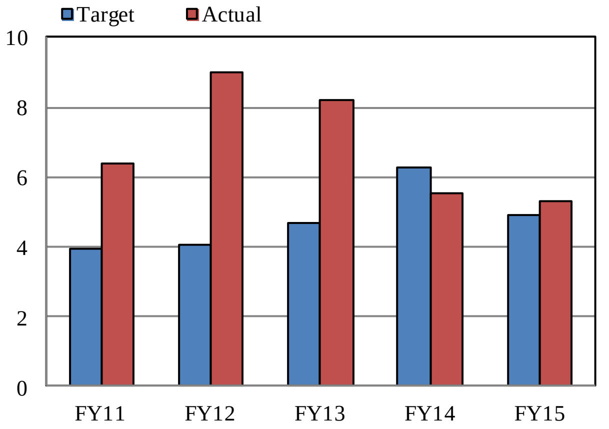
5 Fiscal Policy

5.1 Overview

The budget deficit during FY15 was 5.3 percent of GDP, which was lower than 5.5 percent witnessed during the last year (**Figure 5.1**). If compared with the target for the year, the deficit was slightly higher.[1] While the fiscal consolidation during the year was challenged by lower than expected tax revenues, expenditures remained under control. The budget FY15 envisaged a growth rate of 30.1 percent in total taxes – major part of which was to be collected by FBR; however, actual growth rate of taxes realized during the year was 17.7 percent. Key factors affecting tax revenues were: (i) sharp decline in oil prices, which adversely affected sales tax collection; (ii) continuing issues with tax enforcement; and (iii) subdued manufacturing activity.

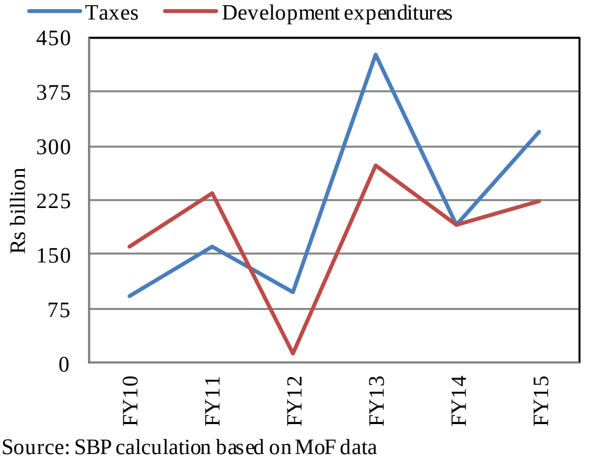
Figure 5.1: Fiscal Deficit - Target and Actual (percent of GDP)



Source: Ministry of Finance

Sluggish tax collection, in turn, squeezed the space for development expenditures: in order to consolidate fiscal account and to keep overall deficit within target, the government could increase public sector development expenditures by 14.1 percent instead of the target of 35.8 percent.[2] In fact, a shortfall in revenue has a direct bearing on development expenses, as shown by **Figure 5.2**. As public development expenditure are key to stimulate overall investment and growth, the shortfall in tax revenues eventually hurts economic growth.

Figure 5.2: Deviations from Target



Source: SBP calculation based on MoF data

Despite taking several measures to raise tax collection, FBR could not achieve its target.[3] This indicates structural problems in the taxation system, including: (i) large informal economy and lack of documentation, (ii) low social and economic cost of tax evasion, (iii) complexities involved in voluntary tax payments; and (iv) administrative issues in tax collecting authority. These issues cannot be addressed by makeshift measures to increase revenues. This needs a national campaign for

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[1] The FY15 target for the budget deficit was Rs 1,421.8 billion; whereas actual deficit turned out to be Rs 1,456.7 billion.

[2] Although the government maintained a high pace of development expenditures up to the third quarter of FY15 with a growth rate of above 27 percent (**SBP 3rd Quarterly Report FY15**), it had to hold them back in the last quarter as revenue shortfall continued.

[3] Revenue measures introduced in the budget FY15 included: expanding the scope of withholding tax; introducing differential tax rates for filer and non-filer; increasing sales tax rate on petroleum products; imposing regulatory duties on certain import items (which also had revenue implications); sending notices to prospective taxpayers, etc.

taxation by taking all segments of the society on board. Further delay in such an all-inclusive campaign may impede the growth momentum of the economy.

Another factor making fiscal consolidation difficult in FY15 was low level of provincial surplus. The provinces could not show targeted amount of the budget surplus: actual surplus was only Rs 87.3 billion in FY15, against the target of Rs 289 billion. One reason was that they did not receive budgeted amount from divisible pool due to revenue shortfall; and second, their current expenditures also increased sharply with a growth rate of 18.2 percent in FY15 (see **Section 5.4** for details). However, it is encouraging that the federal government was able to contain its current expenditure with 7.3 percent growth in FY15, compared with 10.4 percent in the year before (**Table 5.1**). In fact, federal current expenditure, excluding interest payment and defence, declined during the year.

