4 Fiscal Policy & Public Debt

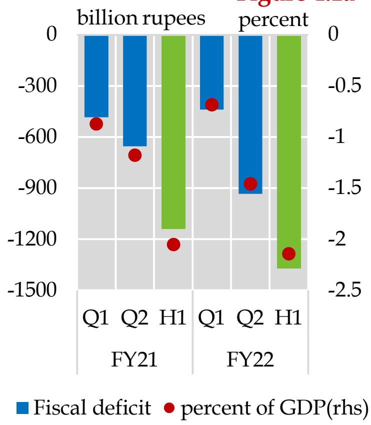
Fiscal indicators slightly deteriorated during H1-FY22 compared to the same period last year, as the primary surplus edged down. A sharp rebound in non-interest expenditures outweighed an otherwise decent increase in revenues. Provinces continued with their fiscal consolidation efforts and delivered a combined surplus of 0.8 percent of GDP in H1-FY22, which helped in containing the overall fiscal deficit. Quarterly analysis shows that deterioration in fiscal indicators was concentrated in Q2-FY22. The fiscal deficit more than doubled while the primary balance recorded a deficit in Q2-FY22. This was despite a sizeable increase in tax collection that neutralized the impact of a decline in non-tax revenues. Specifically, FBR taxes posted a notable import-led increase during the H1-FY22. Social protection grants and subsidies to power sector led to a sharp rise in current spending. Interest payments on debt also increased during Q2-FY22 due to a persistent rise in the outstanding debt stock and increasing interest rates. The accumulation of public debt gained pace during H1-FY22. Revaluation losses due to the depreciation of PKR against the US Dollar contributed almost 60 percent of the increase in public debt. The maturity profile of domestic debt lengthened with an increase in the stock of variable rate long-term instruments. This, however, increased the debt-servicing burden amid increasing interest rates. External debt servicing increased in H1-FY22 amid a scheduled repayment of US$ 1 billion Sukuk in Q2-FY22.

4.1 Fiscal Trends and Policy Review

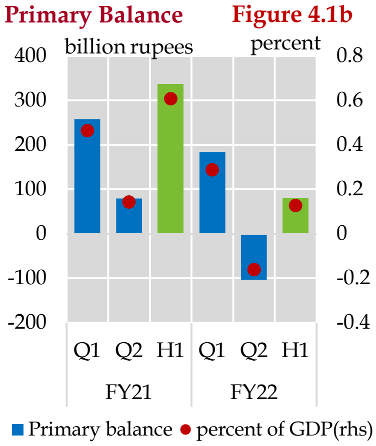
The fiscal deficit remained unchanged at 2.1 percent of GDP in H1-FY22 – the level seen in the same period last year (**Figure 4.1 a and Table 4.1**). However, a sharp rebound in non-interest spending outpaced a strong increase in tax collection, narrowing the surplus in the primary balance to 0.1 percent of GDP in H1-FY22, from 0.6 percent in the same period last year (**Figure 4.1b**). Provinces met the commitment of fiscal consolidation and posted a combined surplus of 0.8 percent of GDP in H1-FY22, which was higher than last year.

Most of the expansion in expenditures came in Q2-FY22, with increased current spending on social protection grants and subsidies followed by interest payments. Around one-half of the entire increase in current spending during Q2-FY22 stemmed from social protection grants, where Covid vaccine procurement under the Economic Stimulus Package (ESP) and BISP were the key focus areas.

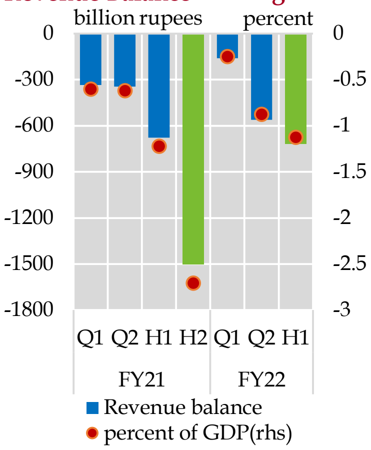
Fiscal Balance Figure 4.1a



Primary Balance Figure 4.1b



Revenue Balance Figure 4.1c



Source: Ministry of Finance

Consolidated Fiscal Indicators **Table 4.1**

billion Rupees, growth in percent

	Q1		Q2		H1		Growth Q1		Growth Q2		Growth H1	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
1. Total Revenue (a+b)	**1,478.7**	**1,808.5**	**1,872.4**	**2,147.5**	**3,351.2**	**3,956.0**	**-0.7**	**22.3**	**7.4**	**14.7**	**3.7**	**18.0**
(a) Tax Revenue	1,122.4	1,532.8	1,333.5	1,658.3	2,455.9	3,191.0	-1.8	36.6	7.6	24.4	6.4	29.9
Of which: FBR taxes	1,010.6	1,398.0	1,199.4	1,521.8	2,210.0	2,919.8	4.8	38.3	6.2	26.9	5.6	32.1
(b) Non-Tax	356.3	275.7	538.9	489.2	895.3	764.9	-15.2	-22.6	6.9	-9.2	-3.1	-14.6
2. Total Expenditure (a+b+c)	**1,963.1**	**2,247.0**	**2,526.0**	**3,081.0**	**4,489.1**	**5,328.0**	**10.6**	**14.5**	**3.0**	**22.0**	**6.2**	**18.7**
(a) Current Expenditure	1,812.6	1,968.2	2,216.8	2,707.5	4,029.3	4,675.7	14.6	8.6	3.6	22.1	8.3	16.0
Of which : Mark-up Payments	742.1	622.7	733.1	830.2	1,475.2	1,452.9	29.8	-16.1	3.3	13.2	15.1	-1.5
Defence	224.5	261.7	262.1	258.8	486.6	520.5	-7.5	16.6	-8.6	-1.3	-8.1	7.0
Non-markup expenditure	1,070.5	1,345.4	1,483.7	1,877.3	2,554.2	3,222.8	5.9	25.7	3.8	26.5	4.7	26.2
(b) Development Expenditure & net lending	215.2	264.7	242.6	306.8	457.9	571.5	46.2	23.0	-25.6	26.4	-3.3	24.8
(c) Statistical Discrepancy	-64.7	14.2	66.6	66.5	1.9	80.6	n-a	n-a	n-a	-0.2	-94.1	
3.Overall budget balance	**-484.3**	**-438.5**	**-653.6**	**-933.3**	**-1,137.9**	**-1,371.8**	**69.3**	**-9.5**	**-7.8**	**42.8**	**14.4**	**20.6**
percent of GDP	*-0.9*	*-0.7*	*-1.2*	*-1.5*	*-2.1*	*-2.1*						
4.Primary balance	**257.7**	**184.2**	**79.5**	**-103.2**	**337.2**	**81.1**	**-9.8**	**-28.5**	**n.a**	**n-a**	**17.7**	**-76.0**
percent of GDP	*0.5*	*0.3*	*0.1*	*-0.2*	*0.6*	*0.1*						
5. Revenue balance	**-333.9**	**-159.7**	**-344.3**	**-560.0**	**-678.2**	**-719.7**	**n-a**	**-52.2**	**-13.1**	**62.6**	**38.6**	**6.1**
percent of GDP	-0.6	-0.2	-0.6	-0.9	-1.2	-1.1						
6. Financing (a+b)	**484.3**	**438.5**	**653.6**	**933.3**	**1,137.9**	**1,371.8**	**69.3**	**-9.5**	**-7.8**	**42.8**	**14.4**	**20.6**
(a) External (Net)	161.4	466.1	293.1	559.5	454.4	1,025.6	-3.1	n-a	-15.6	90.9	-11.5	n-a
(b) Domestic (Net)	323.0	-27.6	360.5	373.8	683.5	346.2	n-a	n-a	-0.3	3.7	42.1	-49.4

Source: Ministry of Finance

Similarly, a large volume of power sector subsidies necessitated by the partial payment of arrears to IPPs under the Circular Debt Management Plan (CDMP) further inflated current spending during Q2-FY22. Interest payments also showed a sizeable increase during Q2-FY22, which mainly reflects the impact of the increasing share of floating rate domestic debt in an increasing interest rate environment. However, to contain the overall level of fiscal deficit, the authorities curtailed the pace of development spending during Q2-FY22.

On the revenue side, a notable increase in FBR tax collection shored up overall receipts during H1-FY22. Whereas non-tax revenues saw a sizeable reduction because of lower collection from petroleum development levy (PDL). Around three-quarters of the increase in tax collection came from import related taxes that reflected the impact of increase in international commodity prices, higher import volumes and PKR depreciation. In addition, expansion in economic activity, a general increase in price level and continued tax administration reforms also supported tax collection. However, the decline in domestic sales tax collection, amid a reduction in GST rates on petroleum products, slightly trimmed the pace of tax collection during Q2-FY22. To protect the domestic consumers from the impact of rising international oil prices, the government substantially reduced GST rates on petroleum products during Q2-FY22.

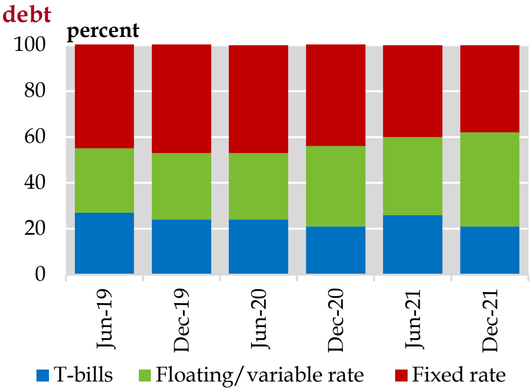
Although a large import-led increase in taxes aided in containing the fiscal imbalance, a long-term improvement in tax revenues hinges on broadening the tax base. The lacunas in tax rules and procedures engender low tax compliance, inhibiting the extension in the tax base (**Box 4.1**). The efforts to improve the tax to GDP ratio are already underway. A greater focus on rationalization of tax exemptions, simplification of tax procedures, and increasing degree of formality will be instrumental for achieving sustainable improvement in tax collection.

In overall terms, the pickup in current spending overshadowed the expansion in revenues, leading to deterioration in fiscal indicators during Q2-FY22. The fiscal deficit more than doubled to 1.5 percent of GDP in Q2-FY22, from 0.7 percent in Q1-FY22 and 1.2 percent of GDP in the same period last year. Similarly, the surplus in the primary balance in Q1-FY22 turned into a deficit, whereas the revenue deficit also widened in Q2-FY22 (**Figure 4.1c**).

With the increased availability of external inflows, the financing requirements of the deficit were mostly met through external resources. Large revaluation losses and deficit financing needs contributed to a sizeable increase in public debt during H1-FY22. In terms of composition, most of the increase in debt was sourced through long-term instruments. However, with the introduction of long-term domestic debt securities carrying floating rates, the composition of domestic debt has shifted towards variable rate instruments replacing the stock of Market Treasury Bills (MTBs) and fixed rate debt (**Figure 4.2**). While this has improved the overall maturity profile of public debt, the interest-rate risk has intensified as most of the funds are contracted on variable/floating rates in an interest rate rising environment.

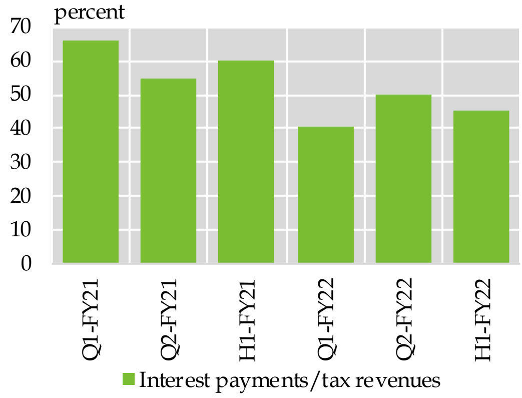
Keeping a balance between lengthening of maturity profile and repricing risks is important to ensure debt sustainability.

Increasing Share of Floating/Variable Rate Domestic debt **Figure 4.2**



Source: State Bank of Pakistan

Debt Repayment Capacity **Figure 4.3**



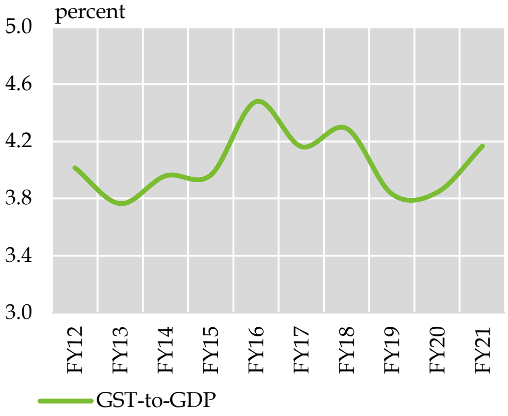
Source: Ministry of Finance, State Bank of Pakistan

Already, with the increasing share of variable-rate paper, the debt servicing capacity of the country as measured by interest payments-to-tax revenues started to deteriorate in Q2-FY22 (**Figure 4.3**). Furthermore, there is a need to diversify the financing options to keep a check on the cost of borrowing. This can be achieved by reforms to deepen the debt market by focusing on non-bank financing resources, e.g., pension funds, corporations, etc.

