Domestic and External Debt

Public debt grew at a faster pace during FY23 compared to the previous year. Both the domestic and external components contributed in the sharp rise in the public debt. Domestic debt increased on account of high financing needs and limited external inflows, while entire increase in external debt stemmed from depreciation of PKR against US dollar. The external debt, however, declined in dollar terms owing to higher scheduled payments and lower-than-expected external disbursements in the backdrop of delay in the completion of the 9th review under the IMF's EFF program and downgrading of Pakistan's credit rating by the international rating agencies. In case of domestic debt, the government raised funds mainly through borrowing from the non-bank entities, contrary to the previous year, when borrowing had been majorly sourced from the banking sector. Further, the bank borrowing was concentrated in T-bills, while there was a net retirement in unfunded debt. As a result, the maturity profile of the public debt marginally shortened, which more than offset the improvement in the maturity profile of external debt. Furthermore, the debt repayment capacity of the government somewhat weakened on the back of higher interest payments, slowdown in FBR tax revenues, and decline in foreign exchange earnings. The external debt sustainability indicators, however, displayed a mixed picture.

5

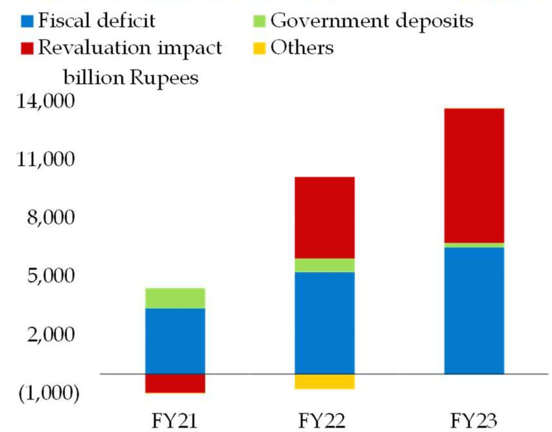
5 Domestic and External Debt

5.1 Public Debt

The pace of debt accumulation accelerated, with gross public debt rising by 27.7 percent during FY23 compared to 23.5 percent in the previous year. Resultantly, gross public debt to GDP ratio increased to 74.3 percent in FY23 from 73.9 percent in FY22 (**Figure 5.1 & Table 5.1).** The increase in debt largely emanated from higher government financing needs due to large fiscal deficit and depreciation of PKR against the US dollar **(Figure 5.2)**.

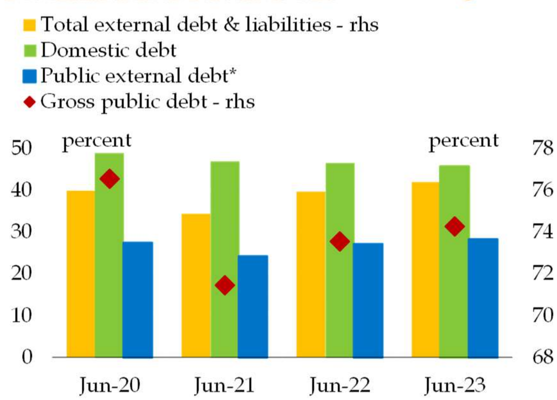
In terms of composition, major impetus came from domestic debt; it contributed around 56.6 percent in the expansion of public debt in FY23, compared to 51.4 percent in FY22 **(Figure 5.3)**. This resulted from increased government reliance on domestic sources to finance the deficit due to less than estimated external inflows. On the other hand, the increase in external debt (in PKR terms) solely stemmed from the depreciation of PKR against the US dollar during FY23.[1] This has more than offset the decline in external debt in dollar terms because of higher scheduled repayments and limited external inflows. Within the domestic debt, the government mainly raised funds through non-bank sources during FY23. This is contrary to FY22, when banking sector was the major source.[2,3] The main reason behind this shift was lucrative rates with lower risk vis-à-vis other investment avenues, which attracted non-banks' investment in government securities.

Sources of Increase in Public Debt — Figure 5.2



Sources: State Bank of Pakistan and Ministry of Finance

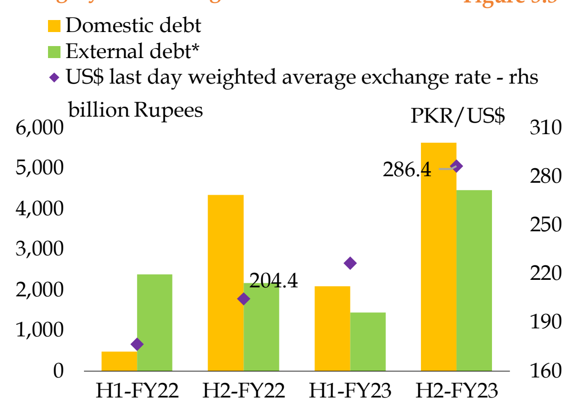
Debt Indicators as Percent of GDP — Figure 5.1



*government external debt + debt from IMF

Source: State Bank of Pakistan

Category-wise Change in Public Debt — Figure 5.3



*including debt from the IMF

Source: State Bank of Pakistan

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[1] The PKR depreciated by around 28.6 percent against the US dollar at end June 2023 compared to end June 2022.

[2] Non-bank institutions include insurance companies, holding companies, investment companies, refinance companies, etc. that does not have full banking license and cannot accept deposits from the public. However, they do facilitate alternative financial services such as investment, risk pooling, financial consulting, brokering, money transmission and check cashing.

[3] The banking sector includes both scheduled banks and SBP.

Summary of Pakistan's Debt and Liabilities — **Table 5.1**

billion Rupees

	Stock		Flows	
	End-June 2022	End-June 2023	FY22	FY23
Gross public debt (sum I to III)	49,242.0	62,880.1	9,375.9	13,638.1
I. Government domestic debt	31,085.4	38,808.9	4,820.0	7,723.5
II. Government external debt	16,747.0	22,030.9	4,307.9	5,283.9
III. Debt from IMF	1,409.6	2,040.2	248.0	630.7
IV. External liabilities	2,275.6	3,101.9	897.2	826.3
V. Private sector external debt	3,697.7	5,159.1	1,122.7	1,461.4
VI. PSEs external debt	1,667.1	2,150.8	602.5	483.7
VII. PSEs domestic debt	1,393.4	1,687.2	-43.3	293.7
VIII. Commodity operations	1,133.7	1,485.9	229.7	352.3
IX. Intercompany external debt	837.6	1,114.0	204.6	276.5
Memorandum Item				
Gross public debt (as percent of GDP)	**73.9**	**74.3**	-	-
Total debt of the government*	44,361.5	57,778.3	8,693.0	13,416.8

