector because it would reduce the cost of establishing an enterprise.

Duties / Taxes lowered / exempted

Exemptions and cuts in duties/rates has been allowed in the Budget to encourage investment. Customs duty on basic raw materials for chemical, pharmaceuticals, textiles, confectionary and soap industry exempted or reduced; to promote investment of capital and engineering machinery making industry, duty structure is proposed to be rationalized; raw material, components and sub components to manufacture home appliances are proposed to be given reduction in customs duty among other such reductions.

Other measures

Besides the positive budgetary measures to reduce poverty, increase exports, raise the investment level in the economy, steps has been taken for the development of the agricultural sector, increasing employment opportunities, by focusing on the development of small & medium enterprises, increasing the outreach of micro loans so that people can start some small job and earn a livelihood for themselves, opening of training institutes at district and tehsil level so that young men receive technical training and village products are to be promoted.

Government employees have been provided a relief package, and while social sector spending shows an increase, the poor social indicators, require massive intervention to improve them. Needs of the poor are enormous for they have been neglected far too long and though steps have taken and larger allocations made to address issues related to poverty, results would take some time.

Another worrying aspect is the pick up in the inflation rate since last year, which is in double digits now. Rising prices of utilities, items of daily consumption badly affects the poor man's pocket. One hopes that with the tightening of monetary policy, the mounting inflationary pressures would be curbed.

Budgetary Measures

The Budget has announced certain specific tax policy measures for the focused sectors of the economy. This section highlights some of the tax initiatives.

Relief for salaried class / senior citizens / and others	*Industrial Sector*	*Agriculture*	*Poverty/Rural Development*	*Exports*	*Energy*
• Income tax rates for the salaried class reduced from a higher range of between 7.5% to 35% to a lower slab ranging from 3.5% to 30% proposed. • Annual statement filed by the employer proposed to be considered as sufficient discharge of liability to file a return on the part of the employee. • Tax rebate to teachers and researchers proposed to be enhanced from 50% to 75%. • Senior citizens are presently allowed tax rebate at 50%, subject to the upper income limit of Rs.300,000/=. This limit has been enhanced to Rs.400,000/=. • Exemption to employees proposed in respect of perks carrying zero marginal cost to the employers. • Monetary limit of investment for claiming tax credit in the prescribed shares of listed companies and TFCS is proposed to be enhanced from Rs.100,000 to Rs.150,000 • Exemption proposed for insurance companies in respect of capital gains derived from sale of shares. • Reduction of 1% in tax proposed for new enlistment on stock exchanges. • Concept of group relief proposed to be extended to services sector. • Reduced corporate tax rate of 20% applied to those SMEs that transform into companies, and no turnover tax would be payable by them. • Withholding tax @6% imposed on purchase of new cars. • Minimum wages revised from Rs.2500/= per month to Rs.3000/= per month. • Income from certain services rendered abroad proposed to be taxed @1%.	• Customs duty on raw material for chemicals, pharmaceuticals, confectionary, soap and toilet preparations reduced. • Duty on over 200 items reduced to boost the textile sector. • Components like compressors and evaporators used in the manufacture of deep freezers and air conditioners exempted from duty. • Import of raw material/components for assembling computer monitors, TV, refrigerators, washing machines are proposed to be given reduction in customs duty. • Machinery, equipment and parts used by the civil aviation and tourism industries exempted from customs duty. • Imports for infrastructure projects at Gwadar have been exempted. • Karachi Textile City is being established. • Garment Cities being set up in Karachi and Lahore. • Machinery imported for the ginning industry to be exempted from customs duty. • Customs duty on 55 plastic goods items reduced. • Duty on raw material for zinc and chrome coating is proposed to be exempted. • To promote investment in engineering machinery making industry their duty structure rationalized. • Customs duty on all bicycle parts reduced from 35% to 25%. • Reduced duty on raw materials used in the production of man made fibres. • Rate of withholding tax on ships imported for the purpose of breaking reduced from 3% to 1%.	• Duty on import of tractor in CBU condition reduced from 20% to 15%. • Import of agricultural machinery like bulldozers, angle dozers, graders and levelers proposed to be exempted from payment of customs duty. • Customs duty reduced on some raw materials, especially vitamins used in the poultry feed. • 10,000 water courses would be lined. • Allocation for agriculture has been increased from Rs.7 billion to Rs.9.1 billion. • In FY05, Rs.21 billion was spent on the water project of WAPDA, and this year the allocation has been doubled to Rs.43 billion. • 5% customs duty on urea withdrawn. • New canals and small dams to be constructed. • Exemption of custom duty on import of ginning machinery.	• A special programme developed for 32 less developed districts of the country. • Number of people who will benefit from micro financing to increase to 3 million during the next four years. • By 2007, Khushali Bank to make 563,000 micro loans available. • Rs.7.5 billion will be spent under the Khushal Pakistan Programme next year. • Under this programme, clean drinking water, sanitation, electricity and farm to market metal roads will be provided. • Under the Programme, young people will get local jobs. • Basic health programme for women being initiated in all the provinces. • Government is establishing an institution; NTEVTA to provide professional and technical training to 300,000 young people every year. • Village products to be promoted. • 13000 villages to be provided with electricity.	• Suitable changes being made in the DTRE Scheme. • Zero sales tax on the import and supply of raw materials and parts used in the manufacturing of plant and machinery. • Reduction in duty drawbacks due to zero rating of major inputs used in textile, leather, surgical and sports goods.	• Rs.15.58 billion allocated for projects of power sector under the National Development Programme. • Work to begin on Neelum Jhelum Hydro Electric Plant. • The plant to produce 969MW electricity. • Alternate Energy Board set up for developing alternate sources of energy. • Liquefied petroleum gas to be used in 2.1 million households against 1.8 million households that currently use it.

Box

Economy at a Glance 2004-05

Growth Trends

- GDP grew by 8.4%, surpassing the target of 6.6%; the highest growth in the South Asian region.
- Agriculture grew by 7.5% against the target of 4%, large scale manufacturing 15.4% against 12.2 and services sector by 7.9%.
- Major crops grew by 17.3%, Cotton output is estimated at 14.6 million bales against previous year's 10.0 million bales; rice production rose to nearly 5.0 million tones against 4.8 million tones, while wheat is estimated at 21.1 million tones against 19.5 million tones a year ago.
- Agricultural loans disbursed amounted to Rs.73.8 billion, (July-March) against Rs47.9 billion during the corresponding period last year. Loans given by commercial banks surpassed Zarai Taraqiati Bank for the third consecutive year.
- The main contributors to the impressive large scale industrial growth are textiles, chemicals, petroleum, electrical items, and automobiles.