Table 5.1: Summary of Fiscal Operations
Rs billion

	FY14	FY15		% of GDP		% Growth	
		Target	Provisional	FY14	FY15	FY14	FY15
Total Revenue	**3,637.3**	**4,220.6**	**3,931.0**	**14.5**	**14.4**	**22.0**	**8.1**
Tax revenue	2,564.5	3,337.2	3,017.6	10.2	11.0	16.6	17.7
Non-tax revenue	1,072.8	883.3	913.4	4.3	3.3	37.0	-14.9
Total Expenditure	**5026.0**	**5,642.4**	**5,387.8**	**20.0**	**19.7**	**4.7**	**7.2**
Current	4,004.6	4,462.3	4,424.7	16.0	16.2	9.4	10.5
Federal	2,831.2	3,097.3	3,037.6	11.3	11.1	10.4	7.3
Interest payments	1,147.8	1,325.2	1,303.8	4.6	4.8	15.8	13.6
Defence	623.1	700.1	697.8	2.5	2.5	15.3	12.0
Other federal	1,060.4	1,072.0	1,036.0	4.2	3.8	2.6	-2.3
Provincial	1,173.3	1,365.0	1,387.2	4.7	5.1	7.1	18.2
Development	1,135.9	1,180.1	1,113.2	4.5	4.1	46.2	-2.0
PSDP	865.5	1,175.0	987.8	3.5	3.6	24.5	14.1
Others	270.5		125.5	1.1	0.5	229.8	-53.6
Net lending	100.6		27.4	0.4	0.1	-72.3	-72.8
Statistical discrepancy	-215.1		-177.6	-0.9	-0.6		
Overall Budget Deficit	**1,388.7**	**1,421.8**	**1,456.7**	**5.5**	**5.3**	**-24.3**	**4.9**
Revenue deficit	367.3	241.7	493.7	1.5	1.8		
Primary deficit	240.9	96.6	153.0	1.0	0.6		

Source: Ministry of Finance

Financing mix of the fiscal deficit

After a considerable improvement in the financing mix of the fiscal deficit in FY14, when external receipts financed 36.8 percent of the deficit, FY15 witnessed lower level of external inflows – financing only 12.4 percent of the budget deficit. While large amounts under Pakistan Development Fund and through Eurobonds were mobilized during the last year, the current year could not maintain the same pace. Receipts under both the project aid and program loans were lower in FY15, compared with the last year. Moreover, US$ 1 billion were mobilized through issuing Sukuk in the international market in FY15 – half the amount mobilized through Eurobond in FY14. Total external financing (net of repayments) stood at Rs 181.0 billion during the year, compared with the target of Rs 508 billion (**Table 5.2**).

Table 5.2: Financing of the Budget Deficit
Rs billion

	FY11	**FY12***	**FY13**	**FY14**	**FY15**	
					Budget	**Provisional**
External sources	107.7	128.7	-1.7	511.7	508.0	181.0
Domestic sources	1,086.7	1,632.1	1,835.5	877.0	913.9	1,275.7
Banks	615.1	1,102.7	1,457.5	323.7	227.9	892.1
SBP			505.9	159.9	0.0	-434.3
Commercial banks			951.7	163.9	227.9	1,326.4
Non-bank	471.6	529.4	378.0	553.3	686.0	366.1
Privatization						17.5
Total	1,194.4	1,760.8	1,833.9	1,388.7	1,421.9	1,456.7

*: The deficit in FY12 includes the one-off payment of Rs 391 billion for PSEs' debt settlement.
Source: Ministry of Finance

As a result, the pressure of budget financing increased on the banking system. However, within the banking system, government relied more on commercial banks and retired the central bank's debt (see **Chapter 4** for detail). Domestic non-bank is the third source of financing the budget deficit, which should be preferred over banks as it also reflects savings trend in the economy. There are two main sources of non-bank financing: national saving schemes (NSS) and private sector's investment in government securities. While mobilization of funds through national saving schemes increased sharply from Rs 140.0 billion in FY14 to Rs 260.2 billion in FY15, mainly on the back of institutional investment, private sector's investment in government securities declined following the reduction in interest rates.

5.2 Revenue

The total revenue receipts (tax and non-tax) stood at Rs. 3,931.0 billion in FY15, showing a growth of 8.1 percent – half the growth targeted in the budget. This was entirely due to a shortfall of Rs 319.6 billion in tax revenues from their target. The non-tax revenues, on the other hand were more than the target, mainly due to high SBP profit and receipts under coalition support fund.

