Chapter 6

External Sector

Pakistan's external account came under considerable stress during FY22. The current account deficit rose to four-year high of 4.6 percent of GDP. Rising global commodity prices primarily drove this increase, which elevated the import bill by 32.9 percent during the year. In addition, the expansion in economic activity and import of Covid vaccines further intensified imports. Exports continued the growth momentum of last year and marked a 26.6 percent broad-based increase. Rising global prices, gains from depreciation, and expansion in global demand explain this increase. In particular, textile exports gained from the rising global prices of cotton, which contributed around three quarters to the overall expansion in sector exports. Non-textile exports showed an encouraging performance with some broadening of the export base. The inflows from export of services and workers' remittances also rose considerably. However, the increase could not compensate for the surge in imports during the year. Furthermore, the expiry of G-20's Debt Service Suspension Initiative and increase in global interest rates added further pressure to the current account deficit, as external borrowing became very expensive. The country received higher net inflows of external debt and liabilities during FY22, which rose to US$ 12.1 billion – compared to US$ 5.7 billion in FY21. However, FDI showed a sluggish increase; whereas equity securities witnessed net outflow of portfolio investment. In overall terms, net financial inflows were not adequate to meet the financing requirements of the current account deficit during FY22. Hence SBP's liquid forex reserves declined by US$ 7.5 billion during the year. The impact of external account pressures was exacerbated by uncertainty surrounding the resumption of IMF program, domestic policy uncertainty and political instability leading to a 23.1 percent depreciation in PKR during FY22.

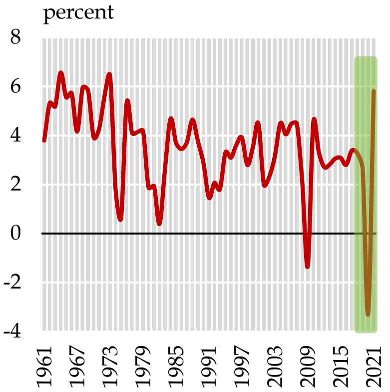
6.1 Global Economic Review

CY21 saw a continuation of the post-pandemic recovery of the global economy. The global economy rebounded, with the world real GDP growth at around five decades' highest level in 2021 (**Figure 6.1a**). The pace of economic growth was uneven with advanced economies that were able to provide substantially higher policy support and inoculation to their population, outpacing emerging economies. The expansion in consumer spending and investment also pushed the volume of global trade in goods above pre-pandemic levels during the year. However, the momentum of economic activity began to taper off with strengthening inflationary pressures, supply chain bottlenecks, and emergence of new Covid variants (including Omicron and Delta) that necessitated re-imposition of lockdowns in some countries, towards the end of 2021.

As the year progressed, the uptrend in prices intensified, as supplies of primary commodities could not adequately meet the

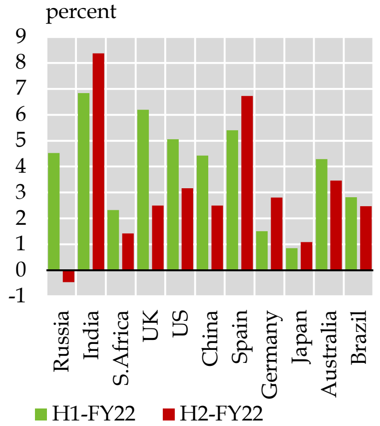
Global Macroeconomic Indicators **Figure 6.1**

a: Global Annual GDP Growth



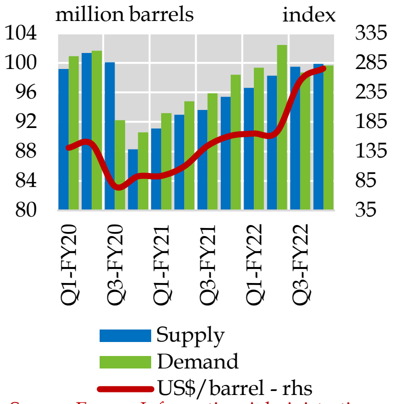
Source: World Bank

b: Average Real GDP Growth in Major Economies FY22



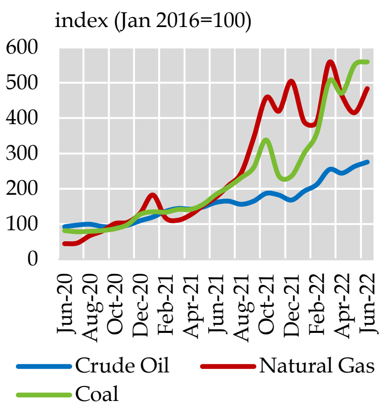
Source: Haver Analytics

c: Global Liquid Fuels' Supply, Demand and Price



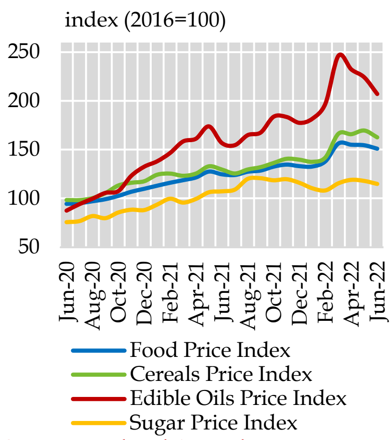
Source: Energy Information Administration, IMF

d: Global Fossil Fuel Price Indices



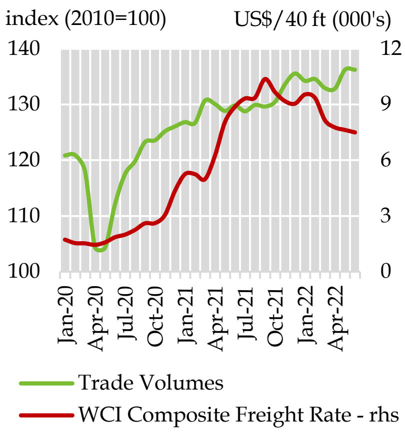
Source: International Monetary Fund

e: Global Food Prices



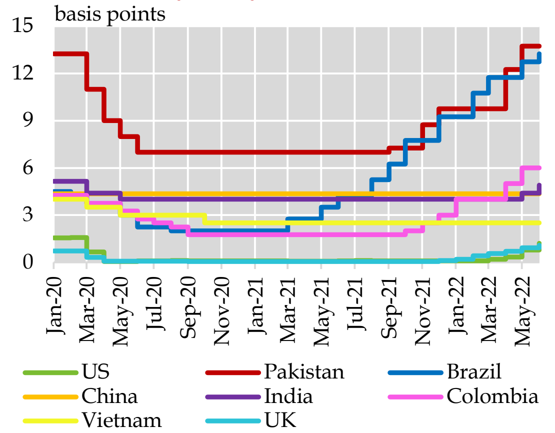
Source: Food and Agriculture Organization

f: Global Trade Volume Indices and Shipping Rates



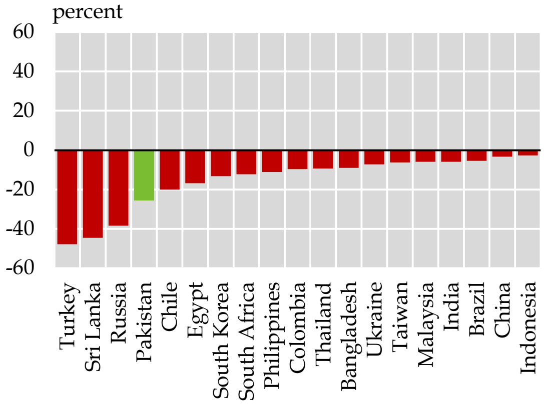
Source: CPB World Trade Monitor, Drewry Supply Chain Advisors

Global Monetary Policy Rates **Figure 6.2**



Source: Haver Analytics

Change in EM Currencies during FY22 **Figure 6.3**



Source: Haver Analytics

rising demand. In particular, the global fuel supplies showed a sluggish increase as OPEC+ member countries adhered to the output quotas, whereas supplies by non-OPEC+ members also remained lackluster, giving rise to a supply-demand gap for crude (**Figure 6.1c**). Some emerging and developing economies were also hit by higher food prices because of poor harvests (**Figure 6.1d and 6.1e**). Alongside the rigidities in commodity supplies, the spread of Omicron also contributed to price volatilities and aggravated supply chain bottlenecks. Similarly, robust increase in global trade volumes pushed freight costs amid rising strains on global distribution networks because of port congestions, shipping delays and worker quarantine requirements (**Figure 6.1f**).

In response to the exacerbating price increases, central banks across emerging and advanced economies resorted to unwinding the post-Covid policy stimulus to stem the expansion in demand. Moreover, some emerging economies such as Brazil, Argentina, Ukraine and Turkey had begun to raise their policy rates before H1-FY22 (**Figure 6.2**). Similarly, hawkish statements from the US Federal Reserve from November 2021, followed by its first post-Covid rate hike in March 2022 and expectations of multiple rate increases in the remainder of 2022, contributed to the US Dollar's appreciation against a wide range of emerging market (EM) and advanced economy currencies (**Figure 6.3**). The resulting currency depreciations amplified inflationary pressures in emerging economies, leading to further rate hikes.

The global economy was only beginning to recover from the impact of the pandemic, when the Russia-Ukraine conflict broke out in February 2022, triggering a serious supply shock.[1] Russia and Ukraine particularly faced considerable GDP contractions in H2-FY22. The effects of the Russia-Ukraine crisis dispersed to other economies through trade, financial linkages and commodity markets. Russia is a crucial supplier of oil, gas and metal; Russia, along with Ukraine, is a primary supplier of corn and wheat as well. Advanced economies placed substantial financial sanctions on Russia, which further spurred inflationary pressures globally. The increase in commodity prices had a material imprint on the pace of economic activity across countries during H2-FY22 (**Figure 6.1b**).

Additionally, China faced a considerable slowdown in economic growth during H2-FY22, largely due to continuing lockdowns to prevent the spread of Omicron in the region, thus worsening global supply bottlenecks. Before the Russia-Ukraine crisis, emerging economies had begun to raise policy rates during H1-FY22, which increased volatility in financial markets. With the Russia-Ukraine

[1] World Investment Report, 2022, UNCTAD

crisis, global financial conditions tightened even further with a lowering of risk appetites and capital flight to quality assets. In addition, monetary tightening in advanced economies resulted in rising sovereign bond yields in these economies. Weak currencies amidst tightened financial conditions drove up costs of external borrowing in emerging economies. On the fiscal side, Covid-related spending eroded policy space in several countries, drawing up debt levels, leaving little to no fiscal space to shield households and firms from the impact of rising inflation.[2]

The Russia-Ukraine crisis also impacted the global trade by strengthening commodity prices. Trade in goods was well above the level in 2019, for major economies during Q3-FY22, with the exceptions of South Korea and China. With the increase in commodity prices, exports grew strongly in commodity-exporting regions, bolstered by increasing demand and increased fuel prices. However, the growth in global trade slowed down during Q4-FY22. (**Figure 6.1f**)

The intensification of the Russia-Ukraine conflict has increased downside risks to global growth. The global growth projections were revised down to 3.2 percent in CY22, from the earlier projections of 6.1 percent in CY21.[3] In advanced economies, the US is particularly facing reduced purchasing power of households and monetary policy tightening. Europe is facing significant spillovers of the Russia-Ukraine crisis and monetary tightening. For emerging market economies, downward revisions in economic growth are largely due to the Chinese economic slowdown and a moderating growth in India.

Pakistan's Balance of Payments during Jul-Jun **Table 6.1**

million US$

	FY21	FY22	Change
Current account balance	**-2,820**	**-17,405**	**-14,585**
Merchandize trade balance	**-28,634**	**-39,681**	**-11,047**
Exports	25,639	32,471	6,832
Imports	54,273	72,152	17,879
o/w Energy imports	9,747	18,743	8,996
Non-energy imports	44,526	53,409	8,883
Services balance	**-2,516**	**-5,019**	**-2,503**
Primary income balance	**-4,400**	**-5,296**	**-896**
o/w interest payments	2,176	3,240	1,064
Secondary income balance	**32,730**	**32,591**	**-139**
o/w Workers' remittances	29,450	31,279	1,829
Financial account balance^	**-8,768**	**-11,149**	**-2,381**
Direct investment inflow	1,819	1,869	50
Portfolio investment inflow	2,762	-78	-2,840
o/w Eurobonds/Sukuk	-	1,000	1,000
Build-up in FX assets abroad	1,345	2,490	1,145
FX loans & liabilities (net)	5,691	12,057	6,366
o/w General government	5,738	6,073	335
SBP	-1,468	-1	1,467
Banks	499	879	380
SDR allocation	-	2,773	2,773
SBP's liquid reserves (end-period)*	**17,299**	**9,816**	**-7,483**
SBP's forward liabilities (end-period)*	-4,870	-3,998	872
PKR app(+)/dep(-) in percent*	**6.7**	**-23.1**	**-**

*Change in reserves, forward liabilities and PKR exchange rate during the period (Jul-Jun). ^Negative sign with financial account balance means net FX inflow into Pakistan and vice versa. Positive sign with change in financial acct. balance means higher net FX inflow into Pakistan on YoY basis and vice versa.
Source: State Bank of Pakistan

[2] World Investment Report, 2022, UNCTAD
[3] World Economic Outlook, July 2022, IMF

6.2 Pakistan's Balance of Payments

Pakistan's external account deteriorated significantly in FY22 (**Table 6.1**). The CAD rose to US$ 17.4 billion in FY22 from US$ 2.8 billion in FY21. Although the country received higher inflows of external loans and liabilities during the year over the previous year, these were not sufficient to meet the financing requirements, leading to US$ 7.5 billion drawdown of SBP's liquid FX reserves during FY22. With the rising pressures in external account, along with appreciation of USD against other currencies, the PKR depreciated against the US dollar by 23.1 percent YoY in FY22.

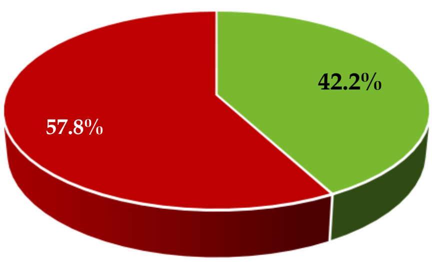
The upsurge in global commodity prices was mainly responsible for the deterioration of the country's external account. Imports of goods surged by 32.9 percent YoY during FY22, where about half of the increase solely came from rising prices of crude (**Figure 6.4a**). In addition, the need to import Covid vaccine and expansion in domestic economic activity also spurred the demand for imports. Hence, despite a sizeable 26.6 percent expansion in exports, the merchandize trade deficit rose to US$ 39.7 billion during FY22, from US$ 28.6 billion in FY21.

Exports also benefited from the rising global prices, particularly cotton, whereas volumes also remained strong (**Figure 6.4b**). Major textile export products included apparel (knitwear and readymade garments), and home textiles. Non-textile exports showed an upbeat performance, as rising volumes contributed around one-tenth in the total increase in exports during the year. In addition to some traditional commodities such as rice, the country also witnessed expansion in some non-traditional categories such as sesame seeds; maize (corn); and refined copper.

Country's foreign exchange earnings from the export of services and workers' remittances also posted a notable expansion during FY22. Most of the increase in remittances came from the advanced economies (especially the US and the UK), that compensated for stagnant inflows from the key Middle Eastern corridors. However, the upsurge in imports overshadowed the gains from these inflows. Also with the expiry of Debt Servicing Suspension Initiative (DSSI) in December 2021, increasing stock of external debt, amid rising global interest rates, interest payments on external debt further widened the CAD during the year.

Net inflow of forex loans and liabilities rose to US$ 12.1 billion in FY22. Key sources of loans in FY22 were bilateral; specifically time deposits of US$ 3 billion from Saudi Arabia in Q2-FY22, and a commercial loan of US$ 2.3 billion from China. Other sources included organizations like the ADB, the AIIB, and the World Bank for capital market development programs, energy sector reforms and Covid support. The IMF also released a tranche of

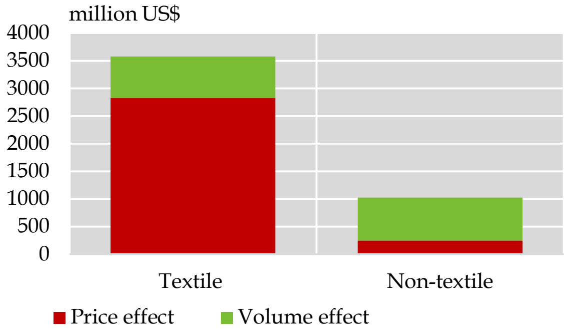
Rising Energy Prices Drove the Increase in Imports during FY22 — **Figure 6.4a**



*Others include price and volume effect of all other imports, and volume effect of petroleum crude and petroleum products.

