2 Real Sector

2.1 Overview

The FY15 Annual Plan aimed to achieve GDP growth of 5.1 percent on account of better energy supplies, favorable weather conditions, improved investment outlook, some fiscal consolidation, and political stability. The Plan relied on industrial and services sector to steer GDP growth, as the target for agriculture sector was closer to the historical average.

Table 2.1: GDP Growth Rate
percent

	Share FY15	Growth FY14^R			Contri. to growth
		FY14 R	FY15 P	FY15 Target	
Agriculture	**20.9**	**2.7**	**2.9**	**3.3**	**0.6**
Of which					
Crops	8.3	3.2	1.0	2.4	0.1
Livestock	11.8	2.8	4.1	3.8	0.5
Industry	**20.3**	**4.5**	**3.6**	**6.8**	**0.7**
Of which					
LSM	10.6	4.0	2.4	7.0	0.3
Construction	2.4	7.2	7.0	7.5	0.2
Services	**58.8**	**4.4**	**5.0**	**5.2**	**2.9**
Of which					
Finance & insurance	3.1	4.2	6.2	5.8	0.2
General govt.	7.4	2.9	9.4	4.3	0.7
GDP	**100**	**4.03**	**4.24**	**5.1**	
Memorandum item					
Investment rate		15.0	15.1	15.7	

R: Revised; P: Provisional
Source: Pakistan Bureau of Statistics

The GDP growth rate did pickup and reached 4.24 percent (a seven-year high), but this still remained well below the target. While the services sector showed a modest recovery, the expected revival in industry could not materialize. Even the marginal recovery in agriculture envisaged in the Plan did not transpire (**Table 2.1**).

Several constraints continue to holdback economic growth during the year: though better than the last year, the security condition remained difficult; the investment rate could not pickup as desired; the crop sector suffered from heavy rains during *kharif* and prolonged low temperature in *rabi*. More importantly, performance of the industry remained sluggish due to weak external demand and persistent energy shortages.

In this situation, some support to GDP growth came from construction sector showing the increased focus on public infrastructure development projects during the year. The major contribution to growth came from the services sector.

Specifically, *general government services* recorded a sharp recovery, reflecting the impact of higher salaries and pension of government employees. In addition, *finance & insurance* posted a recovery on account of strong profitability of the banking sector.

Table 2.2: Value Addition by Agriculture
Share and growth in percent; contribution in percentage points

	FY15 Share	Growth			Contr. to growth in agriculture	
		FY13	FY14^R	FY15^P	FY14^R	FY15^P
Crop	39.6	1.5	3.2	1.0	1.3	0.4
Major crops	25.6	0.2	8.0	0.3	2.0	0.1
Other crops	11.1	5.6	-5.4	1.1	-0.7	0.1
Cotton ginning	2.9	-2.9	-1.3	7.4	0.0	0.2
Livestock	56.3	3.4	2.8	4.1	1.5	2.3
Forestry	2	6.6	-6.7	3.2	-0.1	0.1
Fishing	2.1	0.7	1.0	5.8	0.0	0.1
Overall	**100**	**2.7**	**2.7**	**2.9**		
Annual target		*4.0*	*3.7*	*3.3*		

Source: Pakistan Bureau of Statistics

2.2 Agriculture

A better performance by the livestock subsector during FY15 helped agriculture surpass the previous year's growth level (**Table 2.2**). However, the overall growth in agriculture fell short of the target for the third consecutive year.

The main reason was the weak performance of the crop sector. While wheat, sugarcane and maize (having a combined share of over 60 percent in value addition by major crops) could not achieve last year's production levels, cotton remained short of an ambitious target set for the year. Production of rice surpassed both last year's level, as well as the target (**Table 2.3**).