Within tax revenues, FBR taxes were Rs 2,588.2 billion in FY15, compared with the original target of Rs 2,810 billion for the year (**Table 5.3**). The FBR target was subsequently revised downward to Rs 2,605 billion. However, actual collection still could not get to the mark.

Although FBR takes a number of measures every year to increase tax collection, it could not improve its achievements. As structural problems in the taxation system persist, the FBR tax-to-GDP ratio remained stagnant in the range of 8.5 percent to 9.5 percent over the last ten years (**Figure 5.3**). The government has envisaged this ratio to increase to 11.3 percent in FY18 by taking various measures to document the economy, and to broaden the tax base. Significant structural tax measures are needed to bolster the tax to GDP ratio.

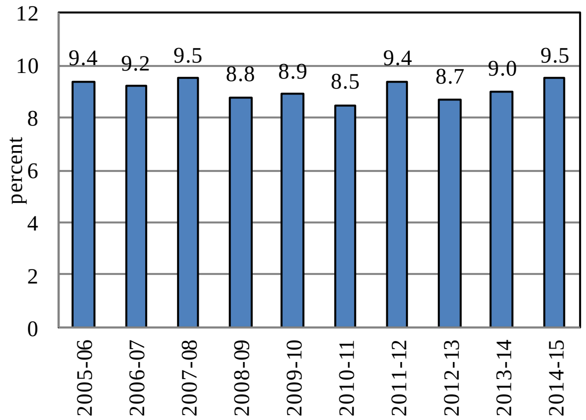
Table 5.3: FBR Tax Collection

Rs billion

	FY 14	FY 15		% Growth	
		Budget	Actual	FY14	FY15
Direct tax	884.1	1,180.0	1,029.2	18.0	16.4
Sales tax	1,002.1	1,171.0	1,088.8	18.3	8.6
Customs duty	241.0	281.0	306.1	1.4	27.0
Federal excise	139.1	178.0	164.0	14.1	17.9
Total	2,266.3	2,810.0	2,588.2	15.8	14.2

Source: Ministry of Finance

Figure 5.3: FBR Tax-to-GDP



Source: Federal Board of Revenue

Direct tax

Direct taxes posted a growth of 16.4 percent in FY15, compared to 18.0 percent in FY14. Withholding tax, having largest share in direct taxes, grew by 20.9 percent.[4] Main economic activities contributing to the withholding tax are international trade and contracts. Withholding tax from international trade showed a growth of 15.6 percent in FY15 – lower than the last year, mainly due to sharp fall in commodity prices. Meanwhile, tax collection from contracts showed a considerably high growth rate of 36.1 percent in FY15 – more than double the growth in the last year (**Table 5.4**).

[4] Withholding tax has the share of above 60 percent in total direct taxes.

Voluntary payments, constituting one fourth of the total income tax, recorded a growth of 9.5 percent, compared to 7.2 percent during the previous year, which is quite encouraging. On a positive note, collection on demand recovered radically by reflecting a growth rate of 43.3 percent in FY15, which was negative during the previous year. FBR has started issuing notices to potential tax payers, identified through NADRA data base and other information. If this campaign succeeds, the collection on demand can be a promising head of income tax collection.[5]

Table 5.4: Break-up of Direct Taxes*
Rs billion

	FY14	FY15	Growth (%)	
			FY 14	FY 15
Voluntary payments	262.6	287.6	7.2	9.5
Collection on demand	80.6	115.5	-9.8	43.3
Withholding tax	571.7	691.2	31.1	20.9
Imports and exports	150.2	173.6	18.8	15.6
Contracts	129.9	176.8	16.5	36.1
Salary	64.6	79.5	28.9	23.1
Interest & securities	40.7	49.8	15.3	22.4
Cash withdrawal	19.1	23.9	54.0	25.1
Dividends	24.2	29.4	26.0	21.5
Electric bills	19.8	27.5	23.8	38.9
Telephone	52.0	44.7	91.9	-14.0
Others	71.4	86.1	163.5	20.6
Miscellaneous	4.0	10.0	-28.6	150.0
Gross Income tax	918.9	1,104.3	18.4	20.2
Other direct taxes	22.1	24.3	6.3	10.0
Total direct taxes (gross)	941.0	1,128.6	18.1	19.9

*: Break-up is based on provisional data; overall numbers may not tally with Table 5.3.
Source: Federal Board of Revenue

Sales tax

Sales tax collection showed a modest growth of 9.3 percent in FY15, compared to 18.3 percent in FY14. Despite the increase in sales tax rate, the growth rate of sales tax collection on domestic goods & services was only 6.0 percent in FY15, compared to 23.6 percent in FY14. Likewise, the growth rate of sales tax collection on imports also fell from 15.3 percent in FY14 to 12.4 percent in FY15 **(Table 5.5).**

Main factors adversly affecting sales tax collection were: (a) an overall decline in the inflation rate largely due to sharp fall in prices of petroleum products, which are the largest source of sales tax collection;[6] and (b) decline in sales tax collection on fertilizers and natural gas due to lower supplies. Moreoever, lack of documentation in retail trade activites continued to be a source of concern.

