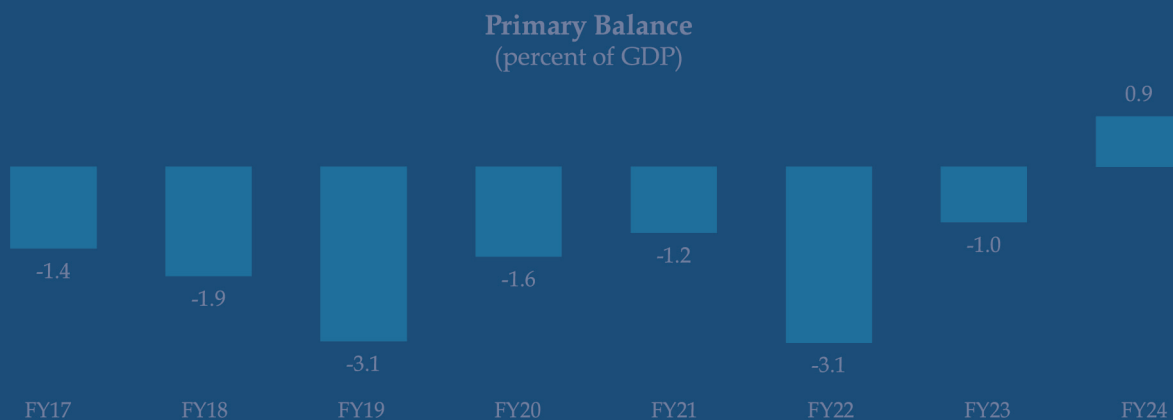


Fiscal Policy

Fiscal consolidation continued in FY24, as primary balance posted a surplus for the first time in 17 years. Overall fiscal deficit as well as revenue deficit also decreased by about one percent of GDP. Increase in total revenue largely explains the improvement in fiscal balances. The major contribution to total revenue came from non-tax revenue, supported by higher SBP profit and PDL collection. Meanwhile, tax revenue also recorded a modest increase in terms of GDP. In case of expenditure, a slight decline in terms of GDP was primarily due to non-interest spending on account of lower subsidies and development spending, more than offsetting the increase in interest payments amid high debt stock and elevated interest rates. In this context, sustaining the fiscal consolidation is imperative to contain debt servicing and create fiscal space for social and development spending to support growth over medium to long term. This could only be achieved through reforms aimed at broadening the tax base, and reducing untargeted subsidies and grants by addressing structural issues, particularly in the energy sector, and privatisation of state owned enterprises.



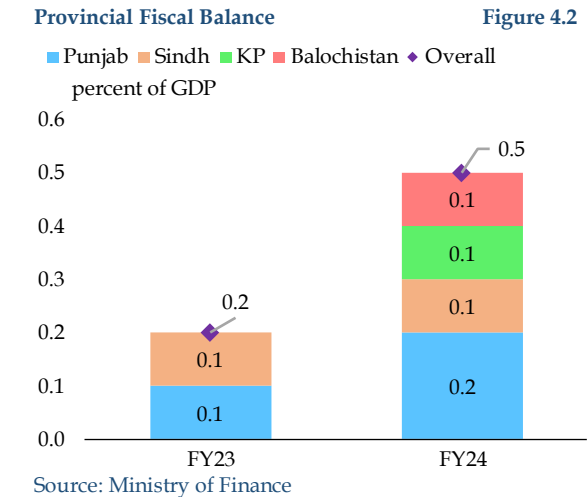
4 Fiscal Policy

4.1 Fiscal Trends and Policy Review

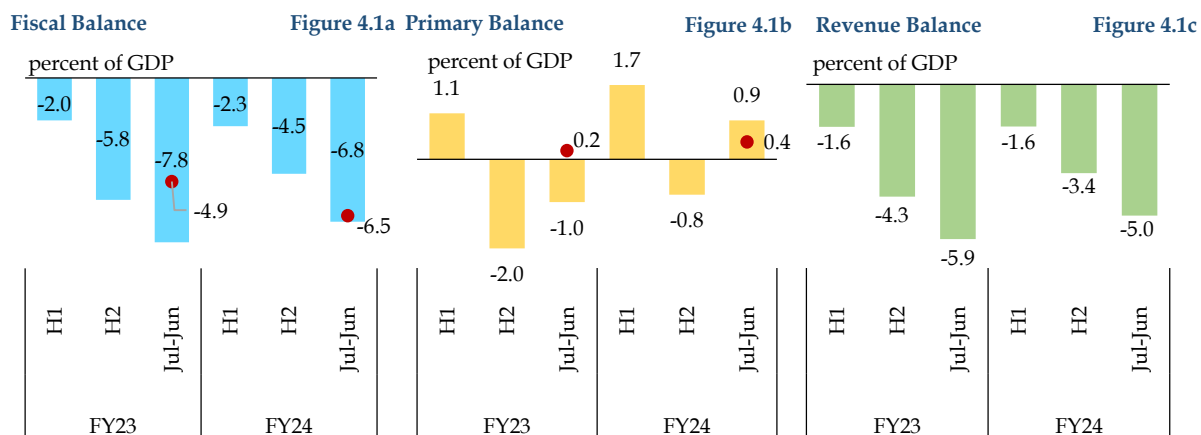
Robust growth in total revenue helped the government in achieving desirable fiscal consolidation during FY24. The fiscal deficit decreased by one percent to 6.8 percent of GDP in FY24, while primary balance recorded a surplus of 0.9 percent – first time since FY07 (Figures 4.1a & 4.1b, Table 4.1). The provinces contributed 0.5 percent to the consolidated surplus, compared to 0.2 percent in the previous year (Figure 4.2). Meanwhile, revenue balance posted a lower deficit compared to the previous year, as increase in total revenue outpaced the increase in current expenditure (Figure 4.1c).

The major thrust to revenue growth came from non-tax revenue (NTR), which contributed 80 percent of the increase in total revenue in terms of GDP. Higher SBP profit, petroleum development levy (PDL) collection, and federal mark-up receipts on loans to PSEs/provinces were the major contributors to the substantial increase in the NTR during FY24.

By comparison, tax revenue accounted for only 20 percent of the increase in total revenue. This



was despite a substantial growth in tax revenue. Both economic factors and revenue mobilization measures contributed to this growth. Major economic factors included high interest rates and inflation, as well as PKR depreciation compared to the previous year.¹ These were supported by a host of tax measures, like widening the scope of super tax, increase in withholding tax (WHT) and general sales tax rates (GST), and rationalization of tax expenditure to some extent.



Note: Maroon dots represent respective Budget Estimates
Source: Ministry of Finance

¹ On average, PKR depreciated by 12.4 percent against USD during FY24.

Consolidated Fiscal Position

Table 4.1

	Values (billion Rupees)				Growth (percent)			
	FY23	FY24		Jul-Jun	FY23	FY24		Jul-Jun
	Jul-Jun	H1	H2		Jul-Jun	H1	H2	
1. Total revenue (a+b)	9,634	6,854	6,415	13,269	19.9	45.9	30.0	37.7
(a) Tax revenue	7,819	4,834	5,251	10,085	15.7	29.5	28.5	29.0
o/w FBR taxes	7,169	4,469	4,842	9,311	16.7	30.3	29.4	29.9
(b) Non-tax	1,815	2,020	1,164	3,184	41.8	108.8	37.3	75.4
2. Total expenditure (a+b+c)	16,155	9,262	11,214	20,476	21.5	45.1	14.8	26.7
(a) Current expenditure	14,583	8,565	10,006	18,571	26.6	41.3	17.4	27.3
o/w Mark-up payments	5,696	4,220	3,940	8,160	79.0	64.0	26.2	43.3
(b) Development expenditure & net lending	1,953	661	1,417	2,078	17.8	3.9	7.7	6.4
o/w PSDP	1,893	673	1,354	2,027	17.1	13.9	4.0	7.1
(c) Statistical discrepancy	-381	36	-209	-173	-	-	-	-
3. Fiscal balance	-6,521	-2,408	-4,799	-7,207	-	-	-	-
percent of GDP	-7.8	-2.3	-4.5	-6.8	-	-	-	-
4. Primary balance	-826	1,812	-859	953	-	-	-	-
percent of GDP	-1.0	1.7	-0.8	0.9	-	-	-	-
5. Revenue balance	-1,464	-1,711	-3,591	-5,302	-	-	-	-
percent of GDP	-5.9	-1.6	-3.4	-5.0	-	-	-	-
5. Provincial balance	155	289	229	518	-	-	-	-
percent of GDP	0.2	0.3	0.2	0.5	-	-	-	-
6. Financing (a+b)	6,521	2,408	4,799	7,207	-	-	-	-
a) External (net)	-680	608	-288	321	-	-	-	-
b) Domestic (net)	7,201	1,799	5,087	6,886	-	-	-	-

Note: Fiscal balance is total revenue minus total expenditure; primary balance is fiscal balance excluding interest payments; revenue balance is total revenues minus total current expenditures

Source: Ministry of Finance

At the same time, total expenditure decreased slightly in terms of GDP. The decline was primarily due to a fall in non-interest expenditure, led by subsidies and development spending. Reduction in subsidies was on account of lower disbursement to Pakistan State Oil (PSO), as well as government decision to restrict gas subsidies to the industrial sector.² However, power subsidies continued to remain elevated. In case of development spending, both the federal public sector development program (PSDP) and provincial development expenditure witnessed a decline in terms of GDP. This could be traced to tight fiscal space and caretaker governments in place till elections in February 2024.³ In contrast to non-interest expenditure, interest payments rose

considerably due to elevated debt stock amid high interest rate environment.