Table 2.3: Major Crops
Production in million tons; for cotton, in million bales; growth in percent

	% Share in Major Crops (FY15)	Production			Growth	
		FY14	FY15	FY15^T	FY14	FY15
Cotton	28.0	12.8	14.0	15.1	-2.0	9.5
Rice	12.4	6.8	7.0	6.8	22.8	3.0
Sugarcane	12.1	67.5	62.7	65.5	5.8	-7.1
Wheat	39.3	25.9	25.5	26.0	7.3	-1.9
Maize	8.4	4.9	4.7	4.3	17.2	-5.0

Source: Pakistan Bureau of Statistics

Minor crops posted a modest growth of 1.1 percent against the expectation of a strong recovery from significant losses last year. This poor performance of the crop sector was mainly due to low prices received by growers in the last season and adverse weather.[1]

[1] Although it would be early to quantify the impact of falling international commodity prices on the country's crop sector, we believe the crop production has remained largely unaffected, as most of the

Specifically, stagnant sugarcane prices in 2013-14 amid rising input costs, discouraged farmers from growing sugarcane during FY15.[2] Similarly, in the case of cotton, growers did not wait for third or fourth picking due to unattractive market prices. Finally, the prolonged low temperatures and hailstorm at the time of harvest partly damaged the wheat crop.[3]

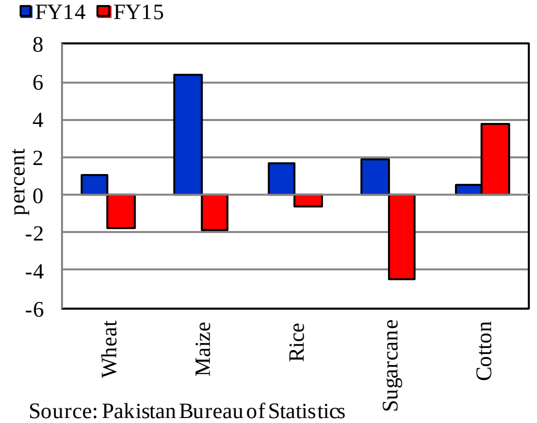
In terms of farm inputs, water availability remained higher than last year for both kharif and rabi crops (**Table 2.4**). In addition, credit disbursement to agriculture recorded a strong YoY growth of 27.5 percent during Jul-Mar FY15. As expected, production loans in the crop sector constituted the bulk of disbursements. However, the fertilizer off-take was low as income of growers came under pressure due to falling prices of agri produce.[4]

Table 2.4: Availability of Inputs

	FY14		FY15	
Water (MAF)				
Kharif		65.5		69.3
Rabi		26.9		28.2
Fertilizer (% change)				
Kharif		6		-4.1
Rabi		17		1.2
Agri Credit Disbursement (Jul-Mar)				
	Disbursement		**YoY Growth**	
	FY14	**FY15**	**FY14**	**FY15**
Total loans	255.7	326.0	10.7	27.5
Production loans	234.7	288.5	10	22.9
Development loans	21.0	37.5	19.4	78.9

Source: Suparco (for Water); NFDC (for fertilizer); and SBP (for credit)

Figure 2.1: Growth in Crop Yield



Source: Pakistan Bureau of Statistics

kharif crops were already near their harvesting stage when the global prices crumpled in September 2014 (even the area under wheat cultivation – the major rabi crop which is sown in December – did not change much from the last year's level). In the meanwhile, farmers' income has come under pressure, when (a) domestic market prices of agri produce declined in line with the international trends (and also due to local dynamics, as in the case of sugarcane); and (b) the input prices (except for diesel) increased despite their falling trends in the global market.

[2] The area under sugarcane crop fell by 2.7 percent during FY15.

[3] The prolonged cloudy weather coupled with hail/wind storms, and untimely rains at the time of harvest, has resulted in a decline in yield of wheat in irrigated areas of northern Punjab and KPK.

[4] Despite an ease in the international prices, the domestic price of urea increased from Rs 1,844 per 50 kg in Mar 2014 to Rs 1,929 in Mar 2015.

One of the key concerns in agriculture is the decline in yield of all major crops (except cotton) during FY15 (**Figure 2.1**). This is disappointing given that the yields are already low in Pakistan. While the use of quality seeds and an efficient application of fertilizer are important for improving the crop yields, there is a need to make farmers aware of best agriculture practices (in the area of land preparation, sowing, water application, use of fertilizers, plant protection, harvesting and post harvesting).

In the case of minor crops, a strong recovery was expected this year as the crops had already suffered extensive damages last year. However, the recorded growth was only 1.1 percent, perhaps due to adverse weather. Within minor crops, pulses (gram, mash and moong), vegetables (especially potatoes and onion), and fruits performed better, whereas oilseeds (rapeseed & mustard, sunflower and canola) recorded a decline as falling international prices translated into lower domestic prices of oilseed crops.