Box 4.1: Tax Exemptions Erode the Tax Base of General Sales Tax (GST) in Pakistan

Pakistan has a large dependence on GST for mobilizing tax revenues like other developing economies. The country's GST revenues slightly increased from 4.0 percent of GDP in FY12 to 4.2 percent in FY21, which was accompanied by an increase in the tax rates from 16 percent to 17 percent (**Figure 4.1.1**).[1] In overall terms, the share of GST collection in total taxes almost remained unchanged at 41 percent during this period. An international comparison suggests that while the GST rate in Pakistan is close to the median of the peer countries, tax collection is lower by international standards (**Figure 4.1.2**). This lackluster performance is driven by a range of issues, including extensive tax exemptions, weak tax administration and low tax compliance. These factors have impaired the efficiency of the country's GST regime by corroding the tax base. In this background, this box estimates the efficiency of GST in Pakistan to evaluate the impact of these structural bottlenecks on tax collection.

Performance of GST in Pakistan **Figure 4.1.1**



Source: Federal Board of Revenue

The efficiency of GST is the ratio of actual GST revenues mobilized in a year with the potential revenues that could be collected if the tax was perfectly enforced at the standard rate, on all consumption, in the absence of exemptions. This notion is referred to as C-efficiency in the literature and is measured as follows: $E^c = \frac{V}{\tau_s C}$

where V is VAT revenues, τ_s is the standard tax rate, C is consumption and E^c shows C-efficiency. C-efficiency is the ratio of actual VAT revenues with the product of standard tax rate and consumption [Ebrill et al (2001), Keen (2013)].[2,3] A value of 100 indicates the best possible case, where all consumption is taxed at a uniform rate. A lower value of E^c indicates departure from a standard tax rate on consumption, tax avoidance, exemptions and other administrative issues. Likewise, a value greater than 100 indicates double taxation arising from levies on both intermediate and final consumption and the inclusion of investment in the VAT base. Thus, revenue mobilization in countries having similar tax rates may differ because of variations in the efficiency of the tax system.

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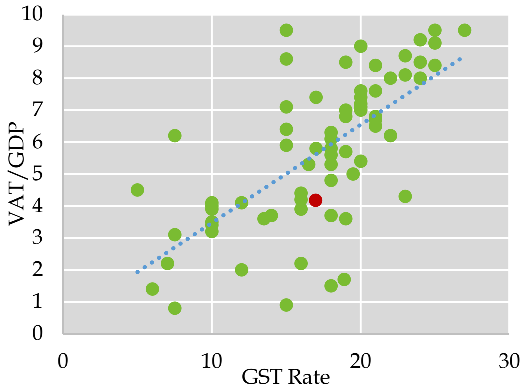
[1] During the economic slowdown of FY19 and the Covid-led contraction of FY20, GST collection fell to 3.8 percent of GDP.
[2] The data for consumption is obtained from National Income Accounts.
[3] Ebrill, L. P., Keen, M., and Perry, V. J. (2001). Understanding the Revenue Performance of VATs. In The Modern VAT. International Monetary Fund; M. Keen (2013). The anatomy of the VAT. Working Paper/13/111. Fiscal Affairs Department. Washington D.C.: IMF;

An International Comparision of GST Rates **Figure 4.1.2**



Sources: OECD Revenue Statistics & Trading Economics

A large strand of literature has used the concept of C-efficiency to evaluate the performance of value-added taxes (VAT). For instance, Wahid, (2010) estimated average C-efficiency of GST in Pakistan during FY00-10 to be at 28 percent and identified that multiple tax rates and a high volume of tax exemptions lead to low tax efficiency in Pakistan.[4] Similarly, Cevic (2016) estimated that C-efficiency of GST in Pakistan increased from 0.11 in 1990 to 0.23 in 2015 and highlighted that a low C-efficiency of GST in Pakistan reflects a significant use of tax exemptions.[5] Ueda (2017) analyzed the key drivers of C-efficiency of VAT revenues in advanced economies and identified that variations in C-efficiency correlates with output gap.[6] The literature suggests that the impact of GST taxes on economic growth depends on tax design. An increase in GST revenues through an improvement in C-efficiency is considered to be growth enhancing compared to general increase in tax rates [Ormaechea, et al (2019)].[7] C- efficiency is a commonly used indicator for measuring revenue performance across countries. OECD publishes the VAT efficiency ratio in the annual publication on *'Consumption Tax Trends'* OECD (2020).[8]

Based on the formula, the C - efficiency of Pakistan's GST revenues oscillated between the range of 24 to 29 percent during FY12-21, showing little variation. For FY21, the ratio stood at 26 percent with a marginal improvement in FY19 and FY20 (**Figure 4.1.3 a, b and c)**). This indicates that a one point GST was associated with 0.26 percentage points increase in the GST-to-GDP ratio in FY21. This implies that during FY21, 74 percent of the potential GST revenue was not collected because of inefficiencies of the tax system such as tax exemptions, low compliance, and issues in tax administration. An international comparison shows that while the C - efficiency of GST in Pakistan is better than the worst performing African countries, it is one of the lowest in Asia, and is also below the least efficient VAT systems in the EU and OECD countries (**Figure 4.1.4**)[9].

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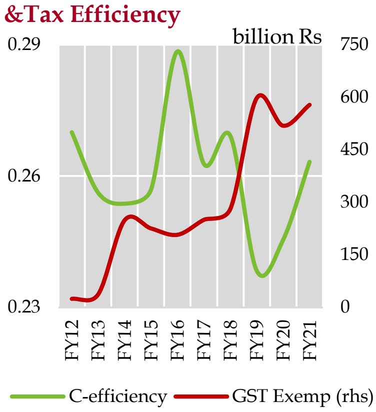
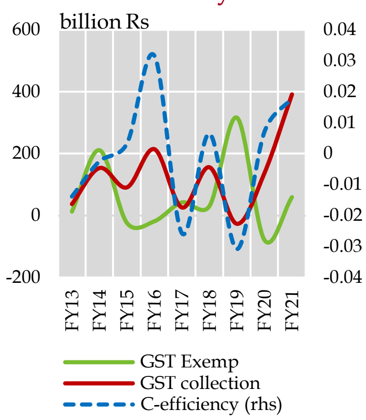
[4] U. Wahid (2010). Economic Analysis of the Reformed General Sales Tax/VAT in Pakistan. Volume 10 No.1. FBR Quarterly Review. Strategic Planning and Research & Statistics Wing. Islamabad: Federal Board of Revenue. Federal Board of Revenue.
[5] M. S. Cevik (2016). Unlocking Pakistan's revenue potential. Working Paper/16/182. Fiscal Affairs Department. Washington D.C.: IMF;
[6] M. J. Ueda (2017). The evolution of potential VAT revenues and C-efficiency in advanced economies. Working Paper/17/158. Fiscal Affairs Department. Washington D.C.: IMF;
[7] Ormaechea, M. S. A., & Morozumi, A. (2019). The value added tax and growth: Design matters. Working Paper/19/96. Institute for Capacity Development. Washington D.C.
[8] OECD (2020), Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues, OECD Publishing, Paris, https://doi.org/10.1787/152def2d-en.
[9] OECD Revenue Statistics, 2020, available at: www.stats.oecd.org/Index.aspx?DataSetCode=RS_GBL, accessed on January 15, 2022.

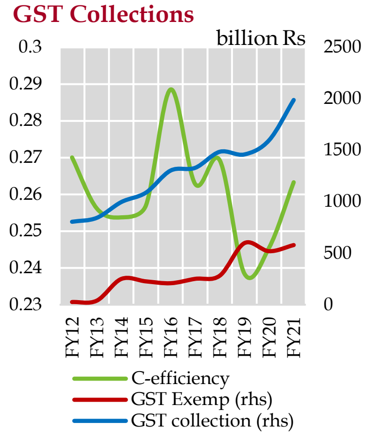
GST Exemptions &Tax Efficiency **Figure 4.1.3a**



Trend in GST Follows C-efficiency **Figure 4.1.3b**



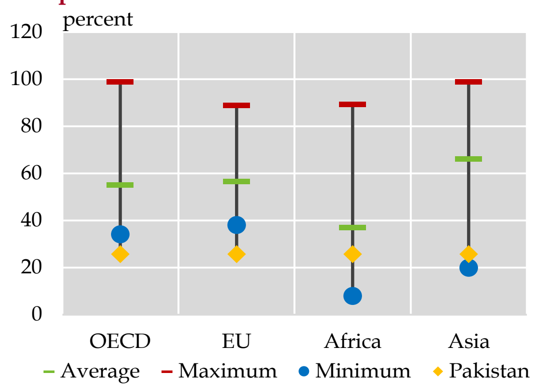
Key Drivers of GST Collections **Figure 4.1.3c**



Source: FBR, SBP estimates

The trend of the GST revenues and its key drivers shows that C- efficiency had a large bearing on GST collection during FY12-21. This implies that GST collection can be enhanced by improving the C-efficiency of tax system without introducing a general increase in tax rates. A long-term comparison shows that a significant increase in GST exemptions during FY12-21 hampered the C-efficiency of GST during this period. For instance, five export-oriented sectors (textile, leather, carpets, sports goods and surgical goods) had been enjoying zero-rating since FY12. In FY19, the revenue impact of these exemptions stood at Rs 86.7 billion. To improve the revenue generation, these exemptions were withdrawn in FY20, which led to Rs 73 billion reduction in tax exemptions during FY20.

C-Efficiency of VAT - Country Comparison **Figure 4.1.4**



Source: OECD Revenue Statistics & Trading Economics

These exemptions reduced the taxable consumption and narrowed the tax base for GST; hence, the years with increase in exemptions are marked by a decline in c-efficiency. Moreover, in Pakistan, efforts to improve tax administration and broaden the tax base are already underway. A sustained focus on rationalization of tax exemptions, expanding the tax base and improved tax administration would be instrumental in ensuring a long-term increase in tax revenues.

4.2 Revenues

Revenue collection posted a notable increase of 18 percent in H1-FY22, compared to 3.7 percent last year. The entire increase came from tax revenues, which offset the 14.6 percent decline in non-tax revenue (NTRs) during this period (**Table 4.2**). In terms of quarterly performance, the growth in tax receipts marked a slight slowdown in Q2-FY22, compared to Q1-FY22. On the other hand, NTR receipts somewhat improved during Q2-FY22.

The slowdown in tax receipts during the Q2-FY22 mainly emanated from decline in

Consolidated Revenue Collection **Table 4.2**

billion Rupees, growth in percent

	Collection						Growth					
	Q1		Q2		H1		Q1		Q2		H1	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
Total Revenue (1+2)	**1478.7**	**1808.5**	**1872.4**	**2147.5**	**3351.2**	**3956.0**	**-0.7**	**22.3**	**7.4**	**14.7**	**3.7**	**18.0**
1. Tax Revenue (a+b)	1122.4	1532.8	1333.5	1658.3	2455.9	3191.0	5.0	36.6	7.6	24.4	6.4	29.9
(a) Federal	1010.6	1398.0	1199.4	1521.8	2210.0	2919.8	4.8	38.3	6.2	26.9	5.6	32.1
(b) Provincial	111.8	134.8	134.1	136.4	245.9	271.2	7.0	20.6	22.0	1.8	14.7	10.3
2. Non Tax Revenue	356.3	275.7	538.9	489.2	895.3	764.9	-15.2	-22.6	6.9	-9.2	-3.1	-14.6

Source: Ministry of Finance

domestic sales tax collection. Specifically, the GST collection on POL products showed a decline because of both a reduction in GST rate as well as a slowdown in POL sales. On other hand, the pace of contraction in NTRs slightly reduced in Q2-FY22 with an increase in PDL rates on POL products.

FBR Collections

During H1-FY22, FBR tax collection posted a 32.5 percent expansion, against a 5.3 percent increase in the same period last year (**Table 4.3**). This was despite a decline in GST collection on the domestic stage during Q2-FY22. Import related taxes – GST and custom duty – had a major share in this increase (**Table 4.4**). In addition, improvement in economic activity relative to last year and continued tax administration efforts further augmented this increase. These factors helped FBR surpass the half-yearly collection target by Rs 285 billion. Tax collection during H1-FY22 stood at 50 percent of the annual budgeted target, which exceeded the level seen in the past few years – FY20 being an exception, when the target was revised down twice amid outbreak of Covid-19 (**Figures 4.4 and 4.5**).

Tax administration efforts

Tax authorities stepped up tax administration reforms during H1-FY22 with an aim to improve administrative efficiency,

FBR Tax Collection **Table 4.3**

billion Rs, growth in percent

	Collection						Growth					
	Q1		Q2		H1		Q1		Q2		H1	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
FBR Taxes (a+b)	**1,010.2**	**1,396.4**	**1,193.8**	**1,523.4**	**2,204.0**	**2,919.9**	**4.8**	**38.2**	**5.7**	**27.6**	**5.3**	**32.5**
(a) Direct Taxes	362.7	481.4	463.5	539.9	826.2	1,021.4	2.0	32.7	8.1	16.5	5.3	23.6
(b) Indirect Taxes	647.6	915.0	730.3	983.5	1,377.8	1,898.5	6.4	41.3	4.3	34.7	5.3	37.8
Import related	390.1	644.2	452.7	725.3	842.8	1,369.5	3.7	65.1	13.5	60.2	8.8	62.5
Customs Duties	154.2	218.8	179.9	258.4	334.1	477.2	-0.9	41.9	4.3	43.6	1.8	42.8
Sales Tax	434.9	625.3	481.9	649.7	916.8	1,275.0	7.7	43.8	6.0	34.8	6.8	39.1
Imports	235.9	425.4	272.7	466.9	508.6	892.3	7.0	80.4	20.5	71.2	13.8	75.4
Domestic	199.0	199.9	209.1	183.8	408.1	383.7	8.1	0.4	-7.8	-12.1	-0.7	-6.0
Federal Excise	58.4	70.9	68.5	75.4	126.9	146.3	18.8	21.4	-6.2	10.1	3.8	15.3

Source: Federal Board of Revenue

Import Related Taxes during H1 **Table 4.4**

billion Rs, growth in percent

			Growth	
	FY21	FY22	FY21	FY22
Import related taxes	**937.3**	**1,505.1**	**21.0**	**60.6**
Sales tax (imports)	508.6	892.3	13.8	75.4
Customs duty	334.1	477.2	3.0	42.8
WHT (imports)	90.8	132.4	-14.2	45.8

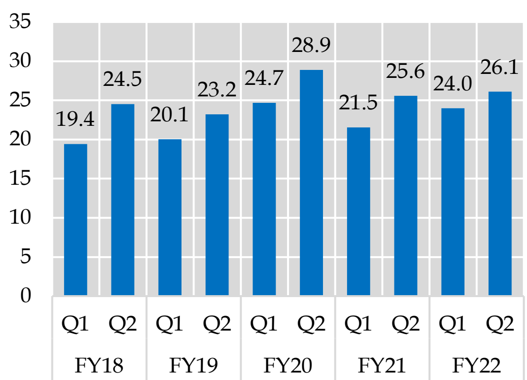
Source: Federal Board of Revenue

limit tax evasion and ensure ease of doing business.