*as per FRDLA definition

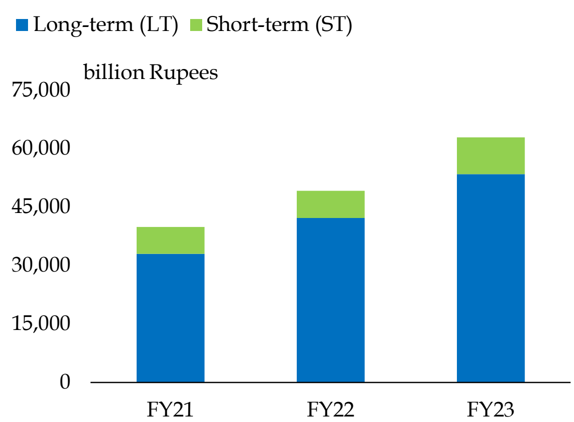
Source: State Bank of Pakistan

Funds mobilized through the banking sector (on net basis) decreased slightly in FY23, mainly due to retirement of loans to the SBP.[4]

The maturity-wise analysis shows a slight deterioration in maturity profile of the public debt. This largely owed to increase in the share of T- bills as well as reduction in unfunded debt in the domestic debt, which offset the improvement in maturity profile of external debt amid retirement of short-term commercial and multilateral debt **(Figure 5.4a and Figure 5.4b)**. The increase in share of short-term debt has given rise to rollover risk.[5,6]

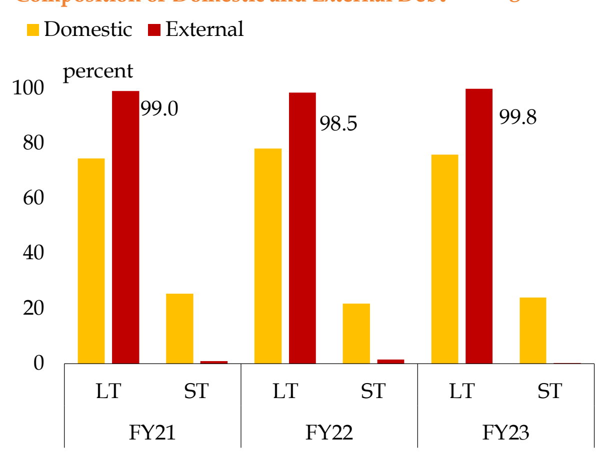
Moreover, the repayment capacity of the government also weakened on the back of higher interest payments (both domestic and external), lower foreign exchange earnings and decelerated FBR tax revenues.[7] Specifically, the

Composition of Public Debt — **Figure 5.4a**



Source: State Bank of Pakistan

Composition of Domestic and External Debt — **Figure 5.4b**



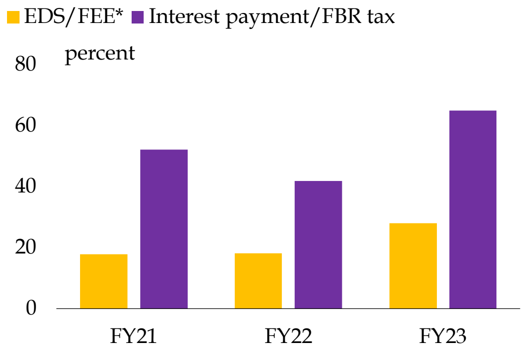
[4] As per the amended SBP Act, "The Bank shall not extend any direct credits to or guarantee any obligations of the Government, or any government-owned entity or any other public entity."

[5] Rollover risk is associated with the refinancing of debt if interest rates increases by the time debt is about to mature and is needed to be rolled over. The issuer would have to refinance their debt at a higher rate and incur more interest charges.

[6] Short-term debt includes debt instruments having maturity of less than or equal to a year.

[7] The repayment capacity is assessed by two ratios: domestic interest payments-to-FBR taxes and public external debt servicing (EDS)-to-foreign exchange earnings (FEE).

Debt Repayment Capacity **Figure 5.5**



*EDS: External debt servicing
*FEE: Foreign exchange earnings
Source: Ministry of Finance and State Bank of Pakistan

FBR tax revenues grew by 16.6 percent during FY23, compared to 29.6 percent last year. Meanwhile, interest payments on domestic debt grew by 71.2 percent, compared to 13.5 percent in the previous year. Consequently, the interest payments-to-FBR tax ratio deteriorated in FY23 **(Figure 5.5)**.

Similarly, the rise in external debt servicing and decline in foreign exchange earnings led to increase in external debt servicing-to-foreign exchange earnings ratio. The decline in foreign exchange earnings resulted from sluggish exports and workers' remittances. Meanwhile, the surge in external debt servicing stemmed from higher scheduled repayments, expiration of DSSI and increase in LIBOR/SOFR.[8]

The short-term public external debt (STPED) to reserves and external ratios strengthened amidst a considerable reduction in short-term debt, while solvency indicators deteriorated on the back of higher external debt servicing and muted external inflows. Moreover, there were net outflows from investment in Naya Pakistan Certificates (NPCs) due to global monetary tightening and domestic uncertainties.[9]

These developments created some challenges for debt sustainability and fiscal position. First, with more debt being raised through floating rate long-term instruments, the government's interest rate risk has increased.[10] Second, inadequate external inflows have resulted in increased reliance on domestic borrowings at relatively higher interest rates, which has increased government's funding cost. Third, within the domestic market, investors' interest remained tilted towards relatively shorter-tenor instruments which increased the rollover risk. Fourth, increased reliance on commercial banks, amid higher financing requirements, has left little space for the government to bargain on the cost of borrowing.

To maintain debt sustainability and improve repayment capacity, it is important to take various structural and non-structural measures aiming at: (i) reducing fiscal deficit by widening tax base and maintaining fiscal discipline; (ii) increasing external inflows by diversification of exports and remittances; (iii) attracting Foreign Direct Investment (FDI); and (iv) keeping a balance between lengthening of the maturity profile and the cost of borrowing while contracting debt.[11]

5.2 Domestic Debt

The stock of domestic debt rose to Rs 38.8 trillion at the end of June 2023, up by 24.8 percent compared to 18.4 percent increase in FY22 **(Table 5.2)**. Persistently higher fiscal deficit and inadequate external inflows were the main reasons behind this sharp increase, which forced government to meet its financing

[8] Secured Overnight Financing Rate (SOFR) measures the cost of overnight borrowing in cash against treasury securities as collateral; whereas, the LIBOR is the rate banks used to borrow from each other internationally. The LIBOR has now been replaced by SOFR. Most of the interest payments in Pakistan have been shifted to SOFR as of June 2023, while the remaining shall be converted either at the time of rollover/renewal or new coupon payment, etc.
[9] For instance, the average Economic Policy Uncertainty (EPU) Index of Pakistan increased to 196.5 during FY23 compared to 149.5 in FY22 (source: State Bank of Pakistan).
[10] Interest rate risk arises for bond owners from fluctuating interest rates.
[11] To attract more external inflows Pakistan needs to work on ease of doing business and political stability.

