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Press Release

Pakistan's economy faced several challenges during Q1-FY15 - says SBP report

The State Bank of Pakistan submitted its First Quarterly Report of FY15 titled 'The State of Pakistan's Economy' to the Parliament today. The Report says that Pakistan's economy faced several challenges in the initial months of FY15 as the fourth review of the Extended Fund Facility (EFF) could not be finalized in early-August meetings with the Fund. The Report also refers to political events in mid August in Islamabad that impacted the economic activity in the country. In September, floods inundated a large part of the country's agriculture land in the Punjab. It was feared these losses may push the price of perishable food items up, which fueled inflation expectations.

'Against this backdrop, key macroeconomic indicators could not follow up positive developments observed in the second half of FY14. Q1-FY15 saw higher deficits in the current and fiscal accounts, which had to be financed via domestic resources,' the report concludes. According to the Report, however, there has been a marked improvement in the economy during the second quarter of FY15, which is likely to persist through rest of the year.

Highlighting developments in the external sector during the First Quarter of FY15, the Report says 'Overall trade deficit increased by US$ 1.6 billion in Q1-FY15, compared to the same period last year'. This increase was partly compensated by US$ 765 million increase in home remittances during the quarter. The Report avers that the rising current account deficit, coupled with the uncertainty in the FX market, was one of the key factors that guided SBP's decision to keep monetary policy tight during July-September, 2014.

The Report adds that government borrowings remained lower during Q1-FY15 compared to last year because the government was able to borrow more from non-banks via PIBs and NSS. 'Within the banking system, instead of borrowing from the central bank, the government borrowed from commercial banks, which also remained lower than the same period last year', observes the Report.

According to the Report, industrial sector is presenting a mixed picture. 'Higher cement dispatches, steel imports and strong PSDP spending, suggest a pick-up in construction activity in Q1-FY15. Adding further, the report says, 'In contrast, LSM growth posted a decline in Q1-FY15, as local manufacturers faced gas shortages (especially in fertilizer, textiles, paper, glass and leather sectors). Furthermore, textiles also remained dull on account of lower demand for yarn and fabric from China and Bangladesh. The fall-out of a weak commodity producing sector can also be seen in *wholesale and retail trade* activity. However, the vibrancy in *finance and insurance*, and *telecommunications,* appears to have provided services a boost this year. '

While discussing the outlook of the economy, the Report maintains that Pakistan's external sector would benefit most from the decline in oil prices, as petroleum directly makes up nearly 35 percent of import bill. Inflation is also likely to end up much lower than initial expectations, as the government has steadily been reducing retail POL prices in line with international prices.

The Report underscores the need for important reforms to reduce the structural component of the fiscal deficit. 'The government has formulated a medium-term strategy to implement fiscal reforms, ranging from improving revenue generation to promoting private sector participation in loss making PSEs,' the Report remarks. Plans are also underway to restructure Pakistan Railways, Gencos and Discos, so that these PSEs can contribute positively to Pakistan's economic development. 'However, these plans should be fast-tracked, with a specific focus on their managerial and operational inefficiencies, and their spillovers on the fiscal sector and the rest of the economy,' concludes the Report.