Some of the important measures include: (i) Introduction of Track and Trace system (TTS) for tobacco and sugar sectors to facilitate documentation of the economy and address tax evasion in these sectors (**Box 4.2**);[10] (ii) Initiating integration of large retailers on POS system. FBR introduced POS invoicing system in FY21 by integrating tier 1 retailers. To improve documentation and expand tax base, this system is now extended to large retailers. A total of 1572 retailers were integrated in this system with installation of 14,160 POS machines during FY21.[11] In continuation of these efforts, FBR has targeted to integrate the largest 500 retailers in this system in FY22; and (iii) Introduction of a single sales tax portal in collaboration with the provincial revenue authorities. This step will reduce the cost of doing business by containing the time and expense of tax compliance. For instance, this portal will allow taxpayers to file single monthly sales tax returns instead of six returns on provincial revenue portals, previously; (iv) FBR has introduced Pakistan Single Window (PSW) in order to reduce clearance times for legitimate trade; (v) the mechanism of e-hearing has been formulated to provide contact-less tax administration resulting in reduced compliance time.

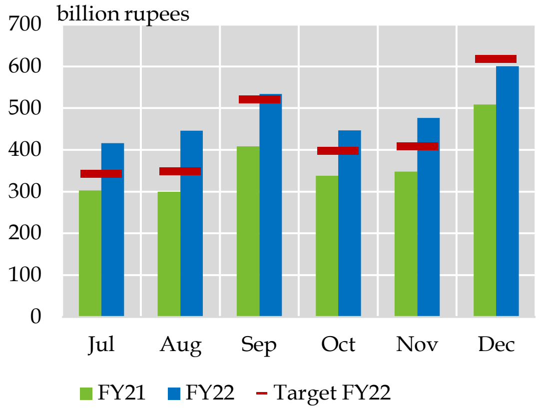
In addition, the authorities continued compliance with the Financial Action Task Force (FATF) action plans regarding anti-money laundering/countering the financing of terrorism (AML/CFT) for Designated Non-Financial Business and Professions (DNFBPs). In this backdrop,

Revenue Collection as Percent of Target **Figure 4.4**



Source: Ministry of Finance

Tax collection Against Target **Figure 4.5**

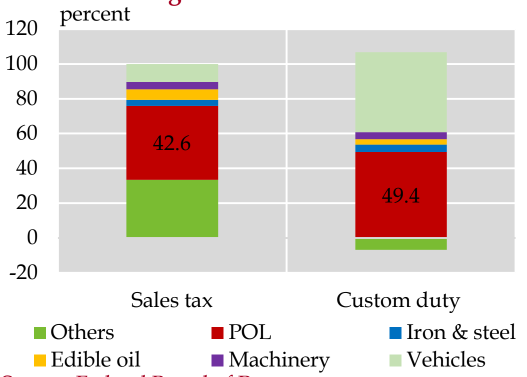


Source: Federal Board of Revenue

[10] TTS on tobacco and sugar was introduced October and November 2021 respectively.

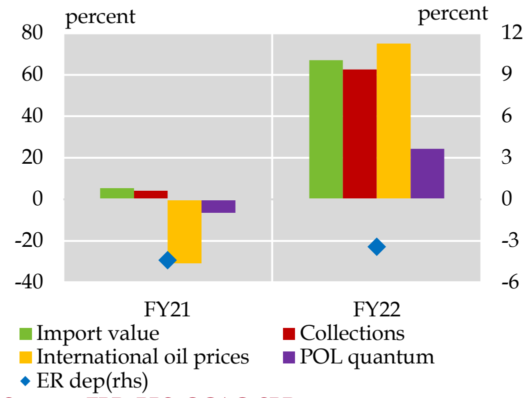
[11] FBR Biannual Review July-December 2021-22 (Vol. 21, No. 1) - A Review of Resource Mobilization Efforts of Federal Board of Revenue

Major Revenue Spinners in Indirect Taxes - Share in Growth during H1 **Figure 4.6**



Source: Federal Board of Revenue

Drivers of Increase in Import Related Taxes during H1 (YoY Growth) **Figure 4.7**



Sources: FBR, PBS, OCAC, SBP

the FATF plenary had approved two actions specific to Designated Non-Financial Business and Professions in June 2021, which are being regulated by the FBR. Since then, the FBR has launched an online portal and a mobile app to facilitate the DNFBPs in implementing AML/CFT regulations, including generating Suspicious Transaction Reports. Meanwhile, the FBR has carried out number of inspections of DNFBPs to minimize tax evasion and imposed fines on non-compliance.[12]

Indirect taxes displayed a strong performance

Collections from indirect taxes grew strongly during H1-FY22. The entire increase came from import related taxes, whereas domestic sales tax collection tapered off during this period.

Specifically, around one-half of the surge in these taxes came from POL products alone during H1-FY22 (**Figure 4.6**). This increase shows the combined impact of rising import volumes, surge in international oil prices as well as PKR depreciation (**Figure 4.7**).

Box 4.2: Track and Trace System - A step towards containing tax evasion in Pakistan

FBR implemented Track and Trace System (TTS) on tobacco and sugar sectors during Q2-FY22, with an aim to improve tax collection. TTS ensures electronic monitoring of goods through the entire supply chain from production/imports to retailers to curb tax evasion and illegal production/supply of goods. It is implemented by means of Unique Identification Marking (UIM) or tax stamps that carry digital features to ensure electronic traceability of goods. These stamps are applied to each batch of the goods produced and supplied to the market and help in differentiating between the registered and unregistered supplies. This system aids tax authorities to check supply of smuggled, counterfeit and unregistered products.

12. Source: FBR Press Release dated October 21, 2021, available at https://www.fbr.gov.pk/pr/fbr-completes-fatf-actions-on-dnfbps-ahead-of/163201, accessed on January 15, 2022.

Furthermore, TTS provides a near real time data of production volumes at a centralized point to the tax collection authority.

Various forms of monitoring systems to check tobacco trade have existed for more than a decade, globally. As of now, track and trace system is being used in over 80 countries worldwide.[13] However, Protocol to Eliminate Illicit Trade in Tobacco Products (ITP) from the WHO Framework Convention on Tobacco Control (FCTC) came into force in 2018.[14] The ITP requires all parties to introduce track and trace system to monitor tobacco trade.

The absence of a reliable system to monitor and collect information about production/sales activities has remained a significant impediment in the tax collection efforts of FBR. Particularly, a sizeable amount of revenues from indirect taxes at domestic stage (GST and FED) is lost each year because of under-reporting of production and sales of various goods. For instance, according to FBR estimate, Rs 70 billion tax evasion takes place each year in tobacco sector alone. [15,16] To tap these potential revenues, FBR was in the process of introducing TTS since the past few years. However, the system could not be introduced because of various challenges such as lack of expertise and legal issues.[17] During Q2-FY22, the authorities successfully implemented this monitoring system on tobacco and sugar sectors, with an aim to extend coverage to fertilizer, cement and beverages in the near future.

FBR specified the rules for TTS in 2019, in an earlier attempt to introduce the system.[18] According to these rules, the TTS service provider is responsible for ensuring installation of the stamping machines at all the production facilities and import stations of the specified sectors. These machines have to be integrated with the centralized system (centralized control room) at FBR, for recording the production volumes in real time. Every manufactured package (including a tin, container or bottle, of the specified goods) is required to be stamped before dispatch from the production premises. The tax stamp could be a banderole, sticker, label, barcode, etc. While at the manufacturer end, all the production facilities have to be made available for installation of the system, routine operations and inspection of the system. Also, the manufacturer is responsible for providing the requisite quantity of tax stamps/stickers.

FBR established an enforcement and monitoring wing named Inland Revenue Enforcement Network (IREN) in February 2019 to ensure the smooth functioning of TTS with the aim to curb tax evasion in these specific sectors. The IREN mobile squads check the supplying vehicles and storage places to make sure

[13] Source: FBR News Letter, ReveNews, issue month – November 2021, available at: https://download1.fbr.gov.pk/Docs/2022161614145437ReveNewsIssueNovember2021Eng.pdf

[14] World Health Organization, available at: https://www.who.int/fctc/protocol/illicit_trade/protocol-publication/en/, https://www.who.int/fctc/mediacentre/news/2018/protocol-officially-entering-into-force/en/, accessed on January 15, 2022.

[15] FBR News Letter, ReveNews, issue month – November 2021 https://download1.fbr.gov.pk/Docs/2022161614145437ReveNewsIssueNovember2021Eng.pdf

[16] The indirect tax revenues (at domestic stage) from tobacco sector stood at Rs 135.3 billion during FY21.

[17] TTS was initially introduced in 2019, however, the system could not be implementation because of litigation issues https://download1.fbr.gov.pk/SROs/2019226162246842SRO250of2019SalesTaxRules2006.pdf, https://www.fbr.gov.pk/fbr-clarifies-the-delay-in-the-implementation-of-track--trace-system/132239, accessed on January 15,2022.

[18] S.R.O. 250(I)/2019 dated 26th February, 2019

that the products are stamped; the products without tax stamps are confiscated. For instance, IREN has detected a sizeable amount of tax evasion in tobacco and sugar sectors during Jul- November 2021[19].

Import Related Taxes in Indirect Taxes during H1 **Table 4.5**

billion rupees, growth in percent

			Growth	
	FY21	FY22	FY21	FY22
Sales tax (A)	**508.6**	**892.3**	**9.7**	**75.4**
POL	109.8	273.2	-14.0	148.9
Iron and Steel	59.4	72.1	10.7	21.4
Edible oil	31.1	55.0	28.1	76.8
Machinery	33.3	49.3	4.6	48.2
Vehicles	28.2	67.6	21.6	140.1
Custom duty (B)	**334.1**	**477.2**	**3.0**	**42.8**
POL	40.3	110.9	-11.1	175.1
Vehicles	36.9	102.6	20.7	177.9
Iron and Steel	27.3	33.4	20.0	22.5
Machinery	17.7	23.6	7.7	33.4
Edible Oil	15.9	20.3	3.6	27.5
Total (A+B)	**842.8**	**1,369.5**	**4.1**	**62.5**

Source Federal Board of Revenue

Similarly, the rising automobiles' demand in the domestic market and the ensuing increase in import of CKD and CBU vehicles also bolstered import related taxes during the entire H1-FY22 (**Table 4.5**). Further impetus in tax collection came from food imports, which was mainly price-led; higher prices of food items in global markets boosted import values and helped increase collection this year.

Reduced GST rates on POL dragged domestic tax collection

Domestic sales tax collection dropped by 6.2 percent in H1-FY22 compared to a 3.2 percent expansion last year (**Table 4.6**). This decline was skewed toward Q2-FY22 when the GST rate on petrol was brought down to zero in December 2021 (**Figure 4.8**). In

Domestic Taxes during H1 **Table 4.6**

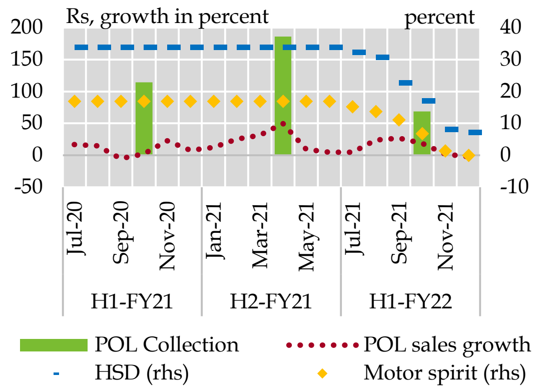
billion rupees, growth in percent

			Growth	
	FY21	FY22	FY21	FY22
Sales tax (A)	**408.1**	**382.7**	**-0.6**	**-6.2**
POL	114.6	68.9	-16.1	-39.8
Electricity	77.0	78.7	37.0	2.3
Cement	27.3	31.0	147.0	13.6
Sugar	14.2	17.8	-14.1	25.9
Cigarettes	11.2	14.0	23.9	25.0
Vehicles	4.8	2.4	27.8	-50.0
FED	**126.9**	**146.3**	**1.5**	**15.3**
Cigarettes	44.7	52.7	26.1	18.1
Cement	37.5	35.1	5.8	-6.5
Vehicles	1.9	9.4	n-a	408.3
Total (A+B)	**535.1**	**529.0**	**-0.1**	**-1.1**

Source: Federal Board of Revenue

addition, weakening sales of POL products during Q2-FY22 further dented collection in the second quarter. (**Table 4.7**). Notably, the contraction in the GST on POL at the domestic stage alone offset the expansion in

GST (Domestic) Collections Declined on Account of Lower Rates **Figure 4.8**



Source: FBR and OCAC

[19] Rs. 178 million worth of illegal cigarettes were confiscated during Jul-Nov FY22. Similarly, in case of sugar, 172 bags of unstamped sugar were seized by IREN in November 2021.