While it is encouraging to see significant fiscal consolidation continuing in FY24, it is important to look at its contributory factors from the standpoint of sustainability. The major sources of revenue gains included SBP profit, the PDL collection, and cyclical factors like interest rate and inflation, rather than broadening of tax base. Measures to boost tax revenue through efficient use of tax policy and administration, both at federal and provincial levels, remained insufficient. This is reflected in only a marginal increase in the tax-to-GDP ratio.⁴

Furthermore, within the tax revenue, though direct taxes posted a reasonable increase in terms of GDP, GST on goods and services either

² Unlike last year, government did not have to pay subsidy on account of valuation losses on FE-25 loans of PSO during FY24.

³ As per constitution, the caretaker governments have limited powers in terms of spending decision.

⁴ Subdued growth in non-agriculture GDP in FY24 also explains this phenomenon, to some extent.

deteriorated or remained unchanged, notwithstanding increase in the standard GST rate on goods in the latter half of FY23.

On the expenditure side, interest payments overshot the budget estimate for the second year in a row. Amid fiscal constraints, overall development spending as percent of GDP decreased, which has negative repercussions for economic growth and thus, future revenue generation capacity.⁵ Moreover, provincial social spending on health and education also decreased in terms of GDP in FY24, which has implications for availability of skilled labor force and productivity in the economy.⁶

In view of these factors, it is imperative to implement reforms aimed at increasing tax

revenue through broadening of the tax base and rationalizing non-interest expenditure, particularly subsidies. These reforms are particularly important in the context of sustaining fiscal consolidation needed to reduce debt levels, as well as stimulate social and development spending to support inclusive growth.

4.2 Revenue

Total revenue rose by one percent to 12.5 percent of GDP in FY24, edging above the average of last five years (Table 4.2). While non-tax revenue predominantly contributed to this increase, the tax revenue also increased, both in terms of GDP and growth.

Breakup of Consolidated Revenue

Table 4.2

	Values (billion Rupees)			Percent of GDP			Growth (percent)			Contribution to Growth (ppts)*		
	FY19-23 avg.	FY23	FY24	FY19-23 avg.	FY23	FY24	FY19-23 avg.	FY23	FY24	FY19-23 avg.	FY23	FY24
Total Revenue (a+b)	7,149	9,634	13,269	12.1	11.5	12.5	13.6	19.9	37.7	-	-	-
a) Tax revenue	5,698	7,819	10,085	9.6	9.3	9.5	13.5	15.7	29.0	10.4	13.2	23.5
Federal	5,181	7,169	9,311	8.7	8.5	8.8	13.8	16.7	29.9	12.5	15.2	27.4
Direct taxes	2,051	3,272	4,531	3.4	3.9	4.3	17.7	43.5	38.5	6.5	16.1	17.6
Indirect taxes	3,130	3,897	4,780	5.3	4.6	4.5	11.6	0.9	22.7	7.3	0.6	12.3
Sales tax	2,035	2,592	3,099	3.4	3.1	2.9	12.3	2.4	19.5	5.0	1.0	7.1
Federal excise duty	290	370	577	0.5	0.4	0.5	12.5	15.2	56.2	0.7	0.8	2.9
Customs	804	935	1,104	1.4	1.1	1.0	10.2	-7.4	18.1	1.6	-1.2	2.4
Provincial	517	650	774	0.9	0.8	0.7	10.5	6.1	19.2	1.0	0.6	1.6
Sales tax on services	300	417	505	0.5	0.5	0.5	14.0	17.2	21.0	7.8	10.0	13.5
b) Non-tax revenue	1,451	1,815	3,184	2.5	2.2	3.0	30.8	41.8	75.4	3.2	6.7	14.2
Federal	1,325	1,649	2,961	2.3	2.0	2.8	35.3	43.1	79.6	30.7	38.8	72.3
SBP profit	489	371	972	0.9	0.4	0.9	1,439.7	-21.6	161.9	19.0	-8.9	36.4
PDL	326	580	1,019	0.5	0.7	1.0	77.4	354.7	75.8	9.0	39.3	26.6
Mark-up receipts	90	145	355	0.1	0.2	0.3	37.5	64.8	145.4	2.0	4.9	12.8
Provincial	127	166	223	0.2	0.2	0.2	7.8	29.3	34.5	0.1	2.9	3.2
Net hydel profit	26	5.5	24	0.05	0.01	0.02	-14.5	-76.4	334.0	-5.9	-13.9	11.1
Memorandum Items												
Nominal GDP	59,542	83,875	106,045	-	-	-	-	-	-	-	-	-

Note: 1) Tax revenue numbers reported by FBR and Ministry of Finance may not tally

* 'contribution to growth' measures contributions of the components in percentage points to growth of the immediate aggregate

Sources: Ministry of Finance; SBP staff calculations

⁵ Federal government had set the PSDP target of Rs 950 billion in the FY24 budget, with the aim "to accelerate growth and generate employment", but fell short of the target by almost 33 percent. Similarly, overall provincial development spending was shy of the target by 10 percent, with Punjab—the province with the largest development portfolio—witnessing a decline in spending by about 6 percent. Source: Budget in Brief FY24, Ministry of Finance

⁶ Provincial development spending on health and education stood unchanged at 0.2 percent of GDP, while current spending decreased from 1.4 percent in FY23 to 1.3 percent in FY24. To put in perspective, mark-up payments were 7.7 percent of GDP in FY24, up from 6.8 percent in the previous year.

i. Tax Revenue

Total tax collection grew by 29 percent in FY24, compared to 15.7 percent in the previous year. In terms of GDP, it inched up slightly from 9.3 percent in FY23 to 9.5 percent in FY24. The tax-

to-GDP ratio remained low both in comparison to the recent peak of 12.6 percent achieved in FY16, as well as the average of 13.5 percent in peer countries.⁷ In this regard, **Box 4.1** lays down key tax reforms to enhance tax revenue in Pakistan.

Box 4.1: Tax Reforms in Pakistan

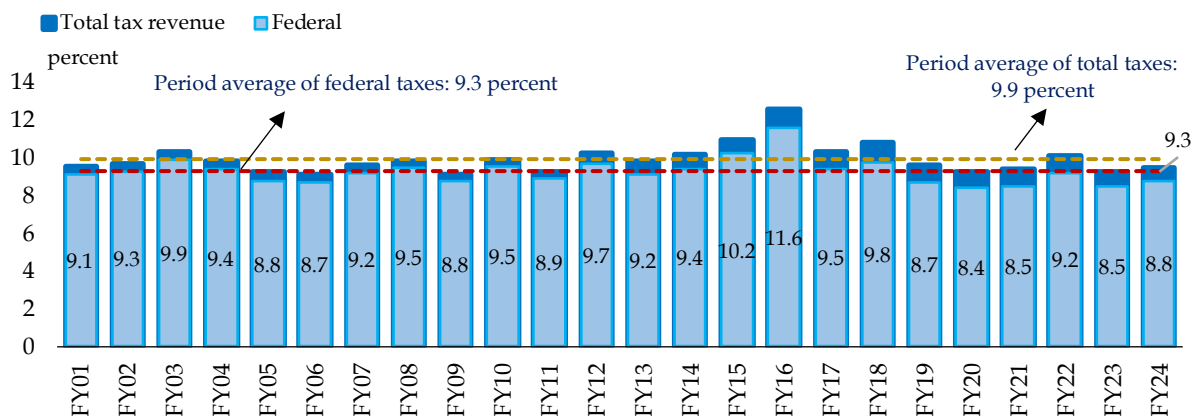
Pakistan's tax-to-GDP ratio has stagnated close to 10 percent in the last two and a half decades (**Figure 4.1.1**). This is significantly lower than the country's capacity, which is estimated at 22.3 percent of GDP.⁸ The tax-to-GDP ratio in Pakistan is also one of the lowest compared to the emerging and developing economies, as well as the regional peers. Given federal tax collections constitute about 90 percent of the total tax revenue, this box provides recommendations for federal tax reforms, drawing from the best international practices, with the goal of raising Pakistan's tax-to-GDP ratio.⁹

1) Proper implementation of the value added tax (VAT): VAT, one of the most widely implemented consumption-based taxes around the world, is not fully embedded in the tax system of Pakistan.¹⁰ The environment of skepticism between the taxpayers and the tax authorities weighs on proper functioning of refund and input tax credit process, which is pivotal to VAT's success. Moreover, the VAT tax base is narrow, necessitating rate increases every now and then, as well as delays in refunds by the tax authorities, to maintain or achieve higher revenue.¹¹ To optimize VAT, Pakistan should focus on streamlining the refund process through digital solutions that minimize human intervention and establish a broad-based, low, and uniform VAT on goods and services across all jurisdictions. This approach would strengthen VAT's role as a vital indirect tax.

2) Rationalization of the corporate income tax (CIT): At 29 percent, Pakistan is among the countries with high standard corporate income tax rates in the world (**Figure 4.1.2**), with certain sectors such as the banking sector subject

Breakup of Pakistan's Total Tax Revenue as Percent of GDP

Figure 4.1.1



Source: Ministry of Finance

⁷ The average refers to 33 select peer countries, including Vietnam, Thailand, Egypt, Myanmar, Central Asian Republics (CARs), South Africa, Iran, among others. It is based on the latest available data for these countries, spanning from 2018 to 2021. Data source: IMF WORLD Database (2024)

⁸ a) Fenochietto, M. R., & Pessino, M. C. (2013). Understanding countries' tax effort (No. 13-244). International Monetary Fund; b) World Bank (2023). *Strengthening Government Revenues. Towards an Equitable, Efficient, and Sustainable Tax System*. Policy note 6. Reforms for a Brighter Future. World Bank Group: Washington DC

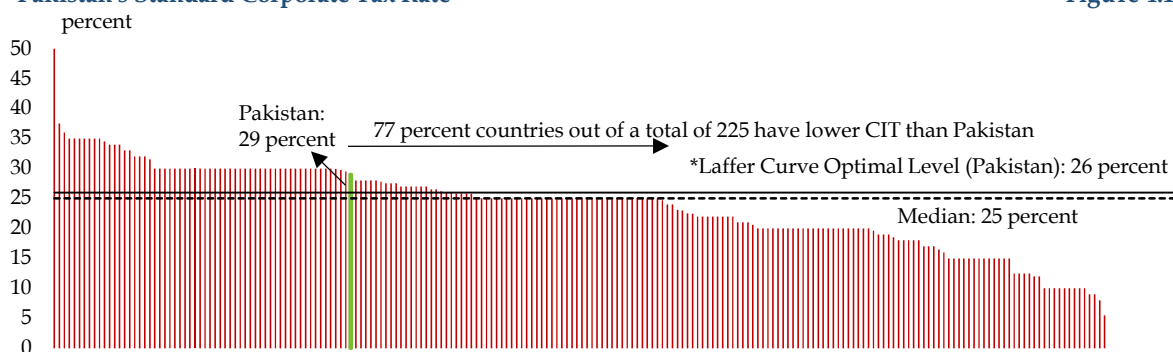
⁹ These suggestions are based on the SBP Staff Note, *Federal Tax Reforms in Pakistan: Lessons from the Best International Experience* (forthcoming).

¹⁰ In Pakistan, general sales tax and VAT are used interchangeably.

¹¹ See Box 4.2 for details on efficiency of VAT as a tax instrument.

Pakistan's Standard Corporate Tax Rate

Figure 4.1.2



Note: Around 15 countries have no corporate income tax in the list of 225 countries

*Mehmood et al. (2022). *Does Laffer Curve Exist in Tax Structure of Pakistan? A Threshold Regression Analysis*. Journal of Economic Impact, Science Impact Publishers

Data source: Tax Foundation

to even higher rate. When additional taxes, such as super tax, are taken into account, the effective CIT rate turns out to be much higher. Such kind of taxation distorts economic incentive structure, as well as fosters opportunities for tax fraud, tax evasion, and misreporting. In Pakistan, there are different effective rates for businesses that have led to the resource misallocation and the slowing down of economic growth (Alm and Khan 2015).¹² Moreover, based on his review of 79 empirical studies, Jacob (2021) found that higher corporate tax rates adversely affect corporate investment, foreign direct investment, innovation, and aggregate growth.¹³ In this background, improving CIT efficiency and lowering the standard and effective corporate rates could stimulate economic growth, increase revenue collection, and curb tax-related corrupt practices.

3) Rationalizing tax expenditure: Tax expenditure is the tax forgone due to exemptions, concessional rates, tax credits, and tax holidays. Pakistan's tax expenditure, estimated at 4.6 percent of GDP for FY23, is high compared to the average of 3.2 percent in low-middle income countries.¹⁴ As international experiences suggest, preferential treatment does not usually yield intended results. Therefore, all tax expenditures, except those on account of exporters, need to be rationalized and gradually eliminated after carrying out cost-benefit analysis. Moreover, concessions and exemptions granted via statutory regulatory orders instill ad-hocism into tax policy, making it unreliable and unpredictable, with serious consequences for economic incentives. This ad-hocism is often influenced by powerful business lobbies, leaving SMEs and small taxpayers at disadvantage.

4) Simplification of the entire tax system: The tax system is complex and fragmented in Pakistan. Complex tax laws tend to lead to multiple interpretations of tax statutes, giving way to appeals and litigation by taxpayers, as well as rent-seeking opportunities for tax administrators. Fragmented tax bases, such as VAT on goods versus services and tax on agricultural versus non-agricultural incomes, raise compliance and administrative costs, hindering revenue mobilization. Such a system also causes inter-jurisdictional frictions, as well as non-uniform taxation. A promising step towards simplification includes the recent implementation of Single Sales Tax Portal/Return system for the telecommunication sector by the FBR in collaboration with World Bank. This has reduced the number of returns filed by the sector; however, the sales tax rates still vary across jurisdictions. A broader effort to simplify tax laws and harmonize tax rates across sectors and regions is critical for lowering costs and developing a more efficient revenue system.

5) Efficient use of federal excise taxes (FED): As per the international experience, FED can serve as a complementary tool to aid revenue mobilization, especially as other types of long-term reforms develop and mature

¹² Alm, J. & Khan, M.A. (2015). Assessing and Reforming Enterprise Taxation in Pakistan. Working Papers 1513. Department of Economics. Tulane University. Louisiana

¹³ Jacob, M. (2021). *Real Effects of Corporate Taxation: A Review*. SSRN Electronic Journal

¹⁴ Sources: Federal Board of Revenue; Global Tax Expenditures Database (GTED) Flagship Report 2023

to fruition. However, Pakistan's FED collection as percent of GDP is low and falling. To increase FED collection, the country should remove distortions caused by varied tax rates and implementation challenges.

6) Improving tax administration: Use of information and communications technology (ICT) can play a key role in improving enforcement and compliance. There is a need to boost FBR's spending on ICT as percent of total operational expenditure that is currently low. Digital solutions applied so far, like Track and Trace System and FASTER Plus, are facing operational headwinds. There are issues of integration among these solutions as well, not to mention lack of data governance policies. Further, initiatives like Single Sales Tax portal, SWAPS, Track and Trace System, need to be applied comprehensively across all sectors of the economy. The cost of adoption of digital gadgets, like point of sale (POS) machines, also needs to be rationalized such that the users are not burdened. These interventions can help formalize economy, as well as expand revenue.

Additionally, risk-based audits, introduced only recently in 2019, are yet to apply across-the-board at all functional levels of the tax apparatus. Currently, regional offices are still carrying out manual interventions that may be phased out gradually over time. Furthermore, effectiveness of audits is undermined by poor recovery rates, requiring stronger enforcement strategies. Finally, across-the-board ownership of all these reforms is imperative for their success.

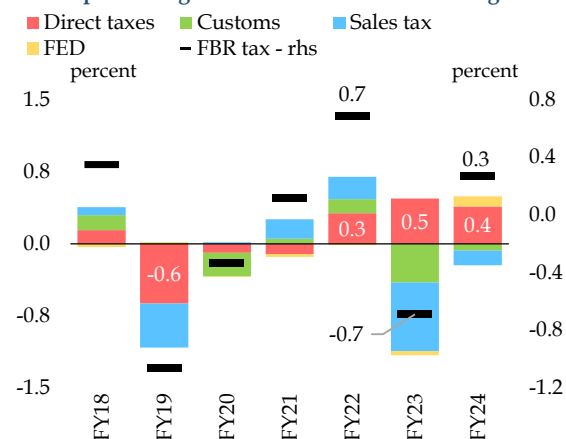
Federal taxes

Growth in federal taxes accelerated to 29.9 percent in FY24 compared to 16.7 percent in the previous year. In terms of GDP, federal taxes rose to 8.8 percent in FY24 from 8.5 percent in FY23. Consistent with the previous year's trend, direct taxes led the increase in federal taxes, more than offsetting the slight decline in indirect taxes in terms of GDP (**Figure 4.3**). Within the direct taxes, withholding taxes and voluntary payments made major contributions, while collection on demand declined. In case of indirect taxes, FED increased, while sales tax and customs, in continuation of the previous year, decreased further in FY24.

In nominal terms, despite a slight deceleration, growth in direct taxes stayed robust at 38.5 percent in FY24, pushing their share in total federal taxes to the highest level (**Figure 4.4**). WHT dominated the mix with about 60 percent share (**Figure 4.5**). Share of voluntary payments in direct taxes edged up in FY24, mainly supported by income tax paid by banks that has increased considerably in recent years (**Figure 4.6**). Meanwhile, growth in indirect taxes accelerated to 22.7 percent, compared to 0.9 percent in the previous year.

The economic factors – elevated interest rates and inflation, and the PKR depreciation – played a major role in accelerated growth of tax

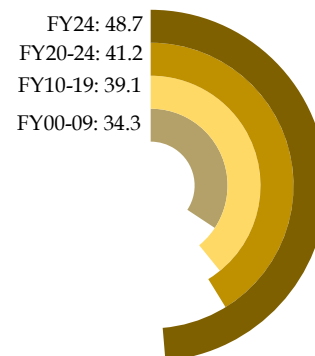
Breakup of Change in FBR Tax-to-GDP Ratio Figure 4.3



Source: Ministry of Finance

Share of Direct Taxes in Total Federal Taxes percent

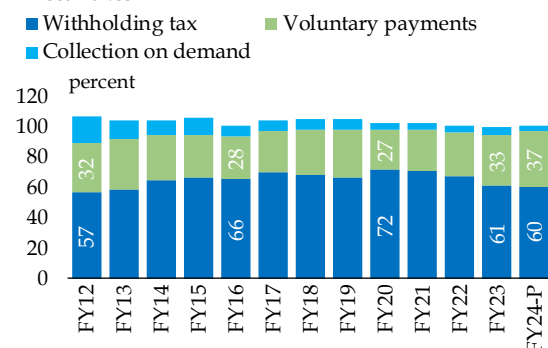
Figure 4.4



Source: Federal Bureau of Revenue

Share of Major Components of Direct Taxes

Figure 4.5



Note: These shares may add to more than 100 percent as these are calculated in relation to direct taxes net of refunds and other direct taxes.

Source: Ministry of Finance

revenue. At the same time, revenue mobilization measures taken by the government amplified the impact of economic factors.¹⁵

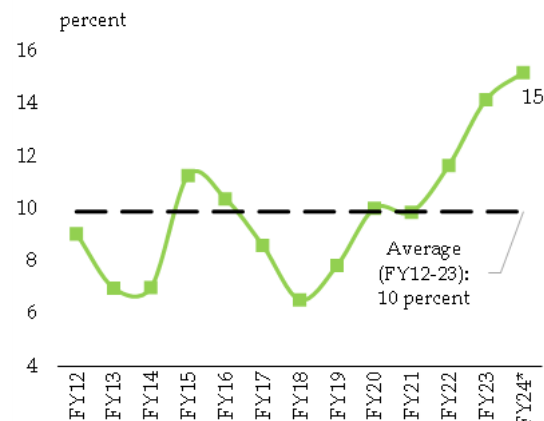
a) Economic factors

High interest rates contributed considerably to the increase in FBR taxes during FY24. This is reflected in income tax paid by banks, and withholding taxes collected on individuals' earning from bank deposits and investment in government securities. During FY24, the banks earned record profits amid increased government borrowing at higher interest rates, translating into sizeable tax payments.¹⁶

In case of withholding taxes, increase in collection under the head of 'bank interest and securities' could be traced to higher profits earned by individuals from their profit-bearing accounts with the banks, as well as their investment in government securities. These profits could be attributed to both attractive

Share of Banks' Income Tax in Direct Taxes

Figure 4.6



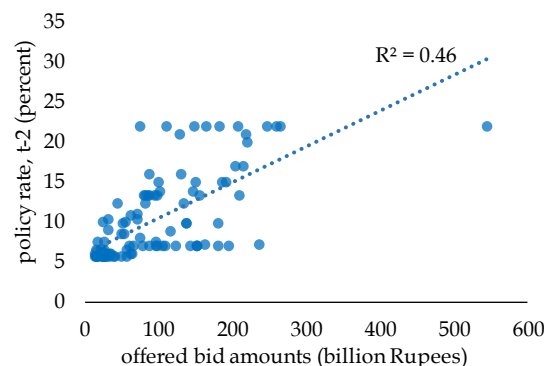
Sources: Federal Board of Revenue; State Bank of Pakistan

returns (price effect), and increased tendency to save and invest in risk-free government securities among individuals (volume effect), as a hedge against inflation.¹⁷ The historical data shows that individuals tend to invest in government securities during high interest rate environment (Figure 4.7).¹⁸

Elevated inflation, albeit decelerating, continued to contribute to tax collection, especially to

Non-Competitive Bids and Interest Rate

Figure 4.7



Note: The scatter plot refers to data spanning from July 2015 to June 2024

Source: State Bank of Pakistan

¹⁵ It needs to be highlighted that all these factors, separately or in combination, led to growth in almost all types of direct and indirect taxes.

¹⁶ Banks' net investment increased by 41.4 percent in CY23, compared to 26.4 percent increase in CY22, with investments in government securities constituting the bulk. Their net interest income as percent of gross income rose from 79.8 percent in CY22 to the new high of 82.9 percent in CY23. Source: Financial Soundness Indicators, State Bank of Pakistan

¹⁷ Growing public awareness of the risk-free investment avenues also likely enabled higher investment in government securities.

¹⁸ Remunerative customer deposits (fixed, savings, and remunerative current) with banks rose by 21.6 percent (the highest growth during last 15 years) to Rs 16.4 trillion in CY23, compared to an increase of 8.4 percent in CY22. Source: Financial Soundness Indicators, State Bank of Pakistan

indirect taxes, in FY24. For instance, around half of the 26.8 percent increase in domestic sales tax collection was due to substantial increase in electricity prices.¹⁹ Similarly, increase in prices of sugar, cement, cigarettes, and other commodities also supported higher sales tax and FED collection. Additionally, better prices also lifted profitability of non-financial firms — in some cases through improved net profit margins.²⁰ Rise in corporate profits also meant higher dividend payments for the shareholders, which led to increase in WHT collection.²¹

Lastly, the PKR depreciation during FY24, and increase in import volumes helped offset the impact of lower unit values on import-related taxes.²² Imports, which fell by 0.8 percent in dollar terms, rose by 14.9 percent in PKR terms.²³ As a result, taxes collected at import stage increased by 20.2 percent, compared to a decline in the previous year.²⁴

b) Tax measures

Implementation of revenue mobilization measures by the government, including increase in rates and rationalization of some tax expenditures, also enabled higher tax collection in FY24. In case of direct taxes, one of the changes was broadening the scope of the super tax on persons earning over Rs 150 million annually, by applying it across-the-board, in an attempt to ensure horizontal equity.^{25,26} Super

tax cap was also increased from four to ten percent for FY23 and onwards.²⁷ This, along with the regular income tax regime and large corporate profits, greatly helped the direct tax collection. Another change was revision in income tax slabs for salaried and non-salaried individuals and association of persons (AOPs) to ensure progressivity. In case of non-salaried individuals and AOPs, minimum threshold was also raised from Rs 0.4 million to Rs 0.6 million, bringing it at par with the threshold of salaried individuals to remove distortions.

Furthermore, various rate increases provided boost to WHT collection. Some of these included: increase in the WHT on commercial importers of goods from 5.5 to 6.0 percent; two to three percent increase on the sale and purchase of immovable property, respectively²⁸; one to two percent increase in tax on sale contracts of goods and services for individuals, AOPs, and companies; resumption of 0.6 percent tax on cash withdrawal on the amount exceeding Rs 50,000 per day by a non-filer. The government also took measures related to indirect taxes, particularly sales tax and FED. The standard sales tax rate on goods was increased from 17 percent to 18 percent in February 2023, and from 18 percent to 25 percent on locally manufactured cars and import of over 800 tariff lines covering non-

¹⁹ Electricity tariffs were revised up through annual rebasing, quarterly tariff adjustments, and fuel charge adjustments (see Chapter 3 for details).

²⁰ It reflected in a 38 percent jump in profit-after-tax earned by the top 58 KSE-100 companies in CY2023. Data source: KSE 100 Index Profitability CY23. February 2024. Arif Habib Limited: Karachi

²¹ Withholding tax collection from dividends increased by 65.5 percent to Rs 87.1 billion in FY24.

²² Quantum index of imports rose by 25.0 percent during FY24, compared to a decline of 17.9 percent in the same period of the previous year. Source: Pakistan Bureau of Statistics

²³ Source: Pakistan Bureau of Statistics

²⁴ These taxes include custom duties, advance income tax, sales tax on goods, and FED.

²⁵ Earlier this tax applied to 16 kinds of businesses only.

²⁶ Super tax ranging from two to four percent was imposed on incomes of high-earning persons via section 4B in FY16 with the goal to provide for rehabilitation of temporarily displaced persons. Later, in FY23, section 4B was replaced by new section 4C, "Super tax on high earning persons". For more details on the graduated new tax rates introduced under section 4C, see Chapter 4, The State of Pakistan's Economy Annual Report FY23

²⁷ Earlier, under the Finance Act 2022, the 10 percent super tax was applied only on non-banking and banking firms with over Rs 300 million annual income for fiscal years 2022 and 2023, respectively. For non-banking firms, the rate was capped at 4 percent for FY23. However, under the Finance Act 2023, graduated rates from one percent to 10 percent were applied across-the-board.

²⁸ WHT is 200 percent and 350 percent more for non-ATL sellers and buyers of property, respectively.

Tax Expenditure Relative to Actual FBR Tax Collection

Table 4.3

values in billion Rupees

	Tax Expenditure				Actual Collection					
	Values		Percent of GDP		Values			Percent of GDP		
	FY22	FY23	FY22	FY23	FY22	FY23	FY24 (P)	FY22	FY23	FY24 (P)
Direct taxes	424	477	0.6	0.6	2,285	3,271	4,531	3.4	3.9	4.3
Sales tax*	1,294	2,859	1.9	3.4	2,532	2,591	3,099	3.8	3.1	2.9
Customs	522	544	0.8	0.7	1,011	932	1,104	1.5	1.1	1.0
Grant total	2,240	3,879	3.4	4.6	6,148	7,164	9,311	9.2	8.5	8.8

*Excludes computation of tax expenditure on account of services

Source: FBR Tax Expenditure Report 2024 (latest available)

essential items in March 2023.^{29,30} The government also rationalized the tax expenditure by increasing concessional GST for tier-1 retailers of different types of goods from 12 percent to 15 percent, and by imposing 5 percent GST on DAP fertilizer, which was exempt earlier.³¹ In case of FED, the duty on sugary fruit juices was doubled to 20 percent, while new duty at 5 percent was imposed on fertilizer.

Nevertheless, it is worth highlighting that the

overall tax expenditure was 4.6 percent of GDP based on FY23 data, up from 3.4 percent in FY22 (**Table 4.3**). It was also higher than the average of peer countries.³² Moreover, it is likely that it remained high during FY24 as well.³³ Higher tax expenditure impacts efficiency of tax instruments. In particular, this could be seen in a decline in the efficiency of GST on goods and services in FY24, reflected by the worsening of the C-efficiency ratio (CER) and much lower effective GST rate in the country (**Box 4.2**).

Box 4.2: C-efficiency Ratio (CER) and Effective GST Rate in Pakistan in FY24

C-efficiency (CER) is the ratio of actual sales tax revenues to the product of the standard GST rate and final consumption. A low ratio generally indicates base erosion either by exemptions and concessional rates or by inadequate enforcement. Conversely, a ratio of 100 percent means perfectly enforced VAT at a uniform rate across a broad base, with no concessions or exemptions. CER is mostly below 100 percent, as every country has indeed some kinds of concessions or exemptions available in its tax structure; for instance, exclusion of basic foodstuffs from GST goods basket to protect the poor households. Furthermore, there are enforcement snags, as well, that keep the CER low 100 percent. At around 90 percent, New Zealand has one of the highest CERs in the world. Its exempted items include only donated goods-services, financial services, penalty interest, and supply of fine metals.

In case of Pakistan, CER works out at 20.7 percent in FY24, down from 22.6 percent in FY23, showing further worsening of its GST yield (**Figure 4.2.1a**). As a result of low CER, its effective GST rate was just one-fifths of the actual weighted GST rate on goods and services in FY24 (**Figure 4.2.1b**). Alternatively, low CER and effective rate also meant application of GST on goods and services on a squeezing tax base, as well as gaps in enforcement and compliance. Although government had taken some corrective measures to broaden the base in the Finance Act 2023, these have yet to deliver desired results.

²⁹ These items included completely built units (CBUs) of cars and appliances; confectionery; articles of jewelry; juices and aerated water, among others.

³⁰ Sales tax on motor vehicles collected domestically and at import stage rose by 161 percent to Rs 13.4 billion and 45 percent to Rs 110.9 billion in FY24, notwithstanding a decline in auto sales.

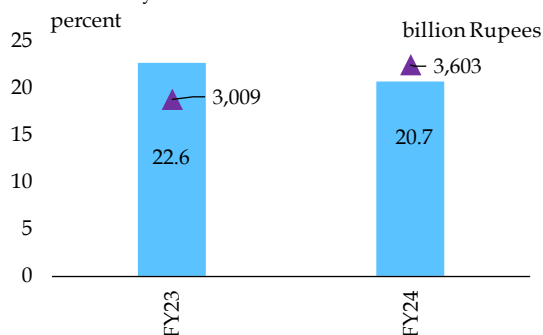
³¹ Goods receiving concessional rate included finished fabrics, locally manufactured finished articles of textile, textile made-ups, leather and artificial leather, among others.

³² Tax expenditure in low middle-income and upper middle-income countries (27 countries each) is 3.2 percent and 3.7 percent of GDP, respectively. Source: Global Tax Expenditures Database (GTED) Flagship Report 2023; gted.taxexpenditures.org/wp-content/uploads/2023/10/von-Haldenwang-et-al-2023_-TEs-in-an-era-of-transformative-change.pdf

³³ Some budgetary measures taken in FY24, like imposing GST on fertilizers – albeit at a concessional rate, might have lowered the sales tax expenditure (FBR's tax expenditure report for FY24 not available yet); however, the impact might be limited, given many other concessions and exemptions were still in place in FY24 – the major one being exemption of POL products.

C-Efficiency Ratio of Pakistan's GST

■ C-efficiency ▲ GST collection - rhs



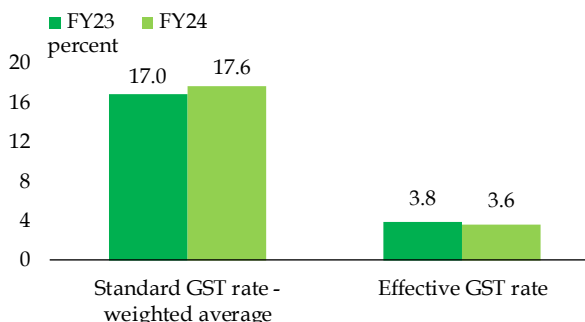
Note: 1) CER is calculated for GST on both goods & services.

2) GDP data used here is based on FY16 base

Sources: FBR, PBS, MoF and SBP staff calculations

Figure 4.2.1a

Standard and Effective GST Rates in Pakistan



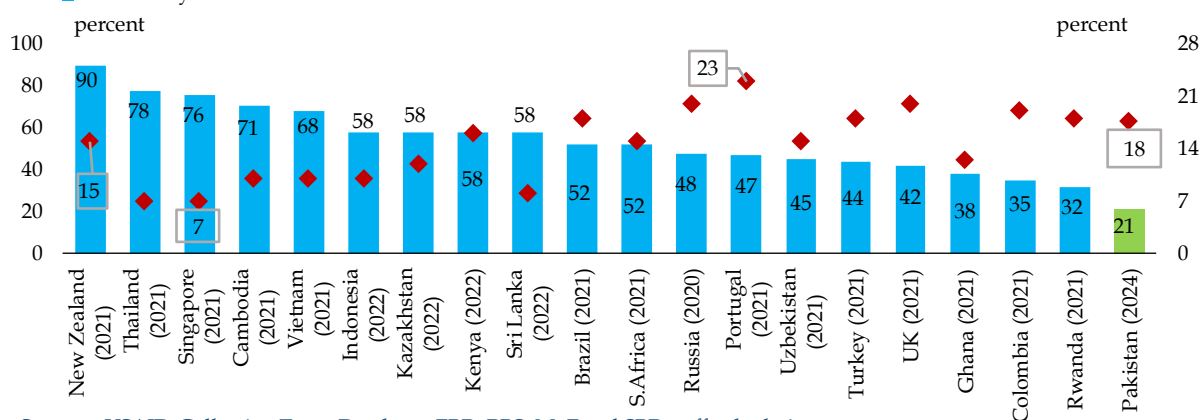
Note: 1) Standard GST is weighted average of GST on both goods & services across all tax jurisdictions. 2) Effective GST rate is calculated by assuming CER=1

Sources: FBR, MoF and SBP staff calculations

Figure 4.2.1b

Cross-country Comparison of C-efficiency Ratios and Standard GST Rates

■ C-efficiency ◆ Standard GST rate - rhs



Sources: USAID Collecting Taxes Database, FBR, PBS, MoF and SBP staff calculations

Figure 4.2.2

In the Finance Act 2024, the government took more measures to rationalize sales tax expenditure in order to broaden the tax base, which is an encouraging development.³⁴ However, elevated standard GST rates on goods and services are still a source of concern from the perspectives of tax burden and compliance, alongside issues related to enforcement. International best practices suggest that properly enforcing a broad-based, uniform and low sales tax may support higher yields. In this connection, cross-sectional comparison depicts an inverse relationship between CER and GST rates (Figure 4.2.2).^{35,36}

Sensitivity analysis of the impact of CERs on the collections in Pakistan suggests that if the C-efficiency ratio improves through broadening of tax base and better enforcement, the revenue collection may increase (Table 4.2.1).

³⁴ Some of these include: withdrawal of zero rating and exemptions on stationary items, tractors, oil cake and other solid residue, local supply of farm feed, and others; such items are now taxed at the reduced rate of 10 percent. Additionally, exemption on edible fruits and vegetables imports from Afghanistan has been removed, as these are now subject to the standard 18 percent rate. Similarly, milk has been brought under the standard GST regime. Moreover, impact of these measures on CER, effective GST rate, and GST collections will be evaluated by the end of FY25.

³⁵ However, this may not be considered as a rule in all cases.

³⁶ Higher CER means broader tax base and better enforcement/compliance. There is a whole body of literature that supports the notion of a broader-base, low-tax rate system. For instance: 1) OECD (2010), *Choosing a Broad Base – Low Rate Approach to Taxation*, OECD Tax Policy Studies, No. 19, Paris: OECD Publishing; 2) Huzaima Bukhari & Dr. Ikramul Haq (2016), *Towards Flat, Low-rate, Broad and Predictable Taxes*, Islamabad: PRIME Institute

In this case, even if the GST rate on goods and services is homogenized and lowered to say 13 percent or 15 percent, Pakistan would see collection rise at least 1.5 times the current level to Rs 5.4 trillion. In a scenario where CER and GST rates are brought at par with the respective medians of the select group of countries (52 percent and 15 percent respectively), Pakistan would see collection increase 2.1 times to Rs 7.7 trillion. This analysis highlights that improved tax efficiency may not only lead to substantial revenue gains, but also allow the government to decrease the standard GST rates without compromising its higher revenue targets.

Provincial taxes

Provincial tax revenue-to-GDP ratio decreased to 0.7 percent in FY24, compared to 0.8 percent in the previous year (Table 4.2). This decrease came despite an acceleration in growth in nominal terms to 19.2 percent, almost three times the previous year. Indirect taxes led this growth on the back of sales tax on services and some other indirect taxes, like infrastructure development cess.³⁷

Sales tax on services received a boost from inflation, similar to the case of sales tax on goods.³⁸ For instance, communication services (call and internet charges) and readymade food served at hotels and restaurants saw a price hike of 7.8 percent and 23.7 percent, respectively, in FY24. However, it may be highlighted here that the sales tax on services to GDP ratio remained unchanged at 0.5 percent in FY24 for the sixth consecutive year, which primarily reflects provincial government's efforts to raise own revenue.

ii. Non-tax Revenue

Non-tax revenue (NTR) grew by 75.4 percent, reaching 3.0 percent of GDP in FY24, up from 2.2 percent the previous year (Table 4.2). The entire increase came from federal sources, while provincial collection remained unchanged, in terms of GDP. The increase in federal NTR could be traced to SBP's profit, PDL collection,

Impact on Revenue Collection by Changing CER and Standard GST Rate Table 4.2.1

Alternate Scenarios of GST Collection - billion Rupees				
GST rate (percent)	CER (percent)			
		21	42	52
	17.6	3,603 (Current scenario)	7,302	9,041
	15	3,063	6,223	7,705
	13	2,654	5,393	6,678
Impact on GST Collection - multiples of current collection				
GST rate (percent)	CER (percent)			
		21	42	52
	17.6	Current collection (C)	2.0 * C	2.5 * C
	15	0.8 * C	1.7 * C	2.1 * C
	13	0.7 * C	1.5 * C	1.9 * C

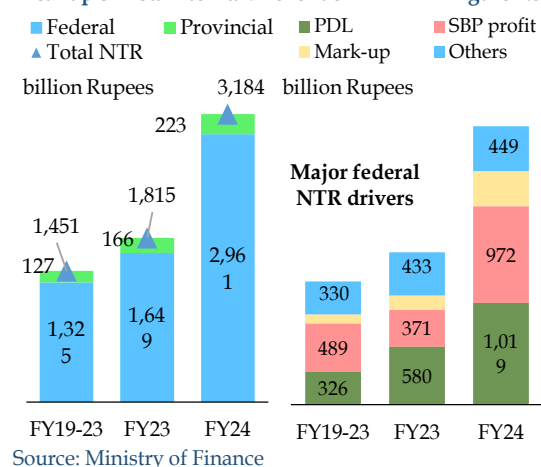
Note: 1) The sensitivity analysis is run on consumption of Rs 98,782 billion (FY24); 2) 52% CER & 15% GST rate are the medians in the group of select countries from Figure 4.2.2

Sources: FBR, PBS, USAID, SBP staff calculations

and federal mark-up receipts on loans to provinces and PSEs during FY24 (Figure 4.8).

Sharp increase in SBP's profit is attributed to revaluation gains, due to exchange rate appreciation, and net interest income that grew considerably following large liquidity injections into banking sector at elevated interest rates.³⁹

Breakup of Total Non-tax Revenue Figure 4.8



³⁷ Infrastructure development cess is levied on transportation of goods to maintain and repair the infrastructure needed to cater to the load of goods traffic, among other things.

³⁸ Services inflation was 16.5 percent in FY24. Source: PBS

³⁹ For details on liquidity injections, see Chapter 3 - Monetary Policy and Inflation

Breakup of Consolidated Expenditure

Table 4.4

	Values (billion Rupees)			Percent of GDP			Growth (percent)		
	FY19-23 avg.	FY23	FY24	FY19-23 avg.	FY23	FY24	FY19-23 avg.	FY23	FY24
Total expenditure	11,608	16,401	20,649	19.5	19.6	19.5	17.3	24.4	25.9
1. Current expenditure (a+b)	10,138	14,448	18,571	17.0	17.2	17.5	20.0	25.4	28.5
(a) Federal	7,239	10,785	13,970	12.0	12.9	13.2	23.7	29.1	29.5
Mark-up payments	3,268	5,696	8,160	5.4	6.8	7.7	32.9	79.0	43.3
Domestic	2,912	5,071	7,164	4.8	6.0	6.8	33.0	79.3	41.3
Foreign	383	760	996	0.6	0.9	0.9	42.2	114.7	31.1
Defence affairs and services	1,335	1,586	1,859	2.3	1.9	1.8	9.0	12.3	17.2
Pension	498	666	808	0.8	0.8	0.8	15.2	23.0	21.2
Running of civil government	544	634	784	0.9	0.8	0.7	8.5	16.0	23.7
Subsidies	718	1,080	1,067	1.1	1.3	1.0	80.8	-29.4	-1.2
Grants to others	850	988	1,292	1.4	1.2	1.2	25.9	-13.5	30.8
(b) Provincial	2,926	3,798	4,601	5.0	4.5	4.3	13.0	19.9	21.1
2. Development expenditure/ net lending (c+d)	1,470	1,953	2,078	2.5	2.3	2.0	5.4	17.8	6.4
(c) Total development expenditure	1,416	1,893	2,027	2.4	2.3	1.9	5.5	17.1	7.1
PSDP	1,364	1,893	2,027	2.3	2.3	1.9	7.8	17.1	7.1
Federal*	493	652	635	0.9	0.8	0.6	5.6	62.8	-2.6
Provincial	871	1,241	1,392	1.4	1.5	1.3	12.8	2.0	12.1
(b) Net lending to PSEs	53	59.9	52	0.1	0.1	0.0	17.3	48.3	-13.7
Memorandum items:									
Non-interest (total) expenditure	8,340	10,704.8	12,490	14.1	12.8	11.8	12.7	7.1	16.7
GDP	59,542	83,875.0	106,045	-	-	-	16.6	25.8	26.4

Note: Tax revenue numbers reported by FBR and Ministry of Finance may not tally exactly

Sources: Ministry of Finance; SBP staff calculations

High interest rates also increased federal mark-up receipts on loans to provinces and PSEs. Meanwhile, the PDL collection maintained the last year's momentum, following revision of the levy to Rs 60 per liter on petrol and diesel in H1-FY24.⁴⁰ The impact of increase in prices was large enough to compensate for the drag from lower POL sale volumes during FY24.⁴¹

In contrast to the federal NTR, provincial NTR stood almost unchanged at 0.2 percent of GDP, although it grew notably by 34.5 percent in FY24. This growth is attributed to higher

extraordinary receipts and net hydel profits (NHP) collected by the provinces.⁴²

4.3 Expenditure

Total expenditure declined slightly to 19.5 percent of GDP in FY24, from 19.6 percent in the previous year (**Table 4.4**). This was mainly due to non-interest expenditure, while mark-up payments increased considerably on account of both higher interest rates, as well as debt stock. All the components of non-interest expenditure either declined or remained stagnant in terms of GDP.