Investment

- During the last five years, there has been an investment of $5.0 billion in the textile sector for modernization and higher value addition.
- 46% of total investment has gone to the spinning sector, followed by weaving (24%), textile processing (12%), made ups (8%) and knitwear, garments and synthetic textiles (5%each).
- Foreign private investment crossed $1.6 billion during July-June FY05. FDI was $1.5 billion during this period, against $949mn in FY04.
- Over 54% of FDI has come from the US, UK and Switzerland and substantial amounts from UAE and Japan.
- The major sectors which attracted FDI include, banking, oil and gas, telecom, chemicals, fertilizers, pharmaceuticals and power sector.
- So far 146 units have been privatized for a sum of Rs.148 billion.

Fiscal & Monetary

- Fiscal Responsibility Law has been passed by the Parliament. This would encourage responsible fiscal management by all governments.
- Public debt to GDP ratio declined to 59.4%.
- Public debt consists of debt payable in rupees and debt payable in dollars. The share of debt payable in rupees had increased while the later had declined. But in the outgoing fiscal year, both rupee and dollar component of public debt are evenly balanced.
- Domestic debt is estimated at 30.8% of GDP.
- There has been some decline in the burden of interest payments on domestic debt.
- Its share in total expenditure declined from 30% to 16%, during the last six years, while as percentage of GDP, interest payments fell from 6% to 2.6 percent in the last six years.
- There was a gradual shift in the monetary policy stance, as rising inflation became a source of concern.
- Treasury bill rates were raised gradually to 7.08% by April 2005.
- Private sector credit rose by a record Rs.370 billion.
- Monetary Assets (M2) grew by 13.1%, a fall from a growth of 19.6% in the preceding year.
- Discount rate was raised by 1.5 percentage points from 7.5% to 9.0%.
- SME's sector share in total private sector credit rose from 8% to 18% in the last one year.
- The economy became more monetized as seen by the M2/GDP ratio. The ratio increased to nearly 45% in FY05 and during July-March 2004-05 it was 42.9%.
- The Karachi Stock Exchange became one of the best performing markets around the world.
- Net accruals with the National Savings Scheme declined by Rs.10.9 billion during July-March 2004-05, as against net receipts of Rs.5.7 billion in the same period a year earlier.
- Massive withdrawals from the NSS was mainly due to ban on institutional investment and decline in the rate of return on NSS.

Prices

- Consumer Price Index rose by 9.28 in 2004-05
- The contributory factors to the rise in inflationary pressures, was among others due to an increase in demand in the economy, alongwith supply constraints of principal commodities. The surge in international oil prices impacted domestic price level.

Trade & Balance of Payments

- Trade deficit surpassed the year's target due to a faster increase in imports compared to exports.
- During FY2004-05, exports are estimated at $14.41 billion, while imports stood at $20.62 billion resulting in a trade deficit of $6.21 billion. A year earlier, the trade deficit was $3.2 billion.
- The substantial increase in imports was largely due to higher imports of machinery, petroleum, and chemicals.
- Workers' remittances received from abroad rose to $4.15 billion during FY05, a rise of 9.2%, against $3.8 billion a year earlier.

External Debt

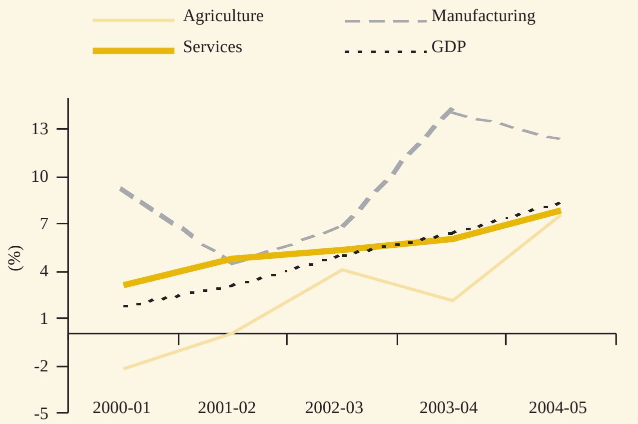
- External debt and foreign exchange liabilities have declined to $36.62 billion by end March 2005, following the debt reduction strategy.
- As percentage of GDP, external debt and liabilities declined to 33.1% by March 05 against 36.7% a year earlier.
- In FY05, (July-March) debt servicing of external debt declined. The actual amount paid fell to $2.17 billion from $5.27 billion a year earlier and the rolled over amount to $1.10 billion from $1.30 billion in the corresponding period in the previous year.

Social Sector Indicators

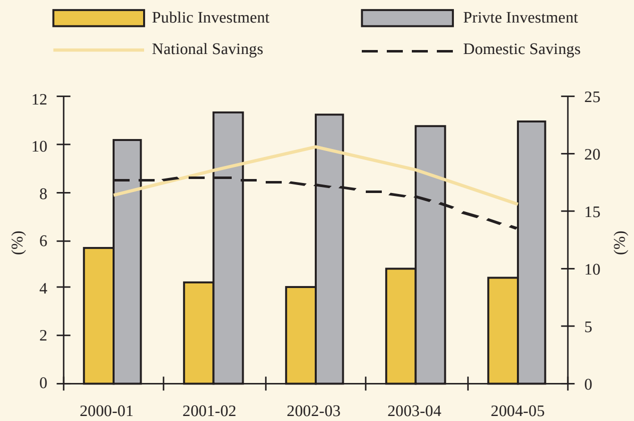
- Literacy rate improved to 53.0%.
- Expenditure on health constitutes 0.6% of GDP.
- Poverty related expenditure is budgeted at Rs.278.1 billion for FY2004-05, which includes expenditure on roads & highways, investment in water supply and sanitation, human development, on irrigation and rural electrification etc.