Economic Growth Indicators **Table 4.7**

percent

	LSM		Auto Sales		POL Sales		Electricity		Steel		FMCG	
	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
Q1	-2.6	9.7	9.9	57.3	10.5	17.9	1.3	7.9	26.0	29.3	23.0	23.1
Q2	5.5	5.6	43.7	46.2	11.5	6.3	4.2	11.7	53.2	43.2	17.8	22.3

Sources: PBS, PAMA,OCAC and SBP

collection from electricity, sugar, electronics and cigarettes. However, the scale of economic activity as well as general price level remained higher compared to last year that provided some support to GST collection. Furthermore, the implementation of Track and Trace System to curb the revenue loss aided collections from sugar and cigarettes at domestic stage in H1-FY22.

In the case of FED, the collections rose to Rs 146.3 billion in H1-FY22 compared to 126.9 billion last year. Cigarettes, being the major contributor, helped increase the overall FED collections, followed by vehicles. Furthermore, the continued momentum of the sales of vehicles in H1-FY22 also boosted these collections.

Higher collection from WHT and voluntary payments improved direct tax collection

The continued administrative efforts and income tax reforms shored up direct tax collection during H1-FY22. Around one-quarter of the overall surge in FBR taxes came from direct taxes in this period. The main contribution to this growth came from withholding taxes (WHT) followed by voluntary payments.

Quarterly analysis reveals some slowdown in the pace of direct tax collection in Q2-FY22 compared to Q1-FY22. This partly reflects the impact of concentration of filing of income tax returns during Q1-FY22 as the last date for the filing of income tax returns fell due on 15th October this year. In overall terms, taxpayers filed 2.6 million returns by the last date, with a tax payment of Rs 48.6 billion. Out of this, 1.86 million returns were filed in Q1-FY22 with a tax payment of Rs 39 billion compared to Rs 6.9 billion in corresponding period last year.[20]

In overall terms, voluntary payments grew by 21.5 percent in H1-FY22, compared to 3.4 percent in H1-FY21 (**Table 4.8**). Collections on demand posted a sharp decline in H1-FY22 against the same period last year. This decline is attributed to an increased recovery period for the amount claimed in demand notices. This relaxation aimed at providing a conducive environment to the businesses.[21] Meanwhile, the recent Corporate Income Tax (CIT) reforms also led to an increase in direct

[20] The filing of income tax returns still continues with total number of returns at 3 million and tax payment of Rs 69.8 billion by end January 2022, against 3.3 million returns filed in FY21 with payment of 52.7 billion.

[21] During Q2-FY22, the recovery date of the taxable amount claimed in demand notices was extended beyond 90 days, compared to maximum 30 days in Q1-FY22.

taxes (net of refunds). This can be seen from a 90.3 percent decline in the amount of refunds during H1-FY22 compared to same period last year. [22]

Within WHT, most of the expansion in tax collection stemmed from imports, followed by salaries and contracts. WHT from imports contributed the most (7.3 percentage points) in overall withholding taxes, followed by salaries and contracts (**Figure 4.9**). As discussed earlier, the higher rupee value of imports propped up WHT collection. The rise in contracts mirror the expansion in construction activity in private as well as public sector. Similarly, the increase in the salaries of government employees as announced in the FY22 budget strengthened WHT collection from salaries. On the other hand, collection from telephone and cash withdrawal declined following the reduction of 5 percent WHT rate on telephone and removal of 0.6 percent tax on cash withdrawals for non-filers as announced in the budget**.**

Non-tax Revenues

Non-tax revenues (NTRs) posted a decline of 14.6 percent in H1-FY22 compared to a 3.1 percent decline last year (**Table 4.9**).

This decline was explained mainly by the decrease in collections from Petroleum Development Levy (PDL) and mark-up payments, which more than offset the increase in other NTR components. Consequently, only a third of the budget estimate was collected during H1-FY22 compared to 55 percent last year.

Direct Taxes during H1 **Table 4.8**

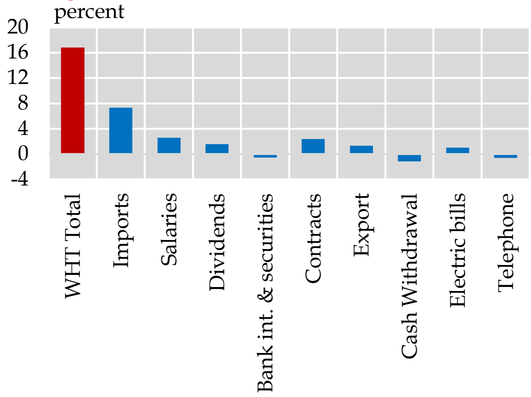
billion rupees, percent

	FY21	FY22	Growth FY21	Growth FY22
Collection on demand	**38.5**	**20.3**	**95.3**	**-47.3**
Voluntary payment	**256.7**	**312.0**	**3.4**	**21.5**
Returns	45.1	66.7	n-a	47.8
Withholding Taxes	**569.3**	**665.1**	**4.6**	**16.8**
Imports	90.8	132.4	-14.2	45.8
Salaries	69.8	84.5	21.4	21.0
Dividends	30.1	39.1	-1.1	30.1
Bank interest & securities	67.6	64.5	19.3	-4.6
Contracts	120.3	133.8	6.7	11.2
Export	20.2	27.8	1.7	37.5
Cash withdrawal	6.9	0.3	-19.5	-96.3
Electricity bills	25.9	31.8	4.1	22.9
Telephone	30.8	27.4	13.8	-11.0
Other WHT	190.6	210.8	5.1	10.6
Total direct taxes	**829.2**	**1,021.4**	**5.6**	**23.2**

Source: Federal Board of Revenue

The decline in NTRs was observed in both the quarters of FY22. However, the pace of this deterioration was lower in Q2-FY22 compared to Q1-FY22. This decline was mainly attributed to lower collections from PDL due to a downward adjustment in PDL rates compared to last year. The authorities

Growth Contribution in WHT during H1 - FY22 **Figure 4.9**



Source: Federal Board of Revenue

[22] Before CIT, the income tax exemptions were claimed in the form of refunds.

Non-tax Revenues (consolidated) **Table 4.9**

billion Rs, growth in percent

	Q1		Q2		H1		Growth		
	FY21	FY22	FY21	FY22	FY21	FY22	Q1	Q2	H1
SBP profits	105.0	109.0	267.5	271.0	372.5	380.0	3.8	1.3	2.0
PTA profits	8.2	30.1	10.5	8.8	18.6	38.9	269.2	-16.1	108.9
Mark-up (PSEs & others)	25.7	19.5	18.3	13.1	44.0	32.6	-24.1	-28.4	-25.9
Royalties on gas & oil	14.6	21.7	20.5	17.3	35.1	39.1	48.5	-15.5	11.2
Dividends	1.5	1.9	10.4	24.1	11.9	26.0	27.3	132.0	118.8
Passport & other fees	3.0	6.1	4.0	4.3	7.0	10.4	106.7	6.8	49.2
Defence	2.9	2.8	3.7	4.9	6.5	7.7	-1.3	34.3	18.6
Petroleum levy	136.4	13.3	139.0	56.7	275.3	70.0	-90.2	-59.2	-74.6
GIDC	5.0	6.5	4.6	4.6	9.5	11.2	30.8	2.1	17.1
Total	**356.3**	**275.7**	**538.9**	**489.2**	**895.3**	**764.9**	**-22.6**	**-9.2**	**-14.6**

Source: Ministry of Finance

had lowered PDL rates during Q1-FY22 to protect consumers from the impact of rising international oil prices. Subsequently, the government managed to collect only 11.5 percent of the budgeted target. However, this relief measure had a large revenue impact; hence, the rates were adjusted up from September 2021 (**Figure 4.10**). Another segment that contributed to the contraction in NTRs was mark-up receipts. These collections dropped on account of a 190 basis points reduction in the mark-up rate charged on development loans to PSEs and provinces.[23]

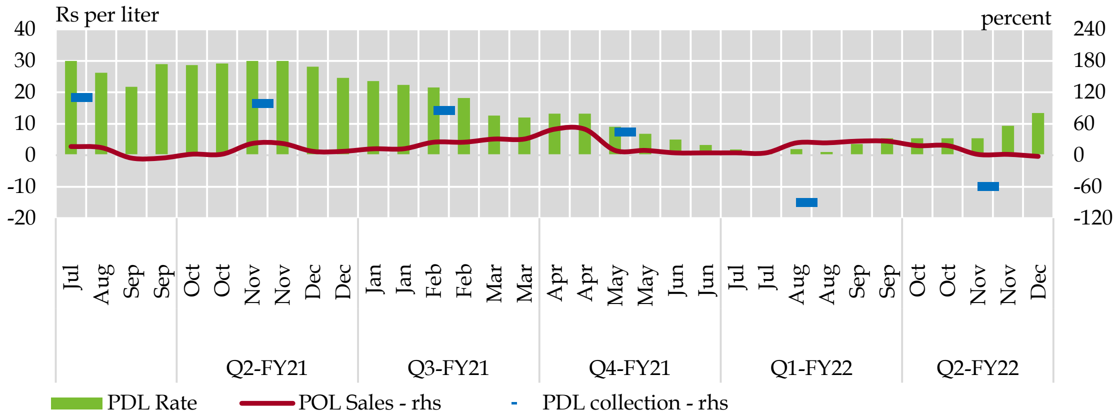
In contrast, the SBP profits remained almost at the last year's level during H1-FY22. The interest earnings from open market operations (OMO) in Q1-FY22 partly offset the impact of net retirement of the government debt stock with SBP. However, in Q2-FY22, the transfer of SBP profits increased as the SBP paid Rs 167 from balance surplus of last fiscal year to the government. It may be recalled that a similar payment was transferred to the government in the same period last year. Moreover, the receipts from dividends also increased in both the quarters of FY22. This rise could be traced to the higher profits of OGDCL and PPL during H1-FY22.[24] The receipts from these two institutions contribute the most (80 percent) of the total dividend income.

4.3 Federal Expenditures[25]

Federal expenditures rose by 20.4 percent during H1-FY22 as compared to 5.0 percent in the corresponding period last year. This was a broad based increase **(Table 4.10),** with a prominent contribution by non-interest spending **(Figure 4.11)**. The quarterly analysis reveals some variations in spending pattern between the two quarters. While the current expenditures edged up strongly during Q2-FY22 (**Figure 4.12**), federal development spending lost steam during Q2-FY22.

[23] https://www.finance.gov.pk/circulars/circular_11102021.pdf, accessed on January 15, 2022.
[24] The earning per share of OGDCL and PPL increased by 63.3 percent and 20.9 percent respectively during Jul-Dec FY22. Also, the dividends disbursed by OGDCL rose by 4.2 percent to 16.1 billion from 15.5 billion last year during this period. (sources: Half Yearly Reports December 2021).
[25] The discussion in this section is based on expenditures excluding statistical discrepancy.

PDL Rates and Quarterly Collections Growth (YoY) **Figure 4.10**



Source: Ministry of Finance

Federal Current Expenditures

Federal current expenditures surged by 19.4 percent during H1-FY22, which is more than twice the growth seen in the same period last year. Most of this increase came in Q2, which was mainly led by expansion in spending on Covid vaccine and grants for social protection followed by subsidies and interest payments **(Figure 4.12)**.

Spending on vaccine procurement and social protection remained robust

The disbursement of grants more than doubled to Rs 548.9 billion in H1-FY22 from Rs 265.2 billion in the same period last year, with most of the expenditures undertaken in Q2-FY22. The major focus areas were spending under Economic Stimulus Package (ESP) and Benazir Income Support Program (BISP). The main thrust of ESP was on supporting Covid related vaccination procurement. In this regard, nearly one-third amount in grants was allocated to National Disaster Management Fund for Covid-19 under ESP. Resultantly, the total number of doses administered reached around 142.7 million up till December 2021, with almost 67.8 million individuals fully and 89.1 million partially vaccinated.

The surge in BISP spending is explained by both an increase in the budget allocation for this program as well as an extension in coverage of beneficiaries. The FY22 Budget earmarked Rs 250 billion for BISP spending, with Rs 50 billion increase against last year. Furthermore, the authorities completed the updation of National Socio Economic Registry (NSER) in October 2021 that increased the coverage of households to around 33 million in 2021.[26] [27] As a result, the spending on social protection especially for

[26] International Monetary Fund (2022). 2021 Article IV Consultation, Sixth Review Under the Extended Arrangement Under the Extended Fund Facility, And Requests For Waivers Of Applicability And Non-observance of Performance Criteria And Rephasing Of Access—Press Release; Staff Report; and Statement by The Executive Director for Pakistan. Country Report No. 22/27. Washington D.C.: IMF.

[27] The last NSER was conducted in 2010-11 that identified 27 million beneficiaries. The government had started to add new beneficiaries on the basis of ongoing updation of NSER since Q3-FY21.