Source: Pakistan Bureau of Statistics

Rising Prices and Volumes Aided Increase in Exports during FY22* — **Figure 6.4b**



*This analysis covers 77 percent exports for which price and volume data is available for FY22

Source: Pakistan Bureau of Statistics

US$ 1.1 billion in February 2022 after the completion of the 6th Extended Fund Facility (EFF) review. Also, the government raised US$ 1.0 billion through sovereign bonds in net terms during the year.

Most of these inflows were received prior to the increase in the country's risk premium in Q3-FY22, following the intensification of the global commodity prices surge and increasing domestic policy uncertainty.[4] The third quarter of FY22 particularly proved to be a challenging one as the country had to make considerable debt and liability repayments.

To address the rising uncertainties in the external account, the government and the SBP undertook several measures to curtail the demand-side pressures on imports. These included (i) increasing fuel prices; (ii) raising the policy rate by a cumulative 675 basis points; (iii) tightening the prudential regulations for auto and consumer financing; [5] (iv) increasing the cash reserve requirement (CRR) for commercial banks; (v) imposition of 100 percent cash margin requirements on additional import items;[6]and (vi) imposition of ban on import of over 500 luxury and non-essential items.

Current Account

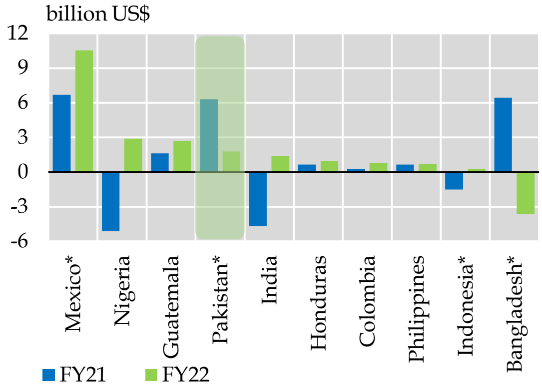
The current account deficit rose to US$ 17.4 billion during FY22, from US$ 2.8 billion last year. The country's FX earnings from exports of goods and services and workers' remittances recorded sizeable increase over the last year, amidst favorable global demand dynamics and continuation of domestic policy incentives (for exporters and remittance-processors, including banks). Textile exports also benefited from higher global cotton prices with volumes of major products positively impacting export receipts. However, the broad-based surge in global commodity prices – especially oil and other energy products, edible oil, and steel – pushed up import payments. Furthermore, higher interest payments on external debt increased the primary income deficit. As a result, the current account deficit widened significantly over last year's level.

Workers' Remittances

The workers' remittances grew by 6.2 percent YoY, reaching a record US$ 31.3 billion in FY22. A number of emerging and developing economies witnessed higher receipts, while some other (e.g., Bangladesh) also saw a decline in inflows in FY22 (**Figure 6.5**). Workers' remittance flows differ across developing countries and regions due to country-specific factors, destination countries' policy stance, international environment, and the economic activity in the host countries.

Specifically, Latin American countries, as well as some Asian economies like India, Pakistan and the Philippines, recorded growth in receipts from advanced economies.[7] Economic stimulus packages announced in the wake of Covid shock in the US and in some European countries had a positive impact on job creation, benefitting foreign workers in general and Hispanics and Latinos in particular.

Changes in Workers' Remittances Inflows in EMEs during Jul-Mar **Figure 6.5**



* Jul-Jun data

Source: Haver Analytics & State Bank of Pakistan

---

[4] CDS spreads on 5-year Pakistan sovereign FX bonds rose by 2,245.4 basis points in Q4-FY22 from Q1-FY22.

[5] BPRD Circular Letter No.29 of 2021 (September 23, 2021), SBP

[6] BPRD Circular Letter No.09 of 2022 (April 7, 2022) and BPRD Circular Letter No.30 of 2021 (September 30, 2022), SBP

[7] Migration and Development Brief 36 (Source: World Bank)

Remittance Inflows to Pakistan from Major Corridors **Table 6.2**

million US$

	FY19	FY20	FY21	FY22	Absolute Change	
					FY21	FY22
GCC	11,739	15,135	17,223	17,225	2,087	2
Saudi Arabia	5,003	6,613	7,726	7,754	1,112	28
UAE	4,617	5,612	6,165	5,846	553	-319
Others	2,119	2,910	3,332	3,625	421	293
UK	3,412	2,569	4,091	4,493	1,522	402
North America	3,522	2,056	3,195	3,795	1,139	601
US	3,309	1,743	2,600	3,087	857	487
Canada	213	313	595	708	282	113
EU Countries	609	1,778	2,729	3,362	950	633
Germany	124	392	432	509	40	77
France	61	240	423	488	183	65
Italy	111	361	607	856	246	249
Spain	151	330	402	513	72	111
Australia	246	340	598	753	258	155
Other countries	2,211	1,253	1,615	1,608	362	-7
Total remittances	**21,739**	**23,132**	**29,450**	**31,279**	**6,318**	**1,829**

Source: State Bank of Pakistan

In the case of Pakistan, North America, Europe including the UK, and Australia, contributed most of the increase. However, inflows from Gulf Cooperation Council (GCC) countries, particularly Saudi Arabia, stagnated around the last year's levels, whereas receipts from the UAE declined during the year (**Table 6.2**).

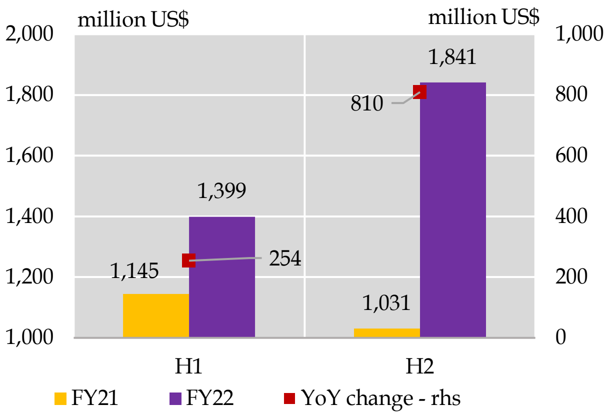
This is despite 61 percent and 103 percent increase in the number of workers emigrating to the KSA and the UAE in FY22. Multiple factors are responsible for this lackluster trend. First, the resumption of cross-border air travel may have led to a shifting of some inflows to informal channels. This factor is cited by the World Bank as a potential risk not just for Pakistan, but also for other major recipients in South Asia (such as India and Bangladesh)[8], as most of the skilled and semi-skilled workers in blue-collar jobs depend largely on the personal networking to send remittances back home. Second, the GoP withdrew the incentive (20 Riyal rebate as a remittances fee) to banks on the remittances originating from KSA. Under this incentive, the government pays the remittance fee (or TT charges) to banks on a minimum remittance above US$ 100. Withdrawal of this incentive may have diverted some of these inflows to the informal channels. However, given the large stock of Pakistani workers employed in the region, the inflows from the GCC countries contributed more than 50 percent of the total remittances inflows in Pakistan in FY22.

The inflows from the advanced economies had slightly different dynamics. The Pakistani remitters in these countries are generally a settled diaspora and many of them are employed in white-collar jobs, or own businesses. Strong GDP and wage growth in these economies, as well as compensations from the Covid-related fiscal stimuli (in the form of cash transfers, deferred rent and utility payments) had a significant impact on their earnings, which may have contributed to increased flows from the advanced economies.[9]

Moreover, Pakistani assets may have become more lucrative, specifically real estate, for

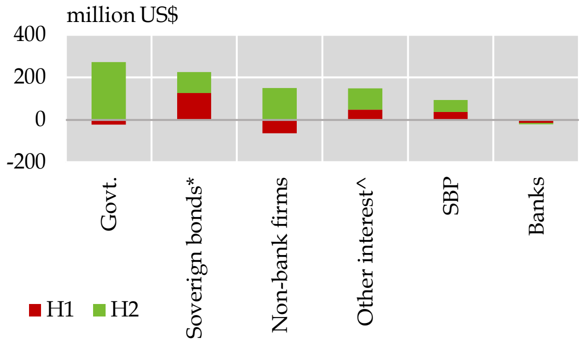
[8] Migration and Development Brief 36, May 2022 (Source: World Bank)
[9] Migration and Development Brief 36, May 2022 (Source: World Bank)

Half Yearly Interest Payments **Figure 6.6a**



Source: State Bank of Pakistan

Breakdown of YoY Change in Total Interest Payments by Source in FY22 **Figure 6.6b**



*Eurobonds & Sukuks; ^other portfolio interest
Note: This breakdown is given based on unadjusted data.
Source: State Bank of Pakistan

swift capital gain as a result of persistent depreciation of the PKR against the US dollar.

Primary Income Account

The primary income deficit rose to US$ 5.3 billion in FY22, up 20.4 percent from last year's US$ 4.4 billion. This increase is partly attributable to low base effect of FY21, when the deficit had contracted by 15.5 percent to a six-year low.

Elevated debt servicing was mainly responsible for expansion in the primary income deficit in FY22. Between May-2020 and December-2021, the country benefitted from the Debt Service Suspension Initiative (DSSI), with the suspension of external debt payments (both principal and interest) worth US$ 3.7 billion. With its expiry, interest payments on government loans increased considerably during H2-FY22 (**Figure 6.6a and 6.6b**), lifting the overall servicing of interest payments to US$ 3.2 billion during FY22, which were —up US$ 1.1 billion YoY. In addition, the payments on Eurobonds/Sukuk also rose by 62.2 percent during FY22, following the issuance of new Eurobonds worth US$ 2.5 billion last year. Finally, the rising global interest rate environment also contributed to the rise in Pakistan's external debt servicing.

Furthermore, a slight increase in repatriation of profit and dividends on foreign investment also contributed to the increase in primary income deficit in FY22. There was moderate growth in the profit and dividend repatriation in the first nine months of FY22 as the companies attracting FDI and FPI made higher profits.[10] However, a decline was witnessed in the last quarter of the year, which could be explained by greater PKR depreciation in this quarter.

Services Account

After declining consecutively for the last three years, the services account deficit more than doubled from US$ 2.5 billion in FY21 to US$ 5.0 billion in FY22. This deterioration came on the back of a large spike in services imports, which overshadowed a notable rise in export of services (**Table 6.3**).

Services imports clocked in at US$ 12 billion, up 41.5 percent from last year, with higher sea and air freight having the largest contribution in this increase. The surge in merchandize imports and soaring global freight costs inflated the sea and air freight payments to US$ 5.6 billion during FY22, from US$ 2.6 billion last year (**Figures 6.7a and 6.7b**).

Furthermore, due to reopening of global air travel in FY22, imports of aerial transport and travel-related services bounced back from the lows of 2020, when Covid had disrupted these services across the globe (**Figure 6.8**). For similar reasons, payments for education-related expenses as well as religious

[10] Source: Quarterly Financial Statements Analysis of Select Listed Non-Financial Companies (March 31, 2022)

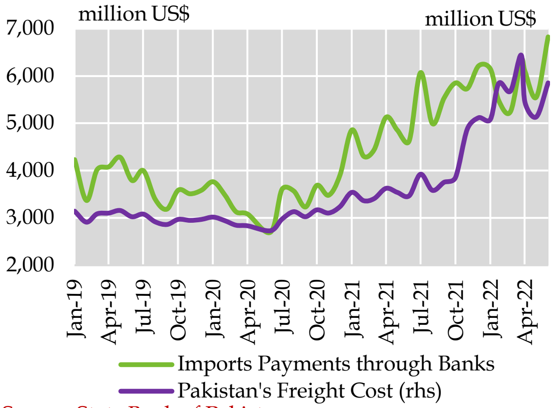
Breakdown of Services Trade Account **Table 6.3**

million US$

	Import (M)		Export (X)		Balance (X-M)	
	FY22	YoY Change	FY22	YoY Change	FY22	YoY Change
a) Transport	**6,787.2**	**3,508.3**	**821.1**	**277.1**	**-5,966.1**	**-3,231.2**
Sea freight	5,377.4	2,918.3	94.0	59.8	-5,283.4	-2,858.5
Air passengers	691.9	485.1	429.3	143.3	-262.6	-341.8
Air freight	255.5	91.9	31.4	2.3	-224.1	-89.7
b) Travel	**1,355.9**	**603.9**	**541.1**	**40.1**	**-814.8**	**-563.8**
Education exp.	265.1	116.6	10.8	-1.8	-254.3	-118.5
Other (personal)	1,075.6	490.3	523.9	39.7	-551.6	-450.6
c) ICT Services	**612.0**	**82.0**	**2,617.9**	**510.1**	**2,005.9**	**428.1**
Software consultancy services	214.1	45.0	795.5	240.9	581.4	195.9
Other Computer services	71.8	5.4	743.8	50.8	672.1	45.5
Export of Computer software	241.7	26.4	564.6	147.1	322.9	120.7
Call centers	0.2	0.1	215.5	61.0	215.3	60.8
Subtotal (a+b+c)	**8,755.1**	**4,194.2**	**3,980.1**	**827.3**	**-4,775.0**	**-3,366.9**
Total services	**11,969.7**	**3,508.4**	**6,950.4**	**1,004.9**	**-5,019.3**	**-2,503.5**

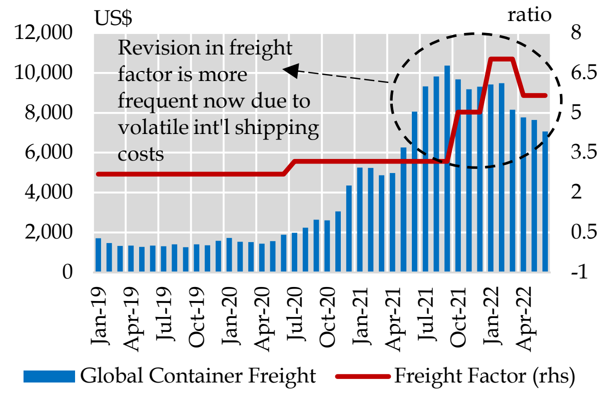
Source: State Bank of Pakistan

Merchandize Import and Freight Payments **Figure 6.7a**



Source: State Bank of Pakistan

Global Shipping Cost and Revision in Freight Factor **Figure 6.7b**



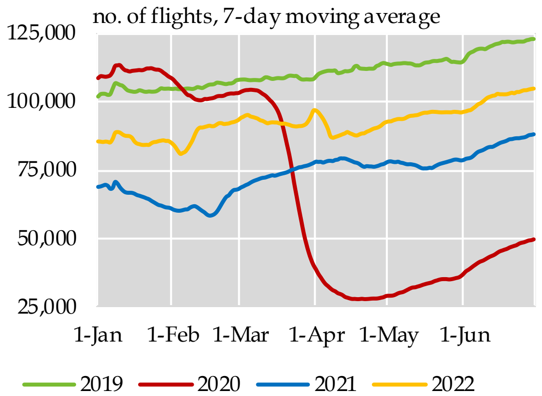
Source: Statista and State Bank of Pakistan

and leisurely travelling out of the country also went up from last year.

Services exports reached US$ 7.0 billion in FY22, up 16.9 percent from the year before. In particular, ICT services fetched US$ 2.6 billion in exports receipts—24.2 percent higher YoY. It was also the largest net export sector in services trade in FY22, with net receipts standing at US$ 2.0 billion. ICT services exports have risen exponentially in recent years; multiple factors have led to this performance, which are discussed in **Box 6.1**.

Besides ICT, payments made by passengers travelling into the country by national airlines registered a 1.2 times YoY increase to US$

Number of International Commercial Flights **Figure 6.8**



Source: Flightradar24

970.4 million in FY22.[11] Nevertheless, these inflows were outweighed by higher outflows on account of travel services, since Pakistani airlines operate on considerably lower foreign routes compared to foreign airlines.

Box 6.1: Factors Underlying Expansion in Pakistan's ICT Services Exports

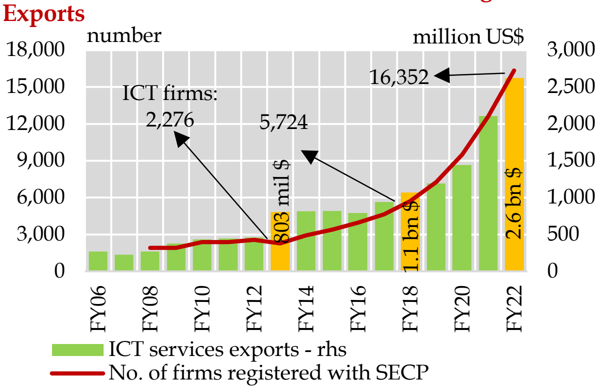
Pakistan's exports of telecommunications, computer and information services (also generally known as information and communications technology, or ICT services) have risen remarkably from US$ 269 million in FY06 (7.2 percent of the overall services exports) to US$ 2.6 billion (37.7 percent) in FY22. In FY18, they crossed the one-billion-dollar mark; and by FY21, the two-billion-dollar mark (**Figure 6.1.1**).

