PAKONOMICS

September 2020

Saturday, October 24, 2020

www.tolaassociates.com

TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

HIGHLIGHTS:

- The IMF, in its World Economic Outlook (WEO) report of 2020 has projected a muted growth of Pakistan's economy at a meagre 1%, the average inflation rate to be at 8.8%, with the current account deficit at 2.5% of the GDP and unemployment to increase by 0.6% to 5.1% for 2020-21.
- Pakistan is eyeing an additional temporary debt relief of nearly $1.2 billion for another six months to June 2021 from G-20 nations.
- The debt of our Central Government, also known as the 'Central Government debt', has increased by 47% in percentage terms and Rs.11,447 billion in monetary terms, to Rs.35,659 billion as of Aug 2020 as compared to Rs.24,212 billion as of June 2018.
- The Large-Scale Manufacturing ("LSM") sector has witnessed a drop of 6.78% in Aug 2020 vs July 2020, when compared on a month-on-month basis. Whereas, the same grew by 1.19% in Aug 2020 vs. drop of 6.39% in Aug 2019 last year.
- The outstanding stock of 'Hot Money' stood at negative $208 million as of 22nd Oct 2020.
- According to the State Bank of Pakistan ("SBP"), foreign remittances sent by our overseas workers to Pakistan have increased by 9% to $2.283 billion in Sep 2020 vs. $2.095 billion in Aug 2020. These remittances have touched the $2 billion mark for the fourth consecutive month since June 2020.
- According to the official statistics of the Federal Board of Revenue ("FBR"), the FBR has collected tax revenue of Rs.1,004 billion which grew by only 4.69% during July-Sep 2020 vs Rs.959 billion last year
- The Broad Money (M2) growth stands at Rs. 103 billion as of 2nd Oct 2020 vs Rs. 28 billion last year.
- According to the Pakistan Bureau of Statistics ("PBS"), CPI inflation has appreciated by 9.04% on a year-on-year basis in Sep 2020 vs. 11.40% last year.
- Per the PBS, our exports have appreciated by 7.03% to $1.88 billion in Sep 2020 vs $1.765 billion last year.
- The Current Account balance has dropped by 153% and stands at a surplus of $792 million during July-Sep 2020 vs. a deficit of $1.49 billion last year mainly because of remittances growth despite weak exports.
- As per the SBP, Foreign Direct Investment ("FDI") has dropped by over 50% from $383.5 million in Sep-2019 to $189 million in Sep-2020.

The outlook of the economy of Pakistan is as follows;

ECONOMY AT A GLANCE

Economic Indicators	Period	Status	Current Year	Last Year
LSM	Aug 2020	↑	1.19%	(6.39%)
Credit to Private Sector	As of 2nd Oct 2020	↓	Rs.(122) billion	Rs. (49) billion
SCRA inflows	As of 22nd Oct 2020	↓	US$(208) million	US$ 88 million
Worker's Remittances	Sep 2020	↑	US $2.284 billion	$1.740 billion
M2	As of 2nd Oct 2020	↑	Rs 103 billion	Rs. 28 billion
Net Government Sector borrowing	As of 2nd Oct 2020	↓	Rs. 163 billion	Rs. 233 billion
CPI	Sep 2020	↓	9.04%	11.40%
FBR Tax Collection	July-Sep 2020	↑	Rs. 1,004 Billion	Rs. 959 Billion
Foreign Exchange Reserves with SBP	As of 16th Oct 2020	↑	US$ 12.066 billion	US$ 7.75 billion
Foreign Direct Investments	July-Sep 2020	↓	US$ 415.70 million	US$ 545.50 million
Trade Deficit in Goods	July-Sep 2020	↑	US$ (5.83) billion	US$ (5.68) Billion
Balance of Payment	July-Sep 2020	↑	US$ 175 million	US$ (1,078) million

1. LARGE SCALE MANUFACTURING:

As per the PBS, Pakistan's Large-Scale Manufacturing has been struggling after the reopening of businesses post-lockdown. Out of 15 major broad-based industries of Pakistan, 7 of them have posted either negative or zero growth. The country's LSM dropped by 6.78% in Aug 2020 vs July 2020 when compared on a month-on-month basis. Whereas, it grew by 1.19% in Aug 2020 vs. drop of 6.39% in Aug 2019 last year. The overall output of LSM increased by 3.66% during July-August 2020-21 as compared to the drop of 6.13% during July-August 2019-20. Pakistan's LSM lacks consistent growth which has to be a key concern for our policy makers.