State of Federal Expenditures **Table 4.10**

billion Rs, growth in percent

			YoY growth		FY22		YoY Growth	
	H1-FY21	H1-FY22	H1-FY21	H1-FY22	Q1	Q2	Q1	Q2
Total expenditures* (a+b)	**3077.2**	**3705.7**	5.0	20.4	1540.1	2165.5	9.9	29.3
(a) Current expenditure	**2807.2**	**3351.3**	6.5	19.4	1360.6	1990.7	7.0	29.6
Mark-up payments	1475.2	1452.9	15.1	-1.5	622.7	830.2	-16.1	13.2
Domestic	1357.0	1312.5	21.1	-3.3	571.1	741.4	-16.6	10.3
Foreign	118.2	140.4	-26.4	18.7	51.6	88.8	-9.7	45.4
Defence affairs and services	486.6	520.5	-8.1	7.0	261.7	258.8	16.6	-1.3
Pension	210.5	251.7	-3.8	19.6	110.7	141.0	27.7	13.9
Running of civil govt.	195.4	209.9	-11.1	7.4	89.5	120.5	0.6	13.1
Subsidies	129.0	313.4	23.8	143.0	73.9	239.5	n.a	89.9
Grants to provinces and others	310.6	603.0	10.3	94.1	202.1	400.9	59.9	117.6
Grants to provinces	45.3	54.1	8.0	19.4	32.6	21.5	80.6	-21.2
Grants to others	265.2	548.9	10.7	106.9	169.5	379.4	56.4	141.8
(b) Development expenditure and net lending	270.0	354.3	-8.5	31.2	179.5	174.8	37.6	25.2
Total development expenditure	**243.1**	**288.3**	-14.4	18.6	143.8	144.5	66.4	-7.8
PSDP	232.1	288.3	-15.9	24.2	143.8	144.5	74.3	-3.4
o/w Development grants to provinces	56.6	88.7	46.8	56.5	35.5	53.2	201.5	18.5
Other development expenditure	11.0		35.4	-100.0	0.0	0.0	n.a	n.a
Net lending	**26.9**	**66.0**	144.2	145.3	35.7	30.3	-18.9	-277.5
Provinces	-16.8	59.9	-724.6	-456.3	33.1	26.8	-591.5	-365.9
Others	43.7	6.1	424.9	-86.1	2.6	3.5	-94.9	-150.2

* Excluding statistical discrepancy

Source: Ministry of Finance

BISP increased significantly during this period

The expenditure under the Prime Minister's Kamyab Jawan Youth Entrepreneurship Scheme (PMKJ-YES) also picked up with a disbursement of Rs 27.4 million till November 2021.[28] Furthermore, a food subsidy program was also initiated in November 2021 that aimed at protecting low-income households from the impact of rising food inflation. Under this initiative, 9.6 million families and over 10,000 retail (Kiryana) stores were registered until mid-December 2021.[29]

Power subsidies rose substantially

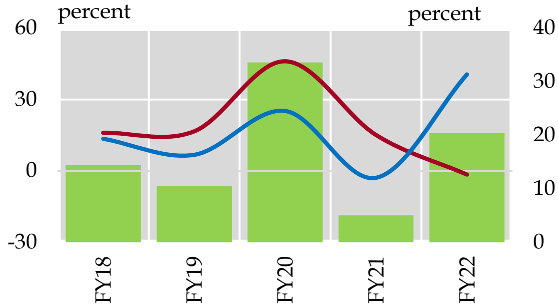
The expenditures on subsidies showed a significant increase during the entire first half. This expansion mainly emanated from power subsidies. The increase was in line with the FY22 Budget estimates that envisaged payment of Rs 266 billion to settle arrears of IPPs/PHPL under the CDMP.

Interest payments moved down slightly during H1-FY22

After rising sharply during FY21, interest payments posted a marginal decline in H1-FY22 because of lower payments on domestic

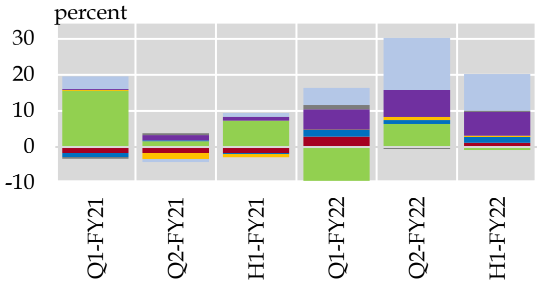
[28] Finance Division (2021). Monthly Economic Update for January 2022. Islamabad: Finance Division
[29] Finance Division (2021). Monthly Economic Update for December 2021. Islamabad: Finance Division

Growth in Federal Spending (H1) **Figure 4.11**



Source: Ministry of Finance

Growth Contribution in Federal Current Expenditures **Figure 4.12**



Source: Ministry of Finance

debt. However, these payments grew significantly during Q2-FY22.

This increase came from an expansion in the government outstanding debt stock amid an increasing interest rate environment during H1-FY22. Moreover, the mark up payments on the foreign debt rose considerably due to the depreciation of PKR against the US dollar.

Pension Spending rose significantly during H1-FY22

Pension expenditures soared by 19.6 percent during H1-FY22 as compared to a decline in H1-FY21. This expansion was underpinned by an increase in pensions of government employees announced in the budget.[30]

Federal Development Expenditures

Federal PSDP increased by 24.2 percent in H1-FY22 in contrast to a decline of 15.9 percent in H1-FY21. This improvement was in line with the budgetary development priorities of the government that aimed at providing further impetus to economic activity. The development preferences were largely focused on the power sector, regional development, and road infrastructure.

However, the federal PSDP spending dropped by 3.4 percent in Q2-FY22, compared to an 18.1 percent decline in the corresponding period last year. A five-year comparison shows that the pattern of quarterly growth in development spending remains volatile during a year **(Figure 4.13).** The government's efforts to contain fiscal figure deficit by slashing spending as well as factors specific to the independent ministries implementing respective PSDP projects are some of the major factors that influence the pace of development spending.[31]

The actual federal PSDP spending during H1-FY22 stood at 32.0 percent of the total annual development outlay announced in

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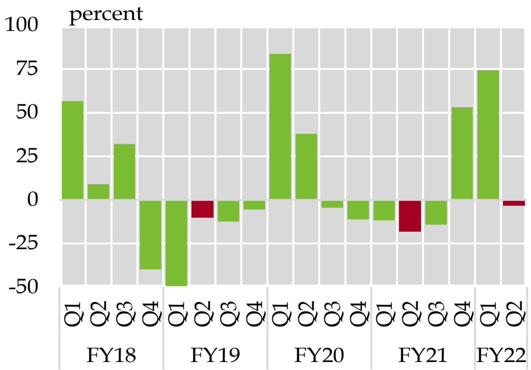
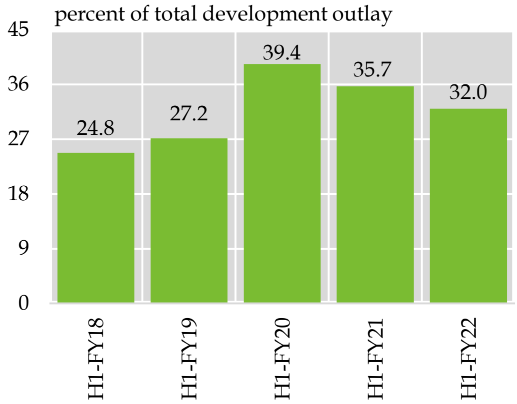
[30] Circular No. 4(1)- Reg.6/2021-486, dated July 8, 2021, Regulations Wing, Finance Division.
Circular No. F.4 (3) R-4/2011 - Revision, dated July 26, 2021, Regulations Wing, Finance Division.
[31] For reference, see Box 4.3 of the SBP Annual Report FY21 on the State of Pakistan's Economy.

Federal PSDP Spending (YoY growth) **Figure 4.13**



Source: Planning Commission

Federal PSDP Spending **Figure 4.14**



Source: Planning Commission

the FY22 budget, which was lower than the last two years **(Figure 4.14).** Furthermore, the actual federal PSDP expenditure was also lower than the benchmark defined in the federal PSDP release strategy.[32]

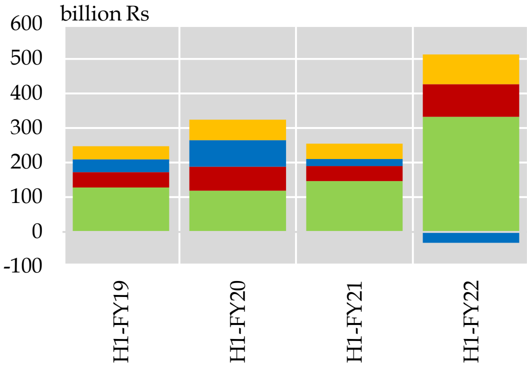
Although the actual spending of federal PSDP declined during Q2-FY22, in overall terms, three areas showed robust spending as seen from PSDP authorization during the second quarter. First, the road infrastructure projects. According to the federal PSDP of 2022, the important projects were Sialkot (Sambrial) – Kharian Motorway (69 km); Improvement, upgradation and widening of Jaglot - Skardu road (S-1, 167 km); dualization & rehabilitation of Karachi - Quetta - Chaman Road (N-25) (460 km); and Hyderabad – Sukkur Motorway (M6). The second priority of federal PSDP during Q2-FY22 was power sector which included Coal Fired Power Project Jamshoro in coordination with Asian Development Bank (ADB), improvement of transmission lines and grid stations of distribution companies in Sukkur and Hyderabad. The third dominant area of federal PSDP authorization was regional development of Kashmir and Gilgit Baltistan that mainly constitutes the block allocation including multiple development projects for these areas. Here it is important to mention that the federal PSDP allocation for AJK and Gilgit Baltistan was around Rs 70.0 billion for FY22, around two-thirds of which is allocated to the block allocation.

4.4 Provincial Fiscal Operations

The consolidated provincial surplus stood at Rs 480.8 billion during H1-FY22, amounting to 0.8 percent of GDP, which was around 84.0 percent of the annual target for FY22. All provinces contributed to the surplus except for KP, which posted a deficit of Rs 32.0 billion **(Figure 4.15)**. A Rs 577.5 billion increase in total provincial revenues offset the Rs 351.9 billion expansion in provincial

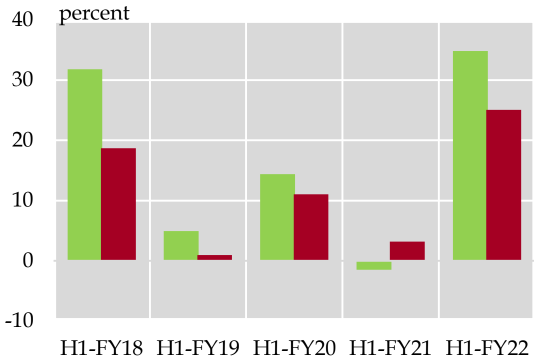
[32] According to the PSDP release strategy, 20 percent of the federal PSDP spending should be spent in the first quarter; 30 percent in the second and third quarters; and 20 percent in the last quarter of every fiscal year. Source: Revised Release Strategy for Funds Allocated for the Public Sector Development Programme (PSDP) 2019-20, Budget Wing, Finance Division.

Provincial Surplus during H1 **Figure 4.15**



Source: Ministry of Finance

Growth in Provincial Revenue and Expenditure **Figure 4.16**



Source: Ministry of Finance

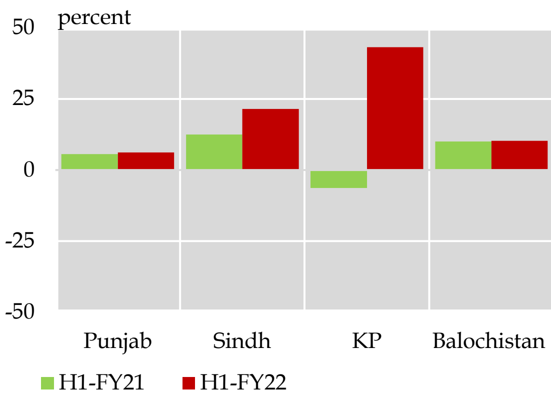
expenditures, driving the overall increase in the surplus **(Figure 4.16)**.

Provincial Revenues

A notable expansion in federal transfers to provinces from the divisible pool resulted in higher provincial revenues. In addition, better revenue collection from provinces' own sources (**Figure 4.17a**) and higher federal grants to provinces further lifted the growth in provincial revenues.