ICT services are divided into three sub-categories: telecommunication services, computer services, and information services. The largest contributor is the computer services, with its share averaging 76 percent between FY18 and FY22. Within computer services, software consultancy, software exports, and other computer services—mainly dominated by the freelancing activities, fetch highest receipts (**Figure 6.1.2**). The convergence of various supportive factors including rising global demand, enabling government policies, and Pakistan's demographics with a large share of young, tech-savvy population supported this sharp expansion in Pakistan's ICT exports as discussed in the following.

Rising global demand: Pakistan's ICT services exports have grown in the backdrop of rising global demand spurred by the tech-driven Fourth Industrial Revolution. Worldwide ICT spending has been on a rising trajectory since 2000's, notwithstanding the ebbs and flows (**Figure 6.1.3**). In view of the globalization of services, Pakistan has been one of the beneficiaries of the rising demand for ICT in the world, particularly in the computer software and other computer-related services (especially freelancing).

Moreover, Pakistan has also benefited from the Covid-19 pandemic, which has accelerated the adoption of technology across the globe, further fanning the demand for the ICT products and services. According to an UNCTAD report, global ICT services stayed not only resilient but grew through the Covid-19.[12] The pandemic enabled strong stimulus for businesses and individuals to leverage digital tools, which drove a 6 percent increase in worldwide ICT exports in 2020 that reached US$ 676 billion. The report notes that the usage of communications services, computer services and software received a boost from the lockdown-related restrictions across the globe. Another report from the Asian Development Bank also found Covid-induced acceleration in global digital services trade, with Asia and Pacific at the core of it.[13] Pakistan was able to capitalize

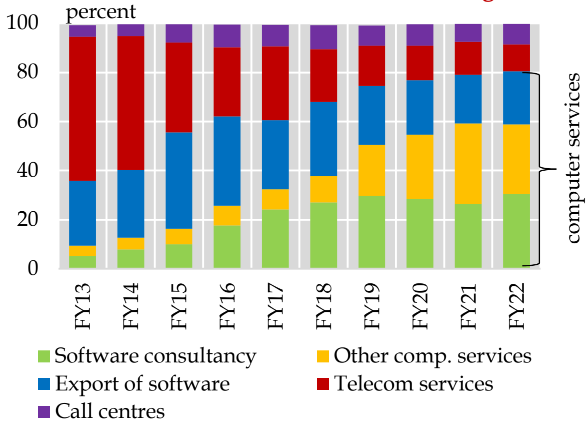
Growth of ICT Services Firms and Exports — **Figure 6.1.1**



*Note: No. of firms data not available for FY06-07

Sources: Securities & Exchange Commission of Pakistan and State Bank of Pakistan

Breakdown of ICT Services Exports — **Figure 6.1.2**



Source: State Bank of Pakistan

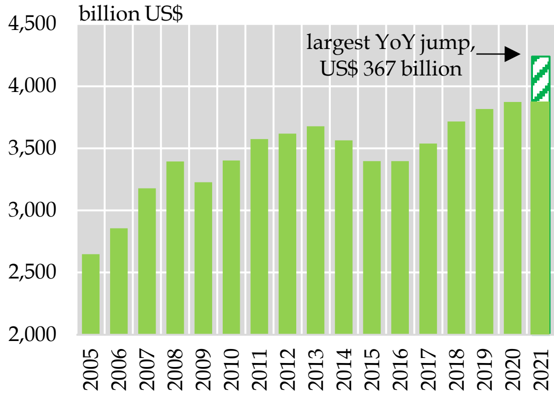
[11] This number is calculated by adding services exports against "Air Passengers" and "Travel" in Table 6.3.

[12] Impacts of the Covid-19 Pandemic on Trade in the Digital Economy. UNCTAD Technical Notes on ICT for Development No. 19. United Nations Conference on Trade and Development. (Available at: www.unctad.org/system/files/official-document/tn_unctad_ict4d19_en.pdf)

[13] Asian Economic Integration Report 2022: Advancing Digital Services Trade in Asia and the Pacific. February 2022. Asian Development Bank. Philippines.

on some of that demand. Various homegrown factors have contributed to this expansion as discussed in the following.

Historic Data Showing Worldwide ICT Spending **Figure 6.1.3**



Source: Statista

a. Dedicated government policies and institutional framework: Expansion of telecommunication infrastructure, including the internet broadband, software parks and call centers, has enabled sustainable growth in the IT sector. The government, in consultation with the industry stakeholders, has announced various policies and incentives in the budgets from time to time that have provided the necessary impetus to the sector's growth, which has eventually translated into higher ICT exports, making it one of the leading net export sectors of the economy. These policies included: IT Policy and Action Plan 2000, Broadband Policy 2004, Mobile Cellular Policy (2003 and 2013), Telecommunication Policy 2015, Digital Pakistan Policy 2018, Digital Pakistan Vision 2019, and Rolling Spectrum Policy 2020-23, among others. One of the objectives of Digital Pakistan Policy 2018 was to double ICT exports by 2020; that was achieved in FY21.

Some of the major incentives for the IT and IT-enabled services include:
a) 100% foreign ownership;
b) 100% repatriation of capital & dividends (subject to SBP approval);
c) IT & ITeS export income tax exemption[14];
d) income tax holiday for venture capital companies or funds till June 2024;[15]
e) exporters of software, including freelancers, can retain up to 35 percent of their net foreign exchange earnings in special FCY accounts, to serve assorted purposes, including payments of commission or discount to the overseas agents or buyers, advertisement expenses, and collection of market intelligence abroad.[16]

The incentives for IT startups included:
a) exemption from income tax, minimum tax and withholding tax for PSEB-registered and certified IT startups offering technology-driven products and services for a period of three years;
b) exemption from sales tax on export of IT services from Islamabad and other federal territories;
c) IT companies allowed to open foreign exchange accounts in Pakistan.[17]

b. Pakistan Software Export Board (PSEB), an apex government body promoting the IT industry both locally and internationally, has also facilitated the growth of Pakistan's ICT services exports. PSEB has so far established 16 Software Technology Parks (STPs), including one in Gilgit in 2020, where many IT companies have relocated their business operations in a short span of time, providing services to customers beyond the borders. STPs provide a stable and reliable ICT infrastructure and other allied services to IT and ITeS companies; and encourage development and export of software and software services.[18] Pakistan's software and software consultancy services exports have increased from around half a billion in FY17 to US$ 1.4 billion in FY22. This was also in line with the global spending on 'enterprise software' that doubled between 2017 and 2021.[19]

---

[14] In FY21, income tax exemption was replaced with 100 percent tax credit scheme through Finance Act 2021. Later, through Finance Act 2022, it was abolished and substituted with 0.25 percent final tax on export proceeds of PSEB-registered IT and IT-enabled entities; the rate was 1.0 percent for non-registered entities.
[15] This facility was extended to June-2025 under Finance Act 2022.
[16] Chapter 12 – Exports, Foreign Exchange Manual.
[17] Digital Pakistan Policy 2018, Ministry of Information Technology and Telecommunications
[18] Source: www.pseb.org.pk/about-us
[19] World IT spending on 'enterprise software' rose from US$ 369 billion in 2017 to US$ 736 billion in 2021. Source: Gartner Inc. (various press releases on "Worldwide IT Spending Forecast"). (note: Gartner Inc. is a management consultant company). (Available at: www.gartner.com/en/search?keywords=press%20release&context=ac)

In 2016, PSEB had also embarked on a project called "Enhancing IT Exports through Industry Support Programs", which aimed at facilitating software developers earn international certifications, like Capability Maturity Model Integration (CMMI)—a de facto international standard for software process improvement and software capability evaluation.[20] Under the program, PSEB would bear up to 80 percent cost for a number of international certifications. Around 173 companies have been certified so far with its assistance, and others are in the pipeline.[21]

c. **Cost competitiveness**: One of the key motivations behind offshoring or outsourcing by any business is the cost advantage in other countries. Pakistan offers cost competitive ICT services. According to a World Economic Forum report that came out in 2016 and A.T. Kearney's Global Services Location Index 2021, Pakistan is the most financially attractive destination for ICT services and services offshoring, respectively.[22, 23] Pakistan's IT industry, with its mature IT ecosystem, can serve at nearly 70 percent lower cost than the developed markets, such as North America.[24] Many international IT firms have established offices in Pakistan, including IBM, HP, Microsoft, Dell, Intel, Mentor Graphics, Oracle, Siemens, NCR, Teradata, and many more. Furthermore, Pakistani companies have many Fortune 500 companies as their clients, including Hallburton, BMW, Motorola, General Electric, Toyota, Daimler Chrysler, AT&T, among others.

d. **Young labor force**: Educated younger population is generally more inclined to adopting new technologies and communication products. According to Tech Destination Pakistan, a PSEB-run website, every year over 25,000 IT engineers graduate in Pakistan, and the number keeps rising. There are over 600,000 English-speaking IT and BPO (business processing outsourcing) professionals in the country, with expertise in current and emerging IT products and technologies. Pakistan is also the third-largest English-speaking country, as well as third-largest contributor of online labour.[25] It is also one of the youngest nations in the world, with 30.2 percent of the population in the age group of 18-35.[26]

e. **Freelancing**: Freelancing, often called as gig economy, is a fast-growing IT-enabled service in the world. In 2019, Pakistan ranked as the third-most popular country for freelancing.[27] It also ranked as number 3rd on the Freelancer and 5th on Upwork (both are popular freelancing websites).[28] A report by Payoneer attributed the freelancing success in Pakistan to the very young population.[29] It says a more technically-oriented education has helped the country's youth partake in the gig economy. The investment in the younger generation seems to be paying off as freelancers younger than 35 contribute around three-fourths in the overall revenues. Digiskills.pk, Pakistan's first large-scale free online training program providing skill-based education for online labor market and funded by the government, has delivered more than 2.7 million trainings since 2018. It offers courses in

[20] Source: www.pseb.org.pk/images/status-of-certification-project.pdf
[21] Source: www.pseb.org.pk/images/list-of-companies-for-certification.pdf, accessed at 28-07-22
[22] The Global Information Technology Report 2016. World Economic Forum. Switzerland. (Available at: www3.weforum.org/docs/GITR2016/WEF_GITR_Full_Report.pdf)
[23] A.T. Kearney Global Services Location Index 2021. A.T. Kearney. United States. (A.T. Kearney is a management consultant company) Available at: (www.kearney.com/documents/291362523/291367053/The+widening+Impact+of+Automation.pdf/95d8d519-e2b0-0e4f-994d-15e8716b339e?t=1505444810000)
[24] Pakistan's IT Industry Overview 2020. Ministry of Information Technology and Telecommunications, Government of Pakistan.
[25] Source: www.techdestination.com/
[26] United Nations, Department of Economic and Social Affairs, Population Division (2022). World Population Prospects 2022, Online Edition
[27] Pakistan's IT Industry Overview 2020. Ministry of Information Technology and Telecommunications, Government of Pakistan.
[28] Pakistan Software Houses Association for IT and ITeS (P@SHA). (Available at: www.pasha.org.pk/knowledge-center/industry-stats/)
[29] The Global Gig-Economy Index: Cross-border Freelancing Trends that Defined Q2-FY19. (Available at: www.cdn.techjuice.pk/wp-content/uploads/2019/08/Index-freelance.pdf)

freelancing; virtual assistance; video editing, animation and vlogging; graphic designing; digital marketing, among others.[30] Digiskills has contributed in fetching US$ 200 million in IT export receipts.[31]

Financial Account

Net financial flows into Pakistan increased by over 27.2 percent YoY to US$ 11.1 billion in FY22 (**Figure 6.9**). Significant inflows came from external loans and liabilities of US$ 12.1 billion – much larger than US$ 5.7 billion received in FY21. The largest inflow was a US$ 3 billion time deposit from Saudi Arabia, along with a US$ 2.7 billion SDR allocation from the IMF, US$ 2.0 billion from issuing Eurobonds and Sukuk, and a US$ 2.3 billion commercial loan from China. With respect to payments, Pakistan retired sovereign bonds worth US$ 1 billion in October of 2021, repaid a commercial loan from China of US$ 2.4 billion. In FY22, the country experienced net FPI outflows of US$ 78 million, versus a net inflow of US$ 2.8 billion in FY21.

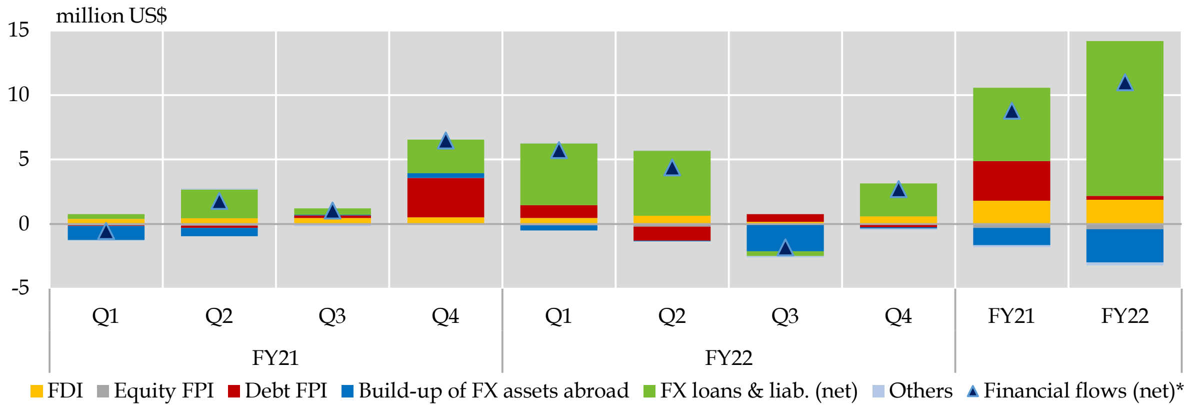
Foreign Direct Investment

Global trends

Globally, the rebound in economic activity, and financial stimulus for infrastructure sector propped up FDI to pre- pandemic levels in CY21. However, with the outbreak of geopolitical turmoil in the shape of the Russia-Ukraine conflict, FDI flows began to reverse direction in Q3-FY22.[32]

Around 75 percent of the upswing in global FDI was in developed economies, mainly due to mergers and acquisitions, retained earnings of multinational enterprises (MNEs) and cross-border financing of infrastructure projects.[33] Accommodative monetary conditions during most of the year and a resurgence in domestic demand underpinned a sharp expansion in MNEs' profitability, leading to higher retained earnings during the year. On the other hand, investment in SMEs declined throughout CY21. Although the green field investments witnessed a small recovery that was concentrated in developed countries, the flows remained below pre-pandemic levels in CY21. Greenfield investments underwent declines in emerging market economies, largely due to declines in investment in the coal, gas and oil

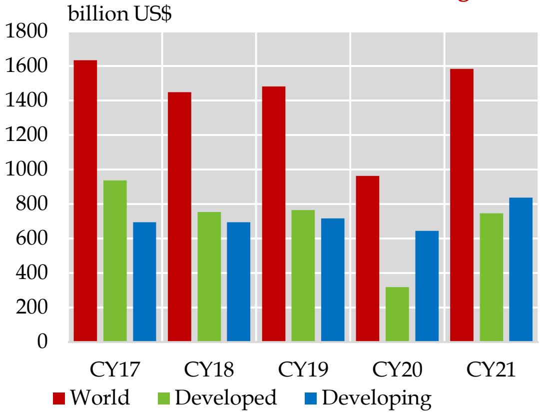
Breakdown of Financial Flows Received by Pakistan **Figure 6.9**



*Financial account balance sign reversed from BPM6 convention. Positive value indicates net FX inflow & vice versa.
Source: State Bank of Pakistan

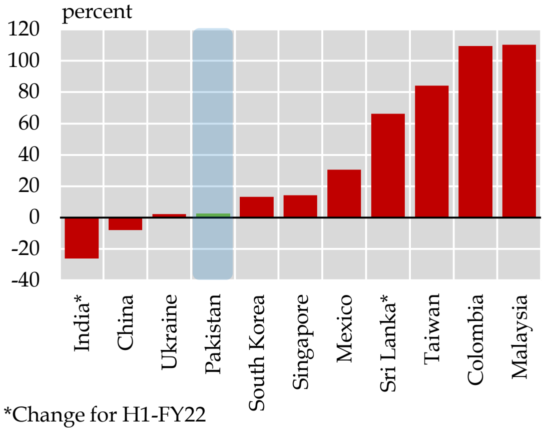
[30] This program is funded by Ignite—a National Technology Fund Source. (Available at: www.digiskills.pk/, accessed at 28-07-2022)
[31] Source: www.ignite.org.pk/, accessed at 28-07-2022; Ignite is a National Technology Fund—a contributory fund maintained by the government.
[32] World Investment Report, 2022, UNCTAD
[33] The leading recipients for global FDI inflows included the United States, China and Australia, while the leading benefactors for FDI outflows were the US, Australia and the UK. (Source: The FDI Report, fDi Intelligence)

Global Net FDI Inflows **Figure 6.10**



Source: United Nations Conference on Trade & Development

Country-wise FDI Change in FY22 **Figure 6.11**



*Change for H1-FY22
Source: Haver Analytics

sectors. This was on the back of a global shift to clean energy investment in the wake of a growing shift towards environmental, social and governance (ESG) oriented investments. (**Figure 6.10**)

In terms of sectoral composition, renewable energy held the top spot for capital investment in CY21, followed by the communication sector. Investment in semiconductors, increased by around four times from CY20 to CY21, making it the third largest sector to receive FDI. In addition, global investment in SDG-relevant sectors including infrastructure, food, water, sanitation and health also grew significantly during the year.[34]

In the developing region, Asia was the largest recipient of global FDI flows, although 70 percent of the FDI to the region was received by six economies.[35] In the South Asian economies, India witnessed a sizeable decline in net FDI flows (**Figure 6.11**). Notwithstanding the decline, India was the top FDI recipient in the Asian region by project numbers. These inflows were mainly in the services sector, constituting banking, research, and insurance, followed by the manufacturing sector, including pharmaceuticals, drugs and automobiles. By capital investment, China remained the top FDI recipient, with most investment channeling into the services and high-tech sectors.