Government Domestic Debt and Liabilities **Table 5.2**

billion Rupees

	Stock		Share in Domestic Debt		Flows		Growth	
	End-June 2022	End-June 2023	FY22	FY23	FY22	FY23	FY22	FY23
I. Permanent Debt, of which	**20,843.7**	**26,021.5**	**67.1**	**67.1**	**4,939.6**	**5,177.8**	**31.1**	**24.8**
GOP Ijara Sukuk	2,279.8	3,150.6	7.3	8.1	1,614.6	870.8	242.7	38.2
PIBs	17,687.0	22,009.3	56.9	56.7	3,097.0	4,322.3	21.2	24.4
Prize Bonds	374.6	382.5	1.2	1.0	-69.1	7.9	-15.6	2.1
II. Floating Debt, of which	**6,804.1**	**9,335.3**	**21.9**	**24.1**	**123.7**	**2,531.2**	**1.9**	**37.2**
Market Treasury Bills	6,752.4	9,269.2	21.7	23.9	75.4	2,516.8	1.1	37.3
III. Unfunded Debt, of which	**3,336.0**	**2,925.6**	**10.7**	**7.5**	**-309.9**	**-410.4**	**-8.5**	**-12.3**
NSS (Net of Prize Bonds)	3,208.3	2,817.6	10.3	7.3	-289.6	-390.7	-8.3	-12.2
IV. Foreign Currency Instruments	**8.7**	**383.8**	**0.0**	**1.0**	**2.0**	**375.1**	**29.3**	**4,315.4**
V. Naya Pakistan Certificates (NPCs)	**92.9**	**142.7**	**0.3**	**0.4**	**64.7**	**49.8**	**228.9**	**53.6**
Government Domestic Debt (I+II+III+IV+V)	**31,085.4**	**38,808.9**	**-**	**-**	**4,820.0**	**7,723.5**	**18.4**	**24.8**

Source: State Bank of Pakistan

requirements through domestic borrowing notwithstanding high borrowing cost.

Non-bank entities were major source of domestic financing

The institution-wise data shows that, in contrast to past trend, most of the increase in domestic debt during FY23 came from non-bank sources (around 51.4 percent), such as Development Financial Institutions (DFIs), Insurance Companies, Money Market Funds, etc. **(Figure 5.6)**. Due to lucrative rates and low risk, these investors showed greater interest in government securities. Investment by scheduled banks was low in first half of FY23, however, it rose significantly in H2-FY23 as government's financing requirements increased amidst falling external financing. Consequently, the share of scheduled banks domestic funding increased from 28.0 percent in H1-FY23 to around 52.4 percent in H2-FY23. However, due to retirement of maturing PIBs held by the SBP (around Rs 291.0 billion), the overall share of banking sector in the change in domestic debt decreased to 48.5 percent during FY23 from 78.8 percent in FY22.[12]

PIBs and T-bills mostly contributed in the domestic debt accumulation

Government mainly raised financing through PIBs and T-bills during FY23. In the first three quarters, most of the increase in domestic debt resulted from PIBs and Ijara Sukuk, while there was net retirement in T-bills due to high cost of borrowing. In Q4-FY23, however, T-bills worth Rs 11.0 trillion were issued due to investors' inclination to lock funds in shorter-tenor T-bills amidst rising interest rates environment and domestic uncertainties. Meanwhile, continuing the previous trends, the National Saving Schemes (NSS), net of prize bonds, registered net outflows during FY23. This compelled the GoP to borrow through T-bills. Consequently, the maturity profile of domestic debt shortened due to surge in short-term debt (floating debt) and decline in the stock of unfunded (long-term) debt during FY23 compared to FY22 **(Table 5.2)**.

[12] Based on stock position, the share of banking sector in the stock of domestic debt declined to 69.4 percent at end- June 2023 from 74.6 percent at the end of June 2022; mainly due to retirement in SBP debt (from 21.3 percent by the end of June 2023 to 16.3 percent at End-June 2023). The share of scheduled banks in debt stock decreased slightly from 53.3 percent to 53.1 percent due to increased borrowing from non-bank.

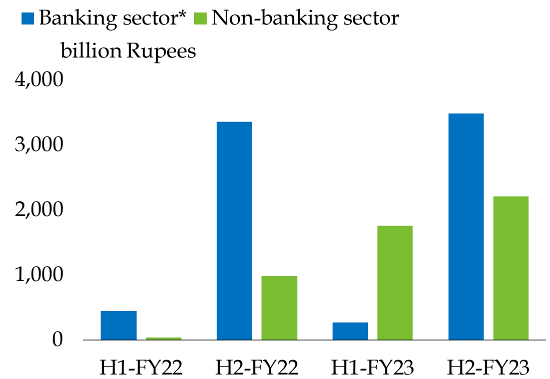
On the one hand, concentration of domestic debt in floating rate instruments, which include floating rate PIBs (PFLs) and variable rental rate (VRR) Sukuk, has increased the interest rate risk. On the other hand, rise in stock of T-bills led to increase in both rollover risk and interest rate risk. The resulting increase in interest payments further added to growing financing needs and hence further accumulation in debt stock.[13]

The share of permanent debt remained unchanged[14]

The stock of PIBs grew by 24.4 percent and reached Rs 22.0 trillion during FY23, compared to Rs 17.7 trillion at the end of June 2022 **(Table 5.2)**. This increase mainly resulted PFLs, accounting for 80.2 percent of debt raised through PIBs, driven by lucrative returns compared to fixed rate PIBs.[15]

The auction profile of PIBs shows that the investors were more inclined towards relatively shorter-tenor instruments in case of PFLs and medium-term instruments (5-year and 10-year) in case of fixed rate PIBs **(Figure 5.7a & Figure 5.7b)**. This was because banks expected increase in policy rate near term over the medium term.

Increase in Domestic Debt Holding-Institution wise — **Figure 5.6**

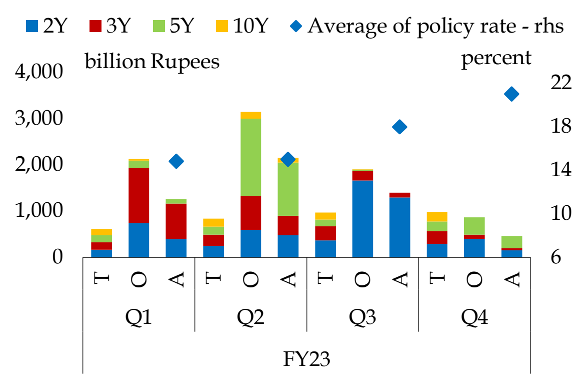


* Banking sectors includes both scheduled banks and SBP

Source: State Bank of Pakistan

The quarterly analysis depicts that investors were inclined towards 5-Year instruments, especially in PFLs, during Q2-FY23, as the market was expecting an increase in policy rate in the short and medium-term owing to persistently rising inflation.[16] Given increased economic uncertainty in Q3-FY23, the market was keen on short-term quarterly coupon