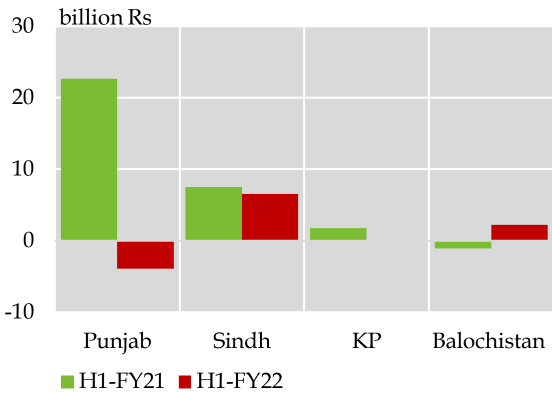
Provincial own revenue grew by 15.6 percent during H1-FY22, against 6.8 percent increase in H1-FY21 **(Table 4.11)**. The increase in own receipts emerged from both tax and non-tax revenues. Within tax revenues, stamp duties followed by sales tax on services were the major drivers of growth. Particularly, an upsurge in stamp duties had a twenty-five percent share in the overall increase in provincial tax receipts during H1-FY22. Most of the increase came from Punjab, followed by Sindh. The expansion in construction activity in the private sector mainly explains

Provincial Own Revenue - YoY growth **Figure 4.17a**



Source: Ministry of Finance

YoY Change in GSTS Collection - Province-wise **Figure 4.17b**



Source: Ministry of Finance

Provincial Fiscal Operations **Table 4.11**

billion Rs, growth in percent

	H1-FY21	H1-FY22	YoY growth H1-FY21	YoY growth H1-FY22	Q1-FY22	Q2-FY22	YoY growth Q1-FY22	YoY growth Q2-FY22
A. Total revenue (a+b+c)	**1,658.3**	**2,235.8**	**-1.5**	**34.8**	**1,077.8**	**1,158.0**	**63.6**	**15.9**
a. Provincial share in fed. revenue	1,280.1	1,694.3	-3.5	32.4	807.5	886.8	60.2	14.3
b. Fed loans and transfers	85.2	202.7	2.3	138.0	101.2	101.5	338.1	63.5
c. Provincial own revenue	293.1	338.8	6.8	15.6	169.0	169.8	28.3	5.3
Taxes	245.9	271.2	14.7	10.3	134.8	136.4	20.6	1.8
Non-taxes	47.2	67.6	-21.2	43.1	34.2	33.4	71.0	22.7
B. Total expenditures (a+b+c)	**1,403.2**	**1,755.0**	**3.2**	**25.1**	**800.9**	**954.2**	**30.3**	**21.0**
a. Current	1,281.0	1,396.2	12.3	9.0	648.0	748.3	14.5	4.6
b. Development	227.7	365.8	3.8	60.7	153.8	212.0	71.2	53.8
c. Statistical discrepancy	-105.5	-6.9	-	-93.4	-0.9	-6.0	-	-94.3
Overall balance (A-B)	**255.1**	**480.8**	**-21.2**	**88.4**	**276.9**	**203.8**	**524.0**	**-3.3**

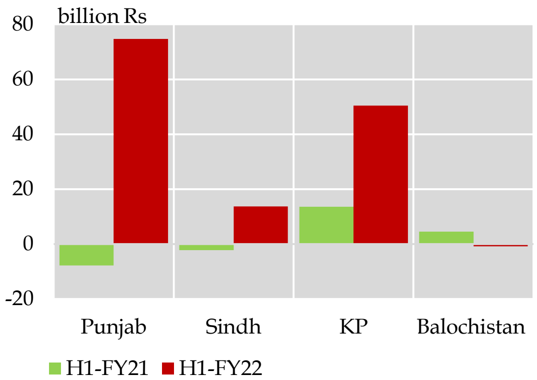
Source: Ministry of Finance

this increase. The rates of stamp duties remained unchanged in Punjab, whereas Sindh announced a reduction in stamp duty rates during FY22.

The pace of collection from general sales tax on services (GSTS) moderated during H1-FY22, compared to the same period last year. Specifically, the GSTS receipts from Punjab and KP marked a y/y decline during H1-FY22 (**Figure 4.17b**), which pulled down the overall growth in the first half. The primary reason of this decline is a higher base in the same period last year when GSTS in these provinces was adjusted for cross input tax adjustment.[33] However, in the case of Sindh, GSTS collection spurred on the back of higher collections from port and shipping services, followed by telecom and financial services.

The uptick in receipts from non-tax revenues stemmed from hydroelectricity profits – primarily from KP - and receipts on civil administration such as revenues from law and order and social services.

Provincial Development Spending-Absolute Change (YoY) **Figure 4.18**



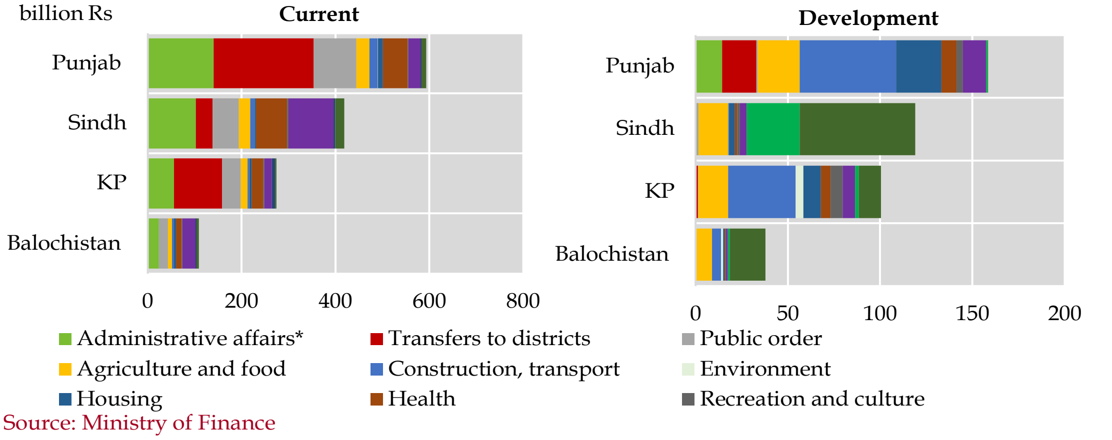
Source: Ministry of Finance

Provincial Expenditures

The total provincial expenditures rose by 25.1 percent in H1-FY22, against a 3.2 percent increase during H1-FY21. The increase was

[33] For reference: State Bank of Pakistan (2021). Chapter 4. Second Quarterly Report on the *State of Pakistan's Economy*. Karachi: SBP.

Provincial Expenditure Priorities during H1-FY22 **Figure 4.19**



Source: Ministry of Finance

observed across current and development expenditures. However, the pace of development expenditures was much higher than the provincial current spending **(Table 4.11)**.

The increase in current expenditures was contributed by salaries and pensions of government employees. Punjab announced an increase of 10 percent in the salaries and pensions and a 25 percent special allowance for the financially distressed employees in the budget for FY22.[34] Likewise, Sindh and KP also announced a 20.0 percent increase in salaries for FY22. This was reflected in higher spending on financial and fiscal affairs of these provinces, specifically for Punjab and Sindh during H1-FY21. In addition, spending on health, education, public order, and district development rose across the provinces to improve service delivery. Some major areas of focus were improvement in hospital services and the continuation of educational projects. Specifically, the volume of current spending on education was the highest in Sindh compared to other provinces in H1-FY22. Similarly, Punjab introduced the 'District Development Package' worth Rs 360 billion in FY22.[35] In this regard, a large sum was transferred to districts during H1-FY22 to expedite the projects.

Moreover, there was some variation in the scale of development spending between the two quarters. While in Q2-FY22, Punjab marked a large increase in development spending, followed by Sindh, whereas KP was the major contributor in provincial development spending in Q1-FY22. In overall terms, Punjab and KP recorded significant increase in development spending during H1-FY22 **(Figure 4.18)**. The development priorities in Punjab mainly addressed agriculture, transport and infrastructure projects. The province of Sindh also focused on agriculture projects along with expenditure on social protection. In KP, allocation to construction and transport

[34] Punjab Budget Highlights for FY22. Government of Punjab.
[35] Source: Government of the Punjab. Highlights of the Budget 2021-22. Lahore: Punjab government.

dominated the development expenditures during H1-FY22 (**Figure 4.19**).[36]

4.5 Public Debt

The stock of outstanding public debt reached Rs 42.7 trillion as of the end December 2021 – reflecting an addition of Rs 2.9 trillion during H1 FY22 compared to a Rs 1.1 trillion increase during the same period of last year. This expansion primarily came from the depreciation of PKR against US dollar during H1-FY22 that inflated the rupee value of external debt by Rs 1.7 trillion. In addition, an increase in the government financing requirements further augmented public debt stock in H1-FY22.[37] In terms of composition, external debt constituted a little more than three-quarters of the increase in public debt.

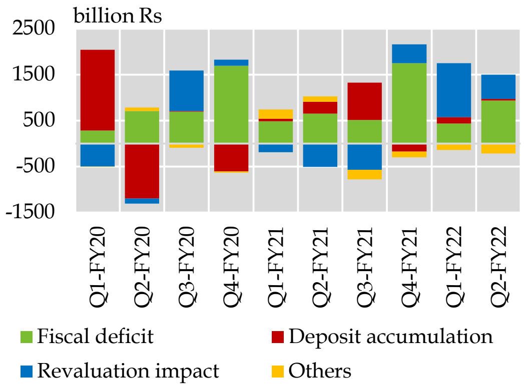
The pace of public debt accumulation slightly eased in Q2

A large part of the increase in public debt i.e., Rs 1.6 trillion out of Rs 2.9 trillion, came in Q1-FY22. The factors underlying the expansion in public debt underwent some change in the two quarters. While Q1-FY22 marked a large Rs 1.2 trillion revaluation loss, the intensity of these losses subsided in Q2-FY22 to Rs 0.5 trillion.[38] On the other hand, the financing needs of the government were higher in Q2-FY22 compared to Q1-FY22 (**Figure 4.20**). Nonetheless, a reduction in revaluation losses kept the pace of debt accumulation lower in Q2-FY22 compared to Q1-FY22.

An important development during Q2-FY22 was the on-lending of the IMF SDR allocation to the government for expenditures related to Covid-19 vaccines. The country received inflow of US$ 2.8 billion from the IMF under the global SDR allocations during Q1-FY22. In Q2-FY22, with exceptional on-lending of this amount to the government, this amount became part of the government domestic debt (**details in section on domestic debt**).

Most of the increase in domestic debt during H1-FY22, particularly in Q2-FY22, was sourced through long-term instruments, which helped the government lengthen the maturity profile of debt. The government has introduced a number of long term instruments with features like floating rates

Source of Change in Public Debt **Figure 4.20**

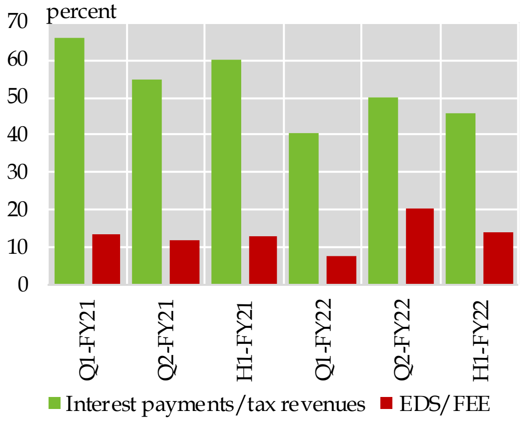


Source: State Bank of Pakistan

[36] White Paper for FY22. Government of Khyber Pakhtunkhwa
[37] Fiscal deficit stood at Rs 1,371.8 billion during H1 FY22 compared to Rs 1,137.5 billion during the same period of last year.
[38] PKR depreciated by 7.8 percent against the US dollar in Q1-FY22 (end September 2021 over end June 2021), whereas depreciation in Q2-FY22 (end December 2021 over end September 2021) was around 3.3 percent.

(quarterly and semi-annual coupon payments)[39],[40]and variable rental rates during the last couple of years. Resultantly, the share of floating and variable rental rate long-term instruments in total outstanding domestic debt stock has increased from 28 percent as on end- June 2019 to 41 percent on end- December 2021. Subsequently the share of T-bills and fixed rate instruments has declined. While this has improved the maturity profile of domestic debt, the interest rate risk has amplified as most of the funds are contracted on floating/variable rates. The rising share of variable rate domestic debt amid an increasing interest rate environment translated into a notable increase in debt servicing burden during Q2-FY22 as measured by interest payments-to-tax revenues (**Figure 4.21**).

Debt Repayment Capacity **Figure 4.21**



Source: Ministry of Finance, State Bank of Pakistan

Similarly, external debt servicing rose to 18 percent of total foreign exchange earnings of the country during Q2-FY22, compared to 9.4 percent same period last year **(Figure 4.21**).[41] A scheduled repayment of maturing sovereign bond and commercial loans magnified external debt servicing pressure during Q2-FY22. Going forward, the debt repayments under DSSI relief will also become due.

Furthermore, the government has adhered to its commitment of zero budgetary borrowing from the SBP since the start of FY20, which has led to avoidance of deficit monetization. However, with the absence of this financing window, the government's reliance on commercial banks for budgetary support has scaled up, which has also increased the cost of borrowing. There is a need to introduce reforms to deepen the debt market by diversifying the financing options and keeping a check on the cost of borrowing by focusing on non-bank financing sources e.g., pension funds, corporations etc. Increasing the share of Shariah compliant instruments would also facilitate the government in diversifying the investor base and attracting Islamic Institutions to place their funds in such instruments.

Domestic debt

The pace of buildup in domestic debt slowed down during H1-FY22, with a growth of 1.8 percent compared to 4.4 percent during the

[39] Government started issuance of 3-, 5- and 10-Year floating rate PIBs with quarterly coupon payment frequency from October 2020, and 2-Year floating rate PIBs in November 2020 with quarterly coupon payment frequency and fortnightly interest rate re-setting.
[40] The government at end of FY19 re-profiled its debt held with SBP. Out of its Rs 7.7 trillion debt held with the SBP, roughly Rs 1.2 trillion was re-profiled into fixed PIBs, while the remaining Rs 5.5 trillion was converted into floating rate PIBs, which also increased the share of floating rate instruments in overall outstanding debt stock.
[41] External debt servicing includes principal repayments and interest payments of public debt only.