Developments in Pakistan

FDI in Pakistan rose marginally by 2.7 percent YoY in FY22 to US$ 1.9 billion, largely due to net inflows into sectors including power, financial firms and energy (**Table 6.4**). A quarterly breakdown of the financial account shows that inflows were at their highest in Q1 and Q2 of FY22.

The power sector continued to dominate FDI inflows in FY22 largely due to CPEC projects (although there was a slight decline YoY from

Sector-wise Net FDI Flows **Table 6.4**

million US$

	FY21	FY22	Abs. Change
Power	911.7	737.6	-174.1
o/w Coal	512.1	423.4	-88.7
Hydel	203.1	174.1	-29
Financial firms	236.4	405.3	168.9
Oil & gas**	188.1	178.4	-9.7
ICT	117.1	118.9	1.8
o/w Telecom	43.6	-29.1	-72.7
IT	73.5	148.0	74.5
Trade	115.9	79.9	-36
Electrical machinery	114.1	36.8	-77.3
Transport	-93.6	34.8	128.4
Electronics	35.7	32.5	-3.2
Chemicals	0.9	29.3	28.4
Food*	12.0	-3.2	-15.2
Others	182.2	217.5	35.3
Total	**1,820.5**	**1,867.8**	**47.3**

*includes food packaging **exploration & refining
Source: State Bank of Pakistan

[34] The fDi Report 2022, fDi Intelligence
[35] China (18%), Malaysia (15%), Japan (13%), India (9.3%), Singapore (7.9%), Vietnam (6.8%). Total capital investment into the region in CY21 was US$ 165.9 billion. Source: The fDi Report 2022, fDi Intelligence

FY21). China and the UAE both significantly invested in the power sector under the Thar Coal Block-I Power Plant as part of the CPEC project, a greater part of which has been completed thus far and is expected to be operational by August 2022.[36] Other important inflows were in coal-powered and hydropower projects under the CPEC umbrella.

Financial firms saw the second highest inflows into FDI during the year; a leading bank received inflows from companies from Switzerland for the extension of fintech services. FY22 saw firms from Hong Kong investing in the oil and gas services segment, in a foreign oil exploration and production company, for maintenance and extension of drilling operations in the country. Although the YoY absolute amount of net FDI into the sector fell in FY22, it remained the third largest source of sector-wise FDI in the country. There was a notable increase in the IT sector in FY22, which rose by US$ 148 million YoY. The increase marked the rise of the start-up venture capital culture in the country, along with angel investment funds.[37]

In the ICT sector, the UAE invested in a telecom company, mainly into cloud services, modernizing the IT infrastructure, and in transforming its billing platform. Inflows also realized into a Dubai based ride-hailing service, running operations in Pakistan, following a merger with a startup company. Investment into the country from Singapore rose to US$ 114.7 million in FY22; one leading benefactor was an e-commerce marketplace for business-to-business (B2B) grocery supplies. The USA also invested in an online grocery-shopping venture, along with a financial firm that had entered into an alliance to facilitate customers with real-time B2B settlements.

Foreign Portfolio Investment

Global trends

Globally, portfolio flows had begun to show signs of improvement during Q1-FY22, supported by economic recovery and improved risk sentiments. Equity flows in emerging economies were also recovering, although slowly; debt flows, on the other hand, remained weak. (**Figure 6.12**). However, amid rising inflation outturns, Q2-FY22 saw tightening of the external financing conditions reflecting normalization of monetary policy in advanced and emerging economies.

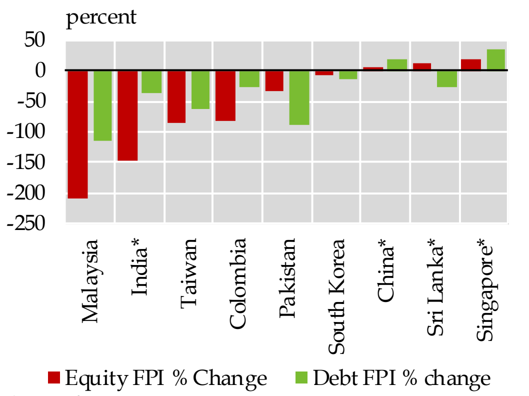
In H2-FY22, global financial conditions underwent further tightening due to the increase in interest rate by the US Federal Reserve and outbreak of the Russia-Ukraine conflict (the effects of which were mostly realized in European and Middle Eastern economies with closer links to Russia); which reflected in higher costs of funding and lowered equity valuations. Emerging economies witnessed more stringent financial conditions amid rising risks to capital flows.

Developments in Pakistan

Pakistan witnessed net FPI outflows of US$ 78 million in FY22, against net inflows of US$ 2.8 billion in FY21. While the debt securities saw US$ 310 million of net inflows in FY22, equity securities reported net outflows of US$388 million during the year. The constrained capital flows reflected global monetary tightening (**Figure 6.13**).

Additionally, MSCI downgraded Pakistan's status from an emerging to a frontier market

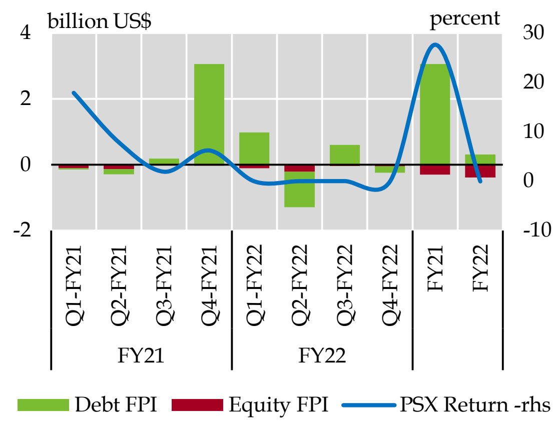
Global FPI Change in FY22 **Figure 6.12**



*Change for H1-FY22
Sources: Haver Analytics

[36] CPEC Project Details, available at: www.cpec.gov.pk
[37] Box 5.1, State of Pakistan's Economy, First Quarterly Report 2021-22, State Bank of Pakistan

FPI into Pakistan and PSX Returns **Figure 6.13**



Sources: Haver Analytics & Bloomberg

economy (September 2021); Moody's also downgraded the outlook of Pakistan from stable to negative (June 2022), citing Pakistan's external vulnerability risks. The vulnerability was multiplied by factors including exchange rate volatility, political instability, and uncertainty around the resumption of IMF program leading to decline in FPI. Pakistan's CDS spreads also showed an increasing trend throughout FY22, particularly in the last quarter of FY22. This resulted in capital flight from the country, as the rise of CDS spreads indicates worsening risk profile, affecting most leading sectors listed at the PSX (**Figure 6.14a & 6.14b**). The FPI equity outflows were largely from the commercial banks' sector (US$201.89 million), followed by the cement sector (US$ 60.1 million), the fertilizer sector (US$ 51.4 million), and the oil and gas sector (US$ 28.7 million) (**Figure 6.15**).

In debt securities, Pakistan raised US$1 billion from the tap issuance of a Eurobond in Q1-FY22. The country repaid a maturing Sukuk of an equal amount in Q2-FY22. Additionally, US$ 1 billion was raised by the issuance of Sukuk bonds in Q3-FY22.

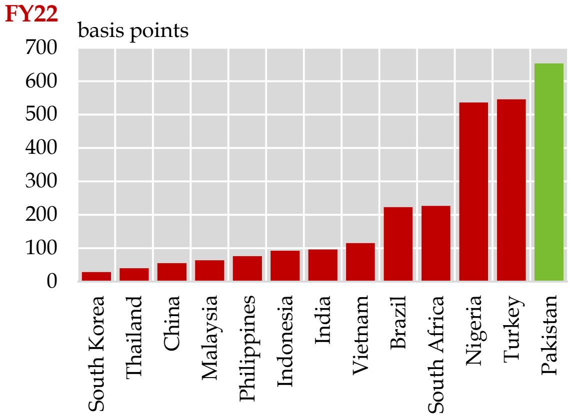
Net Incurrence of Liabilities

The net inflow of FX loans and liabilities into Pakistan rose to US$ 12.1 billion in FY22, against US$ 5.7 billion in FY21. The largest increase was seen in bilateral loans, mainly owing to time deposits from Saudi Arabia amounting to US$ 3 billion during FY22 (**Table 6.5**). Loans from the ADB were concentrated in capital market development programs, energy sector reforms, and Covid vaccine support programs; the World Bank, on the other hand, lent amounts for water resource projects and clean energy programs. A bulk of the loans from AIIB went into power projects. The IDB lent towards Covid support programs (including vaccinations), along with short term financing of the import of oil and LNG by Pakistan.

Pakistan received a commercial loan of US$ 2.3 billion from China to help boost forex reserves. Saudi Arabia had also deposited US$ 3.0 billion to bolster the country's forex reserves to address the ongoing pressure on the balance of payments.

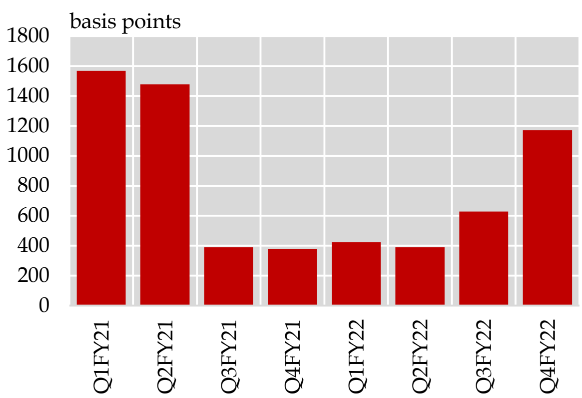
As of June 2022, total inflows into the Roshan Digital Account amounted to US$ 4.6 billion from its inception in September 2020. Of the total, around 65 percent went into NPC's:

Average CDS Rates for Major EMs FY22 **Figure 6.14a**



Source: Bloomberg

Pakistan CDS Rates **Figure 6.14b**



Source: Bloomberg

Gross Loan Disbursements **Table 6.5**

million US$

	FY21	FY22	Change
Comm. loans	4,721.2	4,863.3	142.1
ADB	1,476.1	1,624.0	147.9
Bonds	2,500.0	2,000.0	-500
World Bank*	2,035.5	1,527.1	-508.4
IDB**	623.9	1,406.8	782.9
AIIB	252.1	40.4	-211.7
Bilateral	1,258.9	597.4	2,338.5
Saudi Deposits	-	3,000.0	3,000.0
Others	1,164.7	1,675.5	510.8

*IDA+IBRD; **including short-term

Source: Economic Affairs Division

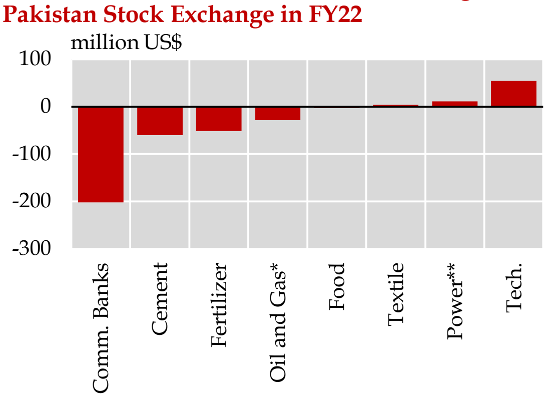
US$1.6 billion into conventional NPC's and US$ 1.4 billion into Islamic NPC's. On the other hand, a small amount of US$ 40 million went into the stock exchange through RDAs. In FY22, US$ 3.0 billion were received in the RDA, out of which US$ 970 million was invested into conventional NPCs, US$ 967 million into Islamic NPCs, and US$ 24 million went into the stock exchange (**Figure 6.16**).

6.3 Exchange Rate and Reserves

Strong pressures on the country's external account took its toll as the country's liquid FX reserves fell by US$ 8.9 billion during FY22. In particular, a wide expansion in CAD, significant external debt repayment pressures, sluggish FDI, net outflows from equity securities and delay in resumption of IMF program contributed to US$ 7.5 billion reduction in SBP's liquid FX reserves, which dropped to US$ 9.8 billion, by the end of FY22. The inflows of external debt & liabilities remained strong, but these were not sufficient to meet financing requirements (**Figure 6.17**). Commercial bank's reserves, on the other hand, dipped by US$ 1.4 billion in this period as banks extended trade financing, and also witnessed outflows from FE-25 deposits.[38]

After a brief respite in Q1-FY22, the SBP's liquid FX reserves saw an almost consistent downward slide since Q2-FY22. The availability of US$ 2.8 billion under the IMF's additional SDR allocation and issuance of a US$1.0 billion Eurobond shored up the level of SBP liquid forex reserves during the first quarter. The country received US$ 3.0 billion deposits from Saudi Arabia in Q2 as well.

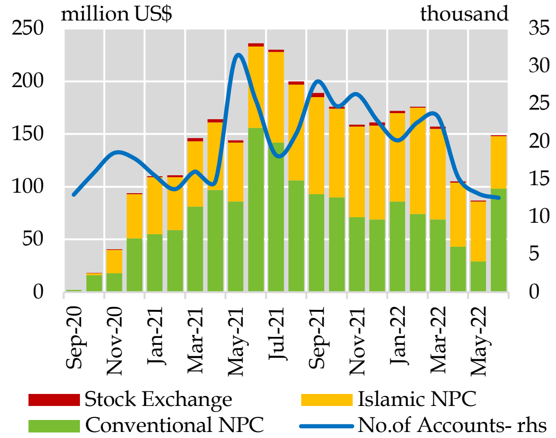
Net Foreign Buying/Selling in Pakistan Stock Exchange in FY22 **Figure 6.15**



*marketing and exploration; **generation and distribution

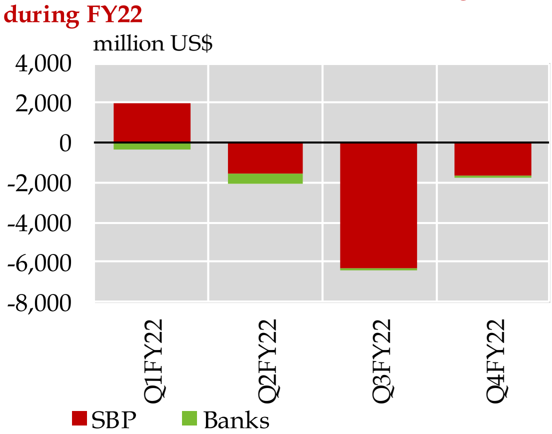
Source: National Clearing Company of Pakistan Limited

Roshan Digital Account Inflows **Figure 6.16**



Source: State Bank of Pakistan

Changes in Liquid FX Reserves during FY22 **Figure 6.17**



Source: State Bank of Pakistan

[38] During FY22, net trade financing extended by banks increased by US$ 695 million, whereas FE-25 deposits dropped by US$ 655 million. In contrast, in FY21, banks extended US$ 9.0 million in net trade financing while its deposits increased by US$ 318 million. Banks' liquid FX reserves are calculated as FE-25 deposits net of trade financing.

However, the available external financing proved insufficient to cover the sizeable debt and liability payments due in this period.

In Q3, despite a moderation in CAD relative to the sharp increase in Q2, and the receipt of US$ 1.0 billion from a *Sukuk* issuance (in January 2022) and another US$ 1 billion from the IMF (in February 2022 after the successful completion of the 6th EFF review), SBP's FX reserves dropped by US$ 6.3 billion to US$ 11.4 billion by end-March 2022. This was mainly because of the gross official loan and liability retirements reaching US$ 3.7 billion during the quarter. Specifically, SBP reserves dropped by around US$ 2.9 billion in the last week of March 2022, due to the repayment of a commercial loan. In Q4, while a steep increase in global commodity prices amid Russia-Ukraine conflict kept CAD at an elevated level, some of the pressure was alleviated in June, when the country received US$ 2.3 billion in commercial loan from China.