Industries	Weight (%)	Aug-20 (%)	Aug-19 (%)	Jul-20 (%)	Y/Y growth Cumulative
Textile	20.915	1.91	0.09	1.66	0.53
Food, Beverages & Tobacco	12.37	8.25	(10.42)	21.73	2.25
Coke & Petroleum Products	5.514	(5.36)	(10.04)	18.34	0.34
Pharmaceuticals	3.62	(0.40)	(15.81)	19.2	0.75
Chemicals	1.717	10.81	1.34	0.19	0.25
Automobiles	4.61	(13.08)	(33.21)	(23.31)	(1.14)
Iron & Steel Products	5.39	(9.64)	(17.71)	(11.13)	(0.46)
Fertilizers	4.44	3.47	15.64	(5.08)	(0.06)
Electronics	1.96	(25.41)	44.72	(33.31)	(1.11)
Leather Products	0.86	(30.19)	5.00	(35.95)	(0.60)
Paper & Board	2.31	9.77	(4.62)	5.04	0.39
Engineering Products	0.4	(33.45)	31.50	(32.6)	(0.11)
Rubber Products	0.26	6.45	1.81	(15)	0.03
Non-Metallic Mineral Products	5.36	15.81	(11.38)	29.01	2.61
Wood Products	0.58	(70.36)	90.92	(18.63)	0.00
Overall LSM Growth Y/Y					1.19%
Overall LSM Growth M/M					(6.78%)

2. SCRA ("SPECIAL CONVERTIBLE RUPEE ACCOUNT") INFLOWS:

Cumulative net inflows in Equity, T-Bills and PIBs During current fiscal year, till 22nd Oct 2020				
Description	**Equity**	**T-Bills**	**PIBs**	**Total**
	('000 USD')			
Inflows	166,297	117,236	22,857	306,389
Outflows	(315,124)	(199,938)	-	(515,061)
Balance Remaining	(148,827)	(82,702)	22,857	(208,672)

- **The outstanding stock of 'Hot Money' stood at negative $208 million till 22nd Oct 2020.**

3. WORKER'S REMITTANCES:

As per the SBP, foreign remittances sent by our overseas workers to Pakistan have increased by 9% to $2.283 billion in Sep 2020 vs. $2.095 billion in Aug 2020. These remittances have touched the $2 billion mark for the fourth consecutive month since June 2020. When adjudged on a month-on-month basis, it can be seen that the country's remittances have plunged by 10.54% from the USA and 4.29% from the UK. Whereas, remittances grew by 12.26% from Saudi Arabia, 15.48% from UAE and around 24% from EU countries.

According to State Bank, "this sustained growth in remittances is driven by Pakistan Remittances Initiative (PRI) to formalize remittances, improvements in Pakistan's Forex market structure & gradual re-opening of businesses in major host destinations such as Middle East, Europe & United States". However, the cost of PRI is unknown as it is a primary concern to the Pakistani migrants, mainly unskilled workers.

The lockdown and travelling restrictions are likely to affect the flow of smooth remittances going forward if the severity of the 2nd wave of the pandemic worsens in Middle East, Europe, and United States etc. Under such a scenario, the sustainability of consistent external inflows is to remain a key concern for the policymakers.