Instrument-wise Changes in Domestic Debt **Table 4.12**

billion Rs

	H1-FY21	Q1-FY21	Q2-FY21	H1-FY22	Q1-FY22	Q2-FY22
1. Permanent debt	**1,565.6**	**898.6**	**667.0**	**1,548.1**	**(67.2)**	**1,615.3**
GoP Ijara Sukuk	363.2	162.0	201.2	632.5	-	632.5
PIBs	1,216.2	729.8	486.4	584.9	(8.6)	593.5
Prize bonds	(13.8)	6.8	(20.6)	(71.7)	(58.6)	(13.1)
SBP loan to GOP against SDRs allocation	-	-	-	474.9	-	474.9
2. Floating debt	**(535.0)**	**(480.0)**	**(54.9)**	**(1,036.9)**	**250.8**	**(1,287.7)**
MTBs	(535.5)	(480.5)	(54.9)	(1,084.8)	250.8	(1,335.5)
3. Unfunded debt	**(3.9)**	**0.8**	**(4.7)**	**(42.0)**	**(14.0)**	**(27.9)**
NSS	3.9	5.7	(1.8)	(32.6)	(13.5)	(19.2)
4. Naya Pakistan Certificates	**5.2**	**0.7**	**4.6**	**10.9**	**8.4**	**2.5**
5. Others	**(7.6)**	**(4.4)**	**(3.2)**	**(33.2)**	**(0.1)**	**(33.2)**
Domestic debt (1+2+3+4+5)	**1,031.6**	**420.0**	**611.6**	**481.1**	**178.5**	**302.5**

Source: State Bank of Pakistan

same period last year. Adequate availability of external inflows kept the financing needs from domestic sources at lower levels. The increase in the government deposits with the banking system also remained lower than last year. The maturity profile of domestic debt also improved with increasing fund mobilization through long-term instruments such as Pakistan Investment Bonds (PIBs), Ijara Sukuk and Naya Pakistan Certificates (NPCs) (**Table 4.12**). Nonetheless, as most of the fresh domestic loan is contracted on floating and variables rental rates, repricing risk has edged up.

In terms of ownership, almost the entire increase in domestic debt during H1-FY22 was sourced through commercial banks. The contribution of non-banks was negligible. The government debt owed to SBP declined during H1-FY22.

On-lending of SDR to the government

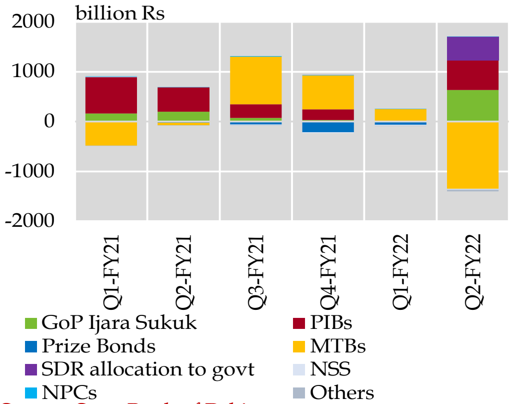
Quarterly analysis indicate that the stock of government debt owed to SBP increased during Q2-FY22. This rise came from the on-lending of SDRs amounting to Rs 474.9 billion (comprising of US$ 2.8 billion SDRs) to the government. In November 2021, the IMF allowed exceptional on-lending of this amount to the government for financing of the vaccine drive.[42] The ceiling on net government budgetary borrowing from the SBP is adjusted upward by the amount of local currency on-lending of the SDRs.[43] Excluding the SDR allocation, the government debt stock with SBP declined by Rs 523 billion during H1-FY22.

Instrument-wise Analysis

Most of the increase in domestic debt during H1-FY22 was sourced through long-term instruments such as PIBs, Ijara Sukuk and Naya Pakistan Certificates. The quarterly analysis indicates that whereas most of the increase in domestic debt was sourced through short-term instruments during Q1-FY22, the trend changed in Q2-FY22 (**Figure 4.22**). The availability of Ijara Sukuk bonds not only facilitated trading of shariah compliant instruments in secondary market

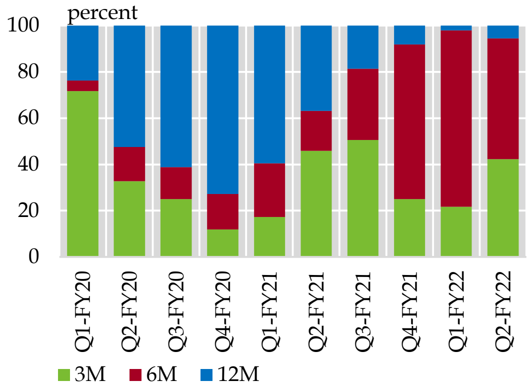
[42] IMF Sixth review.
[43] IMF-Sixth review.

Instrument-wise Change in Domestic Debt **Figure 4.22**



Source: State Bank of Pakistan

Share in Outstanding Stock of T-Bills **Figure 4.23**



Source: State Bank of Pakistan

but also increased government financing options; hence the government retired its maturing short-term debt in the second quarter.

Market Treasury Bills

The outstanding stock of MTBs declined by Rs 1.1 trillion during H1 FY22 compared to a decline of Rs 0.5 trillion during the corresponding period of last year. A quarterly review indicates that during Q2-FY22 the government made net retirement of MTBs, which more than offset the increase seen in Q1-FY22.

The government set the pre-auction MTB target of Rs 5.96 trillion for Q2-FY22 (Rs 416 billion over and above maturities). Overall, the total offered amount stood at Rs 7.9 trillion. However, the government accepted only Rs 4.2 trillion, during Q2-FY22 and made net retirement of Rs 1.3 trillion MTBs in Q2-FY22. With the reversal in monetary policy stance, market was more inclined towards 3-month MTBs, whereas demand for 6-month MTBs edged down (**Figure 4.23**). This is evident from a total offer of Rs 4.3 trillion in 3-month MTBs, against Rs 1.9 trillion offered in 6-month bills during Q2-FY22.

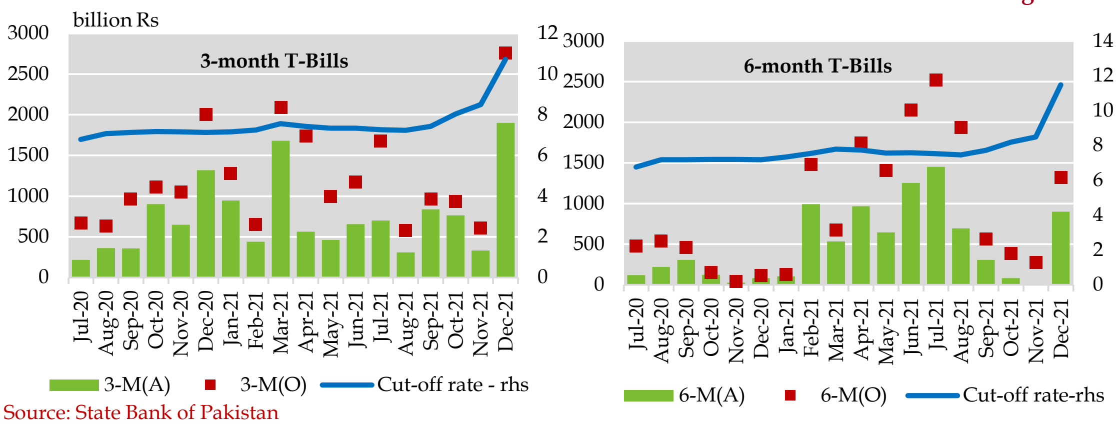
It is important to highlight here that the cut off rates on 3-M, 6-M, and 12-M T-bills increased by 282 bps, 337 bps and 388 bps during Q2-FY22 with 250 basis points increase in the policy rate (**Figure 4.24**). Hence, to contain the burden of interest payments, the government accepted around 70 percent bids in 3-month T-bills, compared to only 50 percent for 6-month MTBs.

The entire increase in PIBs was concentrated in Q2-FY22

The stock of outstanding PIBs reached Rs 15.2 trillion as on end December 2021 compared to Rs 14.6 trillion as on end June 2021 – reflecting an increase of Rs 0.6 trillion. The entire increase in PIBs was concentrated in Q2-FY22. With the reversal of monetary policy stance and a rise in policy rate, the cut off rates of PIBs also increased sharply during Q2-FY22. On average, the cut off rates during Q2-FY22 were 230-280 bps higher than Q2-FY21 (**Table 4.13**).

Keeping in view the market appetite, the government kept the pre-auction targets for

Bidding Pattern in T-bills **Figure 4.24**



Source: State Bank of Pakistan

floater PIBs higher compared to fixed PIBs. The target for fixed PIBs stood at Rs 750 billion during H1 FY22, while the target of floater PIBs was Rs 1,175 billion for the cumulative period. The accepted amount of floater PIBs was also relatively higher than the fixed PIBs. Rising share of floating rate PIBs increases the repricing risk, particularly in an increasing interest rate environment. The share of floater PIBs in total outstanding stock of PIBs has increased by roughly 13 percentage points to 48 percent as on end December 2021, compared to 35 percent as on end June 2021. Keeping a balance between lengthening of maturity profile and repricing risks is important to ensure debt sustainability.

Monthly auction profile suggests that with the rise in the policy rate, the market's participation has increased in floater PIBs (**Figure 4.25**). Within floater PIBs, the share of floaters with quarterly coupon payments increased from 20 percent as of end June 2021 to 45 percent as on end June December 2021. Auction profile suggests that the market remained inclined towards floater PIBs with quarterly coupon payments as evident by the higher offered amount in both quarters of FY22. In line with market's interest, the government also accepted higher amounts in the category of quarterly PFLs (**Table 4.14**). In Q2-FY22, the government rejected the bids of floaters PIBs with semi-annual coupon payments due to lower participation of the market.

Issuance of GoP Ijara Sukuk

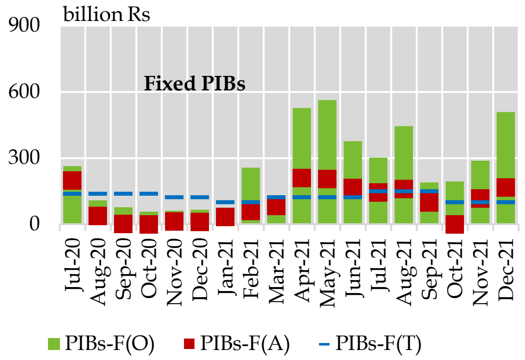
After a gap of two quarters, the government mobilized funds through the issuance of GOP Ijara Sukuk during Q2-FY22 and mobilized Rs 0.6 trillion. In line with the market interest, a large part was issued on the variable rental rate. The offered and accepted amount remained above the pre-auction target (**Table 4.15**). This helped the government in lengthening the maturity

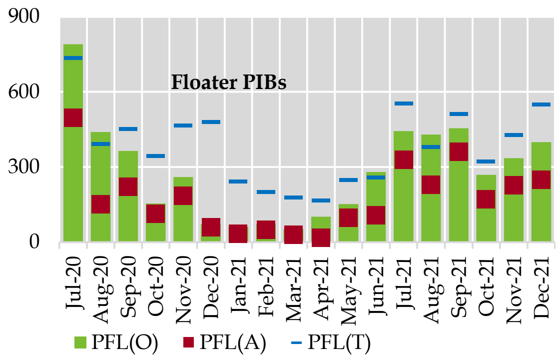
Average Cutoff Rates on PIBs **Table 4.13**

	3-year	5-year	10-year
H1-FY21	8.1	8.4	9.0
H1-FY22	9.85	10.48	10.80
Q2-FY21	8.2	8.5	9.0
Q2-FY22	11.42	11.58	11.77

Source: State Bank of Pakistan

Auction Profile of PIBs **Figure 4.25**





Source: State Bank of Pakistan

O=offered, A=accepted, T=Target

Auction Profile of Floater PIBs **Table 4.14**

billion Rs

	Target	Offered	Accepted
Semi-annual coupon			
Q1-FY22	190.0	175.7	129.5
Q2-FY22	300.0	147.7	-
Quarterly coupon			
Q1-FY22	335.0	1,154.0	787.19
Q2-FY22	350.0	856.7	606.34

Source: State Bank of Pakistan

profile of domestic debt as these instruments have a tenor of 5 years.

Prize bonds and NSS continue to record outflows

Prize bonds recorded net outflows of Rs 72 billion during H1-FY22 – Rs 58 billion in Q1-FY22 and Rs 14 billion in Q2-FY22. Discontinuation of prize bonds of various tenors (7,500, 15,000 and 25,000) and subsequent withdrawals explain the decline in prize bonds. However, monthly analysis shows that the volume of outflows is waning (**Figure 4.26**). Investment in premium prize bonds increased during the period under review. Gross inflows in premium prize bonds stood at Rs 16.5 billion during H1 FY22 compared to Rs 5.4 billion during the same period of last year.