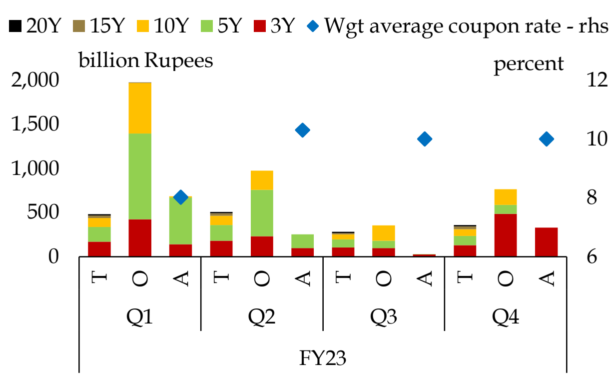
Auction Summary of PFLs — **Figure 5.7a**



T: Target O: Offered A: Accepted

Source: State Bank of Pakistan

Auction Summary of Fixed PIBs — **Figure 5.7b**

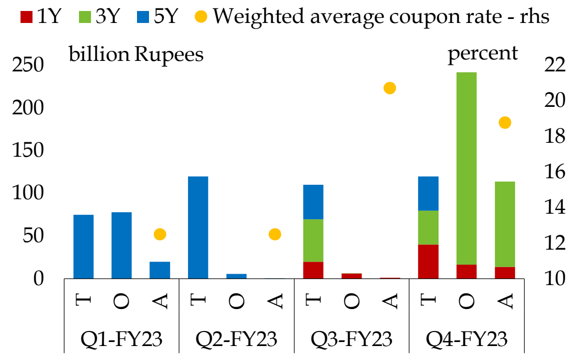


T: Target O: Offered A: Accepted

Source: State Bank of Pakistan

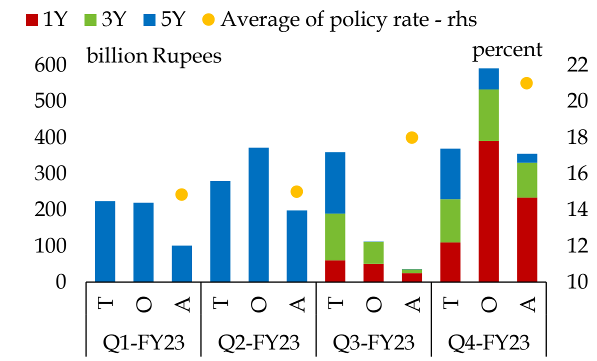
[13] The coupon payments of floating rate instruments are linked to the cut-off rates of 3-month and 6-month T-bills. With the increase in policy rate, the cut-off rates of the T-bills also increased which resulted in higher interest payments.
[14] Permanent debt mainly consists of PIBs, Ijara Sukuk and Prize Bonds.
[15] The offered amount in PFLs was nearly twice of that offered in Fixed PIBs.
[16] In October 2022, CPI reached to 26.6 percent on YoY basis with Food Inflation of around 36 percent which was way more than policy rate of 15 percent.

Auction Summary of GoP Ijara Sukuk- Fixed **Figure 5.8a**



T: Target O: Offered A:Accepted
Source: State Bank of Pakistan

Auction Summay of GoP Ijara Sukuk-Variable (VRR) **Figure 5.8b**



T: Target O: Offered A: Accepted
Source: State Bank of Pakistan

instruments to benefit from the lucrative rates.[17] However, in Q4-FY23, the market moved away from PFLs towards investing in fixed rate PIBs and T-bills (see **Chapter 3** for more details).

The participation of primary dealers (PD) in the auction of Islamic instruments remained limited during FY23. The government raised Rs 870.8 billion (net of maturity) through Ijara Sukuk compared to Rs 1.6 trillion in the previous year **(Table 5.2)**. Overall, major part of this was raised through variable rental rate (VRR) Ijara Sukuk, in line with the tendency in the conventional market and trend seen in the previous year **(Figure 5.8a & Figure 5.8b)**.

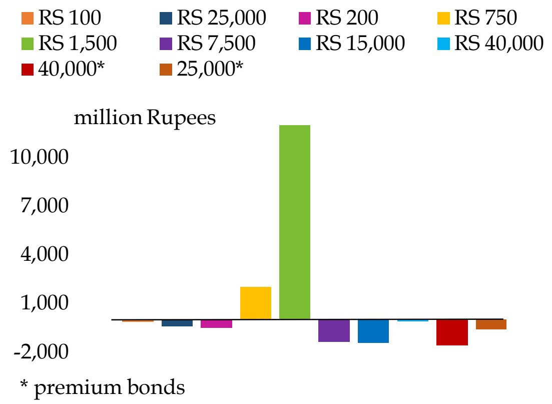
The main reasons for lower subscription of Islamic instruments include: (i) deceleration in Islamic deposits amidst increase in inflation; (ii) prevailing economic uncertainty; and (iii) availability of longer term instruments only. In the first half of FY23, only 5-year Sukuk were available for the investors. The market did not find 5-year fixed rental rate (FRR) Sukuk profitable due to an upward trajectory in inflation and rising interest rate. Therefore, it shifted investment towards VRR Sukuk. Nonetheless, with the introduction of 1-year and reintroduction of 3-year Ijara Sukuk in Q3-FY23, the market started to make offers in Shariah-compliant instruments. After the introduction of these shorter-tenor Sukuk, the market did not bid for 5-Year FRR. Similar was the case with VRR Ijara Sukuk, except for the month of May and June 2023. Therefore, the overall offered amount in Sukuk auctions remained low, thus the government accepted amount was lower than the target.[18] Other reasons for issuing fewer Ijara Sukuk were higher bid rates and longer maturities, which made it less attractive compared to other available options to the government (see **Table 3.3** of **Chapter 3** for details).

Although floating rate instruments helped the government in fulfilling its financing requirements, these increased government's cost of borrowing due to inverted yield curve, higher yields on shorter-tenor compared to the longer-tenor instruments, amidst investors' increased preference for shorter-term bonds.

Prize bonds recorded net inflows in FY23, for the first time since FY19 **(Table 5.2)**. These inflows were concentrated in Rs 1500 and Rs 750 denominations. Meanwhile, prize bonds of other denominations showed net outflows (**Figure 5.9)**. This is due to government's decision to

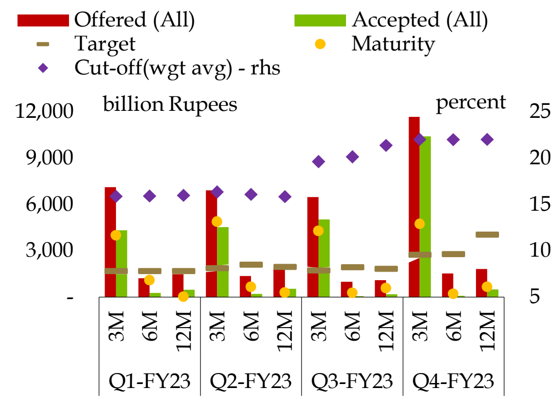
[17] Two and Three Year PFLs are quarterly coupon paying instruments, their coupon is reset either on quarterly basis, or on the day of settlement of each auction of 3-month T-bills during the life of the bond (i.e. fortnightly), as may be announced by the State Bank of Pakistan through the auction calendar.
[18] The overall offered amount in Sukuk was almost close to the target.