Country-wise Worker's Remittances						(USD in million)
Country	**Sep-20**	**Aug-20**	**M/M change**	**July-Sep 2020**	**July-Sep 2019**	**Y/Y change**
USA	180	202	(10.56%)	632	389	62.64%
UK	289	302.27	(4.29%)	985	574	71.68%
Saudi Arabia	666	593	12.26%	2080	1,556	33.68%
UAE	473	409.6	15.48%	1421	1,318	7.80%
other GCC countries	261	226	15.66%	784	726	8.05%
EU countries	207	166.49	24.53%	601	449	33.97%
Others	207	196	5.61%	240	441	(45.58%)
Total	**2,284**	**2,095**	**9.01%**	**7,147**	**5,452**	**31.09%**

(Source: SBP)

4. CONSUMER PRICE INDEX ("CPI") INFLATION:

(Base year 2015-16) Period	National CPI	Food		Core CPI	
		Urban	Rural	Urban	Rural
Sep-20	9.04%	12.40%	15.80%	5.50%	7.80%
Sep-19	11.40%	15.0%	15.0%	8.40%	8.80%

TOLA ASSOCIATES
TAX & CORPORATE ADVISORS

5. TAX REVENUE COLLECTION:

(Rs. In Billion)	July-Sep 2020	July-Sep 2019	change
FBR's Tax collection	1,004	959	4.69%

According to the official statistics of the FBR, the FBR has collected tax revenue of Rs. 1,004 billion which grew by only 4.69% during 1QFY2020-21 vs Rs.959 billion last year. In absolute terms, FBR's tax revenue has increased by Rs.34 billion which is 3.50% higher against the target of Rs.970 billion during July-Sep 2020. Moreover, the FBR has so far collected tax revenue of 20.22%, out of total tax revenue target of Rs. 4963 billion for 2020-21. On average, the FBR needs to collect Rs. 440 billion per month during the next 9 months to accomplish the tax collection target of Rs. 4,963 for 2020-21.

6. FOREIGN EXCHANGE RESERVES:

The SBP's reserves have decreased by around $0.74 billion mainly due to debt repayments. The reserves stood at $12.06 billion as of 16th Oct 2020 vs. $12.80 billion as of 4th Sep 2020. The depletion of foreign exchange reserves is alarming for the country. At this stage, revival of IMF programme is the need of the hour to counter massive outflows and stabilize forex reserves.

($ in million)	16th-Oct-20	11th-Oct-19
Net Reserves with SBP	12,066.6	7,813
Private Banking Reserves	7,235	7,328
Total Forex Liquid Reserves	19,301	15,142

7. FOREIGN DIRECT INVESTMENT

(US $ million)	July-Sep 2020	July-Sep 2019	% Change
Foreign Direct Investment	415.70	545.50	(23.79%)

(Source: SBP)

FDI in Pakistan has deteriorated by 23.79%, or by $130 million in absolute terms, amounting to $415.70 million during 1QFY2020-21 vs $545.50 million last year. During Sep-2020, FDI also dropped by over 50% from $383.5 million in Sep-2019 to $189 million in Sep-2020. The total foreign investment of the country (foreign private investment + foreign public investment) has dropped by 56.30% to $388.90 during 1QFY2020-21 vs $890 million last year.

8. BALANCE OF TRADE IN GOODS:

According to the PBS, the country's exports have appreciated by 7.03% to $1.88 billion in Sep 2020 vs $1.765 billion last year. During July-Sep 2020-21, Pakistan's exports have remained stagnant to $5.47 billion vs. $5.51 billion last year. Likewise, the country's imports have also remained stagnant at $11.31 billion during 1QFY2020-21 vs $11.19 billion last year. However, on a month-on-month basis, exports have appreciated by 19.26% mainly due to a low-base effect. Whereas, on account of the substantial growth in imports, trade deficit grew by 40.42% from $1.73 billion in Aug 2020 to $2.43 billion in Sep 2020.

Balance of Trade in Goods									(Amount in $ Million)
	Sep-20	Aug-20	% change M/M	Sep-20	Sep-19	% change Y/Y	July-Sep 2020	July-Sep 2019	% change Y/Y
Exports	1,889	1,584	19.26%	1,889	1,765	7.03%	5,474	5,510	(0.65%)
Imports	4,321	3,316	30.31%	4,321	3,766	14.74%	11,311	11,199	1.00%
Trade Deficit	(2,432)	(1,732)	40.42%	(2,432)	(2,001)	21.54%	(5,837)	(5,689)	2.60%

(Source: PBS)

The present Government has thus far failed in boosting exports and creating value addition in the manufacturing sector. Resultantly, this stagnation in exports during 1QFY2020-21 have caused detrimental effects on macroeconomic situation of the country.