The Economy in Pictures

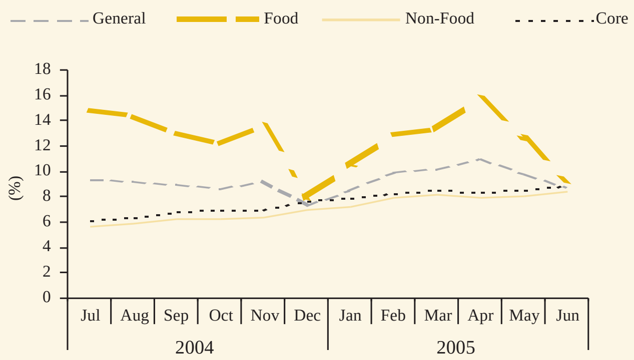
Growth Trends



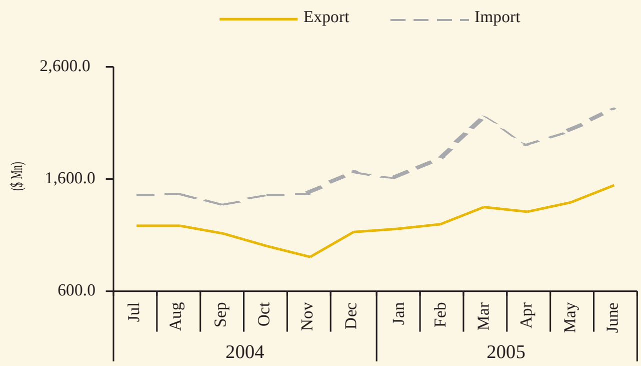
Savings/Investment as % of GDP



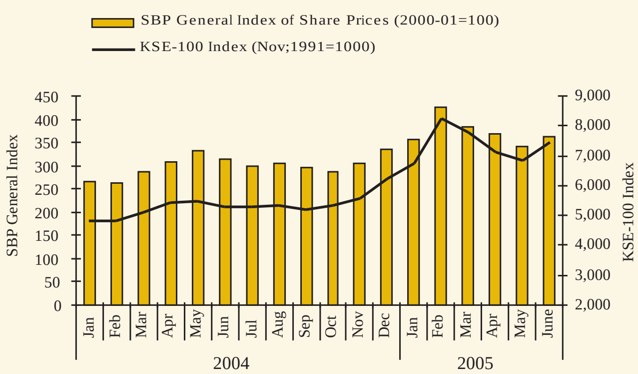
Inflation Year on Year

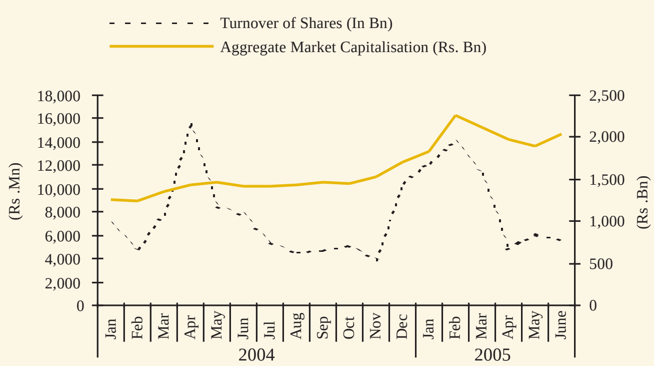


Exports & Imports

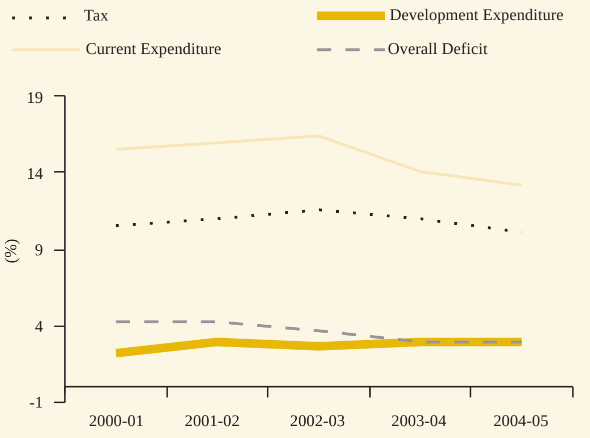


Karachi Stock Exchange

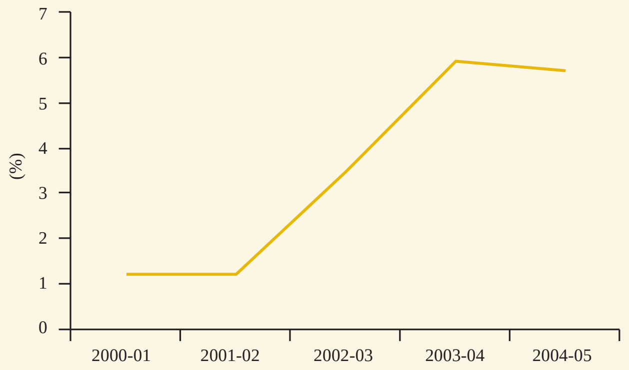




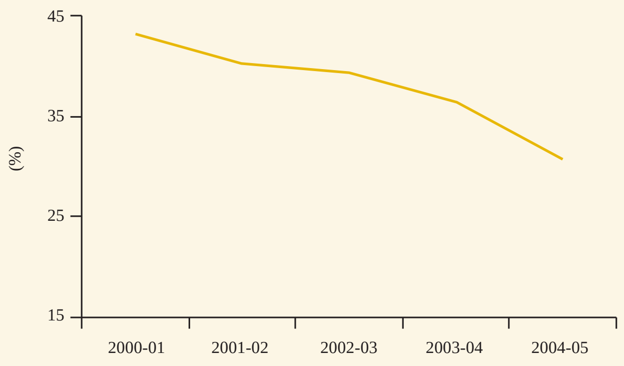
Fiscal Indicators
as % of GDP



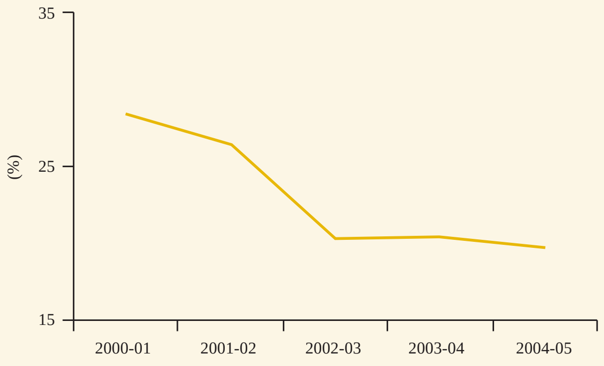
Net Credit ot Private Sector
as % of GDP



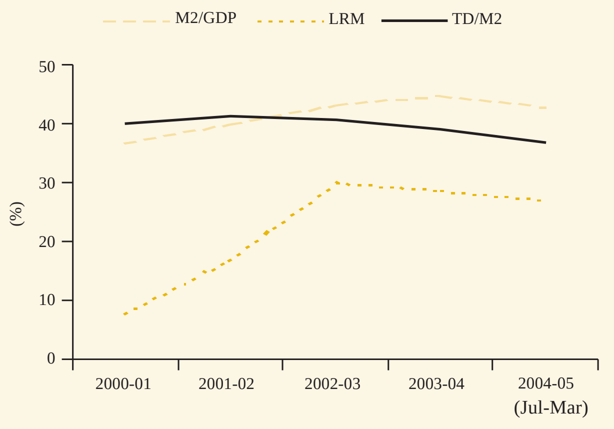
Domestic Debt
as % of GDP



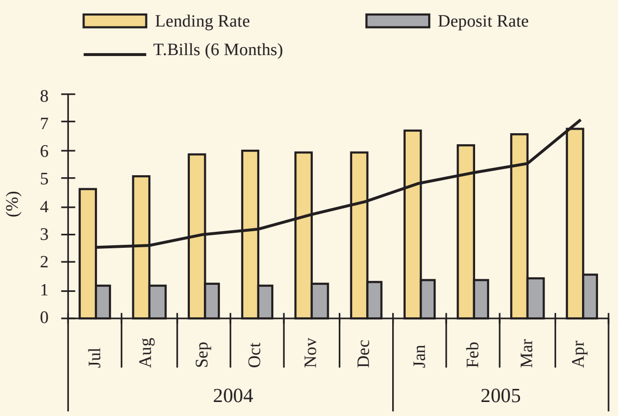
Interest Payment on Domestic Debt
as % of Current Expenditure



Financial Development



Intetest Rate Structure



LRM: Liquid Reserves to Money Supply
TD: Total Deposits
M2: M1+outstanding stock of time deposits+resident foreign currency account.