Net Flows of Prize Bonds during FY23 **Figure 5.9**



Sources: Central Directorate of National Savings and State Bank of Pakistan

Auction Summary of T-bills-Instrument-wise **Figure 5.10**



Source: State Bank of Pakistan

discontinue higher denomination bearer bonds to improve the documentation of the economy and to mitigate risk of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) related risks.[19] Therefore, the investors moved their funds in Rs 1,500 and Rs 750 denomination bearer bonds.

There were net outflows in Rs 100, Rs 200 and premium bonds (Rs 25,000 and Rs 40,000) despite increase in gross receipts. The factors behind encashment were: (i) uncertainty about government policy and investors' lack of trust as they suspected that the government might discontinue these bonds at any time; and (ii) the shift of investors' interest towards government securities due to higher returns.

Significant accumulation in floating debt

Floating debt (instrument maturing within a year) showed a significant increase of Rs 2.5 trillion in FY23, compared to an addition of only Rs 123.6 billion (net of maturity) in the previous year. In view of the prevailing economic uncertainty and increasing interest rates, the market remained inclined towards investment in 3- month T-bills, almost throughout FY23. Resultantly, the GoP mobilized most of the amount through these T-bills despite its target to retire these bonds on net basis.

Overall, on cumulative basis the government made net retirement of T-bills worth Rs 521.8 billion during the first three quarters of FY23, due to higher bid rates demanded by the market. However, during Q4-FY23, in view of growing fiscal needs amidst inadequate external financing, the government accepted a significantly higher amount for 3-month T-bills **(Figure 5.10)**. Resultantly, the stock of T-bills (on net basis) increased by around 3.0 trillion in Q4-FY23. Specifically, the share of 3-month paper in T-bill stock increased from 55 percent in FY22 to 83 percent by the end of FY23.

Net outflows from unfunded debt

Unfunded debt recorded net outflows for the third consecutive year **(Table 5.2)**.[20] Most of the outflows were registered in Special Saving Accounts (SSA), followed by Regular Income Certificates (RIC), Special Saving Certificates (SSC) and Defense Saving Certificates (DSC) **(Figure 5.11a)**. The outflows from the above-mentioned instruments offset the net inflows in Short Term Savings Certificates (STSC), Savings Accounts and Pensioners' Benefit Account

[19] Government discontinued bearer Prize bonds of 7,500, 15,000, 25,000 and 40,000 in FY21. The Rs 25,000 and Rs 40,000 bearer bonds were then replaced with premium bonds of Rs 25,000 and Rs 40,000, respectively.
[20] Unfunded debt mainly comprises National Saving Schemes (NSS)-net of prize bonds.

(PBA). The main reasons for outflows despite increase in gross investments **(Figure 5.11b)** included: (i) institutional withdrawal from DSC; (ii) non-competitive profit rates compared to government securities; and (iii) reinvestment of the withdrawn money on higher rates.[21] This resulted in inflated gross receipts and, at the same time, showed outflows.

An important highlight of the fiscal year is the introduction of Sarwa Islamic Saving Accounts and Sarwa Islamic Term Accounts (SITA) in Q4-FY23. The government was able to mobilize around Rs 5.0 billion via these Shariah-complaint instruments. The data shows that most of the net inflows came from Sarwa Islamic Saving Account.

Decline in investments of Naya Pakistan Certificates (held by residents)

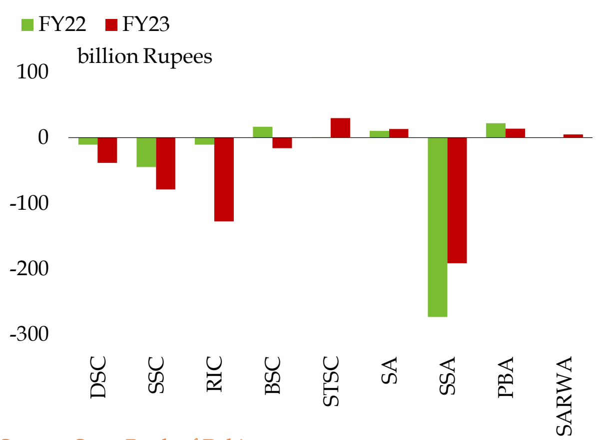
Residents' investment in NPCs declined to Rs 49.9 billion (on net basis) in FY23 against previous year's Rs 64.7 billion despite revaluation gains of US Dollar against PKR **(Table 5.2).** The decline resulted from monetary tightening around the globe and political instability in the country. Given higher returns on other instruments, the domestic investors did not find NPCs lucrative. For instance, the average spread between 3-month NPCs (in US dollar) and 3- month LIBOR (US dollar) decreased to around 69.3 bps in January 2023 from around 349.5 bps in June 2022, making NPCs relatively less profitable for investors given increased risk due to political instability.[22] Furthermore, the increased kerb market premium diverted investors towards other avenues. Resultantly, the investors withdrew their funds from NPCs.

Sharp increase in interest payments on domestic debt

Interest payments on domestic debt rose to around Rs 4.9 trillion during FY23 compared to 2.8 trillion in FY22; a growth of 71.2 percent compared to 13.5 percent last year. This largely emanated from increasing share of floating rate instruments amidst higher borrowing requirements and rising interest rates **(Figure 5.12a)**.

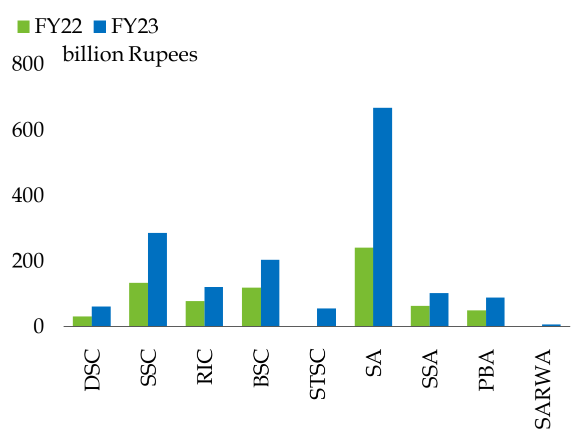
The interest payments on floating rate PIBs and Ijara Sukuk particularly increased as a result of the increasing share of these instruments in the outstanding debt stock and rising interest

National Saving Schemes Net Flows — Figure 5.11a



Source: State Bank of Pakistan

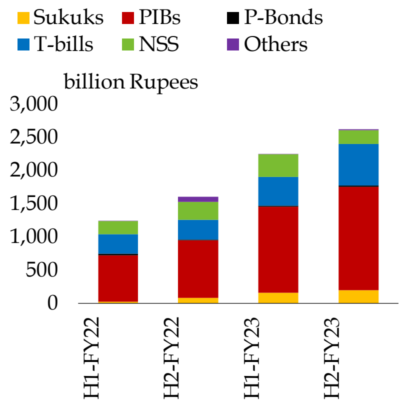
National Saving Schemes Gross Inflows — Figure 5.11b



Source: State Bank of Pakistan

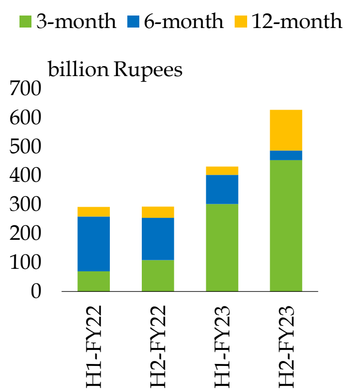
[21] Almost all NSS instruments can be converted into cash any time. However, the tenor of profit payment on these may vary depending on the saving scheme. In increasing profit rates environment, the investors may withdraw their money from previous scheme and invest the same in more profitable schemes.
[22] The interest rates for NPCs in GBP, USD, EUR were not revised till 22 January 2023.