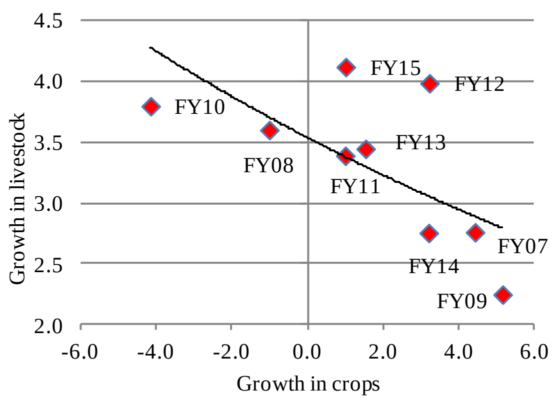
Despite this weak performance from the crop sector, agriculture growth still managed to outweigh last year's level largely due to some recovery in livestock. The value addition in livestock includes headcount of animals and their products (milk, meat and wool, etc.); poultry and its products (meat and eggs); and animal husbandry practices. As shown in **Table 2.5**, the growth in the gross output of livestock has remained unchanged from last year. This was expected as the output is computed by extrapolating results from past

Table 2.5: Value Added in Livestock
billion Rs

			Growth	
	FY14	**FY15**	**FY14**	**FY15**
Gross output (A)	1,461	1,510	3.3	3.3
Animals sold for slaughtering	340	350	2.9	2.9
Natural growth & regeneration	212	218	3.0	3.0
Livestock products	778	801	2.9	2.9
Milk	660	683	3.2	3.4
Others	118	120	1.1	1.3
Poultry products	131	141	7.4	7.5
Intermediate consumption (B)	258	260	6.0	0.8
Gross value addition (A-B)	1,203	1,250	2.7	3.9
Other	5	8	7.3	--
Total Gross VA	**1,209**	**1,258**	**2.8**	**4.1**

Source: Pakistan Bureau of Statistics

Figure 2.2: Livestock and Crop Growth



Source: Pakistan Bureau of Statistics

surveys. The swing factor in FY15 was the intermediate consumption (mainly fodder), which grew by only 0.8 percent compared with 6.0 percent in FY14. Interestingly, the growth in fodder varies directly with the crop sector, i.e., a low crop production results in weak output of fodder. This means, the performance of livestock is also associated with the crop sector: a low growth in crop is generally associated with a strong growth in livestock (**Figure 2.2**).

2.3 Industry

The industrial sector not only recorded a lower growth than the last year, it missed the annual target by a wide margin. The weak performance by the large-scale manufacturing overshadowed a robust growth in the construction sub-sector, and a recovery in mining & quarrying (**Table 2.6**).

Table 2.6: Growth in Industry

Share and growth in percent; contribution in percentage points

	Share in GDP	Growth			Cont to industry growth	
		FY14	FY15	FY15[T]	FY14	FY15
Mining & quarrying	2.9	1.6	3.8	6.5	0.2	0.6
Manufacturing	13.3	4.5	3.2	6.9	2.9	2.1
Large-scale	10.6	4.0	2.4	7.0	2.1	1.3
Small-scale	1.7	8.3	8.2	8.4	0.7	0.7
Slaughtering	0.9	3.4	3.3	--	0.2	0.2
Electricity gene & distt and gas distt	1.7	5.6	1.9	5.5	0.5	0.2
Construction	2.4	7.2	7.0	7.5	0.8	0.8
Industry	**20.3**	**4.5**	**3.6**	**6.8**	**4.5**	**3.6**

Source: Pakistan Bureau of Statistics

Large Scale Manufacturing (LSM)

The LSM growth target of 7.0 for FY15 assumed an improvement in energy availability, and a higher growth for export industries (e.g., textile) due to greater access to EU markets under the GSP plus.

So far, LSM has recorded a YoY growth of only 2.5 percent during Jul-Mar FY15, which is almost half the growth realized in the corresponding period last year (**Table 2.7**).[5] While a part of the slowdown was expected as sugar and fertilizer (the two best performing industries in FY14) could not maintain their growth momentum in FY15, other industries also experienced slowdown. In fact, the number of industries showing a production fall, has increased markedly in Jul-Mar FY15 compared to the corresponding period of FY14 (**Table 2.8**).

[5] The LSM growth of 2.4 percent (used in **Table 2.1**) is the estimated number for FY15, which has been projected on the basis of LSM performance during Jul-Mar FY15.

Table 2.7: Growth in Selected Industries of LSM (Jul-Mar)

In percent

		Cumulative Growth			Percentage Contribution		
	Wt.	**FY13**	**FY14**	**FY15**	**FY13**	**FY14**	**FY15**
LSM	**70.3**	**3.4**	**4.6**	**2.5**	**100.0**	**100.0**	**100.0**
Textile	21.0	0.9	1.5	0.5	8.0	9.2	5.7
Cotton Yarn	13.0	1.3	1.8	0.5	7.0	7.1	3.5
Cotton Cloth	7.2	0.2	0.7	0.1	0.6	1.5	0.2
Food	12.4	7.5	8.4	-1.0	46.8	40.7	-9.6
Sugar	3.5	3.0	10.9	-6.1	8.0	21.0	-23.2
Edible oil	2.2	14.9	0.5	-0.3	14.8	0.4	-0.4
Beverages	0.9	17.1	37.3	14.5	7.5	13.8	13.1
POL	5.4	13.5	9.5	2.5	21.1	12.1	6.2
Steel	5.4	13.2	3.4	35.6	10.4	2.2	41.9
Cement	5.3	6.1	0.2	2.7	18.2	0.5	11.1
Automobile	4.6	-12.0	0.3	17.0	-20.6	0.4	32.9
Jeeps and Cars	2.8	-22.9	1.3	23.1	-21.3	0.7	21.4
Fertilizer	4.4	-5.0	21.6	1.0	-7.7	22.7	2.2
Paper	2.3	17.8	9.3	-7.3	17.2	7.6	-11.5
Excluding sugar & fertilizer	62.4	4.0	3.0	3.6			

Source: Pakistan Bureau of Statistics

The exceptions were consumer durables (e.g., auto and electronics) and construction & allied industries.

There are a number of explanations for this weak performance by LSM. For example:

Table 2.8: Profile of LSM Growth

	Weight in industry		Number of Sectors	
	FY14	**FY15**	**FY14**	**FY15**
Acceleration in growth	57.6	29.6	46	37
Deceleration in growth	31.7	47.5	18	18
Negative growth	10.7	22.9	27	36
Total	**100.0**	**100.0**	**91**	**91**

Source: Pakistan Bureau of Statistics

(1) The decline in sugarcane crop and the price dispute between growers and sugar mills led to a significant fall in sugar production.

(2) Since some of the industries (for instance, POL, fertilizer and edible oil) achieved extraordinary growth in FY14, a slowdown in FY15 was expected.

(3) The sluggish export demand, particularly in China and Bangladesh, has discouraged production in some of the export-led industries (e.g., cotton fabrics).

(4) Finally, energy constraints continue to impede production in a number of industries (e.g., textile, glass, paper, leather).

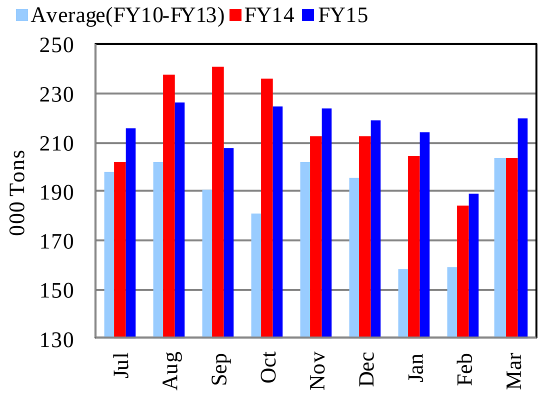
While construction and allied industries (cement, steel) recorded a strong growth, other industries (e.g., chemical, wood and glass) having a small share in LSM index, experienced a slowdown, as new and large entrants have outcompeted smaller units. Since the new players are yet to be included in the PBS dataset, the closure of small units has pulled down the overall LSM growth numbers. For instance, in wood sector, the closure of single manufacturing unit explains one-fifth of the slowdown in LSM growth during Jul-Mar FY15.[6]

Sector-wise detail

Fertilizer

The fertilizer sector recorded a sharp slowdown during Jul-Mar FY15. This deceleration was expected, as last year's growth was abnormally high – one of the Engro plants (i.e., Enven) recorded an exceptional increase in its production due to a better gas supply. Since gas supply to most of the fertilizer plants remain unchanged this year, the industry recorded a nominal growth of 1.0 percent in production during Jul-Mar FY15 (**Figure 2.3**).

Figure 2.3: Monthly Production of Urea Fertilizer



Source: NFDC

Petroleum

The growth in POL production decelerated to 2.5 percent in Jul-Mar FY15 from 9.5 percent achieved in FY14. A higher growth during last year reflected a new refinery which commenced its operation in FY14. Hence, some slowdown in production growth was expected during FY15.

The refining industry also suffered from losses on their inventories, particularly in Q2-FY15, when the crude oil prices plunged in the global markets. However, the

[6] So far, PBS data does not include production data of the newly established manufacturing unit, which is the largest wood-based panel industry in Pakistan.

relatively stable oil prices during Q3-FY15 helped refineries recover some of their losses.

Food

Overall food sector posted a decline of 1 percent during Jul-Mar FY15. This weakest performance in the last five years was on account of a production decline in sugar and edible oil & ghee sectors; beverages on the other hand continue to record a healthy growth. The manufacturers of edible oil & ghee built up large inventories in FY14, when they benefited from a sharp fall in input prices (mainly palm oil).

Sugar production *fell* by 6.1 percent during Jul-Mar FY15 against a strong growth of 10.9 percent realized during the corresponding period last year. In addition to a fall in sugarcane crop, the dispute between growers and sugar mills (over support prices of cane) also played a major role towards this decline in production. Specifically, governments of Sindh and Punjab raised the support price of cane from Rs 170 to Rs 182 and Rs 180 respectively, to compensate growers against the increased input costs. However, sugar mills were reluctant to pay farmers this higher price for cane as the sugar price in the market was already low (mainly due to large domestic inventories and depressed prices in the international market).

Initially, the standoff between growers and sugar mill delayed the crushing activity. Later on, the provincial government of Sindh decided to share the burden of sugar mills by paying a subsidy of Rs12 per 40 kg to farmers.[7] However, as the sugar mills in Punjab region had to pay the entire support price for cane, several units in the province had to shut down their operation to avoid the higher cost of production.

Textile

Textile production recorded a lower growth of 0.5 percent during Jul-Mar FY15, compared to 1.5 percent in the corresponding period of last year. The spinning sector was badly hit as the fall in foreign demand and a better cotton crop compared to the previous year, pulled down the local prices of yarn.

In addition, though the direct impact of the EU recession on Pakistan's textile is low (as the country has been able to uphold its market share in that market), this

[7] At the same time, the federal government offered a rebate of Rs 8 per kg to sugar mills on their export of the surplus stocks. However, the export volumes remained low as the sugar prices in the international market were already under pressure.

has weakened the demand for cotton-based inputs from China and Bangladesh (**Chapter 5**).

As far as other players in the textile value chain are concerned, they have benefited from declining prices of yarn, but the LSM index does not capture their activity.[8]

Paper and Board

The fall in the global prices hit the paper industry. The stiff competition from the imported products forced local firms to cut down their prices. On a cumulative basis, paper production fell by 7.3 percent during Jul-Mar FY15, compared to 9.3 percent growth in last year.

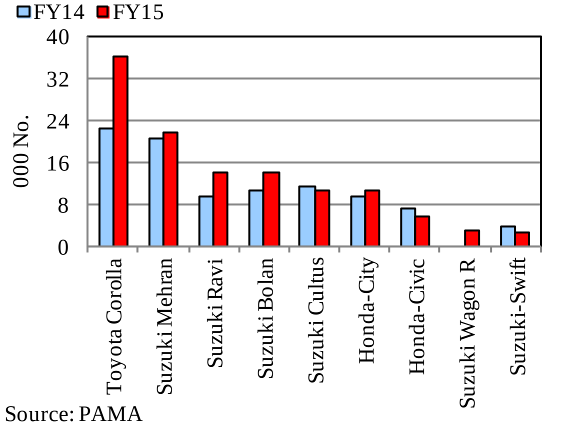
Construction related industries

Cement, steel and paints experienced healthy growth during Jul-Mar FY15 (**Table 2.8**). As stated in SBP's Second Quarterly Report, most of the demand for these construction allied sectors came from mega residential and infrastructure projects.