Provincial Budgets 2005-06
Highligts

Sindh

- § The provincial budget has a total size of Rs.143 billion; 83% is allocated for revenue expenditure and 17% for public sector development programme.
- § Revenue receipts are estimated at Rs.112.95 billion; and includes federal transfers from the divisible pool of Rs.52 billion, straight transfers of Rs.29.52 billion , zila tax grants of Rs.12.15 billion and provincial receipts are expected at Rs.19.28 billion.
- § Revenue deficit is estimated at Rs.5.98 billion.
- § Capital receipts are budgeted at Rs.4.8 billion, while capital expenditure is expected to be Rs.7.81 billion, resulting in a deficit of Rs.3.01 billion.
- § Of the development programme, allocation for improvement of road infrastructure has been raised. Foreign assistance of Rs.2.04 billion would also be available under Sindh Road Sector Development Project.
- § Allocation for education sector, agriculture, development of coal reserves has been raised, alongwith higher funds earmarked for special packages for Karachi, Hyderabad and rural development.
- § Various types of fees charged on account of driving licence have been merged into a single fee, named as Composite Driving Licence Fee to be issued for three years.
- § Levy of certain taxes rationalized.
- § Arms manufacturing licence fee and renewal fee enhanced.
- § Registration fee of private security companies raised.
- § Relief in pay and pension to the provincial government employees proposed.

Punjab

- § The Budget 2005-06 has a total outlay of Rs.224 billion, 24% higher over last year.
- § The annual development programme is budgeted at Rs.53 billion, larger by 22% over Rs.43.44 billion programme in FY05.
- § The ADP for FY06 would be financed to the tune of Rs.43.17 billion from the province's own resources, while Rs.9.83 billion would be the foreign assistance component.
- § Infrastructure receives 43% of the development expenditure, while 35% has been earmarked for social sector.
- § Of the total 1727 schemes to be undertaken during the year by the provincial government, around 1067 or 62% are expected to be completed during the forthcoming fiscal year.
- § Rs.42 billion of the total development outlay has been earmarked for the pro-poor sectors. Poverty reduction is focused upon and the budget hopes to achieve it through creation of jobs and enhancing the delivery of public services.
- § School education allocations have been reduced.
- § Higher allocation budgeted for technical education and vocational training.
- § Higher funds allocated for the health sector.
- § No new taxes imposed.

NWFP

- § With a total budget size of Rs.86.5 billion, against receipts of Rs.84.2 billion, the provincial budget shows a deficit of Rs.2.3 billion.
- § The budget has no new taxes.
- § Of the provincial revenue income of Rs.4.5 billion in FY06, tax revenue contributes Rs.2.1 billion & non tax Rs.2.4 billion.
- § Current revenue expenditure is budgeted at Rs.72.1 billion; of this, welfare budget totals Rs36.2 billion, administrative Rs.9.8 billion and development Rs.20.9 billion.
- § In government run schools, no tution fee will be charged upto matric level.
- § External assistance has helped in the developmental activities of the province. In 2005-06, these form 35% of the budget. ADB has a major stake in the assistance received.
- § Of the development programme of Rs.21 billion, the provincial share is Rs.11.2 billion.

Balochistan

- § The Budget for 2005-06 has an outlay of Rs.46.38 billion.
- § Of the total, Rs.11.78 billion has been earmarked for development purposes and Rs.34.61 billion has been allocated for non-development expenditure.
- § Of total development outlay, 47% has been earmarked for road construction.
- § Next year 1166 development schemes would be implemented, which includes 614 ongoing schemes and 554 new schemes.
- § Higher allocations have been made for education, health, water supply, irrigation, improvement of law & order among others.
- § The government would not be charging any fees, except for admission fee in all state run institutions upto the intermediate level.

Pakistan Millennium Development Goals

At the United Nations Summit in September 2000, member nations made a commitment to work towards a world in which the elimination of poverty and sustained development would have the highest priority. The Millennium Declaration signed by 147 heads of state, including Pakistan, was passed unanimously by the members of the UN General Assembly. Millennium Development Goals (MDGs) drawn from the UN Declaration were set by all government leaders at the Summit.

Millennium Development Goals were formulated to achieve pro-poor economic growth. It was felt that while governments spent huge amounts on military and business interest, more than a billion people lived on less than $1 a day; there was hunger; children suffered from malnutrition; education especially for girls was limited, millions of children of primary school age were out of school; gender disparity existed in primary and secondary education and because of this more women than men worked in low status jobs, their share in paid employment was lower; child mortality was high because of a number of diseases. It was to eliminate such disparities and have a better life for all, where people do not fall into poverty and become objects of exploitation that goals were set, and for each one or several indicators were spelt, which could be subsequently monitored and progress seen.

Signatory countries to the UN Declaration have adopted the MDG in the policy framework and would be submitting a yearly progress report.

The MDGs are: -

MDG

1. Eradicate extreme poverty and hunger.
2. Achieve universal primary education.
3. Promote gender equality and empower women.
4. Reduce child mortality.
5. Improve maternal health.
6. Combat HIV/AIDS, malaria and other diseases.
7. Ensure environmental sustainability.
8. Develop a global partnership for development.

Pakistan has adopted the following goals and indicators for tracking progress towards them.