National saving schemes recorded net outflows during the period under review - Rs 13.5 billion in Q1-FY22 and Rs 19.1 billion in Q2-FY22. Institutions continued to withdraw funds from NSS as they have been barred from participation in such instruments. However, a couple of instruments such as regular income certificates and behbood

Auction Summary **Table 4.15**

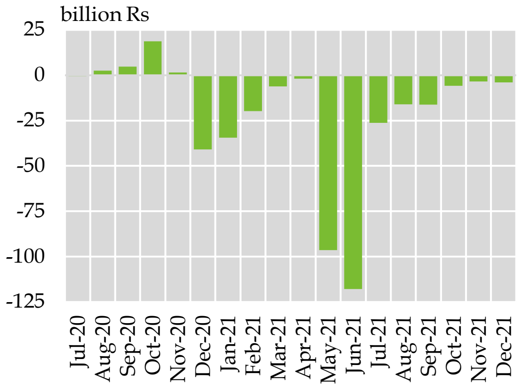
billion Rs

	GoP Ijara Sukuk (VRR)		
Date of Settlement	**Target**	**Offered**	**Accepted**
06-10-21	75	193.1	190.5
29-10-21	75	222.7	168.6
17-11-21	75	162.5	148
15-12-21	75	8.1	0.04
	GoP Ijara Sukuk (FRR)		
Date of Settlement	**Target**	**Offered**	**Accepted**
06-10-21	25	53.8	12.7
29-10-21	25	22.9	0
17-11-21	25	21.5	0
15-12-21	25	109.8	68

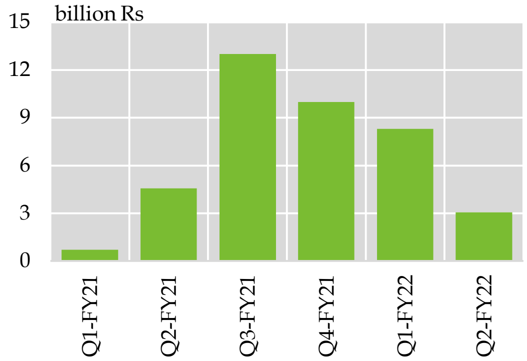
*this does not include Ijara Sukuk issued by GoP to IPPs against their receivables from GoP worth Rs 45 billion.

Source: State Bank of Pakistan

Net Inflows in Prize Bonds **Figure 4.26**



Naya Pakistan Certificates Held by Residents - Quarterly Flows **Figure 4.27**



Source: State Bank of Pakistan

saving schemes attracted relatively higher inflows due to a hike in profit rates. Recent increase in profit rates in December 2021 will help government in attracting funds through these instruments (**Table 4.16**).

Naya Pakistan Certificates

The stock of Naya Pakistan Certificates (held by residents) reached Rs 39.2 billion as on end December 2021 compared to Rs 28.3 billion as on end June 2021. The pace of inflows in these certificates slowed down in Q2-FY22 (**Figure 4.27**).

Interest payments on domestic debt

Interest payments on domestic debt stood at Rs 1.3 trillion during H1-FY22 compared to Rs 1.4 trillion during the same period of last years.[44] Specifically, in line with the rising share of variable rate debt, interest payments gained pace in Q2-FY22 amid an increasing interest rate environment. Most of the increase came from the payments on PIBs, as the increasing share of PIB floaters with the unique feature of fortnightly resets and coupon payments on quarterly basis, fed into debt servicing pressure after an increase in policy rate. Similarly, payments on GoP Ijara Sukuk almost doubled in Q2-FY22 compared to the same quarter last year because of the increase in outstanding stock of GoP Ijara Sukuk. On the other hand, payments on

National Savings Schemes **Table 4.16**

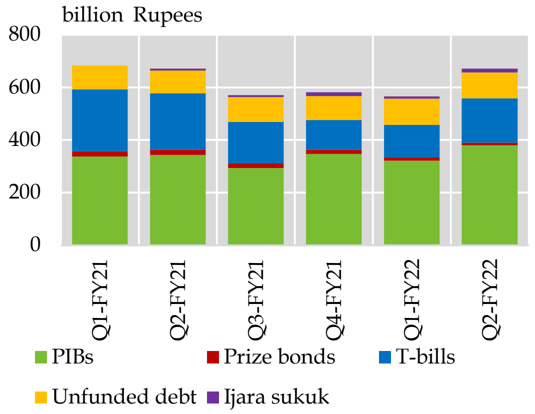
billion Rs, profit rates in percent

	Net Inflows		Profit Rates	
	Q2-FY21	Q2-FY22	Q2-FY21	Q2-FY22
Defence Savings Certificates	-0.8	-3	8.5	9.4
Special Savings Certificates	6.5	-0.5	7.6	8.2
Regular Income Certificates	4.2	3.6	8	10.8
Behbood Savings Certificates	3.3	-2.3	10.3	11

Source: Central Directorate of National Savings

[44] Source: Ministry of Finance, available at: https://finance.gov.pk/fiscal/July_Dec_2021.pdf, accessed on January 15,2022

Instrument-wise Interest Payments **Figure 4.28**



Source: State Bank of Pakistan

prize bonds slowed down in Q2-FY22 as the outstanding stock of prize bonds has been on a decline due to discontinuation of various denominations bonds. Similarly, the payments on MTBs dropped amid a decline in maturing debt stock (**Figure 4.28**).

Public external debt & liabilities

The stock of outstanding public external debt (excluding liabilities) reached US$ 90.6 billion on end-December 2021, with increase of US$ 4.1 billion during H1-FY22 compared to US$ 4.4 billion during the same period last year (**Table 4.17**). The fresh disbursements remained higher in H1-FY22 owing to deterioration in the current account balance. However, revaluation gains of US$ 0.7 billion on the existing stock of external debt (dollar terms) emerging from appreciation of US dollar against other international currencies helped in containing the pace of external debt accumulation.

One-half of revaluation gains due to SDR depreciation

Currency-wise revaluation impact indicates that appreciation of the US dollar against the SDRs constituted more than one-half of the revaluation gains during H1-FY22. It must be recalled that during the same period of last

Change in Public External Debt **Table 4.17**

million US$

	H1-FY21	H1-FY22	Q2-FY21	Q2-FY22
Public external debt (1&2)	4,412.0	4,099.3	2,499.5	2,475.8
1. Government external debt	4,613.3	4,750.6	2,625.3	2,950.6
of which				
i) Long term (>1 year)	5,239.4	4,441.1	2,881.4	2,816.3
Paris club	622.3	(579.9)	343.9	(198.3)
Multilateral	2,267.2	798.3	779.9	434.2
Other bilateral	1,174.4	3,107.3	190.5	3,041.8
Commercial loans/credits	940.8	522.4	1,366.3	382.1
Naya Pakistan Certificates	128.5	528.9	128.0	159.6
ii) Short term (<1 year)	(626.1)	418.9	(256.1)	(12.2)
Multilateral	(238.8)	561.2	64.9	88.5
Local currency securities	(245.9)	(142.2)	(206.0)	(100.7)
Commercial loans/credits	(141.5)	-	(115.0)	-
2. From IMF	(201.2)	(651.3)	(125.8)	(340.5)
Foreign exchange liabilities	(630.5)	2,879.0	228.9	(3.0)
Central bank deposits	(2,000.0)	-	(1,000.0)	-
Allocation of SDR	63.8	2,739.0	32.3	13.8

Source: State Bank of Pakistan

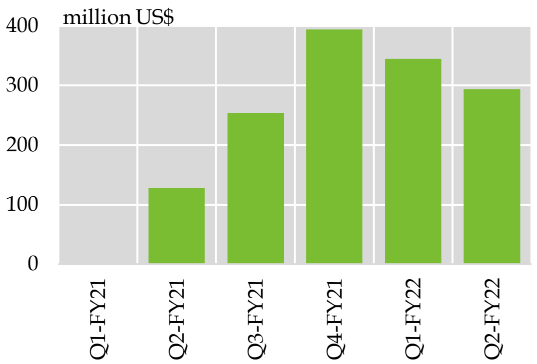
Major Foreign Economic Assistance during H1 **Table 4.18**

million US$

Donor	Name of project	Purpose	Amount
Total disbursements			**9,432.7**
of which			
Project and Budgetary Support			
Saudi Arabia	Time Deposit	Budgetary support	3,000.0
ADB	COVID-19 Vaccine Support Project	Project	488.0
IDA	Prog. For Afford. Clean Energy	Budgetary support	397.0
IDB	Short-term credit	Short-term credit	354.4
ADB	Energy Sector Reforms and Finance Sustainable Project	Budgetary support	300.0
China	Karachi Nuclear Power Project	Project	292.0
IDA	Pandemic Response Effectiveness	Project	108.0
IDA	Sindh Barrages Improvement Project	Project	52.2
Euro Bonds			
5-year Euro Bond		Budgetary support	300.0
10-year Euro Bond		Budgetary support	400.0
30-year Euro Bond		Budgetary support	300.0

Source: Economic Affairs Division

Naya Pakistan Certificates Held by Non- Residents - Quarterly Flows **Figure 4.29**



Source: State Bank of Pakistan

year, the country incurred revaluation losses of US$ 1.9 billion due to depreciation of US dollar against other international currencies, which led to an expansion of external debt stock.

The accumulation of external debt was spread almost evenly across the two quarters. However, the composition of disbursements slightly changed during Q2-FY22 compared to the same quarter last year. The contribution of bilateral sources increased largely due to inflows of US$ 3.0 billion from a friendly country for budgetary support. ADB also funded the project "Energy Sector Reforms and Finance Sustainable Project" worth US$ 300 million during Q2-FY22. Another important area was funding for COVID-19 Vaccine Support Project worth US$ 487.8 million by ADB, out of which roughly US$ 173 million were disbursed in the second quarter (**Table 4.18**). Moreover, the government issued Euro bond of various tenors worth US$ 1.0 billion during Q2-FY22.

Foreign investment in local government securities continued to record outflows

Foreign investment in local government securities recorded net outflows in both quarters of FY22. However, tenor-wise information shows that foreign investment in PIBs recorded net inflows during Q2-FY22.

Naya Pakistan Certificates continued to attract inflows

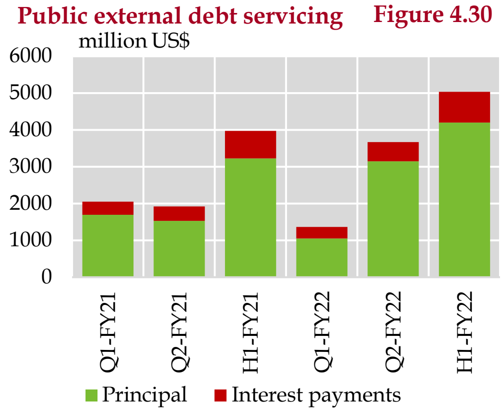
Naya Pakistan Certificates (held by non-residents) attracted US$ 0.5 billion inflows during H1-FY22 (**Figure 4.29**). With this increase the stock of NPCs reached US$ 1.3 billion as on end December 2021 compared to US$ 0.8 billion as on end June 2021. As most of the inflows under NPCs are long term in nature – maturity of more than one year – these inflows have helped lengthen the maturity profile of government external debt. In addition, these inflows have also helped the government diversify its narrow investor base.

Public External Debt Servicing

Public external debt servicing (principal and interest payments) stood at US$ 5.0 billion during H1-FY22 compared to US$ 3.9 billion during the same period of last year.

Quarterly analysis indicates that both components of public external debt servicing (principal and interest payments) increased during Q2-FY22, after showing a slight decline in Q1-FY22 (**Figure 4.30**). This was because of the repayment of a maturing

Public external debt servicing **Figure 4.30**



Source: State Bank of Pakistan

Sukuk bond worth US$ 1 billion during Q2-FY22.

Subsequently the outstanding stock of Euro/Sukuk global bonds fell to US$ 7.8 billion as on end December 2021 compared to US$ 8.8 billion as on end September 2021. In addition, the government also repaid its maturing commercial loans worth US$ 1.2 billion during Q2-FY22.

Debt relief under DSSI continued in Q2-FY22

On a cumulative basis during H1 FY22, the country secured debt relief of US$ 1.1 billion (US$ 0.8 principal and US$ 0.3 billion interest payments) under DSSI.

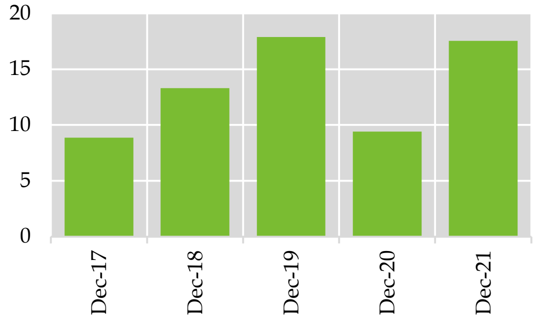
During Q2-FY22, the country received debt relief of US$ 0.5 billion (principal amount US$ 0.4 billion and interest component US$ 0.1 billion) compared to relief of US$ 0.9 billion in Q2-FY21. Without this relief, public external debt servicing would have been higher in Q2-FY22.

In total (May-2020 till December 2021), the country secured relief of US$ 3.8 billion. Under this initiative, the debt repayments were postponed till December 2021. The repayment period for the restructured principal and interest amounts is 4-6 years.

Debt repayment capacity slightly weakens in Q2 due to higher debt servicing

The indicators of debt repayment capacity came slightly under pressure in Q2-FY22 compared to the same period last year. The ratio of public external debt servicing-to-foreign exchange earnings rose to 17.5 percent by the end of December 2021, whereas the ratio of public external debt

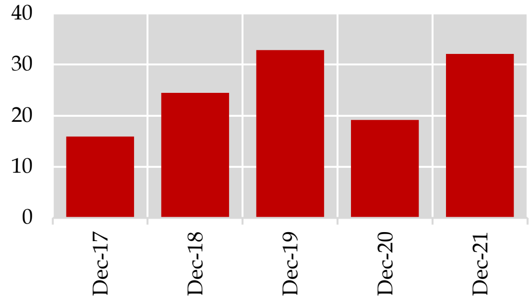
EDS as Percent of FEE **Figure 4.31a**



* EDS external debt servicing (principal component); FEE foreign exchange earnings

Source: State Bank of Pakistan

EDS as Percent of Export Earnings (Goods & Services) **Figure 4.31b**



* EDS external debt servicing (principal component); Exports of goods & services

servicing-to-exports of goods and services increased to 32.1 percent in December 2021 (**Figure 4.31 a & b**). [45]

[45] