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Pakistan's real GDP may grow up to 3 percent in FY11: SBP First Quarterly Report

Pakistan's real gross domestic product is likely to grow between 2 and 3 percent in the current fiscal year (FY11) due to expected better contribution by the services sector, and improvement in the performance by the commodity producing sectors, according to the First Quarterly Report of the State Bank on the State of the Pakistan's Economy which was released today.

According to the Report, performance of the commodity producing sectors of the economy is expected to improve in months ahead. However, expectations of a recovery in agriculture will depend crucially on the wheat harvest (including increased production from the rain-fed – "*barani*" - areas), and the livestock sector. Similarly, large-scale manufacturing growth is expected to turn positive again in the months ahead, as strong agri-prices support demand, and with the additional capacities coming on-line in some industries including fertilizer, cement and steel, the Report added.

SBP Report said that growing macroeconomic imbalances in the economy are still quite manageable but further delay in implementing critical structural adjustments risks significantly increasing the future costs to the economy.

The Report pointed out that inflationary pressures have strengthened more than anticipated during the first half of FY11. "A part of this, reflecting post-flood shocks will fade away, as will part of the price rise of sugar, but the fiscal expansion, proposed reduction in energy subsidies, and prospects of rising imported inflation will continue to drive inflationary expectations," the Report said. 'Consequently, SBP estimates for FY11 inflation have been revised upwards from 13.5 percent to 14.5 percent to 15.0 percent to 16.0 percent', the Report added.

The Report said that strong prices encourage farmers to invest in higher yields and support domestic demand. 'Therefore, the only sustainable way to protect low income groups from inflation is by targeted subsidies and the creation of ample employment opportunities', the Report added.

'In contrast to inflation, the current account deficit (CAD) is likely to deteriorate in H2-FY11. A significantly strong growth in imports is expected to more than offset the gains from rise in exports and workers' remittances. The financing of the CAD will be challenging as inflows under financial accounts are likely to be significantly lower. In this perspective, the continuation of the structural adjustment program of IMF would be helpful in softening the external financial constraints, as well as to enhance the resilience and robustness of the economy', the Report added.

SBP Report it pointed out that the one bright spot in the economy, ironically helped somewhat by the floods, was the strength of the external sector. "A jump in remittances and aid flows for flood relief, helped by robust growth in exports largely due to sharp increase in the prices of cotton overshadowed the growth in imports, turning the current account for July-December FY11 to a surplus," it added.

However, SBP Report said that uncertainty over the extent of damage to private and public infrastructure and the policy response to floods, direct and indirect impacts of supply disruptions, energy shortages and weak consumer & business confidence, took its toll on the domestic economy during the initial months of the fiscal year FY11.

SBP Report opined that the fiscal performance remains a source of concern, given the outstanding issues with expenditure management as well as revenue shortfalls. "The implementation of fiscal reforms and elimination of subsidies in the power sector are likely to broaden the tax net and reduce distortions in the economy. While, these reforms will induce cost-push inflationary pressures in the economy, in the short run, but these will help sustain high growth in the long run," the Report added.

The detailed SBP Report is available at State Bank's website www.sbp.org.pk.

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