Goals / Indicators

MDGs and Targets	Indicators for Pakistan	Targets 1990/91	Targets 2015 MDG
Goal 1: Eradicate Extreme Poverty and Hunger			
Target 1. Halve, between 1990 and 2015, the proportion of people whose income is less than a dollar a day	• Proportion of population below the calorie based food plus non-food national poverty line	26.1%	13%
Target 2. Halve, between 1990 and 2015, the proportion of people who suffer from hunger	• Prevalence of underweight children under-five years of age.	40%	<20%
	• Proportion of population below minimum level of dietary energy consumption	25%	13%
Goal 2: Achieve Universal Primary Education			
Target 3. Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling	• Net primary enrolment ratio • Completion/survival rate to grade 5 • Adult literacy rate	46% Approx 50% 36.3%	100% 100% 88%
Goal 3: Promote Gender Equality and Empower Women			
Target 4. Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education no later than 2015	• Gender Parity Index (GPI) for primary, secondary and tertiary education	Primary 0.51 Secondary 0.50 Tertiary 0.46	Primary 1.00 Secondary 0.94

	• Youth literacy GPI • Share of women in wage employment in the non-agricultural sector • Proportion of seats held by women in National Assembly and Senate, provincial assemblies and local councils	0.51 8.7 National Assembly 2/217 =0.9% Senate 1/87 =1%	1.0 14.0
Goal 4: Reduce Child Mortality			
Target 5. Reduce by two thirds, between 1990 and 2015, the under-five mortality rate	• Under-five mortality rate • Infant mortality rate • Proportion of fully immunised children aged 12-23 months • Proportion of children under 1 year immunised against measles • Prevalence of under-weight children (under 5 years of age) • Proportion of children under five who suffered from diarrhoea in the last 30 days and received ORT • Lady Health Workers' coverage of target population	140 102 75% 80% 40% na na	52 40 >90% >90% <20% <10% 100%
Goal 5: Improve Maternal Health			
Target 6. Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio	• Maternal mortality ratio • Proportion of births attended by skilled birth attendants • Contraceptive prevalence rate • Total fertility rate • Proportion of women 15-49 years who had given birth during last 3 years, and made at least one antenatal care consultation	550 18% 12% 5.4% 15%	140 >90% 55% 2.1% 100%
Goal 6: Combat HIV/AIDS, Malaria and Other Diseases			
Target 7. Have halted by 2015 and begun to reverse the spread of HIV/AIDS	• HIV prevalence among 15-24 year old pregnant women • HIV prevalence among vulnerable groups (e.g., active sex workers)	n/a n/a	Baseline to be reduced by 50% Baseline to be reduced by 50%
Target 8. Have halted by 2015 and begun to reverse the incidence of malaria and other major diseases	• Proportion of population in malaria risk areas using effective malaria prevention and treatment measures • Incidence of tuberculosis per 100,000 population • Proportion of TB cases detected and cured under Directly Observed Treatment Short Course (DOTS)	n/a n/a n/a	75% 45% 85%
Goal 7: Ensure Environmental Sustainability			
Target 9. Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources	• Forest cover including state-owned and private forest and farmlands • Land area protected for the conservation of wildlife • GDP per unit of energy use (as a proxy of energy efficiency)	4.8% 9.1% 26471	6.0% 12.0% 28000

	• No. of vehicles using CNG fuel • Sulphur content in high speed diesel (as a proxy for ambient air quality)	500 1.0	920000 0.5 to 0.25
Target 10. Halve, by 2015, the proportion of people without sustainable access to safe drinking water and basic sanitation	• Proportion of population with sustainable access to an improved water source, urban and rural • Proportion of urban and rural population with access to improved sanitation	53% 30%	93% 90%
Target 11. Have achieved, by 2020, a significant improvement in the lives of at least 100 million slum dwellers	• Proportion of *Katchi abadis* (slums) regularised	n/a	95%
Goal 8: Develop a Global Partnership for Development			
Target 12. Develop further an open, rule based, predictable, non-discriminatory trading and financial system More generous ODA for countries committed to poverty reduction *Target 15.* Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long run			

Source: Pakistan Millennium Development Goals Report 2004
Planning Commission, Government of Pakistan

PRSP

For full implementation of the Millennium Development Goals, Pakistan has prepared a Poverty Reduction Strategy Paper (PRSP), and its targets and indicators have been aligned towards attaining the MDGs. The Government has also developed the Medium Term Development Framework (MTDF) 2005-10, which complements the PRSP process and moves it further. It specifies goals and targets and outlines strategies for their realization. It seeks to sustain the growth of 7-8 percent achieved in the last two years, so that its benefits trickle to the neglected sectors of the economy.

Growth will be made pro-poor by investments in women empowerment, education, health, water supply and sanitation, rural development, SMEs, works programme and an integrated social protection strategy for the poor. MTDF strategy emphasizes on equitable growth with social development. The monitor-able targets have been mentioned above.

MTDF

When we talk about growth, the MTDF recognizes that though economic growth is an essential condition for poverty reduction but it is not sufficient. While in the longer term, sectors such as agriculture, small & medium enterprises, housing and construction have been focused upon for their potential to generate jobs; in the short term, social protection programmes and adhoc measures should be implemented to support the vulnerable groups.

Within the framework of the PRSP, social and poverty related expenditures are expected to rise. The Table below gives the projected PRSP expenditures as percentage of GDP for the plan period 2005-10. The MTDF would aim to speed-up the trickle down effect of larger GDP by allocating more resources to the vulnerable and marginalized segments of society so to achieve the targets of the PRSP.

PRSP Expenditures as percentage of GDP

	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Pro-Poor Expenditure (Rs. Bn)	278.06	324.55	380.10	446.18	524.22	616.20
Pro-Poor Expenditure as percentage of GDP (%)	4.25	4.65	5.07	5.51	5.98	6.49

Source: Medium Term Development Framework 2005-10 Planning Commission, Government of Pakistan

Etisalat offers highest bid

Since the launch of the Poverty Reduction Strategy Programme, quarterly progress reports have been published by the Government of Pakistan, Finance Division. In addition the Pakistan Social and Living Standards Measurement (PSLM) Survey has been designed to provide social and poverty related indicators for the assessment of development programmes initiated by the Government under PRSP. The results of the recently completed PSLM Survey are given below, which shows significant improvement in some of the indicators.

A Comparison of Selected Social Indicators

(%)

Indicators	98-99 PIHS	00-01 PIHS	04-05 PSLM
Major source of Drinking Water (Tap Water)	26.0	25.0	39.0
Type of Toilet Used by Household			
- Flush	41.0	45.0	54.0
- Non-Flush	12.0	12.0	20.0
- No Toilet	46.0	43.0	26.0
Population Ever Attended School	50.0	51.0	55.0
Gross Enrolment at Primary Level (5-9 Years)	71.0	72.0	86.0
Net Enrolment at Primary Level (5-9 Years)	42.0	42.0	52.0
Gross Enrolment at Middle Level (10-12 Years)	40.0	41.0	46.0
Net Enrolment at Middle Level (10-12 Years)	16.0	16.0	18.0
Gross Enrolment at Matric Level (13-14 Years)	40.0	42.0	44.0
Net Enrolment at Matric Level (13-14 Years)	9.0	9.0	11.0

Source: Pakistan Economic Survey 2004-05 Government of Pakistan

Third quarter progress report for the year 2004-05 on Poverty Reduction Strategy Paper, shows increased PRSP budgetary expenditure, reflecting strong commitment of the Government to poverty reduction.