9. BALANCE OF PAYMENT:

Pakistan's Current Account Balance stands at a surplus of $73 million for Sep 2020 as compared to the revised figure of surplus amounting to $211 million in Aug 2020. On a month-on-month basis, this surplus C/A Balance for Sep 2020 dropped by 65% as compared to Aug 2020. Whereas, the Current Account balance, dropped by 153%, stands at a surplus of $792 million during July-Sep 2020 vs. a deficit of $1.49 billion last year, despite weak exports and mainly because of remittances growth. The country's remittances grew by 31% to $7.14 billion from $5.45 billion last year. This current account surplus during July-Sep 2020 has been witnessed after 21 quarters since 3Q of 2014-

15. On a cumulative basis, the Current Account surplus as percentage of the GDP stands at 1.2% during 1Q2020 vs. a deficit of 2.3% last year. The Asian Development Bank expects that Pakistan's Current account deficit is to remain at 2.4% of the GDP in FY2020-21.

($ in million)	Sep 2020 (Provisional)	Aug 2020 (Revised)	% change	July-Sep 2020	July-Sep 2019	% Change
Current account Balance	73	211	(65%)	792	(1,492)	(153%)
Capital Account Balance	39	33	18%	77	110	(30%)
Financial Account Balance	510	249	105%	741	(1,995)	(137%)
Net FDI in Pakistan	**189**	**112**	69%	415	546	(24%)
Net Portfolio investment	**(10)**	**(9)**	11%	(26)	344	(108%)
Net incurrence of Liabilities	**(568)**	**(10)**	NA.	32	957	(97%)
Overall Balance	423	(7)	NA.	175	(1,078)	(116%)
SBP Gross Reserve	**12,154**	**12,738**	(5%)	12,154	7,937	53%

(Source: SBP)

10. TREASURY BILL AUCTION:

The SBP conducted an auction of the Treasury Bills on 21st Oct 2020, with an auction target of Rs.350 billion. The maturities thereof amounted to Rs.484.7 billion. The interest of the investor skewed towards short-term papers only.

T-Bill Auction					
Tenors	**Face Value (Rs. in Million)**	**Previous Cut-Off Yield (7 Oct-20)**	**Current Cut-Off Yield (21 Oct-20)**	**Weighted. avg. yield**	**Change**
3-Months	374,216	7.18%	7.15%	7.15%	**- 3bps**
6-Months	19,683	7.21%	7.20%	7.20%	**- 1 bps**
12-Months	-	7.29%	Bids Rejected	Bids Rejected	-
Total	393,899		-	-	

OUTLOOK:

- The IMF, in its World Economic Outlook (WEO) report of 2020 has projected a 1% growth of Pakistan's economy vs. a negative growth of 0.38% last year. This GDP growth is to remain muted for the third consecutive year i.e. 2020-21, which is very alarming for a country.
- Moreover, the IMF expects the average CPI inflation to be 10.2% in 2020-21 vs. 8.6% last year. The country's CPI inflation is set to rise going forward because of; a) recent quarterly power tariff adjustments; b) supply chain disruptions; and c) estimation of quarterly house rent survey.
- According to the IMF, Pakistan's unemployment to increase by 0.6% to 5.1% for 2020-21 vs. 4.5% last year. This surge in unemployment is almost 13% on a year-on-year basis. This unemployment has become a real challenge for the policy makers and reducing the unemployment rate should now be a priority for this incumbent Government.
- The Financial Action Task Force, through its virtual plenary held on the 23rd of October 2020 has decided that Pakistan will remain on the Grey list. It acknowledged that Pakistan has made significant progress in 21 of the 27 points stated in its action plan. It went on to state that Pakistan must do more by implementing the remaining 6 of the points in the action plan. The next review is scheduled for February 2021, after which an on-site inspection will be due to ensure whether Pakistan is promoted to the White list or not.
- There are considerable downside risks to Pakistan's economy which include; a) resurgence of a 2nd wave of COVID-19; b) delaying in implementation of structural reforms; and c) external financing risks.