Interest Payments - Domestic Debt **Figure 5.12a**



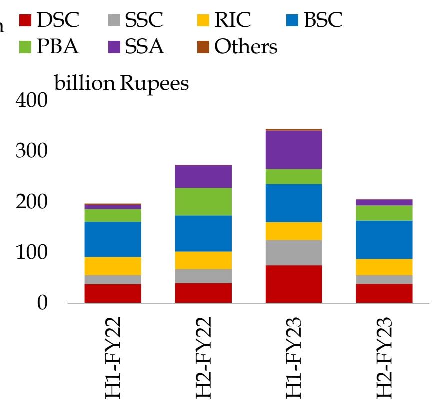
Source: State Bank of Pakistan

Interest Payments - T-bills **Figure 5.12b**



Source: State Bank of Pakistan

Interest Payments - NSS **Figure 5.12c**



Source: State Bank of Pakistan

rates/returns.[23] Moreover, interest payments on T-bills, especially the 3-month paper, also contributed in this increase. For instance, the interest payments on 3-month T-bills increased to Rs 756.4 billion during FY23 from Rs 179.3 billion in FY22 **(Figure 5.12b)**.[24]

The increase in interest payments on NSS resulted from rising profit rates, especially in DSC, SSC, and BSC **(Figure 5.12c)**. However, the profit payments of RICs slightly declined in FY23 due to decrease in stock which more than offset the impact of marginal increase in profit rates.[25]

5.3 External Debt and Liabilities

The stock of public external debt (PED) dropped by US$ 4.8 billion during FY23, compared to an addition of US$ 2.4 billion in FY22 **(Table 5.3)**.[26] This reduction was on account of: (i) higher principal repayments; (ii) limited external financing amidst rising global interest rates and uncertainty surrounding the completion of the IMF's EFF program; and (iii) revaluation gains from appreciation of the US dollar against other international currencies. During FY23, Pakistan made net repayments to commercial banks, Paris Club, multilateral institutions (short-term loans) and Euro/Sukuk bonds. The net foreign exchange liabilities, mainly swaps, also decreased by US$ 303 million during FY23 compared to an increase of US$ 2.4 billion in the previous year **(Table 5.3)**.

As a result, the maturity profile improved slightly due to higher share of long term debt in the stock of overall external debt after net retirement of short-term debt. This led to improvement in short-term public external debt (STPED) to external debt and reserves ratios. Meanwhile, the solvency counterparts weakened.

NPCs (held by non-residents) recorded net outflows

NPCs (held by non-residents) registered a net outflow of US$ 419 million in FY23, despite an upward revision in profit rates in November 2022 and at the end of January 2023. As discussed earlier, this was on account of increasing interest rates and higher inflation in foreign countries (implying low savings), political and economic instability in the country,

[23] The coupon payment of floating rate instrument is linked to the cutoff rates of 3M and 6M T-bills.
[24] The share of 3-month T-bills in interest payments increased to 15.5 percent from 6.3 percent during FY22.
[25] The profit rates were increased by around 247 bps and by 240 bps in case of BSC and PBA, whereas, the interest rates of RIC only increased by 48 bps.
[26] Public External Debt does not include external liabilities.

Summary of Public External Debt **Table 5.3**

million US$

	Stock		Share in Public External Debt (percent)		Change in Stock During		Growth (percent)	
	Jun-22	**Jun-23**	**Jun-22**	**Jun-23**	**FY22**	**FY23**	**FY22**	**FY23**
Public external debt (1+2)	88,838	84,050	-	-	2,381	-4,788	2.8	-5.4
1. Government external debt, of which	81,941	76,926	91.5	92.2	2,868	-5,015	3.6	-6.1
i) Long term (>1 year), of which	80,592	76,766	91.3	90.7	2,377	-3,826	3.0	-4.7
Paris club	9,232	7,901	9.4	10.4	-1,494	-1,331	-13.9	-14.4
Multilateral	34,023	37,363	44.5	38.3	187	3,340	0.6	9.8
Other bilateral	18,053	17,572	20.9	20.3	3,232	-481	21.8	-2.7
Euro Sukuk global bonds	8,800	7,800	9.3	9.9	1,000	-1,000	12.8	-11.4
Commercial loans/credits	9,481	5,564	6.6	10.7	-214	-3,917	-2.2	-41.3
Naya Pakistan Certificates	953	534	0.6	1.1	144	-419	17.8	-43.9
ii) Short term (<1 year),	1,349	160	0.2	1.5	491	-1,189	57.2	-88.1
of which, Multilateral	1,327	160	0.2	1.5	821	-1,167	162.4	-87.9
2. From IMF	6,897	7,124	8.5	7.8	-487	227	-6.6	3.3
Foreign exchange liabilities, of which	11,134	10,831	-	-	2,372	-303	27.1	-2.7
Central bank deposits	2,700	2,700	-	-	-	-	-	-
Other liabilities (SWAP)	4,535	4,225	-	-	-114	-310	-2.5	-6.8
Allocation of SDR	3,897	3,904	-	-	2,487	7	176.4	0.2

Source: State Bank of Pakistan

and downgrading of Pakistan's rating by the credit rating agencies over liquidity concerns.

Gross external disbursements (GED) remained significantly lower than budget estimates

Pakistan received much lower gross external disbursements (around US$ 10.8 billion) during FY23, compared to both budget estimates (US$ 22.8 billion) for the year and actual disbursements in FY22 (US$ 15.4 billion).[27] The main reason for decrease in external financing, as explained above, was uncertainty surrounding completion of the IMF program that affected inflows from other bilateral and multilateral sources as well.

The disaggregated analysis of GED in FY23 shows that around one-half of the foreign financing came from multilateral sources, followed by commercial banks, and friendly-countries **(Figure 5.13)**.[28] In the first three quarters, multilateral institutions, IMF and bilateral sources remained the main sources of GED. However, disbursements from foreign commercial banks in Q4-FY23 increased the share of banks from 11.6 percent to 20.3 percent. Although it helped in stemming fall in reserves, it also resulted in higher interest rate and rollover risks of the external debt.