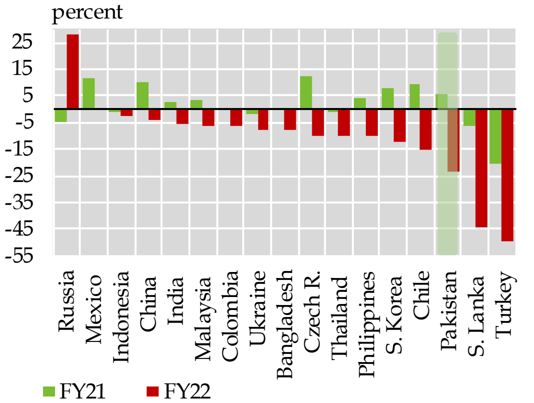
Reflecting these external account developments along with the appreciation of USD index[39], the PKR depreciated by 23.1 percent YoY *vis-a-vis* the US dollar in FY22 in contrast to 6.7 percent appreciation witnessed in FY21 (**Figure 6.18**). It is worth noting that currencies of many other EMEs, especially commodity-importing ones, also depreciated during the period, amidst stressed trade balances as well as the US Dollar's broad-based strengthening against other currencies **(Figure 6.18)**. In the case of Pakistan, the situation was further exacerbated by uncertainty surrounding resumption of the IMF program and domestic political uncertainty. Hence, the PKR depreciated by a sharp 10.4 percent during March-June 2022.

In real terms, Pakistan was among those EMs where the depreciation in the nominal effective exchange rate (NEER) more than offset the rise in the relative price index (RPI) (**Figure 6.19).** Since the currencies of Pakistan's competitors also depreciated significantly during this period, nominal effective exchange rate (NEER) of PKR depreciated by only 10 percent in FY22. Also, with rising inflation in these competitor countries, Pakistan's relative price index (RPI) increased by merely 0.7 percent during the year, allowing real effective exchange rate (REER) to depreciate moderately by 9.3 percent during FY22.

6.4 Trade Account[40]

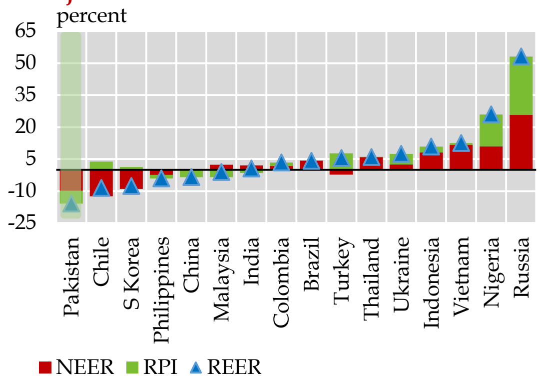
Pakistan's trade deficit worsened in FY22, as it grew by 55.6 percent to US$ 48.4 billion, compared to US$ 31.1 billion last year (**Figure 6.20**). This was despite a notable 25.6 percent

EME's Exchange rate Movements in FY22 **Figure 6.18**



Source: Haver Analytics

Breakdown of Change in REERs of Major EMs in FY22* **Figure 6.19**

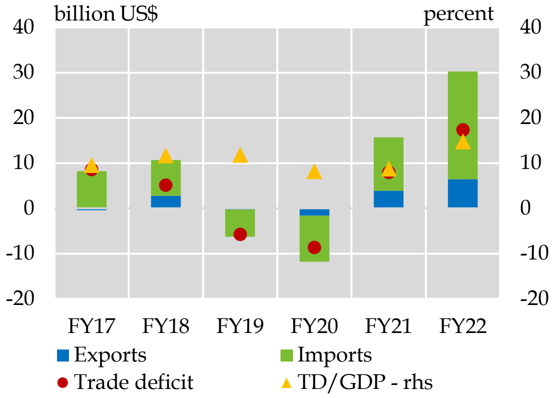


*JP Morgan Effective Exchange Rate
Source: Haver Analytics

[39] US dollar index increased by 13.2 percent during Jul-Jun Y22.

[40] This section is based on customs data reported by the PBS. The information in this section does not tally with the payments record data, which is reported in **Section 5.1**. To understand the difference between these two data series, see Annexure on data explanatory notes.

Breakdown of YoY Change in Trade Deficit **Figure 6.20**



Source: Pakistan Bureau of Statistics

expansion in exports during the year only to be outpaced by a strong 42.1 percent increase in imports. The upsurge in global commodity prices had a significant effect on Pakistan's trade account. The outbreak of Russia-Ukraine conflict further spurred the uptrend in prices of both energy and non-energy commodities, widening the trade deficit of many emerging energy importing economies in FY22 (**Figure 6.21**).[41]

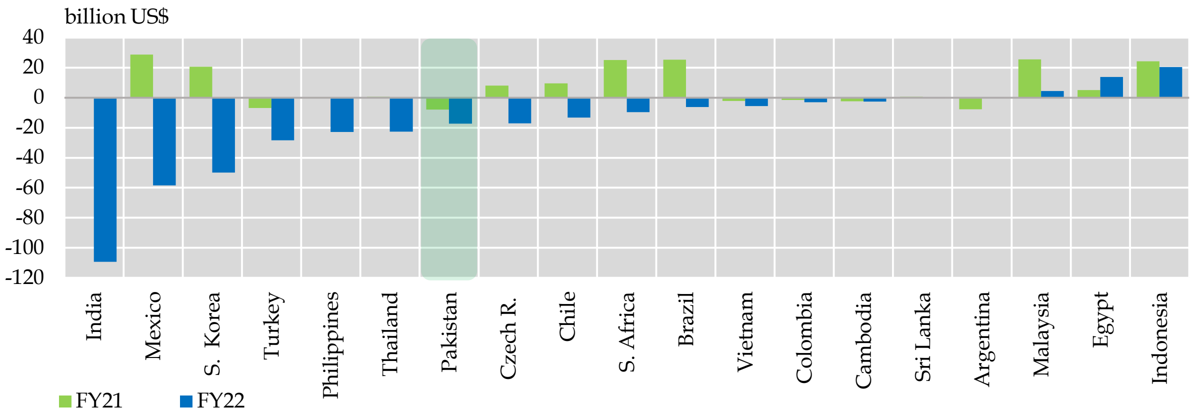
In addition to the spike in import prices, the need to import Covid vaccine, surge in the demand for energy products, machinery, some metals, and transports further augmented the increase in imports. Exports also benefited from the rising global prices, particularly cotton; whereas, volumes also remained strong. In terms of GDP, the trade deficit rose to 14.8 percent of GDP, which is slightly higher than the average level observed during pre-Covid years between FY17-19. This deterioration mainly reflect the impact of commodity price shock during the year.

The large increase in imports intensified pressures on the country's external account, as seen from 10.7 percent depreciation of the PKR during H1-FY22. In the face of rising vulnerabilities, the government and the SBP introduced various demand management measures during the year to contain domestic demand, which succeeded in winding down the pace of expansion in non-energy imports during H2-FY22.[42] However, with the eruption of Russia-Ukraine crisis, commodity prices reached at historic levels in Q3-FY22 that led to a sharp increase in imports, and hence trade deficit during H2-FY22.

Exports

Pakistan's merchandize exports (Customs record) gained further traction during FY22, with 25.6 percent YoY increase reaching US$ 31.8 billion. This was the first time the country's exports crossed US$ 30 billion mark. The increase in exports was broad-based, with a notable share of textile exports (**Figure 6.22**). The sector mainly benefited from elevated

Changes in Trade Balance in Peer Emerging Market Economies in FY22 **Figure 6.21**

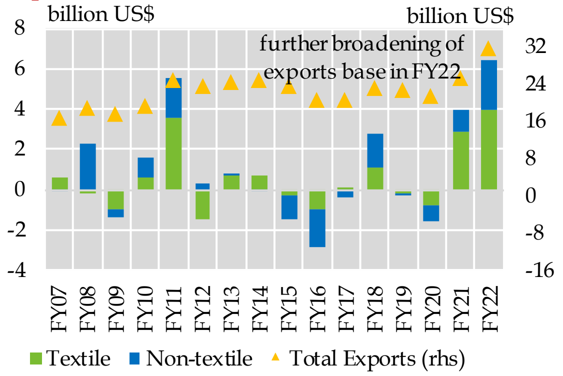


Source: Haver Analytics

[41] Egypt, Indonesia, and Malaysia are three countries showing positive change in the trade deficit in FY22. Trade deficit improved in the case of Egypt from US$ 39.8 billion in FY21 to US$ 26.1 billion in FY22. Both Indonesia and Malaysia are leading exporters of palm oil, price of which witnessed a record increase in FY22.

[42] The growth in non-energy imports slowed to 4.3 percent YoY in H2-FY22, compared to 55.1 percent during H1-FY22.

Pakistan's Merchandize Exports and YoY Change in Textile and Non-Textile Exports **Figure 6.22**



Source: Pakistan Bureau of Statistics

prices of cotton in the international market, as higher unit values constituted around three-quarters share in the entire increase of major textile exports during the year. In addition, policy support in the shape of competitive energy prices, subsidized lending through refinance schemes, particularly Temporary Economic Refinance Facility (TERF), tariff rationalization of key textile imports, and higher sales tax and customs duty refunds on YoY basis provided a further boost to textile exports.

In the case of non-textiles, rising volumes mainly drove the increase, and contributed around one-tenth in the total increase in exports during the year. The increased production of some agriculture commodities, availability of duty-free access under the China Pakistan Free Trade Agreement (CPFTA) Phase II and increased demand in the international market were mainly responsible for this increase.

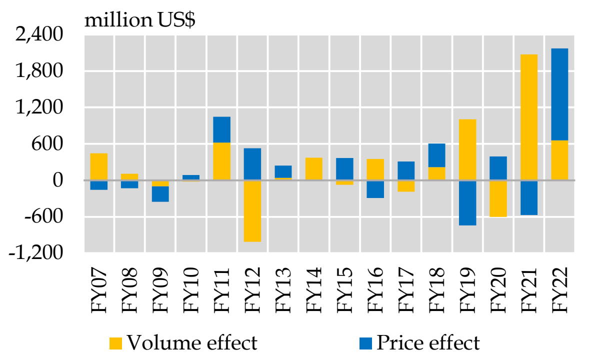
Price upturns led growth in textile exports, with higher volumes complementing

Textile exports continued the growth momentum of the last year and posted 25.5 percent increase, reaching US$ 19.3 billion in FY22, against 22.9 percent increase last year. The country's share in global exports of apparel and textile made-ups (including bed wear and towels) increased by 0.4 percentage points YoY to 2.2 percent in 2021, after staying near-stagnant in the last four years.[43] Rising international prices of cotton had a significant positive impact on the textile export performance during the year, whereas a positive volume effect further reinforced the uptrend in exports (**Figures 6.23a & 6.23b).** Major export products included: apparel (knitwear and readymade garments), home textiles (bed wear and towels), cotton fabrics and cotton yarn (**Table 6.6**).

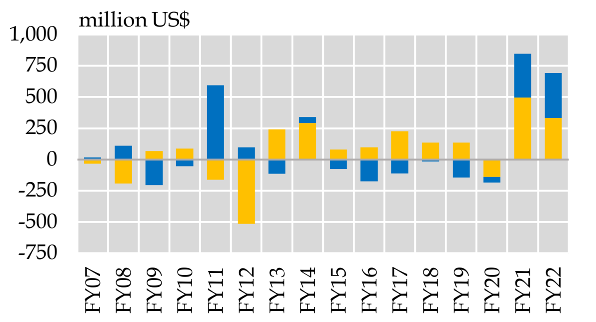
Price effect

International prices of cotton started spiraling up in 2021, amid widening supply-demand gap (**Figure 6.24)**. The domestic prices of cotton also edged up during the year, which inflated the cost of production, and factored into the price of cotton-based products; the

Breakdown of YoY Change in Apparel Exports **Figure 6.23a**



Breakdown of YoY Change in Home Textile Exports **Figure 6.23b**



Note: Sum of volume effect & price effect equals YoY change for a given year
Source: Pakistan Bureau of Statistics

[43] Data source: International Trade Centre. Note: Aggregated, global product-wise data is available for the full calendar year only, hence latest available data is 2021.

Pakistan's Textile Sector Exports — **Table 6.6**

million US$

	FY21	FY22	Change	Volume Effect	Price Effect
Apparel	6,848	9,026	2,178	413	1,765
Home textiles	3,709	4,404	695	327	368
Cotton fabrics	1,921	2,438	517	56	460
Cotton yarn	1,017	1,207	190	-138	328
Synthetic textiles	370	460	90	-151	241
Non-cotton yarn	33	66	33	16	16
Non-home textiles made-ups	756	849	93	-	-
Other textile material	632	761	129	-	-
Overall textile exports	**15,399**	**19,330**	**3,931**	-	-
Total exports	**25,304**	**31,782**	**6,478**	-	-

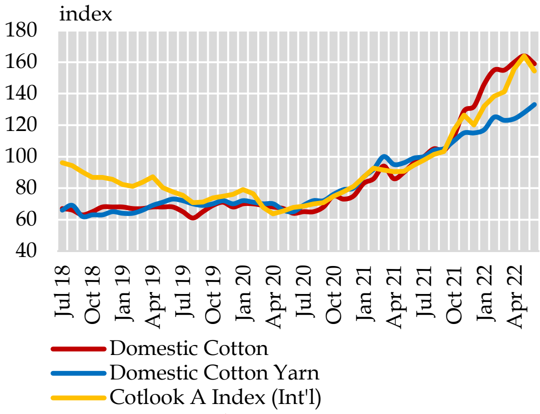
Source: Pakistan Bureau of Statistics

gains from the rising export unit values, exchange rate depreciation and various policy support measures aided the industry to benefit from the expansion in global demand.

Monthly international cotton prices rose by 56 percent YoY on average during FY22. This mainly reflected the widening supply-demand gap, which was aggravated by the supply chain disruptions. Supplies were further constrained by the logistical issues owing to the port congestions around the world, container shortages and delays in sea freight departures and arrivals.[44] These issues also supported commodity prices, as freight costs rose exponentially in 2021-22.

In addition, increase in cotton demand from China further inflated the global cotton prices during the year. China is one of the countries witnessing strong international demand for its value added textiles, besides Vietnam, Bangladesh, Pakistan, and Turkey. However, in December 2020, the US imposed a ban on textile product imports made from cotton produced in Xinjiang province of China[45], which is a large producer of cotton with around 90 percent share in China's total cotton production. Hence, the Chinese textile industry shifted its demand for cotton and cotton intermediaries to the international market that stoked global supply pressures.[46,47] China's effort to replenish its cotton reserves to increase share of imported cotton further boosted global demand.[48]

Domestic and International Prices of Key Textile Inputs — **Figure 6.24**



Source: Emerging Textiles

---

44 A Textiles Intelligence report noted that, "Finished goods have been taking longer to reach their destinations as shortages of containers and outbreaks of Covid-19 have halted operations and caused delays at ports. In fact, in many destination ports, the average median times spent by containers in depots, referred to as dwell times, reached near-record levels in 2021 as a result of severe congestion." Source: Talking Strategy: Apparel Supply Chains Hit by Perfect Storm as Costs Rise on Multiple Fronts, January 2022. Textiles Intelligence. United Kingdom.

45 Source: US Customs and Border Protection press release dated December 2, 2020; Available at: www.cbp.gov/newsroom/national-media-release/cbp-issues-detention-order-cotton-products-made-xinjiang-production

46 Source: Talking Strategy: Apparel Supply Chains Hit by Perfect Storm as Costs Rise on Multiple Fronts. January 2022. Textiles Intelligence. United Kingdom.