The Table below gives the sector-wise pro-poor expenditures. There has been a substantial increase in expenditures on roads, highways and farm to market roads, irrigation, rural development, and rural electrification, among others.

Targeted Annual Expenditures

(Rs. Bn)

	Target FY05	Upto Q3 FY05	Actual expenditures upto Q3 as % of annual projected expenditures
Roads, highways & bridges	16.58	16.61	100.21
Water supply and sanitation	4.88	3.38	69.16
Education	102.38	74.43	72.70
Health	36.08	19.31	53.53
Population planning	4.88	2.52	51.56
Social security & welfare	3.90	3.17	81.21
Natural calamities	0.49	0.41	83.27
Irrigation	32.37	21.32	65.87
Land reclamation	2.44	1.69	69.18
Rural development	7.23	9.16	126.75
Rural electrification	1.00	2.06	205.50
Rood subsidies	14.63	1.22	8.34
Food support programme	3.90	2.65	68.01
Tawana Pakistan	0.50	0.03	6.00
Low cost housing	0.00	0.24	-
Administration of justice	3.41	2.15	62.99
Law & order	43.39	32.16	74.13
Total	278.06	192.51	69.23

Source: Poverty Reduction Strategy Paper, Third Quarter Progress Report 2004-05, PRSP Secretariat, Government of Pakistan

As Pakistan puts in place an enabling environment for achieving the millennium development goals, its key policies are directed towards higher budgetary allocations to allow better access to health care and education, alongwith improving the quality of these services, providing policies to enhance participation of the poor, particularly women. Though an ambitious agenda for reducing poverty, focused development work by Pakistan is expected to yield positive results.

PTCL Privatisation

PTCL privatised

Carrying forward the process of privatization in the country, the government in June this year sold 26% stake of the Pakistan Telecommunications Company Limited (PTCL) to Emirates Telecommunications Corporation, Etisalat for $2.59 billion (Rs.155.16 billion).Etisalat was the highest bidder with a $1.96 (Rs.116) per share offer.

The government has 88% shares of PTCL and after the sale of 26% of the shares, the government would retain a 62% stake in the company.

Etisalat offers highest bid

Three parties, namely China Mobile, Etisalat and Sing Tel participated in the bidding. The second highest was China Mobile (Hong Kong) Limited with a bid of 1.409 billion (Rs.84.2 billion), third was Singapore Telecommunication Limited with a bid of $1.166 billion (Rs.69.66 billion). China Mobile, offered Rs.63.48 per share, while Sing Tel offered Rs.52.54 per share.

Etisalat, UAE's monopoly telecom service provider has acquired a number of ventures, as part of its regional expansion strategy. It is aggressively entering into regional and international markets. It is 60% owned by the government.

It has 50% shareholdings in Atlantique Telecom, with market access to African telecom markets, including Benin, Burkina Faso, Gabon, Niger, Togo and Ivory Coast. Besides this, it has substantial holdings, Etihad Etisalat in Saudi Arabia, Qatar Telecom (Qtel), Suda tel, Africa Zanzibar Telecom (Zantel) among others.

The Pakistan telecom market offers huge opportunities for Etisalat. According to some estimates, mobile penetration in the home market is less than 5% of the total population, against 95% of the UAE's 4.2 million population.

PTCL financial indicators

PTCL is the leading provider of basic telephone services in Pakistan with over 4.4 million telephone lines in service. Besides provding fixed line and ancillary services, PTCL owns Pakistan Telecommunication Mobile Limited, one of five GSM cellular providers in Pakistan and Paknet a countrywide Internet service provider. Its strong financial position demonstrated during FY04 excluding subsidiaries as per unconsolidated financial results of PTCL indicates:

Revenue Rs.74 billion, Operating profit; Rs.41.9 billion, Net Profit after Tax; Rs.29.2 billion, Total Assets; Rs.141.6 billion, Total Equity; Rs.83.6 billion, and the PTCL network has 5.27 million installed lines.

The privatization of PTCL marked the culmination of a process that began in 1994, when 12% of its shares were offloaded. It raised $900 million by selling 9% of PTCL shares on the international market in the form of global depository receipts and 3% was sold in the domestic market that year to list in the Karachi Stock Exchange.

A consortium consisting of JP Morgan and Goldman Sachs International advised the Government of Pakistan on the privatization of PTCL.

As per Privatisation Commission Ordinance, 90% of the proceeds would be used to retire debt, while 10% are meant for poverty alleviation programme.

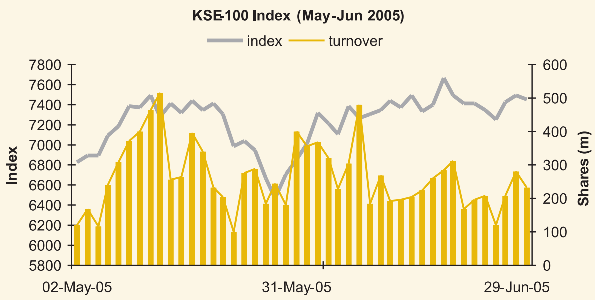
Inflow from the privatization of PTCL would allow the government to retire a part of its debt. Reduced borrowings would have a positive effect on the fiscal deficit. It would help create fiscal space allowing the government to spend on infrastructure and social sectors.

Market Analysis

Market Summary

The market has witnessed extremes since the start of 2005. The index touched an all time high of 10,303 points in Mar '05 and subsequently declined to 6467 points in May '05, representing a decrease of 37% in three months.

The index during May - Jun '05 gained 9% on average daily volume of 265m shares to close at 7450.12 points. Top performers over the May-June 2005 period were PPL, BoP, NBP, SNGP and OGDCL. Pak PTA, Dewan Salman and Pak Suzuki were the main under-performers.



The banking sector in general showed good performance on the back of rising interest rates and higher earnings expectations for some banks given higher dividend announcement made by NIT. Poor performance in the sector was displayed by Union and Askari Bank whose share prices saw a decline of 15% and 11% respectively.

The auto sector failed to perform under the post WTO regime and reduction of import duties on cars announced in the Federal Budget FY'05-'06. Pak Suzuki declined by 22% followed by Dewan Motors whose share price declined by 16% during the two month period.

The cement sector also gave very disappointing results may continue to remain under pressure as scheduled expansions are coming online along with the end of the cartel agreement. Maple Leaf Cement declined by 18%, followed by Fauji Cement 17%, D.G Khan Cement 13% and Lucky Cement 5%. Other decliners included Fauji Fertilizer, Nishat Mills, Hubco and NRL.

The most influential factor during the period was the badla phase out issue, which along with exposure limits in the futures market had caused the market to remain volatile. The market during the period under review was also influenced by privatization related developments, led by PTCL. The telecom giant directed the behavior of the market for weeks before finally being auctioned on June 18, 2005.

Phasing out of COT and start of margin finance

The phase out of Badla/ COT financing and its replacement with margin financing has been a much debated topic during recent times. The Badla financing was originally planned to be completely phased out by Jun '05. The phasing out of 22 out of the 30 scrips from the badla list was completed smoothly but the market reacted adversely to the withdrawal of the 7 remaining scrips whose turnovers were higher in both the ready and COT market. The main investor concern was the lack of availability of alternative, suitable margin financing products.

The SECP in addressing the concerns of market participants and the KSE decided to amend its strategy relating to the phasing out of badla. It was agreed that instead of withdrawing each scrip from the badla list on a weekly basis, the COT volume on April 29, '05 is to be frozen and an equal proportion (initially 12.5%, which was later reduced to 8.25%) of each of the 7 scrips be phased out on a weekly basis. Under the new approach, all scripts would completely be phased out from the COT market by Aug 26, '05.

Although some banks have introduced their margin financing products in the market, it is generally felt that banks have been slow in honoring their commitment to provide Rs20b margin financing for phasing out of the COT. Consequently there has been a negative impact on the market as the capped badla position is phasing out gradually but investors who do not have an alternative mode of financing are unable to square their COT positions in Ready Market on time.

Amended rules for the Futures Market

On the regulatory front, issues relating to the futures market rules which were announced by the SECP in March '05 have finally been resolved. The SECP which had earlier refused to raise the trading limit from 1% of the free float per scrip for each member to 5%, subsequently raised it to 3% of the free float of a scrip. It has also stated that the limit may be raised to 5% provided the pre-trade margin verification system is installed at the KSE by July '05. The requirement of 100% cash margins in case of exposure exceeding Rs200m has been reduced to 50% with the remaining 50% in the form of eligible securities or guarantees from a scheduled bank.

Sensitive Price Index

The management of KSE has planned to form a sensitive price index comprising 30 leading stocks. The key distinguishing feature between the current index and SPI is that while the current index weights the price with the total outstanding shares of a company, the SPI is based on the free float methodology. Simply put, the free float is the number of shares available for trading, i.e. it excludes directors, associated companies and government holdings from the total outstanding shares of a company. The effect will be to reduce the impact of market giants like PTCL and OGDC on the index and to make it more representative of the market.

Privatization Implications
Completed Transactions

PTCL

The telecom giant was put under the hammer on June 18, 2005, despite all the controversies, labor related issues and strong resistance from the opposition bench.

The 26% stake (1,326,000,000 B-category shares) along with management control in PTCL and its subsidiaries Ufone and Paknet (ISP) was sold to the UAE based Etisalat at a price of US$2.6b (per share US$1.96). The transaction which was the country's largest ever translated into a price of Rs117.01 per share (US$1.96) and was almost double the reserve price set by the government at Rs62 per share.

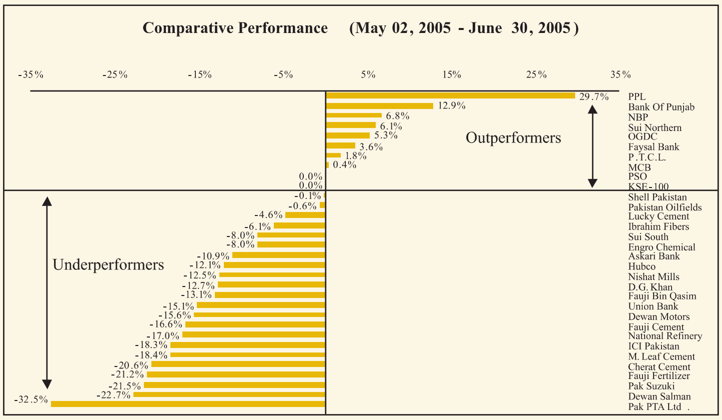
NRL

Attock Oil Group acquired 51% stake (33,985,788 shares) along with management control in NRL at a price of Rs16.415b (Rs483 per share). The Privatization Commission had received 29 EoIs for NRL and 16 parties submitted RSOQs. Amongst the short listed potential bidders, 11 parties were pre-qualified for due diligence in the data room. The pre-bid process ended up with three parties in the run.

UBL

UBL the third largest bank in Pakistan was privatized in October 2002 through a strategic sale in which 51 percent (264.18 million) shares were transferred along with management control of 25.5 % (132.09 million) shares each were acquired by the Abu Dhabi Group and the Bestway Group for Rs12.3b.

The Privatization Commission offered 10% (51.8 million) shares with a green shoe option of additional 5% shares through an IPO. The shares presented in the IPO offered limited upside potential and consequently were highly unsubscribed (subscription rate was 42% approximately). The KSE's board suspended the provisional trading in shares of UBL (w.e.f. June 16, 2005) since balloting of the shares had not taken place. The only option available to the bank is to formally list itself on the ready board.



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

Trade Policy 2005-06

Highligts

- In FY2004-05, exports are estimated at $14.4 billion, an increase of 17% over the preceding year.
- Of the total, textiles and garments exports were $8.6 billion, while exports of non-textile sector was $5.8 billion.
- The government has adopted Rapid Export Growth Strategy based on:
  - ⇒ improved market access.
  - ⇒ focusing on neglected regions/areas.
  - ⇒ strengthening of trade promotion infrastructure of t he government, the Export Promotion Bureau and the trade offices abroad.
  - ⇒ improving skill development.
  - ⇒ providing state of the art physical infrastructure.
- Pakistan has been included in the EU's new GSP Scheme as of January 1, 2006, which allows Pakistan's exports including textiles and clothing to enter the EU markets at concessionary rates of tariff.
- There is a need for all relevant government agencies to launch large scale and good quality technical training.
- A detailed plan has been formulated by the Ministry of Commerce, focusing on diversification, trade facilitation, increased market access, reducing costs, capacity building, developing export of services, improving compliance and quality infrastructure.
- Export target proposed at $17.0 billion for 2005-06.
- Textile Garments Skill Development Board proposed.
- In line with the recommendations of the envoys conference, markets and products have been prioritized to promote the country's exports.
- The priority countries identified are Central Asian Republics; Latin America (Brazil, Chile, Argentina and Mexico); Africa (South Africa, Nigeria, Morocco, Kenya and West Africa).
- To promote trade with the US, which is the largest destination for Pakistan's exports after the EU, a special programme focusing on trade facilitation is proposed. A trade-lobbying firm will be hired in the US to enhance Pakistan's exports.
- Special focus has been laid on enhancing exports to the EU.
- Ministry of Commerce to develop trade competitiveness indicators. These will quantify and internationally benchmark the cost of doing business in Pakistan. These will be kept under constant review.
- Special focus to initiate studies to determine the state of internal commerce. Consequently appropriate policy recommendations will be possible which will be designed to energize this sector so that it can play its due role in enhancing exports.
- Incentives provided for pharmaceuticals exports.
- Establishment of a new customs station on the Afghan border and removal of an existing anomaly in the trade regime between the two countries.
- Services of a consultant of international repute to be used for developing best practices for production of organic cotton in Pakistan.
- To facilitate exports of leather garments, exporters may send 100 samples in a year against 50 samples allowed earlier.
- Package for gems & jewellery.
- Footwear sector to be developed.
- Export of services to be promoted so that it can make a major contribution to export growth.
- Assistance to be provided for quality standards certification.
- Freight costs to be reduced.
- A special textile garments package announced.
- Expo Centres to be built.
- It is proposed to dispense with the condition of obtaining prior recommendation from the Regulatory Authority for import of machinery equipment, specialized vehicles etc, on import-cum-export basis.
- Specified used machinery will be allowed for import.
- Rules governing import of vehicles have been amended.