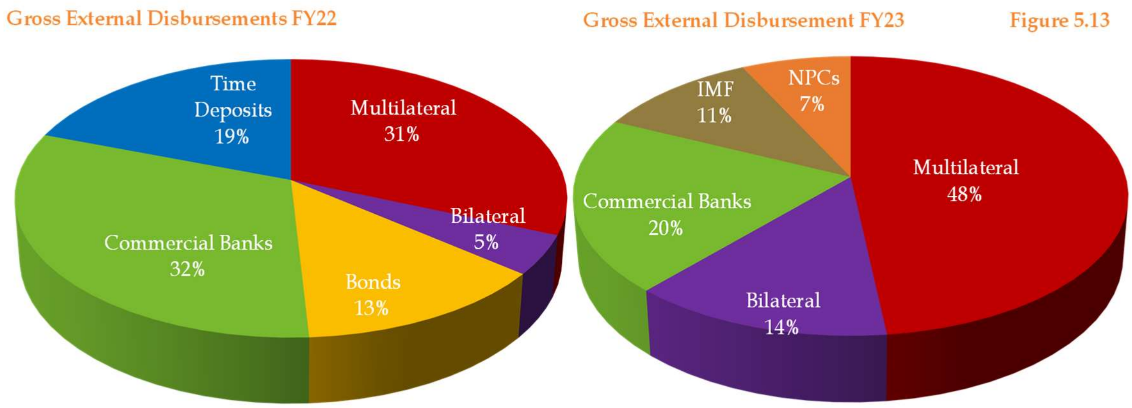
During FY22, around 62.7 percent of the external disbursements came from foreign commercial banks and multilateral institutions, followed by deposits with the central bank and Euro bonds. However, in FY23, no amount could be raised through Eurobonds (despite having a budget estimate of US$ 2.0 billion) as a result of elevated country risk.

In the multilateral category, similar to FY22, Asian Development Bank (ADB) and World Bank (WB) accounted for more than 80 percent

[27] Gross external disbursement during FY23 include loans and grants, while these also included deposits of US$ 3.0 billion, excluding guaranteed loans, in FY22.

[28] In the first three quarters, multilateral institutions, IMF and bilateral sources remain the main external financers.

Figure 5.13



Source: Economic Affairs Division

of the financing from multilateral institutions during FY23 **(Figure 5.14)**. Meanwhile, in bilateral category, major external disbursements in FY23 came from Saudi Arabia and China **(Figure 5.15)**.

In absolute terms, major decrease in external disbursements came from Islamic Development Bank (IDB), international bonds, commercial banks and deposits, which offset the increase in inflows from the IMF, Saudi Arabia, NPCs, ADB, WB and Asian Infrastructure Investment Bank (AIIB) (**Table 5.4**).

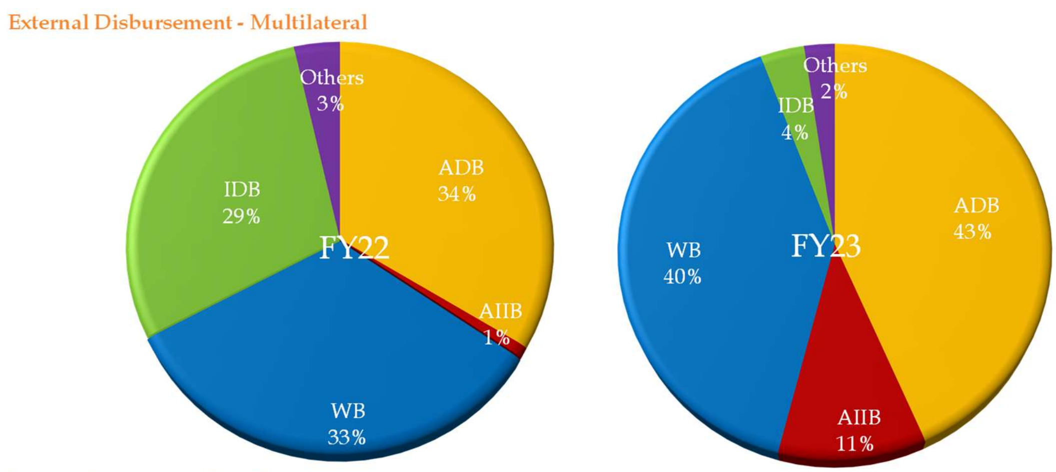
Major external inflows were meant for budgetary support

In terms of utilization, more than two-thirds (around 68.4 percent) of the foreign financing was used for budgetary support during FY23, followed by project-related financing and short-term credit for import of oil and LNG. Similar to the previous year, most of the financing from the WB and loans from the friendly countries consisted of project aid. Nevertheless, contrary to FY22, major inflows from ADB and AIIB were employed to finance budgetary operations in FY23. Meanwhile, all the short-term credit provided by Saudi Arabia and Islamic Development Bank (IDB) was utilized for oil and gas import **(Table 5.4)**

External debt servicing soared to record level in FY23

The government repaid US$ 17.8 billion during FY23 compared to around US$ 13.0 billion in the

Figure 5.14



Source: Economic Affairs Division

Gross External Disbursement and Utilization - Major Contributors **Table 5.4**

million US$

	Project		Program/Budgetary Support		Others		Total		
Donor	**FY22**	**FY23**	**FY22**	**FY23**	**FY22**	**FY23**	**FY22**	**FY23**	**Change**
ADB	905.6	464.3	720.3	1,801.7	-	-	1,625.9	2,266.1	640.2
AIIB	41.6	59.0	-	500.0	-	-	41.6	558.9	517.3
IDB	79.0	16.8	-	-	1327.8 *	161.0*	1,406.8	177.8	-1,229.0
IMF	-	-	-	1,166.2	-	-	-	1,166.2	1,166.2
WB	825.8	1,140.8	721.9	940.8	31.33 **	16.4 **	1,579.0	2,099.5	519.0
China	162.6	128.0	-	-	-	-	162.6	128.0	-34.6
Saudi Arabia	1.1	-	-	-	-	1182.3*	1.1	1,182.3	1,181.2
USA	69.8	31.1	-	-	-	-	69.8	31.1	-38.7
Japan	20.6	35.2	-	-	-	-	20.6	35.2	14.7
France	15.5	33.8	-	-	-	-	15.5	33.8	18.3
NPCs^	-	-	-	789.0	-	-	-	789.0	789.0
Bonds	-	-	2,041.7	-	-	-	2,041.7	-	-2,041.7
Com. Banks	-	-	4,863.3	2,206.0	-	-	4,863.3	2,206.0	-2,657.3
Time Deposits ***	-	-	3,000.0	-	-	-	3,000.0	-	-3,000.0
Others	99.6	85.8	514.3	86.1	0.1	-0.0	614.0	170.4	-442.1
Total disbursements	2,221.1	1,994.8	11,861.6	7,489.7	1,359.2	1,359.7	15,441.9	10,844.3	-4,597.6

*Short-term credit **TDPs *** not included in public external debt as these are part of external liabilities.