Table 5.5: Sales Tax on Domestic and Import Stage*
Rs billion

	FY 14	FY 15	Growth (%)	
			FY 14	FY 15
Domestic				
POL Products	230.7	233.2	29.9	1.1
Natural Gas	31.6	22.8	-12.9	-27.8
Fertilizers	24.0	22.5	53.8	-6.3
Cement	20.1	23.3	84.4	15.9
Electrical energy	19.7	23.8	121.3	20.8
Cigarettes	17.7	21.0	22.1	18.6
Aerated waters/bev.	8.8	8.8	-18.5	0.0
Sugar	9.2	10.9	10.8	18.5
Motor Cars	3.8	9.3	18.8	144.7
Other sectors	135.4	155.6	13.7	14.9
Total	**501.1**	**531.2**	**23.6**	**6.0**
Imports				
POL Products	169.6	166.0	8.5	-2.1
Iron and Steel	27.6	41.9	26.9	51.8
Mech. machinery	26.1	38.0	33.6	45.6
Elec. machinery	18.8	35.4	29.5	88.3
Vehicles	26.0	34.3	-3.0	31.9
Plastic resins etc.	27.8	30.7	35.0	10.4
Edible Oil	33.9	16.6	5.1	-51.0
Fertilizers	12.8	13.7	21.3	7.0
Org. chemicals	13.3	13.0	33.5	-2.3
Others	139.5	167.0	18.7	19.7
Total	**495.4**	**556.6**	**15.3**	**12.4**

*: Break-up is based on provisional data; overall numbers may not tally with Table 5.3.
Source: Federal Board of Revenue

Customs and federal excise duties

In FBR taxes, the importance of customs and federal excise is declining overtime, as sales tax (on domestic goods & services and imports) is replacing them. The two taxes together contributed 18.2 percent in total FBR tax collection duirng FY15, compared with, for example, 33.8 percent in FY00.[7]

[5] According to Ministry of Finance, in order to increase the tax net, existing database of 3.6 million individuals holding the National Tax Number (NTN) is to be merged with the Computerized National Identity Card (CNIC) data comprising information of 150 million people.
[6] Domestic sale of POL products contribute more than 40 percent of the domestic sales tax collection; while contribution of imported POL products is about 30 percent to sales tax collected at imports stage.
[7] Once customs duty alone used to be the largest source of tax revenues, like 1990 when its share was 45 percent in total taxes. However, following the policies of increasing trade liberalization, the tariff rates were reduced significantly. A number of imported items are subject to zero rates. Currently, more than 60 percent of Pakistan's imports are non-dutiable.

The customs duty is concentrated in few items, i.e., vehicles, machinary and petroleum products, which contributed around one third of the total duty collection in FY15. On the other hand, 80 percent of the federal excise duty comes from only five items: cigarettes, beverages, natural gas, cement and edible oil. Going forward, the share of these sources of taxes is expected to decline further as the coverage of sales tax by federal and provincial governments is expanding.

Table 5.6: Non-tax Revenues
Rs billion

	FY14	FY15 Budget	FY15 Provisional
Profits PO/PTA*	94.8	70.7	3.7
Mark-up	67.0	26.0	14.2
Dividend	65.9	82.0	74.1
SBP profit	326.2	270.0	399.0
Defence	117.2	140.0	157.1
Royalities on oil and gas	76.4	81.4	74.1
Citizenship/passport fee	19.0	20.0	18.7
Discount retained on crude oil	40.7	20.0	9.7
Windfall levy on crude oil	14.6	17.0	12.2
Foreign grants	12.3	35.0	21.9
Others	238.6	121.2	128.8
Total	**1,072.7**	**883.3**	**913.4**

*: Including 3G/4G fee
Source: Ministry of Finance

Non-tax revenue

The non-tax revenue collected during FY15 were higher than the target set for the year (**Table 5.6**). This was backed by sharp increases in SBP profit and defence related receipts (essentially CSF), which more than compensated shortfall in other accounts, like 3G/4G auction fees.

Table 5.7: Break-up of Current Expenditures
Rs billion

	FY14	FY15 Budget target	FY15 Actual	% growth Target	% growth Actual
Overall	**4,004.6**	**4,462.3**	**4,424.7**	**11.4**	**10.5**
Federal	**2,831.2**	**3,097.3**	**3,037.6**	**9.4**	**7.3**
General public services	1,991.3	2,177.4	2,105.4	9.3	5.7
Debt Servicing	1,147.8	1,325.2	1,303.8	15.5	13.6
Domestic	1,072.8	1,224.6	1,208.1	14.1	12.6
Foreign	75.0	100.6	95.7	34.1	27.6
Pension	180.2	215.0	185.2	19.3	2.8
Subsidies	305.7	203.2	241.6	-33.5	-21
Grants	283.2	338.0	288.1	19.4	1.7
Others	74.4	96.0	86.7	29.0	16.6
Defense	623.1	700.1	697.8	12.4	12.0
Public order & safety	86.2	86.5	83.3	0.3	-3.4
Economic affairs	43.4	47.6	53.0	9.7	22.2
Education	65.4	64.0	73.2	-2.1	11.9
Health	10.1	10.0	10.9	-1.0	7.6
Others	11.7	11.7	13.9	0.0	19.1
Provincial	**1,173.3**	**1,365.0**	**1,387.2**	**16.3**	**18.2**

* Provisional estimates taken from 2015-16 Budget Documents
Source: Ministry of Finance

Similarly, the FED's share also declined due to removal of items eligible for FED. However, such items were brought under sales tax net..

Moreover, energy related receipts, i.e., royalities on oil and gas, discount retained and windfall levy on crude oil also declined during the year, mainly due to reduction in global oil prices. Similarly, the Mark-up income (PSEs and others) also fell short of target due to declining interest rate scenrio.

5.3 Expenditures

During FY15, total expenditures (federal and provincial) grew by 6.2 percent, compared with 9.5 percent last year.[8] This was mainly due to sharp reduction (53.6 percent) in development spending outside PSDP, and lower net lending to public sector enterprises (PSEs). Expenditures on PSDP also could not maintain the growth momentum witnessed during the last year: they showed a growth of 14.1 percent in FY15, compared with 24.5 percent last year; and remained considerably lower than the target set for the year.

Although current expenditures also were slightly lower than the target, they increased by a growth of 10.5 percent in FY15, against 9.4 percent last year (**Table 5.7**). This was mainly due to growth in provincial current expenditures, which increased sharply with a growth of 18.2 percent in FY15, compared with 7.1 percent in FY14. This is indicates their enhanced role envisaged under the 18th amendment of the constitution (reduction in the concurrent list), as well as higher expenditure for law and order by the provinces.

Regarding the federal government's current expenditures, their growth in FY15 was considerably lower than that in FY14, as mentioned earlier. Major portion of federal current expenditure is interest payments, having a share of more than 40 percent. Running down large fiscal deficits over the years by successive governments have substantially increased interest payments, which in FY15 has reached Rs 1,303.8 billion (4.8 percent of GDP). However, reduction of 350 basis points during FY15 in the policy rate helped reduce the pace of interest expense on government's domestic debt, which increased by 12.6 percent in FY15, compared with 16.6 percent last year.[9]

Table 5.8: Break-up of Development Expenditures

Rs billion

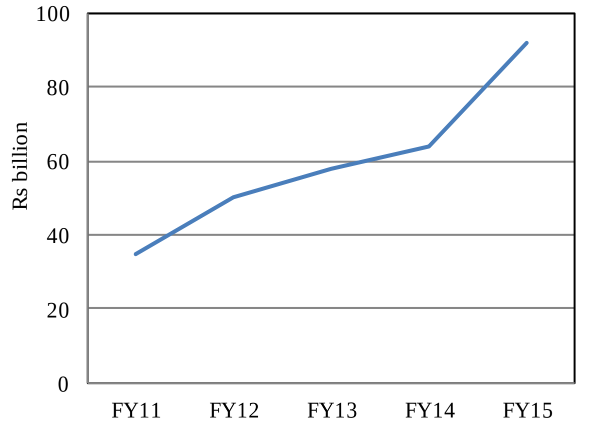
		FY15		% growth FY15	
	FY14	Budget target	Actual	Target	Actual
Development expenditures &. net lending	1,236.5	1,344.1	1,140.6	8.7	-7.8
Development expenditures	1,135.9	1,336.8	1,113.2	17.7	-2.0
PSDP	865.5	1175	987.8	35.8	14.1
Federal*	434.9	525	488.9	20.7	12.4
Provincial	430.5	650	498.8	51.0	15.9
Other development expenditures	270.5	161.8	125.5	-40.2	-53.6
BISP**	63.9	97.2	91.8	52.1	43.6
Others	206.6	64.7	33.7	-68.7	-83.7
Net Lending	100.6	7.2	27.4	-2.6	-72.8

* Net (excluding Rs. 13.258 billion development grants to provinces)
** Provisional estimates taken from 2015-16 Budget documents
Source: Ministry of Finance

[8] Total expenditure discussed in this section does not include statistical discrepancy.
[9] In FY15, the weighted average yield on T-bills has come down to 8.76 percent from 9.70 in FY14. Similarly, weighted average yield on PIBs fell to 10.78 percent compared to 12.26 percent in FY14.