Pakistan Economy - Key Economic Indicators

Economy Size & Growth			2001-02	2002-03	2003-04	2004-05
GNP - Market Prices		Rs. bn	4425.4	4974.6	5657.1	6672.8
GDP - Market Prices		Rs. bn	4401.7	482.8	5532.7	6547.6
Per Capita Income	Market Prices	Rs.	30770	33899	37802	43748
	Market Prices	US$	503	579	657	736
Growth*						
GDP		%	3.1	4.8	6.4	8.4
Agriculture		%	0.1	4.1	2.2	7.5
Manufacturing		%	4.5	6.9	14.1	12.5
Wholesale & Retail Trade		%	2.8	6.0	8.1	12.0
Rate of Inflation		%				
Consumer Price Index**			3.5	3.1	4.6	9.3
Wholesale Price Index			2.1	5.6	7.9	6.9
Balance of Payments		$mn				
Exports (f.o.b)			9140	10889	12395	10572†
Imports (f.o.b)			9434	11333	13607	13950
Trade Balance			(-)294	(-)444	(-)1212	(-)3378
Investment Income (Net)			2430	2381	2392	1884
Private Transfers (Net)			4249	5737	6110	6258
Current Account Balance			1338	3165	1313	(-)1358
Fiscal Balance		% of GDP				
Total Revenue (Net)			14.2	14.9	14.3	13.0
Tax			10.2	11.5	11.0	10.1
Total Expenditure			18.8	18.6	17.5	16.0
Overall Fiscal Defict			4.3	3.7	2.4	3.0
Domestic & Foreign Debt						
Domestic Debt		Rs. bn	1774.7	1894.5	2012.2	2018.1
As % GDP			40.3	39.3	36.4	30.8
Total External Debt & Liabilities		$bn	36.531	35.47	35.26	36.62
as % of GDP			51.0	43.1	36.7	33.1
as % of Foreign Exchange Earnings			236.8	181.2	164.6	145.9
Investment & Savings		% of GDP				
Total Investment			16.8	16.7	17.3	16.9
Gross Fixed Investment			15.5	14.8	15.6	15.3
National Savings			18.6	20.6	17.7	15.7
Domestic Savings			18.1	17.4	17.6	13.7
Foreign Private Investment (Net)		$mn	475.0	820.1	949.4	1027.0
Portfolio			(-)10.1	22.1	(-)27.7	135.5
Direct			485	798.0	949.4	891.5
Monetary Aggregates		%				
M_1			15.2	26.2	24.0	23.3†
M_2			15.4	18.0	19.6	20.5†
Literacy Rate		%	50.0	51.6	53.0	-
Foreign Exchange Reserves		$mn	6432	10719	12328	13000°
Exchange Rate++		Rs./$	61.4258	58.4995	57.5745	59.3014†
Stock Market Growth Rate		%				
General Index of Share Prices			(-)30.9	91.2	53.2	22.8
Aggregate Market Capitalisation			20.2	83.1	81.9	55.8

Source: Pakistan Economic Survey 2004-05

* Constant Factor Cost of 1999-2000
** Base 2000-01
++ Average during the year.
M_1 Outstanding stock of currency in circulation+demand deposits of scheduled banks+other deposits with SBP.
M_2 M_1 +outstanding stock of time deposits+outstanding stock of FRCDs.
† July-March
° By end April

NBP Performance at a Glance

(Rs. Bn)

Items	2000	2001	2002	2003	2004
Total Assets	371.6	415.1	432.8	468.9	549.7
Deposits	316.5	349.6	362.9	395.5	465.6
Advances	140.3	170.3	140.5	161.3	221.4
Investments	72.6	71.8	143.5	166.2	144.7
Shareholders' Equity	11.4	12.0	14.3	18.1	25.2
Pre-Tax Profit	1.03	3.02	6.04	9.01	12.02
After-Tax Profit	0.46	1.15	2.25	4.20	6.24
Earning Per Share (Rs.)	1.24	3.08	5.49	8.53	12.68
Return on Assets (Pre-Tax Profit) (%)	0.3	0.8	1.4	2.0	2.4
Number of Branches	1428	1245	1204	1199	1226
Number of Employees	15351	15163	12195	13272	13745

NBP Products

NBP Saiban

- Finance available for home purchase, home construction and home improvement.
- Period of repayment ranges between 3-20 years.
- Loans available upto a maximum of Rs.10 million.
- Mark-up choices available. Rate ranges between 9.0 - 12.85%. Rates subject to change
- Minimum approval and disbursement timing.
- Limited to areas where there are no documentation, fee, resale and foreclosure related issues, so to protect the bank's interest.

NBP Advance Salary

- 15 months salary in advance (certain conditions apply).
- Minimum documentation.
- Repayable in 5 years.
- No processing charges; no collaterals, no guarantees, no insurance.
- Mark-up charged at 13% per annum on reducing balance method.

NBP Cash n Gold

- Facility of Rs.5000 against 10 gms of gold.
- Mark-up 9% per annum.
- No maximum limit of cash.
- Repayable after one year.
- Roll over facility.
- No penalty for early repayment.

NBP Kisan Dost

- Loans available for the farmers for production, development purposes, for purchase of tractors, for installation of tubewells, for purchase of agricultural implements, mirco loans, for godown construction, for construction of fish pond, for livestock farming, for milk processing, for cold storage, bio-gas plants etc.
- Mark-up 9% per annum.
- Loans available at the farmer's doorsteps.
- Agricultural experts to guide farmers.
- Loans available against agricultural passbooks, gold ornaments and paper security.