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Economy showing gradual recovery, likely to achieve GDP growth target for FY10: SBP Annual Report

Pakistan's economy is showing a gradual recovery and real gross domestic product (GDP) growth is likely to be close to the target of 3.3 percent during the current fiscal year (2009-10), according to State Bank's Annual Report on State of the Economy for the year 2008-09 released today.

The Report said that signs of recovery during FY10 are evident from a rise in imports during July 2009, which points towards a possible pick up in domestic demand, comparatively lower decline in large scale manufacturing (LSM) growth and resolution of circular debt problem that would support production activities in oil and energy sectors.

"The anticipated recovery may also be supported by the re-stocking of inventories and a small recovery in exports as the incipient recovery in major economies gathers pace," it said and added that as a result, growth in LSM production is likely to turn positive during the first quarter of FY10. Moreover, SBP Report pointed out that a sharp fall in inflation in recent months has reduced uncertainty over relative prices and would support increase in investment demand. Although current SBP projections indicate that average annual inflation for FY10 is likely to ease, there remain significant risks to the inflation outlook.

Going forward, the Report projected that GDP growth is likely to be between 2.5 - 3.5 percent in FY10, while average CPI annual inflation is expected to be 10 - 12 percent and both the fiscal and current account deficits are likely to be 4.7 - 5.2 percent.

SBP Report said that external sector too is expected to show a continuation of positive recent trends and exports are expected to pick-up a little, especially if the energy crisis eases, helped by favorable exchange rate trends. Similarly the strong growth in remittances may continue, aided by the new initiative fostering increased usage of the formal system, and the concurrent crack down on illegal activities of exchange companies. Recently, as Pakistan's macroeconomic picture stabilized, portfolio flows have also resumed. "This said, considerable risks remain, as imports are also expected to revive, and there are also risks that some anticipated foreign exchange flows may not be forthcoming or may be delayed," it pointed out.

The Report said that as clearly illustrated by developments in the last two years, and given the weak global economy, the most sustainable impetus to Pakistan's economy will have to come from the agriculture. "Given favorable weather, and in light of high prices of agri-commodities, and supportive government policies, agri-sector performance is expected to be close to the FY10 target," it said.

In the medium to long term, however, it said the upside potential is far greater, with heavy investments required in the sector to improve yields, lower post-harvest losses, improve water management, and increase value addition. "This investment would ensure food security for the country, help contain inflationary pressures, lower the import bill, and offer considerable export prospects, in addition to the considerable potential for employment," the Report said.

The Report said that over the longer term, there are significant shifts already underway in international trade and commerce following the onset of the recent international crisis. Many Asian economies that suffered serious output losses due to their earlier focus on major Western economies are raising questions on their export-led growth models and are also increasing focus on regional trade.

"Pakistan has to be an active participant in this re-alignment, as it will be crucial to developing new trade markets and relations, and to diversify the export base," it added.

It also said that given restricted capital flows because of recent international financial market crisis, it is imperative to mobilize domestic savings to finance a greater part of domestic investment. To mobilize savings, it is necessary to build savings institutions that can tap pension and provident funds, it said and added that establishment of efficient secondary debt market, particularly for tradable government paper, is also needed to offer competitive returns on savings and increase public participants. "A side benefit of such developments is likely to be improvement in the efficiency of the banking system, and improved monetary policy transmission," the Report added.

The Report said that the Government's macroeconomic stabilization program in FY09 resulted in considerable fiscal consolidation during the year. The crux of the macroeconomic policy involved tightening monetary and fiscal conditions to contain the demand for domestic goods (to curb inflationary pressures), foreign goods (to cut imports and mitigate exchange rate pressures), as well as other measures to remove (or ease) structural bottlenecks, it added. As a result, overall fiscal deficit dropped to Rs 680.4 billion during FY09 from Rs 777.2 billion in the preceding year. As a percentage of GDP, the fiscal improvement led to a reduction in the budget deficit by 2.4 percentage points to 5.2 percent during FY09. "The consolidation of fiscal balance largely represents a steep deceleration in the growth of total expenditures," the Report added.

The Report said that during FY09 real GDP growth remained at 2 percent, while average inflation stood at 20.8 percent whereas fiscal and current account deficits remained at 5.2 percent and 5.3 percent, respectively.

The detailed Report can be accessed at SBP website www.sbp.org.pk.

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