Encouragingly, subsidies have declined by 21.0 percent over last year to reach Rs 241.6 billion in FY15 (0.9 percent of GDP)[10] – especially electricity subsidies. Instead, electricity tariffs for commercial and industrial users were revised upwards through the imposition of surcharges. Defense spending also slowed down in FY15 with a growth of 12.0 percent, compared with 15.3 percent growth witnessed last year.

Figure 5.4: Expenditures under BISP



Source: Provisional estimates taken from budget documents

Historically, defense expenditures are the second largest item in the federal current outlays, which remained broadly in line with the FY15 budget: Rs 697.8 billion versus the budget target of Rs 700.1 billion. Similarly, growth in pension also declined significantly from 4.4 percent in FY14 to 2.8 percent in FY15.

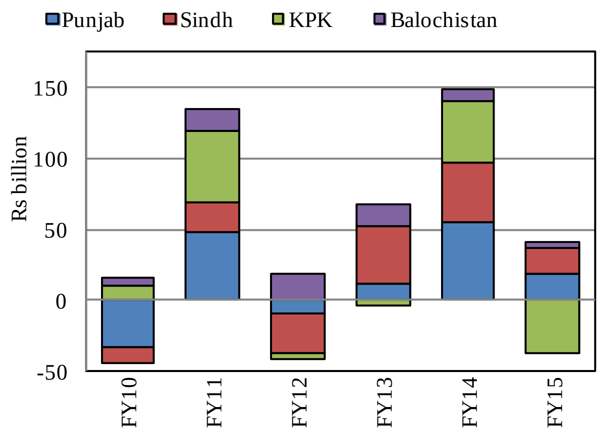
Development expenditures & net lending to PSEs[11] fell by 7.8 percent in FY15, compared to the last year (**Table 5.8**).[12] Specifically, development outlays other than PSDP and lending to PSEs witnessed negative growth rates during the year. However, expenditure under Benazir Income Support Program – a part of development spending outside PSDP – continued to show a robust growth (**Figure 5.4**).

Although expenditures under PSDP, both by the federal government and provincial governments, were 14.1 percent higher than the previous year, they remained short of their respective targets. As discussed earlier, main reason for this shortfall was underperformance of tax revenues, which adversely affected the availability of resources for both federal and provincial government.

5.4 Provincial Fiscal Operations

Unlike FY14, the budget surplus target assigned to provinces was missed by a wide margin in FY15. Against the target of Rs 289.3 billion, the actual balance stood at only Rs 87.3 billion during the year (**Figure 5.5**).[13] This decline was brought about by fall in tax revenues as well as healthy growth in current expenditures.

Figure 5.5: Provincial Balances



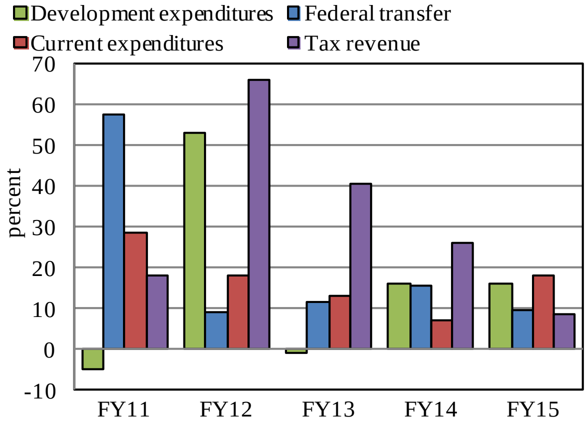
Source: Ministy of Finance & Budget Documents

As usual, the provinces continued to rely mainly on transfers from federal revenues. Despite significant untapped potential of resource mobilization, provinces are still struggling with capacity and procedural

[10] This was in line with the commitment made to IMF to bring down the subsidies to 0.8 percent of GDP.
[11] Net lending is a part of overall development expenditure. This includes development loans and advances to Provinces, Government of Azad Jammu & Kashmir, Public Sector Enterprises (PSEs), Financial / Non-Financial Institutions, District Governments / TMAs, and Others to assist them in carrying out their development programs.
[12] However, last year an amount of Rs 157.2 billion was included in 'Other development expenditure'. If we adjust for this amount, the growth in total development expenditure comes out 5.7 percent.
[13] The gap between provincial revenue and expenditures is Rs 3.6 billion; however, as per practice by the Ministry of Finance, the provincial fiscal balance is defined as the outstanding balances of provinces with the banking system.

issues in collecting their own taxes on sales of services and agriculture. As provinces have higher fiscal responsibility and resources after 18th amendment and 7th NFC award, they have to move fast to increase their capacity of taxation and handling large public projects.

Figure 5.6: Provincial Revenue & Spending Growth



Source: Ministry of Finance

During FY15, taxes collected by provinces themselves showed a growth rate of 8.4 percent – a five years lowest level (**Figure 5.6**). Only Sindh has shown a robust growth in its own tax collection. Although the standard rate of GST on services was lower in Sind compared to Punjab, improved tax collection by Sindh was based on relatively wider tax base and low level of exemptions.[14] Apart from Sales tax on services, the provinces are required to raise more revenue through untapped areas like “agriculture income tax”.[15] Such efforts will not only help to fill the revenue gap of the provinces but could also lift the low tax-to-GDP ratio in the region.

Table 5.9 : Provincial Fiscal Operations
Rs billion

	Punjab		Sindh		KPK		Balochistan		All Provinces	
	FY14	FY15	FY14	FY15	FY14	FY15	FY14	FY15	FY14	FY15
A. Total revenue	**803.6**	**892.1**	**490.6**	**533.7**	**302.8**	**288.7**	**170.6**	**187.9**	**1767.4**	**1902.4**
Share in divisible pool	646.3	726.9	383.7	406.2	234.4	250.7	141.9	154.9	1406.3	1538.7
Taxes	96.5	98.1	79.1	93.8	11.7	11.4	2.8	2.6	190	205.9
Non-taxes	23	45.3	5.4	8.4	16.8	18.4	4.2	3.5	49.4	75.6
Federal loans & grants	37.8	21.9	22.4	25.3	39.8	8.2	21.7	26.9	121.8	82.3
B. Total expenditure	**748**	**872.9**	**449.1**	**516.5**	**259.7**	**326.9**	**161.1**	**182.7**	**1617.9**	**1899**
Current*	551.7	662.9	328.2	383.4	187.1	221.8	120.4	131.9	1187.4	1400
Development	196.3	210	120.9	133	72.6	105.1	40.7	50.7	430.5	498.8
C. Overall balance (A-B)	**55.6**	**19.3**	**41.4**	**17.2**	**43**	**-38.2**	**9.5**	**5.3**	**149.5**	**3.6**
Financing#	**-98.5**	**-43.0**	**-37.7**	**-27.5**	**-40.4**	**7.9**	**-20.4**	**-24.7**	**-196.9**	**-87.3**

*: Overall provincial current expenditures in this table does not tally with those in Table 5.1, which give consolidated federal and provincial numbers. The consolidated numbers exclude fiscal transactions among federal and provincial governments.
#Balance of provincial accounts with the banking system
Source: Ministry of Finance

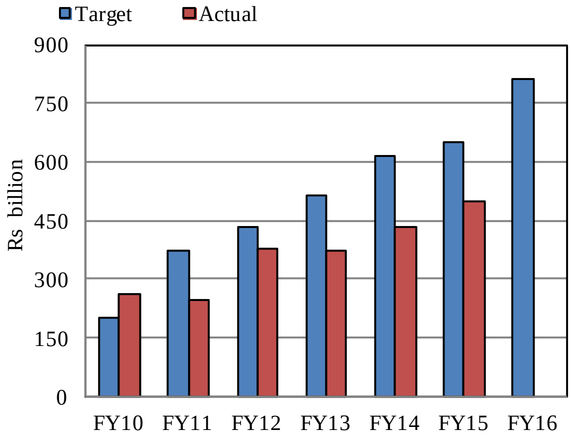
Another important development on the provincial revenue side was the 26.2 percent increase in non-tax revenue in FY15, compared with 7.0 percent decline last year. Grants from the federal government, was the major contributory factor to this increase in non-tax revenues. It is important to note here that the federal grants which are the part of federal PSDP are utilized through provinces; and about 60 percent of these grants were spent in the Punjab.