47 China's cotton imports—mainly fiber and yarn—were recorded at US$ 10.6 billion in 2021, 16 percent above 2018-20 average. Source: China Customs Statistics

48 Source: World Cotton Markets and Trade. December 2021. United States Department of Agriculture. United States

Imports of the US, EU-27 and UK from Major Origins and Breakdown of YoY Change in FY22 **Table 6.7**

million US$

	US				EU-27				UK			
	FY21	FY22	VE	PE	FY21	FY22	VE	PE	FY21	FY22	VE	PE
Pakistan	1,787	2,701	415	500	2,727	3,551	708	116	853	940	11	75
Bangladesh	5,890	9,034	2,451	693	15,251	20,448	3,558	1,639	2,772	3,508	441	295
Cambodia	2,996	4,135	459	680	2,731	3,303	457	116	674	651	25	-49
China	16,699	22,547	3,851	1,997	24,370	27,824	1,281	2,173	5,756	4,647	-109	-1,000
India	3,516	5,360	1,253	590	3,814	4,603	627	162	1,014	1,275	155	107
Turkey	669	1,008	256	83	10,535	11,938	1,377	26	1,840	1,868	-93	121
Vietnam	13,725	16,756	1,706	1,325	3,430	3,768	109	229	459	509	7	44
World	**71,565**	**95,791**	**15,564**	**8,661**	**83,138**	**94,903**	**9,042**	**2,723**	**16,360**	**16,253**	**681**	**-788**

Note:1) VE stands for Volume Effect and PE for Price Effect;

2) In case of the UK, PE of 'World' minus 'China' is positive

Sources: Office of Textile & Apparel (US); Eurostat (EU-27); UK Trade Info (UK)

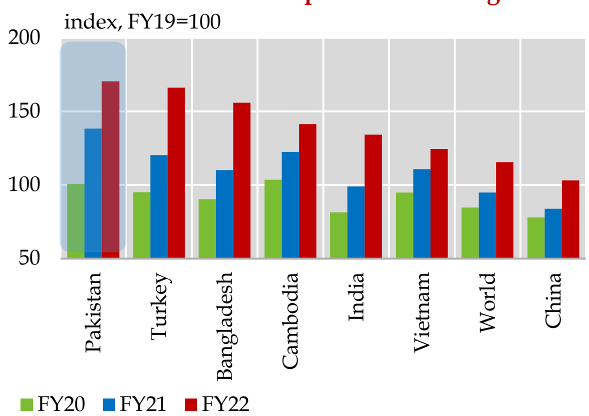
Table 6.7 shows that Pakistan, along with the other major exporters of textile and made-ups, passed on the impact of elevated cotton prices to final products, as reflected in notable price effects across the major import markets of the US, EU-27, and the UK. It is worth mentioning here that this trend was also true for the overall apparel imports of the US and EU-27; in case of the UK, barring China, the cumulative price effect was positive.

Volume effect

The volume of Pakistan's textile exports, particularly apparel and home textiles reached the highest level for the second consecutive year. Both demand and supply side factors drove the growth momentum of the textile sector. On the demand side, there were higher orders from the traditional buyer countries or blocs—the US, EU-27 and the UK (**Table 6.7, Figures 6.25a, 6.25b & 6.25c**). Starting in FY21, Pakistan received deflected orders from the supplier countries mired in the pandemic-led economic disruptions.[49] That trend not only carried on into FY22, but also strengthened further due to increased appetite for cotton-based products in the buyer countries.

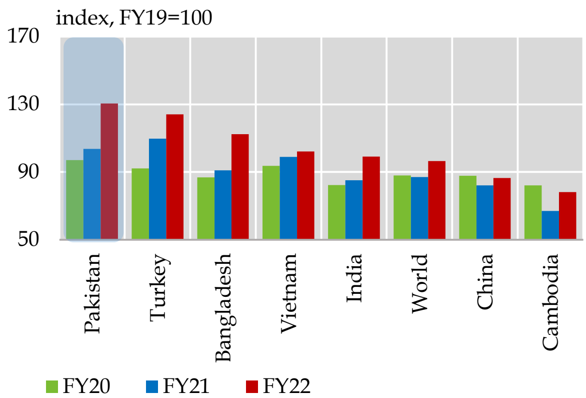
A United States Department of Agriculture (USDA) report noted that demand for cotton products in the US in 2021 was the highest since 2010. With the persisting trend of people working from home, consumers' choice for soft-knitted and comfortable clothes remained strong during FY22. In addition to that, strong U.S. home purchases and improvements

Volume Index of the US' Imports **Figure 6.25a**



Source: Office of Textile & Apparel (US)

Volume Index of the EU-27's Imports **Figure 6.25b**



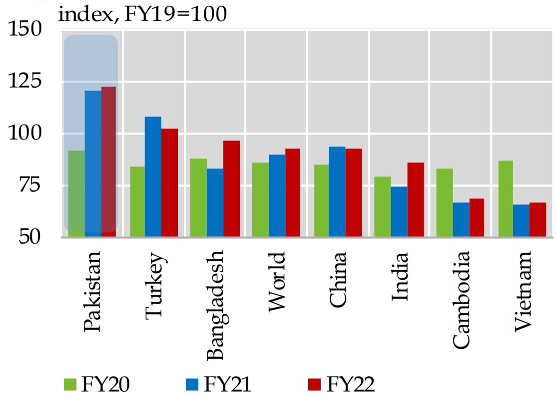
Source: Eurostat (EU-27)

[49] For details, see Chapter 6 – External in the State of the Economy's Report FY21.

prompted new home textiles purchases. Moreover, release of pent-up demand from 2020 and an increase in discretionary incomes also lifted imports; as, in 2020, the U.S. cotton product imports had reduced to the lowest level in almost 20 years.[50]

On the supply side, textile industry enjoyed policy support that enabled optimal capacity utilization and expansion. Some of the support measures are discussed in the following: **a)** tariff rationalization on imports of textile inputs, like cotton yarn, artificial staple fibers, synthetic yarn, knitted fabric, and polyester yarn, announced in the budget of FY22 [51]; **b)** provision of subsidy on energy tariffs—power at US 9 cents per KWh, and gas at US$ 6.5 per MMBtu [52]; **c)** higher sales tax and customs duty refunds [53]; **d)** subsidized lending under TERF and LTFF schemes. Net fixed investment (LTFF and TERF) by the textile and apparel industry was Rs 131 billion, which was Rs 49 billion higher than last year.

Volume Index of the UK's Imports **Figure 6.25c**



Source: UK Trade Info (UK)

Disbursement under TERF and ongoing LTFF, underpinned capacity addition in the textile sector, particularly the upstream segments (cotton spinning, weaving and finishing). This can be seen from a sharp increase in textile machinery imports during FY22 that was 42.6 percent higher YoY in FY22.[54] Textile machinery import has increased sharply since the introduction of TERF in March 2020 (**Figure 6.26**).[55]

Besides apparel and home textiles, cotton fabrics registered growth of 26.8 percent to US$ 2.4 billion in FY22, and cotton yarn exports grew by 18.6 percent to US$ 1.2 billion. Growth in these products came mainly on the back of high-trending cotton prices. As domestic demand for both intermediary products was quite robust, growth in their volumes was either negative (yarn) or muted (fabric).

Non-textile exports help broaden the exports base

Non-textile exports posted growth of 25.7 percent to US$ 12.5 billion in FY22. Importantly, rising volumes had a pronounced share in the non-textile export increase during the year. Major items included agro-food products—rice, sesame seeds, and maize (corn); refined copper; petroleum crude (condensate); ethyl alcohol; leather garments and gloves (**Table 6.8**).

Agro-food exports

Exports of the agro-food sector—second largest after the textile sector—grew by US$ 1.0 billion to US$ 5.4 billion in FY22. The

[50] Source: World Cotton Markets and Trade. March 2022. United States Department of Agriculture. United States
[51] There were some items, mainly raw cotton, whose tariffs had been already rationalized in FY21. This had been done to facilitate the import of key textiles for the value addition. Available at: www.commerce.gov.pk/decisions-of-tariff-policy-board-tbp-implemented-under-finance-act-2021-22/
[52] Gas tariff subsidy was revised in November-2021 from US$ 6.5 to US$ 9.0 per MMBtu for the province of Punjab; this revision was made for the gas being used by the industry in its captive power plants for power generation. For general industrial use, the subsidy rate stayed unchanged at US$ 6.5 per MMBtu.
[53] These refunds totaled Rs 317 billion in FY22, Rs 84.2 billion more than last year. Source: Federal Board of Revenue
[54] Compared to the FY17-FY21 average, textile machinery imports were up 89 percent in FY22.
[55] TERF is a concessionary refinance facility aimed at promoting investment—both new and expansion—and/or Balancing, Modernization and Replacement (BMR). It had expired in March-2021. However, disbursements under it continued beyond March-21. Source: State Bank of Pakistan. It may be noted that impact of fixed investments, as under TERF/LTFF, on a firm's output comes with a lag. So, such investments made in the last two years had a cumulative impact on textile industry's output.

Major Non-textile Exports **Table 6.8**

million US$

	FY21	FY22	Change
Rice	2,041.7	2,512.8	471.1
Basmati rice	*569.5*	*694.5*	*125.0*
Non-basmati rice	*1,472.2*	*1,818*	*346.0*
Refined copper	422.7	733.7	311.0
Sesame seeds	88.3	183.9	95.6
Chemicals	556.1	871.6	315.5
Ethyl alcohol	*302.7*	*544.9*	*242.2*
Maize (corn)	18.6	239.4	220.8
Petro crude	106.8	259.0	152.2
Leather products	562.4	621.1	58.7
Garments	*286.2*	*315.2*	*29.0*
Gloves	*259.7*	*287.2*	*27.5*
Fruits	480.1	477.4	-2.7
Kinnow, fresh	*130.6*	*99.4*	*-31.2*
Mandarin	*59.9*	*25.7*	*-34.1*
Pine nuts (chilgoza)	*15.3*	*107.6*	*92.4*
Mangoes	*141.2*	*136.7*	*-4.5*
Non-textile, total	**9,905.1**	**12,452.3**	**2,547.2**

Source: Pakistan Bureau of Statistics

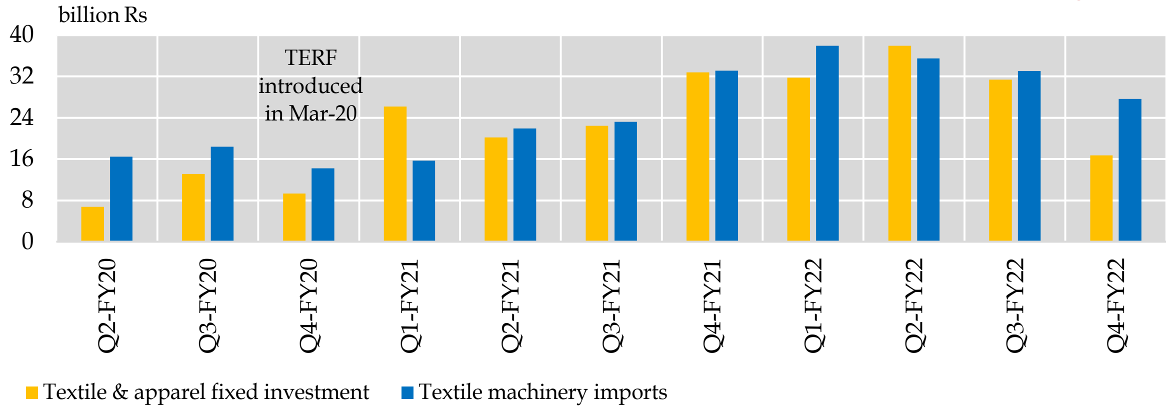
improved production of major agro-food exports in FY22, including rice, sesame seeds, and maize (corn), along with rising demand, shored up the growth in non-textiles during the year.

Rice

Rice exports registered growth of 23.1 percent to US$ 2.5 billion in FY22, after staying stagnant last year. It was the volume-led growth as average export unit values were lower than last year. Importantly, rice production rose to a record high of 9.3 million tons in FY22 —up 0.9 million tons YoY, which had increased the exportable surplus. On the other hand, rice export prices remained in check as average export unit value fell by 8.9 percent during the year. With bumper crop and competitive prices, Pakistan was able to ship 35 percent more grains than last year, resulting in higher shipments supplanting the negative price effect.

Non-basmati rice had a greater share in overall increase, with higher demand from Malaysia and China.[56] A USDA report noted price competitiveness as the primary factor of surging demand from Malaysia; unit value of Malaysia's import from Pakistan declined from US$ 500 per ton in 2020 to US$ 455 per ton in 2021 (**Figure 6.27**).[57,58] The report further noted that Pakistan replaced Vietnam

Textile Machinery Imports and Fixed Investment **Figure 6.26**



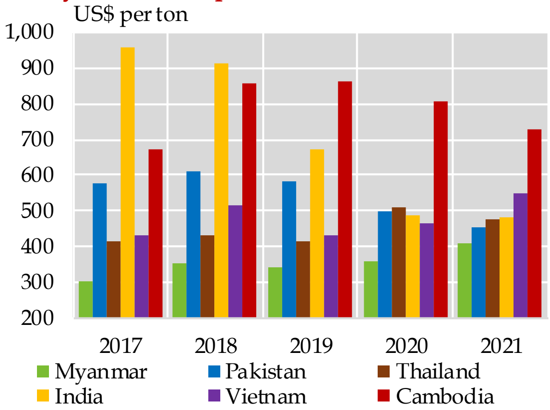
Note: Fixed investment includes LTFF & TERF; values represent outstanding loans at the end of each quarter
Sources: State Bank of Pakistan & Pakistan Bureau of Statistics

56 Share of Malaysia in Pakistan's export volumes of non-basmati varieties rose from 4.4 percent in FY21 to 10.2 percent in FY22. During the same time periods, China's share in the country's broken rice exports increased from 48.1 percent to 66.5 percent.

57 Grain and Feed Annual. Malaysia. April 12, 2022. Foreign Agriculture Service. United States Department of Agriculture. Available at: www.apps.fas.usda.gov/newgainapi/api/Report/DownloadReportByFileName?fileName=Grain%20and%20Feed%20Annual_Kuala%20Lumpur_Malaysia_MY2022-0001.pdf

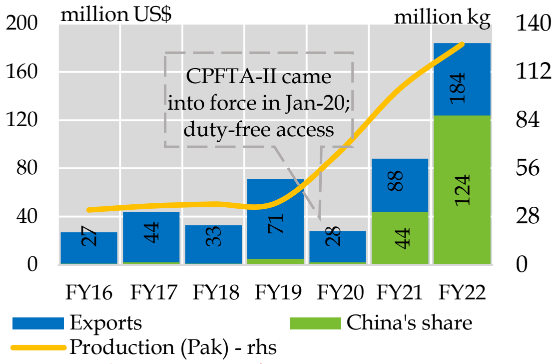
58 It may be noted here that Myanmar (Burma) offered lower prices than Pakistan in 2021. However, its exportable surplus was low due to a fall in milled rice production in 2021-22 amidst constant consumption. (Data source: USDA)

Unit Values Comparison of Malaysia's Rice Imports **Figure 6.27**



Source: Trade Data Monitor via USDA

Pakistan's Sesame Seeds Production, Exports and China's Share **Figure 6.28**



Source: Pakistan Bureau of Statistics & Economic Survey of Pakistan 2021-22

as the second largest rice exporter to Malaysia in 2021.

In the case of China, broken rice was in greater demand. It was primarily due to high corn prices in China that pushed substitution of corn used as feedstock with broken rice. Higher rice prices in China, amid the increase in its Minimum Support Price (MSP) in 2022 for the third consecutive year, also led to diversion of demand to imported rice. Lastly, China had registered seven more rice traders from Pakistan.[59]

Basmati rice exports rose by 22 percent to US$ 694.5 million in FY22, recovering strongly from last year's fall. Shipments to the UAE were significantly up.[60] Share of the UAE in Pakistan's basmati rice shipments jumped from 11.9 percent in FY21 to 22.2 percent in FY22.