^ NPCs became part of external disbursements for the first time in FY23

The total may vary due to round-off impact

Source: Economic Affairs Division

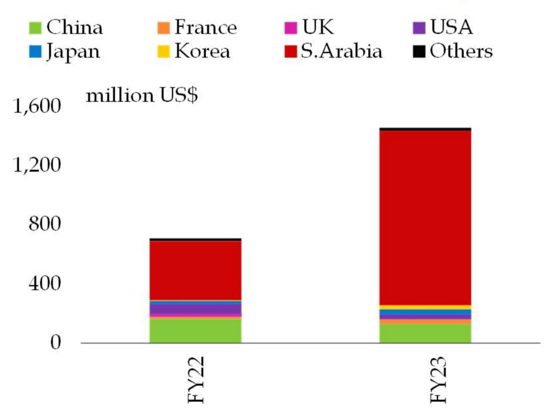
previous year **(Table 5.5).**[29] However, the debt servicing on foreign liabilities declined to US$ 224 million during FY23 from US$ 330 million in FY22 due to reduction in stock.

The disaggregated analysis of debt servicing shows that increase in both principal and interest payments contributed to higher debt servicing during FY23. Nonetheless, the major increase resulted from the scheduled principal repayments **(Table 5.5)**.

Detailed analysis reveals that bulk of debt servicing was made to commercial banks, followed by bilateral and multilateral creditors. In addition to this, a major chunk of debt servicing was made on account of international bonds, multilateral short-term debt, the IMF and NPCs.

Factors behind the higher debt servicing during FY23 included: (i) higher previous outstanding stock; (ii) increase in LIBOR amid global monetary tightening; and (iii) expiration of Debt Service Suspension Initiative (DSSI).[30] As most of the external loans were contracted on floating

External Disbursement - Bilateral **Figure 5.15**



Source: Economic Affairs Division

[29] It includes debt servicing (principal and interest payments) of public external debt. It does not include debt servicing of foreign liabilities.

[30] DSSI helped in lowering external debt servicing in the first half of FY22.

Public External Debt Servicing **Table 5.5**

million US$

	Total		Principal		Interest	
	FY22	**FY23**	**FY22**	**FY23**	**FY22**	**FY23**
1. Public external debt (a + b +c)	12,990	17,820	11,002	14,732	1,988	3,088
a. Long-term Govt. debt, of which	11,276	15,086	9,455	12,438	1,821	2,647
Paris Club	599	1,317	503	1,121	97	196
Multilateral	2,101	2,470	1,654	1,702	447	768
Other Bilateral	763	2,143	502	1,568	261	576
Euro/Sukuk global bonds	1,587	1,611	1,000	1,000	587	611
Commercial loans /credits	5,508	6,380	5,152	5,942	357	438
NPCs	718	1,164	645	1,105	73	59
b. To the IMF	1,154	1,362	1,014	966	140	396
c. Short-term Govt. debt	560	1,372	533	1,328	28	44
2. Foreign exchange liabilities	330	224	-	-	330	224

Source: State Bank of Pakistan

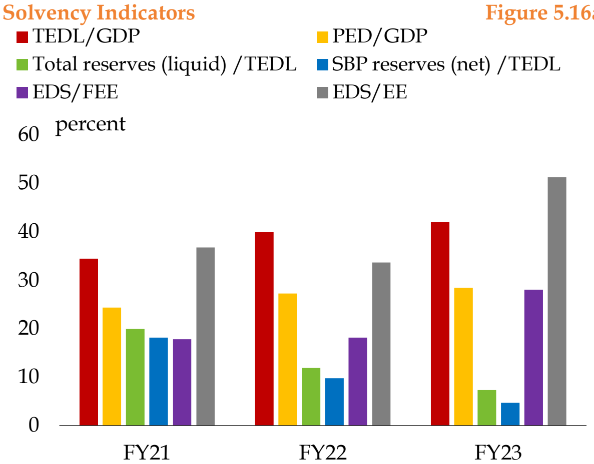
rate, the uptick in LIBOR/SOFR resulted in increased interest payments.[31]

External debt sustainability indicators displayed mixed picture

The short-term debt indicators improved while solvency indicators witnessed deterioration during FY23 **(Figure 5.16a & 5.16b)**.[32] All the solvency indicators somewhat weakened due to: (i) higher debt servicing; (ii) lower foreign exchange earnings such as exports and workers' remittances **(**see **Chapter 6** for more details); and (iii) reduction in dollar denominated GDP compared to external debt.

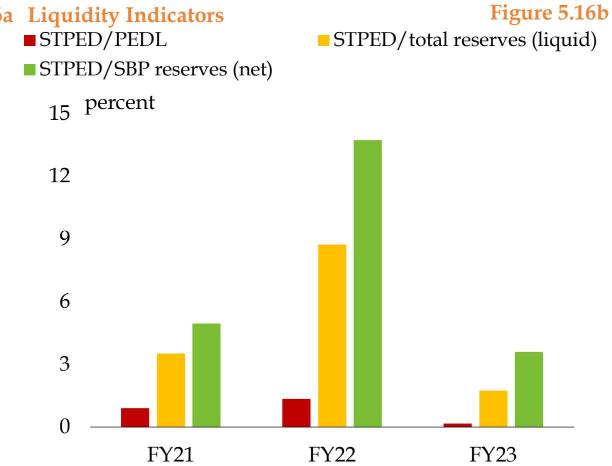
The subsequent fall in foreign exchange reserves of the country, resulted in lower Total Reserves-to-Total External Debt and Liabilities (TEDL) and SBP reserves-to-TEDL ratios. Moreover, decline in export receipts and remittances worsened External Debt Servicing (EDS)-to-Export Earning (EE) and EDS- to- Foreign Exchange Earning (FEE) ratios. The decline in exports resulted from increase in cost of production, unavailability of imported raw materials and global economic slowdown. Meanwhile, slower economic activity squeezed job opportunities and increase in global inflation reduced the savings of Pakistani workers

Solvency Indicators **Figure 5.16a**



Sources: State Bank of Pakistan and Economic Affairs Division

Liquidity Indicators **Figure 5.16b**



Sources: State Bank of Pakistan and Economic Affairs Division

[31] During FY23, the average SOFR increased by 396 bps, whereas LIBOR for 12-month US dollar rose by 247 bps.
[32] See Annual Report 2021-2022 (State of Pakistan's Economy) for explanation of External Debt Sustainability.

abroad, which led to decrease in worker's remittances (see **Chapter 6** for details).

It is important to highlight that the improvement in EDS-to-FEE and EDS-to-EE shown in FY22 had resulted from decrease in EDS due to restructuring of debt under the DSSI and uptick in both exports and remittances. Nonetheless, the short-term public external debt (STPED) ratios to reserves and external debt improved in FY23 on the back of lower outstanding short-term debt at the end of FY23. The reduction in short-term debt was primarily due to retirement of around US$ 1.2 billion short-term multilateral debt. This offset the effect of lower FX reserves. Resultantly, Short Term Public External Debt (STPED)-to-Public External Debt and Liabilities (PEDL); STPED-to–total liquid reserves and STPED-to- SBP net reserves showed significant improvement **(Figure 5.16b)**.