Automobile industry

Except for buses and motorcycles, all other segments of automobiles (including tractors, cars & jeeps, trucks and light commercial vehicles (LCVs)) posted a strong growth (**Figure 2.4**). Within cars & jeep and LCV categories, the demand was led by new model of locally produced sedan and 'Apna Rozgar Scheme' launched by the government of Punjab.

Figure 2.4: Production of Different Models of Cars an LCVs (Jul-Mar)



Source: PAMA

[8] The LSM index includes only cotton yarn and cloth categories; higher value added items are not part of LSM index. We can however make some assessment on the basis of their export performance. According to trade data, exports of the value added items (e.g., knitwear and garments) have experienced a higher growth over the last year mainly due to GSP status (for details, see section on Trade in **Chapter 5**).

2.4 Services

The services sector contributed more than two-third of the GDP growth in FY15. The overall growth in services accelerated from 4.4 percent in FY14, to 5.0 percent in FY15, which more than offset the sluggish performance by the commodity producing sector (**Table 2.1**). The growth impetus came from *general government services* and *finance and insurance* (**Table 2.9**)

Table 2.9: Value Addition by Services
Share and growth in percent; contribution in percentage points

	Share in FY15	Growth		Contribution to growth in services	
		FY14 R	FY15P	FY14R	FY15P
Wholesale & retail	31.0	4.0	3.4	1.3	1.1
Transport, storage and communication	22.7	4.6	4.2	1.0	1.0
Finance and insurance	5.3	4.2	6.2	0.2	0.3
Housing services	11.5	4.0	4.0	0.5	0.5
General govt. services	12.7	2.9	9.4	0.4	1.1
Other private services	16.8	6.3	5.9	1.0	1.0
Overall	**100**	**4.4**	**5.0**	**4.4**	**5.0**

P: Provisional; R: Revised

Source: Pakistan Bureau of Statistics

A strong growth in *general government services* was expected due to: (a) higher government spending on public infrastructure development projects; and (b) increase in salaries and pension of public sector employees. In addition, strong profitability of the banking sector (driven by massive investments in risk free government securities) was reflected in the higher value addition by *finance and insurance sector*.

The value addition in *wholesale and retail trade* (almost a one-third of the services sector) is computed by applying fixed ratios of tradable surpluses and traders' margins, on domestic commodity producing sectors and imports. During FY15, a subdued growth in LSM and the crop sectors led to weaker performance of the *wholesale and retail trade* sector.

Transport, storage and communication sub-sector posted a slightly lower growth in FY15, compared to the previous year. As evident in **Table 2.10**, this was mainly due to slowdown in the communication sector. As explained in SBP's Second Quarterly Report, despite the roll out of the 3/4G spectrum, this segment continues to face

Table 2.10: Transport, Storage and Communication
Percent

	Share in FY15	Growth	
		FY14	FY15
Railways	0.5	233.6	121.4
Water transport	3.5	10.1	-4.0
Air transport	6.0	12.7	27.3
Pipeline transport	0.2	-6.1	-7.9
Communication	15.3	4.4	0.0
Road transport	72.1	3.7	3.8
Storage	2.5	3.9	3.2
	100.0	**4.6**	**4.2**

Source: Pakistan Bureau of Statistics

multiple challenges during FY15, for example, the financial burden due to the drive for biometric verification of SIMs in the country.

The operational performance and financial indicators of Pakistan Railways and PIA improved during the course of year. The performance of Railways has improved mainly due to increase in number of freight trains and locomotives.[9] Moreover, delays in departure and arrival of passenger trains have been considerably reduced. In the case of PIA, lower losses were mainly attributed to declining jet fuel prices, and increased use of fuel efficient planes on lease.

[9] Specifically, locomotives for freight pool has been increased up to 50 on daily basis, which has allowed PR start more than six freight trains daily from Karachi Port.