⁴⁰ PDL on petrol was raised from Rs 50 to Rs 55 per litre on July 01, 2023, and Rs 60 on September 01, 2023. Likewise, PDL on diesel was hiked to Rs 55 on October 16, 2023, and Rs 60 on November 01, 2023. The latest round of PDL revisions had begun at the start of FY23. Sources: Oil and Gas Regulatory Authority (OGRA); Pakistan State Oil (PSO)

⁴¹ POL sales declined in 8 out of 12 months in FY24, with the annual sales falling by 3.5 percent compared to the previous year.

⁴² Extraordinary receipts include payments by the United Nations in lieu of services rendered by the Pakistani troops contributing in various peacekeeping operations around the world.

Non-interest expenditure

The non-interest expenditure, despite acceleration in growth to 16.7 percent in FY24 from 7.1 percent in the previous year, declined in terms of GDP by one percent (Table 4.4). This decline is traced to decrease in subsidies, development spending, defence affairs, and provincial current spending, while spending on grants, pensions, and running of civil government remained unchanged in terms of GDP.

Total disbursement of subsidies declined slightly by 1.2 percent to Rs 1.1 trillion in FY24, with a fall in non-power subsidies offsetting the marginal growth in power subsidies. At 1.0 percent of GDP in FY24, subsidies have declined sizably from the peak of 2.3 percent in FY22, followed by 1.3 percent in FY23. While still higher than the average of 0.5 percent during FY17-FY21, slight decrease in FY24 for the second year in a row is encouraging.

Non-power subsidies, about 16 percent of total subsidies, decreased from Rs 210 billion in FY23 to Rs 174 billion in FY24, mainly due to lower petroleum subsidies. Unlike last year, there was no disbursement on account of exchange losses on FE-25 loans of PSO that helped reign in petroleum subsidies. It was probably the outcome of reduced exchange rate volatility during FY24 compared to FY23.⁴³ Moreover, the government had restricted gas subsidy to the industrial sector, in view of its revised policy on energy subsidies to the sector.⁴⁴

In contrast to non-power subsidies, power subsidies rose by 2.6 percent from Rs 870 billion in FY23 to Rs 893 billion in FY24 (Table 4.5). The share of power subsidies in total subsidies increased further, continuing to pose challenges amidst scarce resources. The breakup of power subsidies indicates increase in disbursements to the Independent Power Producers (IPPs) as the

Breakup of Subsidies

Table 4.5

estimates, values, & change in billion Rupees

	Budget estimates		Actual values		Change
	FY23	FY24	FY23	FY24	
Total	664	1,064	1,080	1,067	-13
Power subsidies	535	894	870	893	23
IPPs	180	262	93	262	169
K-Electric (TDS)	60	171	267	298	31
AJK (TDS)	-	-	-	105	105
Inter-disco TDS	225	150	213	149	-64
KE for ISP	20	7.0	5.0	-	-5.0
Zero-rated industries	20	-	79	-	-79
PERF	-	48	53	30	-23
Tube-wells	7.0	10	9.0	10	1.0
Non-power subsidies	129	170	210	174	-36
Petroleum	71	51	128	51	-77
Exchange Losses (PSO)	-	-	35	-	-35
RLNG to industry	-	-	31	1.0	-30
LNG to industry	40	-	6.5	-	-6.5
Credit Facility (KPC)	-	-	27	-	-27
Others	58	120	82	124	41
Fertilizer plants	15	25	15	25	10
NPHFS	1.0	12	8.0	23	15
USC	17	35	33	35	1.8

Note: 1) TDS: tariff differential subsidy; ISP: industrial support package; PERF: Pakistan Energy Revolving Fund; PSO: Pakistan State Oil; KPC: Kuwait Petroleum Corporation; NPHFS: Naya Pakistan Housing Finance Scheme; USC: Utility Stores Corporation

Source: Ministry of Finance

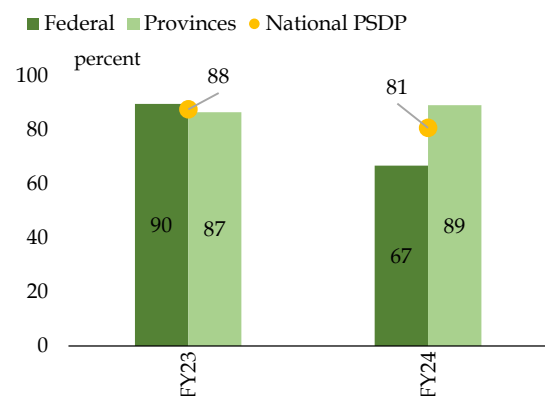
major factor. These disbursements, in line with the budget target, were part of the Circular Debt Management Plan (CDMP) FY24, which requires government to earmark subsidies for power producers every year, as well as increase power tariff regularly, to stem circular debt accumulation.

Furthermore, the government disbursed subsidies of Rs 562 billion to power distribution companies. In particular, K-Electric received Rs 298 billion in view of uniform tariff adjustment, which was 11.7 percent higher than the

⁴³ In contrast to FY23, PKR appreciated between September 7, 2023 and June 30, 2024. Source: State Bank of Pakistan

⁴⁴ Subsidy on LNG supply to industry was almost nil in FY24 against Rs 6.5 billion in the previous year. While subsidy on RLNG to industry was negligible at Rs 730 million in FY24, against Rs 31.1 billion in the previous year.

Actual PSDP Spending as Percent of Budget Estimates **Figure 4.9**



Source: Ministry of Finance

previous year.⁴⁵ In addition, the government also issued unbudgeted subsidies – about 14 percent of the budgeted subsidies.⁴⁶ Among these, the largest was tariff differential subsidy of Rs 105 billion to Azad Jammu Kashmir (AJK). On the other hand, in an effort to rationalize subsidies, the government ended power subsidy to zero-rated (export-oriented) industries, which had received around Rs 80 billion in FY23 – four times the budgeted amount of the year.⁴⁷

In case of development spending, national PSDP, federal plus provincial, fell short of the target by a larger margin than the previous year (Figure 4.9). Decline in federal PSDP, compared to a strong growth in the previous year, mainly explains this phenomenon. In terms of budget

utilization, the federal government spent only 72.8 percent of the annual allocation during Jul-May FY24, compared to 98.5 percent same period last year.^{48,49}

This could be attributed to limited fiscal space, squeezed by rising interest payments. Moreover, given longer than usual tenure of caretaker federal as well as provincial governments, there was a slowdown in the authorization and thus disbursement of funds for development projects.⁵⁰ This reflected in the government prioritizing the ongoing national projects nearing completion rather than the new ones, particularly infrastructure projects in the energy, transport and communication, water resources, and physical planning and housing.⁵¹

In line with the trend in federal PSDP, provincial PSDP also recorded a decline in terms of GDP, despite growing by 12.1 percent compared to 2.0 percent in the previous year. Sindh led this acceleration, followed by Balochistan and Khyber Pakhtunkhwa, while Punjab witnessed a slump in development expenditure. Sindh's development expenditure, which was 49 percent higher compared to FY23, was partly in response to the 2022 floods. In particular, it spent around 74 percent and 21 percent higher on social protection projects and economic affairs, respectively. One of the social protection development projects included *Strengthening Social Protection Delivery System in Sindh*, in collaboration with the World Bank.⁵²

⁴⁵ In order to ensure uniform tariff application across all Ex-WAPDA DISCOS (XWDISCOS) and K-Electric, government picks up the positive tariff differential between K-Electric tariffs based on its revenue requirements and tariffs determined for XWDISCOS by NEPRA.

⁴⁶ Unbudgeted subsidies here refer to those for which no resources were earmarked in the FY24 budget, but were subsequently disbursed through the course of the year.

⁴⁷ Although it did not result in lowering of power subsidies in FY24, it was still a positive development from the perspective of rationalizing subsidies expenditure

⁴⁸ Source: Summary of PSDP Jul-May 2024 (latest available). Ministry of Planning, Development & Special Initiatives

⁴⁹ These statistics may or may not tally with the MoF numbers on PSDP spending.

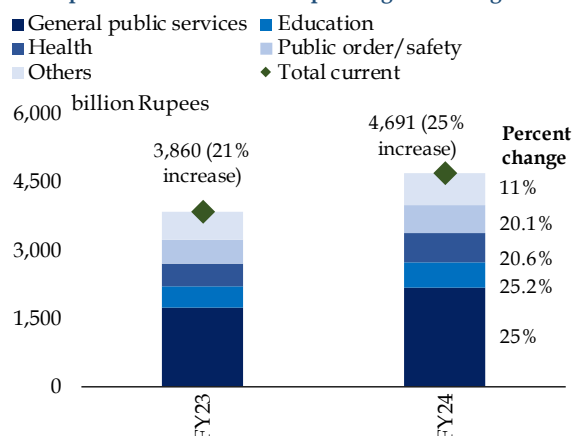
⁵⁰ In FY18, the previous election year, there was a sharp dip in the ratio of actual federal development spending to the budgeted target: 58 percent compared to 91 percent the previous year. Similarly, in FY24, this ratio declined to 67 percent compared to 90 percent in the previous year. Data source: Various Budgets in Briefs and Fiscal Operations Reports. Ministry of Finance

⁵¹ Source: Pakistan Economic Survey 2023-24

⁵² World Bank – Government of Sindh funded five-year Conditional Cash Transfers (CCT) program, covering 65 percent of the total flood-affected union councils in the province to help alleviate flood impacts, especially food insecurity, and monetary constraints for continuous utilization of maternal and children health services. For more details, visit:

<https://www.worldbank.org/en/news/factsheet/2022/12/19/factsheet-strengthening-social-protection-delivery-system-in-sindh>

Breakup of Provincial Current Spending



Source: Ministry of Finance

In case of provincial current spending, there was a decline in terms of GDP, despite notable growth in nominal terms. General public services led most of this growth, followed by public order and safety, health and education (Figures 4.10a & 4.10b).

Federal grants, another major component of non-interest expenditure, stood unchanged at 1.2 percent of GDP, despite growing by 30.8 percent in FY24, as opposed to a decline in the previous year. This growth could mainly be traced to higher disbursements on account of contingent liabilities of PSEs, Benazir Income

Figure 4.10a Province-wise Current Spending

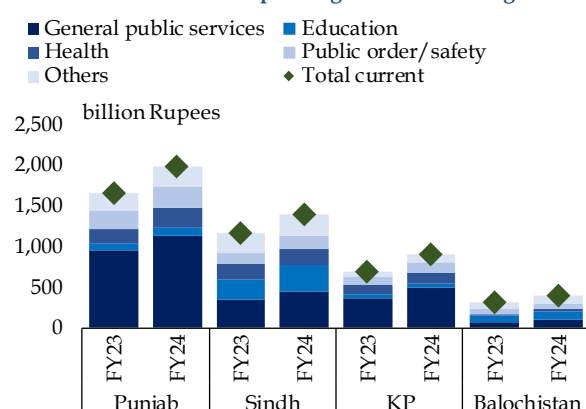


Figure 4.10b

Support Program (BISP), and reimbursement of T.T charges for remittances. Uptick in budgetary allocation in tandem with the broadening social net of the program explains higher BISP disbursements.⁵³ Meanwhile, grants in respect of T.T charges reimbursement, aimed at incentivizing formal remittance inflows, increased following higher remittances from Saudi Arabia (the volume effect). In the same vein, the reimbursement rate on inflows from Saudi Arabia was increased from SAR 20 to SAR 30 in September 2024 (the price effect).⁵⁴

Interest Expenditure

Interest expenditure rose by 43.3 percent to Rs 8.2 trillion, from Rs 5.7 trillion in the previous year, leading to a substantial increase in terms of GDP (Table 4.4). As a result, the mark-up payments as percent of major fiscal variables has considerably increased during FY24 (Table 4.6). For instance, interest payments rose to 202 percent of the FBR tax revenue, adjusted for National Finance Commission (NFC) transfers to provinces. Similarly, interest payments were about 50 times the provincial spending on health and education (Figure 4.11). These trends

Mark-up Payments as Percent of Major Fiscal Variables and GDP Table 4.6

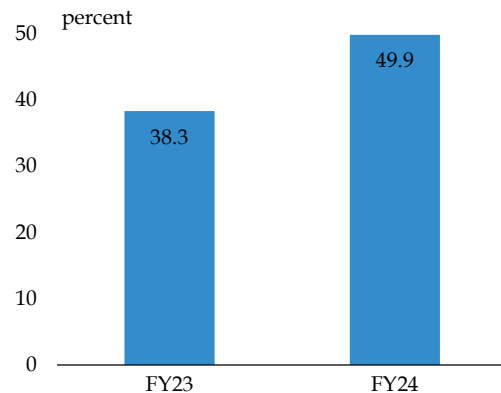
	FY19-23 avg.	FY22	FY23	FY24
Total expenditure	27	24	35	40
Current expenditure	31	28	39	44
PSDP	234	197	301	403
Non-interest expenditure	38	32	53	65
Total revenue	45	40	59	61
FBR tax	62	52	79	88
Net FBR tax*	155	125	193	202
GDP	5.4	4.8	6.8	7.7

* FBR tax revenue adjusted for NFC transfers to provinces

Sources: Ministry of Finance; SBP staff calculations

⁵³ Number of eligible beneficiary families increased from 7.6 million in CY2022 to 9.0 million in CY2023. Quarterly stipend under Benazir Kafaalat Program saw a raise of 25 percent to Rs 8,750 per family. Similarly, the number of children receiving Benazir Taleemi Wazaif scholarships almost tripled from 2.6 million in 2022 to 7.52 million in 2023. Source: BISP Press Release dated August 02, 2024; <https://bisp.gov.pk/SiteImage/Misc/files/Aug%202%2c%2024.pdf>

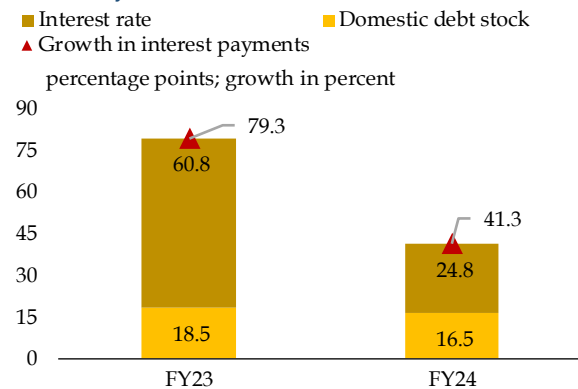
⁵⁴ Source: EPD Circular Letter No. 14 of 2023, dated September 21, 2024 (effective 30 days later); <https://www.sbp.org.pk/epd/2023/FECL14.htm>

Ratio of Interest Expenditure to Cumulative Provincial Spending on Health & Education Figure 4.11

Source: Ministry of Finance

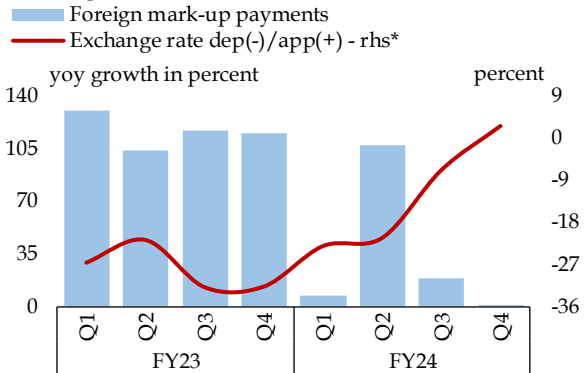
reflect accumulation in public debt due to large fiscal deficits in recent years, as well as the elevated interest rates.⁵⁵

Although growth in interest payments decelerated in FY24, it still remained considerably high. The slight deceleration is explained, in part, by the slowdown in domestic interest payments as the policy rate remained almost unchanged during the year, albeit elevated (Figure 4.12a).⁵⁶ Moreover, the pace of foreign mark-up payments also decreased due to stable exchange rate, particularly in the second half of FY24 (Figure 4.12b)

Estimated Contribution to Growth in Domestic Interest Payments Figure 4.12a

Note: FY21 is taken as the base year

Source: Ministry of Finance; SBP staff calculations

Foreign Mark-up Payments and Exchange Rate Figure 4.12b

*this change is relative to same period year ago

Source: Ministry of Finance; Pakistan Bureau of Statistics

⁵⁵ While fiscal deficit declined to 6.8 percent of GDP in FY24, it was still quite large. Moreover, in absolute terms, it saw an increase of 10.5 percent to Rs 7.2 trillion in the year under review.

⁵⁶ For details, see Chapter 5 – Domestic and External Debt