Sesame seeds

Sesame seeds saw a significant growth of 108 percent to US$ 183.9 million in FY22. Pakistan's sesame seeds production has increased exponentially in the last few years (**Figure 6.28**).[61] Anecdotes suggest that farmers are increasingly interested in the seeds cultivation, as they offer high export unit values.[62]

On the demand side, almost the entire increase came from higher shipments to China. Under the CPFTA Phase II, Pakistan's sesame seeds were among the products that got duty-free access to China—a market with a strong demand for the seed's oil and other uses in food.[63]

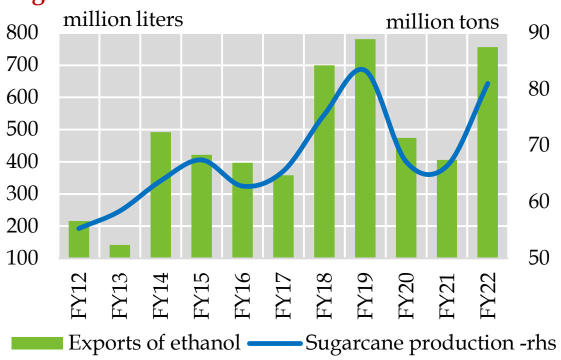
Maize

Maize (corn) exports increased from US$ 18.6 million in FY21 to US$ 239.4 million in FY22, with volumes rising significantly to 755.2 thousand tons in FY22 from 84.5 thousand tons. Major destinations included Vietnam and Malaysia. Corn is often used as a feedstock. Vietnam, where Pakistan shipped US$ 139.7 million worth of corn in FY22 against US$ 11.9 million last year, has been substituting its own production with imports for last many years.[64]

---

[59] Source: Grains: World Market and Trade. Various issues. United States Department of Agriculture. US.
[60] The anecdotal evidence suggests that in the absence of formal financial linkage with Iran, Pakistan's basmati rice is transshipped to Iran through the UAE.
[61] Sesame seeds production increased from 102 million kg in FY21 to 128 million kg in FY22 (p); it was 36 million kg in FY18. Source: Economic Survey of Pakistan 2021-22
[62] Moreover, yield of sesame seeds in Punjab is also on the increasing trend in recent years; it increased 1.5 times between FY16 and FY21. Source: Crop Reporting Services, The Government of Punjab
[63] China's total imports of sesame seeds (not for cultivation) rose from 1.0 billion kg in 2020 to 1.2 billion kg in 2021; they stood at 828 million kg in 2018. Source: China Customs Statistics
[64] Source: www.fas.usda.gov/data/vietnam-feed-importing-powerhouse#:~:text=Vietnam%20has%20turned%20to%20imports,importer%20globally%20in%202021%2F22

Pakistan's Exports of Ethanol and Sugarcane Production **Figure 6.29**



Sugarcane production data is plotted with lag of one year.
Source: Pakistan Bureau of Statistics and Pakistan Economic Survey 2021-22

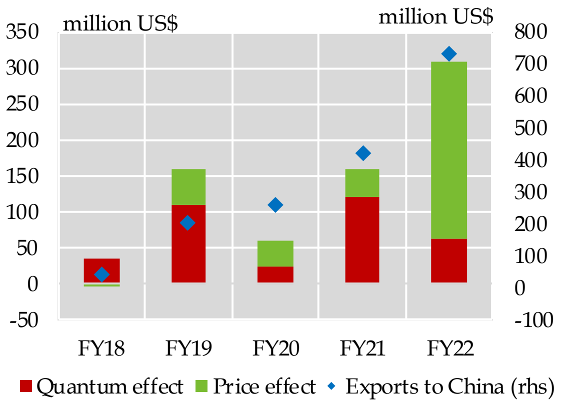
In FY22, Vietnam partly substituted costlier wheat imports from the US with corn imports to use in feedstock.[65] Moreover, ample supplies from Pakistan were available to fulfil the international demand.[66]

Other non-textile exports

Ethanol (ethyl alcohol)

Exports of ethanol increased by 80 percent to US$ 544.9 million in FY22. It was all volume-led increase, with China and European countries—mainly the Netherlands, Italy and Spain—posting highest YoY increases. Ethanol, often used as a biofuel, is produced mainly from sugarcane fermentation in Pakistan. Exports of ethanol are linked to production of sugarcane in the preceding year (**Figure 6.29**). In FY21, sugarcane production was up 22 percent that boosted its exports in FY22.

Breakdown of Pakistan's Copper Exports to China **Figure 6.30**



Source: PBS, World Bank & SBP calculations

Refined copper

Refined copper exports almost doubled from US$ 422.7 million in FY21 to US$ 733.7 million in FY22. The entire increase can be traced to China. Pakistan is enjoying duty-free access to Chinese market under the CPFTA Phase II since January 2020. Inflated international copper prices also significantly supported Pakistan's copper exports during the year (**Figure 6.30**), as export unit values increased 51.1 percent YoY in FY22.

Petroleum crude

Petroleum crude (condensate) exports increased by US$ 152.2 million to US$ 259 million. Both volume and price effects were positive, with the latter having a more dominant contribution because of soaring international crude prices. Volume effect is partly due to the low base effect last year. Moreover, Thailand's demand for imported crude and condensate rose as economic activity increased post-lockdowns.[67]

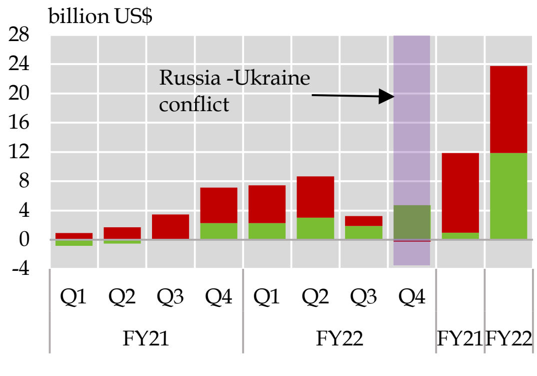
Fruits

Fruit exports stagnated at the last year's level during FY22. The volume of fruit exports dipped as there was a significant YoY drop of 51.5 percent in volume of the country's largest fruit export category, i.e. kinnow, in FY22. The decline in exports to Afghanistan owing to slowing down of mutual trade in the aftermath of political changes mainly explains this decline. It offset the increase in shipments of pine nuts that increased six times YoY in FY22.

---

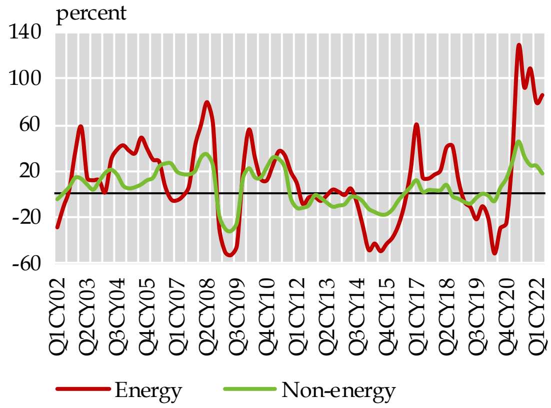
[65] Source: www.agflow.com/agricultural-markets/vietnam-corn-imports-rise-while-wheat-tumbles/
[66] Maize (corn) production was estimated to be up 19 percent in FY22 (p), reaching record high of 10.6 million kg. Source: Economic Survey of Pakistan 2021-22
[67] Source: www.spglobal.com/commodityinsights/en/market-insights/latest-news/oil/050522-thailand-ramps-up-crude-imports-to-feed-high-refinery-runs-amid-tourism-revival

YoY Changes in Total, Energy and Non-energy Imports **Figure 6.31**



Source: Pakistan Bureau of Statistics

Growth in Quarterly Global Commodity Price indices **Figure 6.32**



Source: World Bank

Imports

Pakistan's imports increased by 42.1 percent YoY in FY22, reaching US$ 80.1 billion, compared to US$ 56.4 billion in FY21. Soaring global commodity prices had a dominant contribution in this increase. In particular, rising prices of petroleum crude and products alone contributed around one-half of the entire increase in imports during the year. In addition, the need to import Covid vaccine and the expansion in domestic economic activity also pushed up import volumes of some capital goods and raw materials.

Specifically, first two quarters of FY22 saw continued momentum of both energy and non-energy imports (**Figure 6.31**). To contain import demand, SBP introduced various policy measures.[68] These measures along with the reduction in import of Covid vaccine arrested the growth momentum in imports, which posted MoM declines during January and February 2022.

However, the outbreak of Russia-Ukraine conflict provided new impetus to the global commodity market; both energy and non-energy products prices reached multi decade high in Q3-FY22 (**Figure 6.32 & 6.33**). This reinvigorated the otherwise slowing imports, thereby pushing the YoY quarterly growth to 21.7 percent, to US$ 18.3 billion, in Q3-FY22.[69] In tandem, energy imports started dominating the import growth from Q3-FY22 onward.[70]

Amidst the mounting pressure of energy imports, political instability in the country, and uncertainty around the IMF program, PKR remained under pressure, which depreciated by 10.4 percent in Q4-FY22. Consequently, SBP introduced additional demand management measures such as, adding 177 more items in the list of products attracting CMR on imports[71], and raising policy rate gradually.[72] Furthermore, the Government also imposed ban on imports of certain non-essential items in May 2022. As a result, Q4-FY22 witnessed YoY decline in non-energy imports, albeit marginally by 2.4 percent. However, a steep 123.7 percent YoY

---

[68] These include, restricting consumer financing by amending the relevant prudential regulations (www.sbp.org.pk/bprd/2021/CL29.htm), expanding list of items attracting CMR on imports (www.sbp.org.pk/bprd/2021/CL30.htm), increasing the cash reserve requirements (CRR) for banks by 100 bps (www.sbp.org.pk/dmmd/2021/C20.htm), and raising the policy rate by 275 bps.

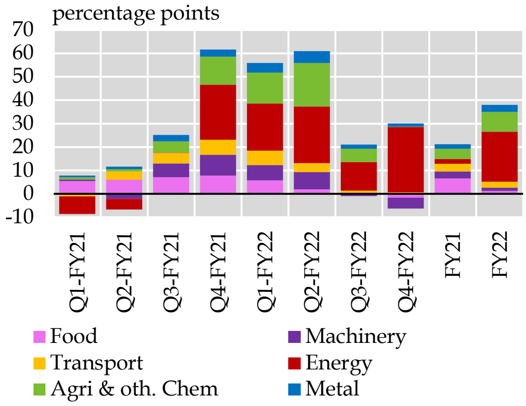
[69] In March 2022, imports increased by 9.5 percent on MoM basis. Nevertheless, energy imports declined by US$ 1.0 billion while non-energy imports declined by US$ 2.6 billion in Q3-FY22 compared to the previous quarter of FY22.

[70] Energy imports contributed 12 percentage points in 21.3 percent growth in Q3-FY22 imports.

[71] BPRD Circular Letter No. 09 of April 07, 2022 (Available at: www.sbp.org.pk/bprd/2022/CL9.htm)

[72] Policy rate was raised by 400 bps during Q4-FY22.

Sectoral Contribution to Import Growth **Figure 6.33**



Source: Pakistan Bureau of Statistics & SBP calculations

increase in the energy imports driven by Russia-Ukraine conflict propelled the Q4-FY22 imports to US$ 21.3 billion with 26.0 percent YoY increase (**Figure 6.31**).[73]

On aggregate, price effect mostly dominated the imports in FY22, specifically in case of energy products and for some non-energy products such as, palm oil, fertilizer and steel scraps (**Table 6.9)**.[74]

Energy had a pronounced share in FY22 imports

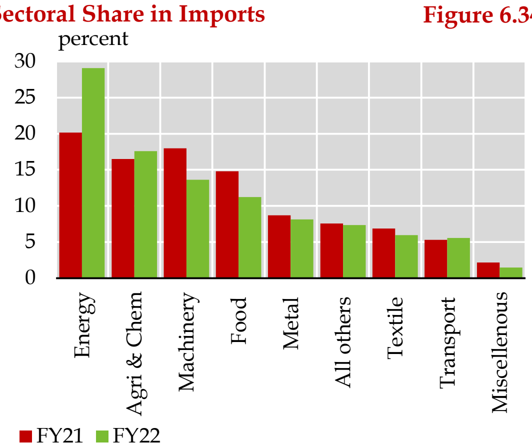
Pakistan's energy import bill more than doubled to US$ 23.3 billion in FY22 from US$ 11.4 billion in FY21.[75] Resultantly, the share of energy in total imports increased to 29 percent in FY22, compared to 20 percent in FY21 (**Figure 6.34**).

Prices of energy products such as, crude oil, natural gas, and coal rose sharply in FY22, specifically in the first half due to factors influencing demand and supply of these products. Most importantly, economic stimulus provided to revive economic activity from Covid shock resulted in stronger than expected recovery in most of the advanced and emerging economies in 2021.[76] However, the supply of energy products remained lackluster as OPEC+ members adhered to their output quota.

On the other hand, Covid led unforeseen repair works and project delays weighed heavily on the gas supply.[77] The situation further aggravated as some of the energy demand was switched to gas due to lower wind power generation in Europe. Moreover, drought like situation that constrained hydropower generation in Brazil and in some surrounding countries also fueled gas demand, which further widened the gas supply-demand gap. During CY21, European natural gas index rose by a record 449.1 percent. On the other hand, coal prices also soared by 1,060.5 percent during CY21, as many countries switched to coal for electricity generation.[78]

Given Pakistan was procuring gas partly from the spot market, the increase in LNG prices disrupted its energy supply chain and

Sectoral Share in Imports **Figure 6.34**



Source: Pakistan Bureau of Statistics

[73] Energy imports contributed 28 percentage points in the overall 26.2 percent growth in Q4-FY22 imports.
[74] Government also imposed ban on imports of certain non-essential items on May 2022 for the two months. (Source: S.R.O. 598(1)/2022, May 19 2022 of Ministry of Commerce).
[75] On aggregate, energy contributed 21.3 percentage points in 42.1 percent growth in the FY22 in overall imports (**Figure 6.37**).
[76] Besides, commodity prices dipped significantly during February 2020 to February 2021 in the wake of Covid shock. This lower base led to a sharp YoY rise in FY22.
[77] For further detail, see The State of Pakistan's Economy, Half Yearly Report of the Board of Directors 2021-22 (Source: State Bank of Pakistan).
[78] South African Coal Index. (Source: World Bank)

Pakistan's Major Imports in FY22 **Table 6.9**

million US$

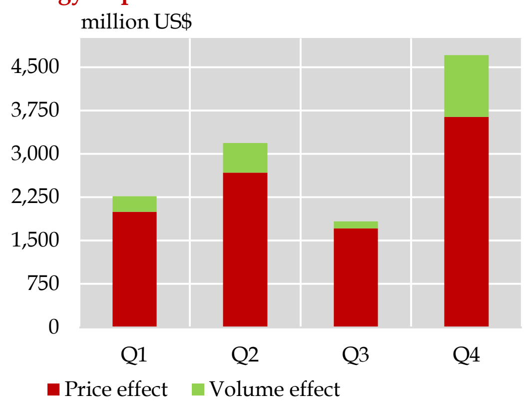
Items	FY21	FY22	Abs. change	Volume Effect	Price effect
Energy group	**11,358**	**23,319**	**11,961**	**1,869**	**10,092**
POL prods.	5,160	12,069	6,909	1,459	5,450
Crude oil	3,107	5,599	2,491	163.55531	2,328
LNG	2,617	4,990	2,373	291.28034	2,081
Agriculture and other chemicals group	**9,300**	**14,086**	**4,786**	**-**	**-**
Fertilizer	719	846	127	-195	322
Plastic Material	2,473	3,136	663	84	579
Medicinal Products	1,390	4,063	2,673	2040	632
Other Chemicals	4,529	5,840	1,311		
Transport group	**2,987**	**4,454**	**1,466**	**-**	**-**
Cars	1,247	2,007	760	-	-
CBUs	127	336	209	-	-
CKDs	1,120	1,671	551	-	-
Truck & buses	515	989	474	-	-
Aircraft & ships	514	761	248	-	-
Metals group	**4,897**	**6,524**	**1,627**	**-**	**-**
Steel scrap	1,858	2,305	448	-350	798
Iron & steel	1,960	2,937	977	309	668
Food group	**8,348**	**9,016**	**668**	**-**	**-**
Wheat	983	795	-188	-383	195
Sugar	129	192	63	14	49
Palm oil	2,669	3,549	881	-330	1211
Textile group	**3,866**	**4,787**	**921**	**-**	**-**
Raw cotton	1,480	1,828	349	-140	489
Syn. yarn	656	879	223	-50	273
Machinery group	**10,147**	**10,920**	**774**	**-**	**-**
Power gen	1,912	1,473	-439	-	-
Electrical	1,664	1,929	265	-	-
Cell phones	2,065	1,979	-87	-	-
Other machinery	2,688	3,192	504	-	-
All other items	**4,259**	**5,839**	**1,580**	**-**	**-**
Total imports	**56,380**	**80,136**	**23,756**	**-**	**-**

Source: Pakistan Bureau of Statistics and SBP calculations

constrained gas-based power generation in the country.[79] However, the country continued energy imports to fulfill the requirements of the growing economy. Accordingly, energy contributed around one-third in 65.6 percent YoY increase in import during H1-FY22.