Coming to expenditure side, the growth in provincial expenditures was 17.4 percent in FY15 compared to 9.2 percent last year. This growth was primarily due to current expenditures, as their development budget was underutilized in FY15. They utilized Rs 498.8 billion during the year,

[14] Standard rate of GST was reduced to 15 percent in Sindh, whereas it stood same at 16 percent in Punjab in Budget 2014-15. Further, the exemption provided by Sindh government to property developers and on insurance premium (below threshold of Rs 500,000) was withdrawn in budget 2014-15.
[15] Although the provinces set targets for agriculture income tax, actual realization is much lower than its capacity, measured in terms of its contribution in GDP.

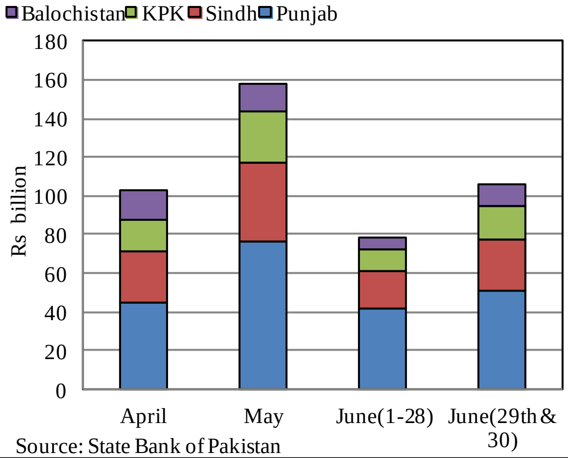
compared with the target of Rs 650.0 billion set for provincial PSDP (**Table 5.9**). The main factor behind this shortfall was: (i) understanding between federal and provincial to generate surpluses; and (ii) the timing of the federal transfer of funds to the provinces. Specifically, the pattern of federal transfers to provinces suggests that the amount equivalent to 70.0 percent of PSDP shortfall was transferred on 29 and 30th June 2015, and that, in turn, reflected as the major part of the surplus recorded in FY15 (**Figure 5.7**).

Figure 5.7: Provincial PSDP



Source: Ministry of Finance

Federal Transfer to Provinces



Source: State Bank of Pakistan

During FY15, the provincial current expenditures increased by 17.9 percent, compared with 7.0 percent last year. This was broadly driven by increase in *social sector spending* and *public order & safety* by all provinces. The province-wise composition of current spending suggests that Punjab spent the most on social sector, mainly on account of rehabilitation of flood affected population in September 2014.[16]

Distribution of development outlays:[17]

Punjab spent a significant portion of development budget on *economic affairs* (including mainly construction) and *housing & community amenities* (**Table 5.10**). Interestingly the Punjab government spent more than budgeted amount on construction of roads, which also included rehabilitation of flood damaged roads.[18] On the contrary, the share of health and education constitutes about 15.0 percent of total development spending for FY15, which was the lowest among provinces.

Like Punjab, expenditure on infrastructure development remained priority area for other three provinces. On positive, both Sindh and KPK spent higher amounts on education, health, and social protection during the year, compared with the last year. Furthermore, spending on agriculture and irrigation (a part of economic affairs head) also represents major share of Sindh development outlay. In addition, Balochistan spent a large portion of development outlays on education, health, housing and community amenities.

[16] The Government of Punjab allocated Rs. 18.9 billion for the rehabilitation of flood affected population of the province (Source: PUNJAB: White Paper Budget 2015-16).

[17] The sectoral distribution of development expenditures by provinces has been taken from their respective budget documents. Since there is no standard format of presenting details in these documents, we face difficulties in getting comparable numbers under different heads. Therefore, there may be some difference in our calculations regarding shares of different sectors.

[18] During 2014-15, Rs 2.8 billion was allocated for rehabilitation of flood damaged roads.

Table 5.10: Composition of Development Spending

	Rs billion				Percent Share			
	Punjab	Sindh	KPK	Balochistan	Punjab	Sindh	KPK	Balochistan
General public services	41.9	35.4	20.3	3.9	14.4	24.4	15.1	6.1
Public order and safety affairs	1.0	17.6	0.4	1.1	0.3	12.1	0.3	1.7
Economic affairs	111.8	31.0	44.3	28.9	38.5	21.4	32.9	45.4
Environment protection	0.0	1.1	6.0	5.2	0.0	0.8	4.5	8.2
Housing and community amenities	86.2	1.1	16.4	8.3	29.7	0.8	12.2	13.0
Health	25.7	13.7	10.1	3.8	8.8	9.4	7.5	6.0
Recreation, culture and religion	1.2	1.6	1.9	2.3	0.4	1.1	1.4	3.6
Education affairs and services	19.1	32.5	30.3	10.0	6.6	22.4	22.5	15.7
Social protection	3.6	11.0	4.9	0.2	1.2	7.6	3.6	0.3
Total	**290.5**	**145.0**	**134.7**	**63.7**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Provincial Budget Documents