The energy prices had started to ease at the dawn of Q3-FY22, amid slowdown in the pace of economic activity across countries. However, the outbreak of Russia-Ukraine conflict in February 2022 added new impetus to the receding prices (**Figure 6.35**). Proposed sanctions on Russia in the shape of ban on import of Russian crude, gas, coal, and

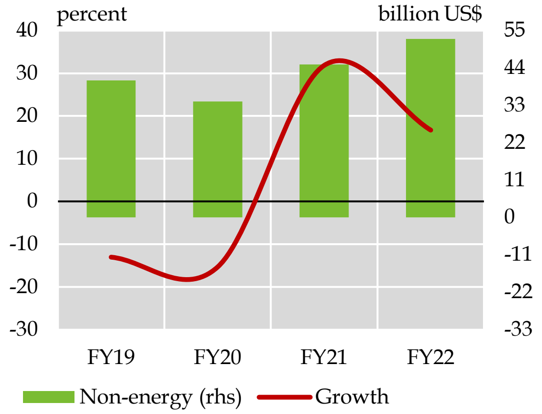
Impact of Price and Volume in Energy Import Growth in FY22 **Figure 6.35**



Source: Pakistan Bureau of Statistics

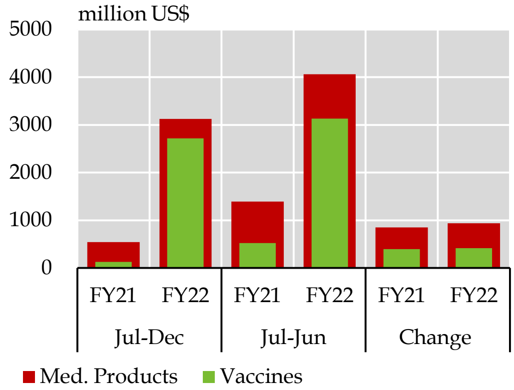
[79] S&P Commodity insight. Available at: www.spglobal.com/commodityinsights/en/market-insights/latest-news/energy-transition/072022-fuel-shortages-hit-nearly-a-quarter-of-pakistans-operational-power-plants

Non-energy Imports **Figure 6.36**



Source: Pakistan Bureau of Statistics

Import of Medicinal Products Including Vaccines **Figure 6.37**



Source: Pakistan Bureau of Statistics

petroleum products jittered the energy market.[80] In addition, prolonged disruption in production in Angola and Nigeria, and marginal increase in the OPEC+ output kept the oil prices at higher level in H2-FY22.[81] Moreover, retaliatory ban imposed by Russia on certain European and non-European energy companies,[82] and expected cut in Russian gas supply to Europe pushed the prices of gas and coal to a new highs.[83] In tandem with these developments, Pakistan's energy import bill soared to US$13.1 billion in H2-FY22, from US$ 6.6 billion in H2-FY21 (**Figure 6.35**).

Non-energy imports

Non-energy imports rose by 16.7 percent, to US$ 52.5 billion, during FY22 (**Figure 6.36**). Nonetheless, its growth tapered off considerably to 19.9 percent in H2-FY22, compared to 38.2 percent witnessed in H1-FY22, as measures taken by the SBP started bearing results. Groups such as, agriculture and other chemicals, transport, machinery and metals, had a significant contribution in growth of non-energy imports during the year (**Figure 6.32**).

Covid vaccines remain a significant driver of import growth during FY22

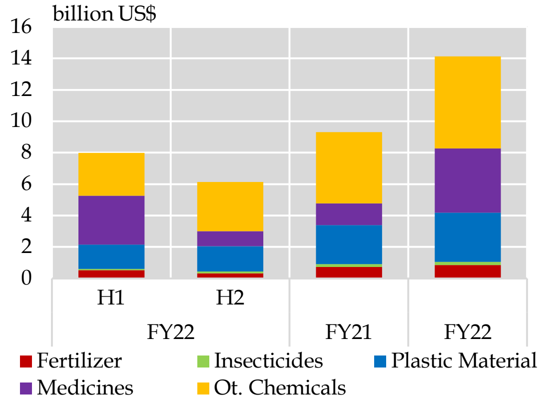
Share of agriculture and chemical group witnessed a considerable increase in FY22, largely due to procurement of Covid vaccines in H1 (**Figure 6.34**). In terms of contribution to growth, this group contributed 9 percentage points in 42.1 percent import growth during FY22 (**Figure 6.32**). Covid vaccine procurement slowed down significantly in H2-FY22 with decline in the infection ratio.

Pakistan imported US$ 3.2 billion worth of Covid vaccines during FY22, compared to US$ 525.1 million in the same period of last year (**Figure 6.37**). Though the spread of Covid had remained under control in H2-FY22, as the number of new cases being reported became insignificant, the country continued its import of Covid vaccines to provide booster jabs to the vulnerable people. In Jan-Jun FY22, Pakistan imported US$ 414 million of Covid vaccine.

---

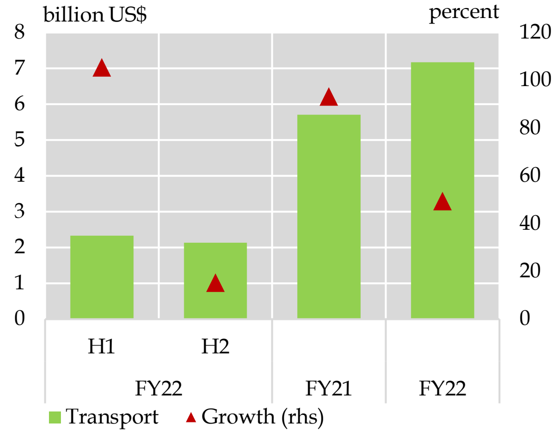
[80] US imposed a ban on imports of Russian crude and natural gas, certain petroleum products and coal. The U.S. imported nearly 700,000 barrels per day of crude oil and refined petroleum products from Russia in CY21. Source: The White House Statement -March 08 2022, available at: www.whitehouse.gov/briefing-room/statements-releases/2022/03/08/fact-sheet-united-states-bans-imports-of-russian-oil-liquefied-natural-gas-and-coal/
[81] Commodity Market Outlook- April 2022 (Source: World Bank)
[82] Russia sanctions 31 energy companies, including ex-subsidiaries of Gazprom in EU (Source: www.tass.com/economy/1449571).
[83] Source: www.reuters.com/business/energy/gazprom-may-lose-third-its-gas-exports-europe-2022-analysts-2022-04-22/

Imports of Agriculture & Other Chemicals — **Figure 6.38**



Source: Pakistan Bureau of Statistics

Transport Imports — **Figure 6.39**



Source: Pakistan Bureau of Statistics

Apart from vaccines, the country imported antibiotics, and other immunological medicines and products during FY22, which also elevated the imports of medicinal products during FY22 (**Figure 6.37**).

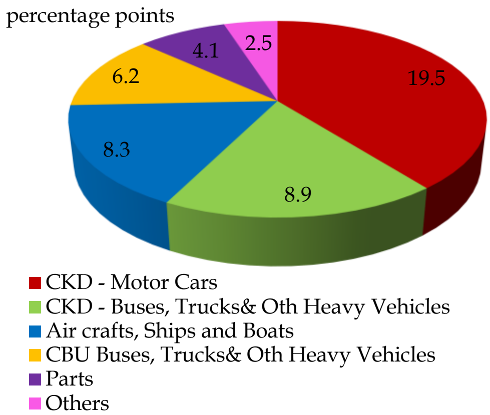
Furthermore, the import of Plastic materials, Other chemicals and Fertilizers also rose significantly in FY22 (**Figure 6.38**). Both plastic materials and other chemicals include mostly raw materials that are used by industries. Therefore, increased economic activity supported imports of these products. Import of fertilizer, on the other hand, witnessed a volumetric decline of 27.2 percent in FY22, due to booming fertilizer prices. Record increase in the natural gas prices had spillover effect on fertilizer prices, as the natural gas is used as feedstock in fertilizer production.

Transport imports show a robust expansion

Transport group imports rose to US$ 4.5 billion in FY22, 49.1 percent higher against last year. Accommodative monetary policy stance, and rising incomes had bolstered automobiles demand since last year. The momentum continued during the first half of FY22, as the commodity's imports more than doubled from US$ 1.1 billion in H1-FY21 to US$ 2.3 billion in H1-FY22. However, demand compression measures, sharp increase in prices, and a large depreciation in exchange rate, slowed the pace of increase in H2-FY22 (**Figure 6.39**). In terms of composition, CKD units of cars, buses and other heavy vehicles explain around one-half of the expansion in transport imports during the year (**Figure 6.40**). In overall terms, while cars continued to dominate the transport imports, heavy vehicles (buses, trucks and other heavy vehicles) also showed a significant increase during FY22 (**Figure 6.41**). Moreover, despite the ban imposed by the government on imports of most of CBU units in Q4-FY22, imports of CBU heavy vehicles increased from US$ 127.3 million in FY21, to US$ 336.3 million in FY22; up by almost 164.3 percent.[84]

CBU heavy vehicle imports registered a sharp increase due to (i) busses being imported for provisioning of public transport under various ongoing BRT schemes in different cities of the country;(ii) demand from

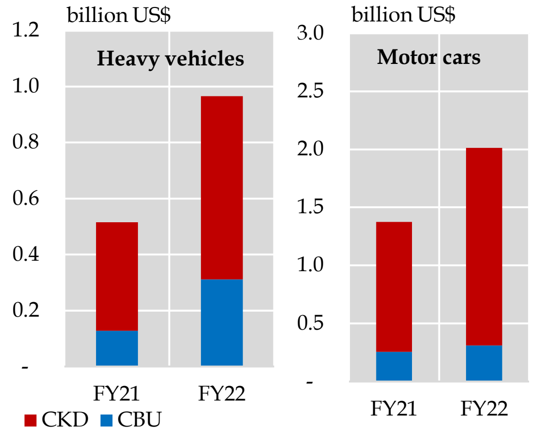
Contribution in Transport Group Import Growth- FY22 — **Figure 6.40**



Source: Pakistan Bureau of Statistics

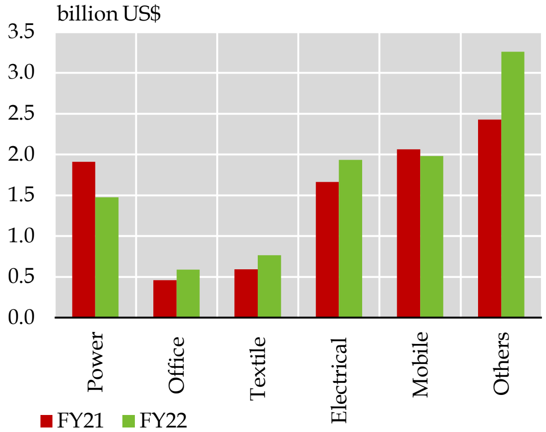
[84] CKD/SKD heavy vehicles imports, on the other hand, rose by 68.2 percent to US$ 652.4 million during FY22.

Category-wise Transport Imports **Figure 6.41**



Source: Pakistan Bureau of Statistics

Machinery Imports **Figure 6.42**



Source: Pakistan Bureau of Statistics

businesses, which are upgrading their transportation using TERF facility; and (iii) increase in households demand for cheaper minivans, as effective import duty is less on the older imported vehicles.[85]

Despite a deceleration, imports of cellular mobile remained significant

Machinery import increased to US$ 10.9 billion in FY22 compared to US$ 10.1 billion witnessed last year. Though telecom equipment, specifically the cellular mobile phone, remained the key contributor of this group, its imports witnessed a decline of 4.2 percent during the year (**Figure 6.42**). In absolute term, Pakistan imported US$ 2.0 billion of mobile Phones in FY22, marginally less than US$ 2.1 billion of imports in FY21.

In FY22, the mobile imports were largely dominated by CKD/SKD units as a number of companies have setup mobile phone assembly plants in Pakistan to produce locally renowned international brands. This has led to substitution of the CBU mobiles with the CKD/SKD mobile phone imports (**Figure 6.43**).[86] Moreover, the government has imposed a ban on imports of CBU mobiles in May 2022, which also arrested the imports of mobile phones.[87]

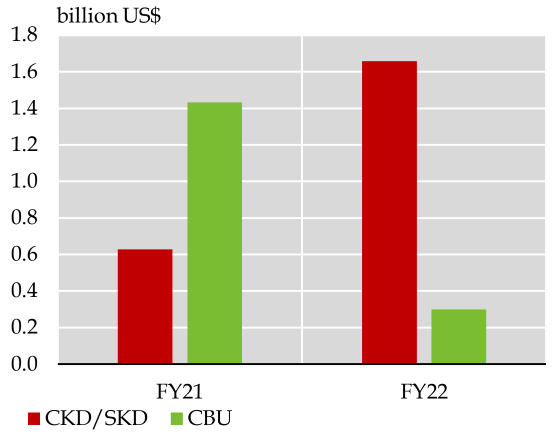
Apart from the telecom sector, imports of electrical machinery and apparatus, and textile machinery also rose significantly. Electrical machinery and apparatus rose to US$ 1.9 billion during FY22, from US$ 1.7 billion last year (**Figure 6.42**). The key imports of this group included photosensitive semiconductors (solar panels), and electrical equipment like static converters, batteries (lithium-ion), multi core cables, and boards panels and consoles.

Amid rising cost of electricity, green initiatives such as, subsidized loan promoted by SBP, [88] and net-metering embraced by the power distribution companies,[89] have promoted households and businesses to move to the alternate power source (specifically solar panels). As a result, import of solar panels increased to US$ 31.5 million during FY22, compared to US$ 30.3 million witnessed in the same period of last year.

Moreover, import of textile machinery rose from US$ 592 million in FY21, to US$ 764.0 million in FY22 (**Figure 6.26**). The textile sector

[85] Under the personal baggage scheme, import of cars- not older than 03 years- are allowed while imports of other vehicles, which also includes minivans- not older than 05 years- are allowed.
[86] For details, see SBP First Quarterly Report on State of Pakistan's Economy FY22.
[87] See footnote No. 16.
[88] For details see, SBP Financing Scheme for Renewable Energy and Islamic Financing Facility for Renewable Energy (Source: IH&SMEFD Circular No. 12 of 2021**).**
[89] Net-metering allows households and businesses to sell the excessive power produced by their equipment to their respective power distribution companies.

Mobile Imports **Figure 6.43**



Source: Pakistan Bureau of Statistics

benefited from the financing approved under the TERF and LTFF. Financing to the sector increased to PKR 348.5 billion during FY22, compared to PKR 237.7 billion witnessed in the same period of FY21.

Metal imports soar amid rising prices and volume

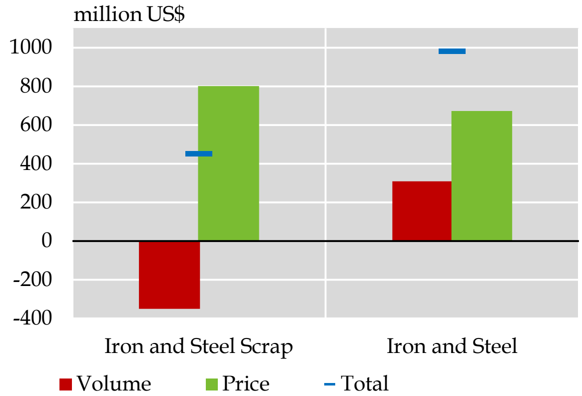
During FY22, import of metals increased by 33.2 percent to US$ 6.5 billion. Import of iron and steel and its scraps- both being the key drivers of metal imports- increased to US$ 2.9 billion and US$ 2.3 billion respectively in FY22, from around US$ 2.0 billion imports of each in FY21.

Importantly, import of iron and steel scrap was entirely driven by the increase in prices, as its volume witnessed a decline during FY22. On the contrary, the import of iron and steel metal witnessed a sharp increase in both volume and value (**Figure 6.44a**).

As energy prices are at record level and there are ongoing efforts to decarbonize the steel industry, ferrous scrap has become a 'new gold' for the industry. Steel produced using scrap in electric arc furnaces leads to just one-third of the carbon emission compared to the steel made from iron ore and coal in a blast furnace. China, Russia and Japan, have announced export restrictions, in order to keep at home more recycled raw materials for their steel and metal production.[90] Other countries and regions, including South Africa, Iran, the UK and the European Union, are preparing to follow the suit.

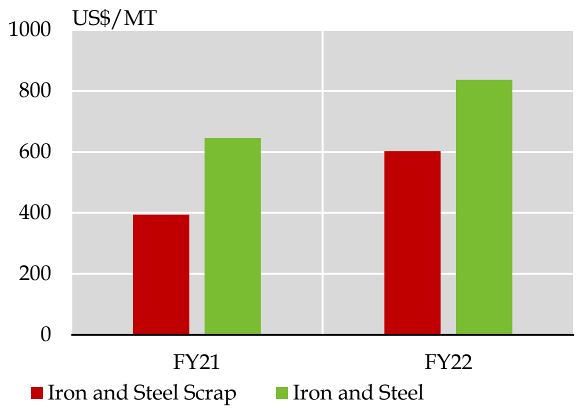
As the supply of scraps has become restricted, its price escalated more sharply compared to iron and steel. Average unit value of imported scrap was US$ 602.8 per MT during FY22, 53.2 percent higher compared to the last year. On the contrary, the average unit value of the iron and steel metal imports were US$ 837 per MT, around 29.6 percent higher than last year (**Figure 6.44b**).

Volume and Price Effect of Steel Imports **Figure 6.44a**



Source: Pakistan Bureau of Statistics

Average Unit Value of Iron & Steel and Scrap Imports **Figure 6.44b**



Source: Pakistan Bureau of Statistics

[90] The 's' word: Recycling scrap metal's image, S&P Global Commodity Insight, Available at: www.spglobal.com/commodityinsights/en/market-insights/blogs/metals/081822-scrap-metal-green-steel-decarbonization-circular-economy

Besides this global development, higher energy cost has driven out the small and inefficient billet producers from local market, which uses scraps as its key raw material. This also has contributed to the decline in the imports of the iron and steel scraps.[91]

[91] For details, see Chapter 2 of this report.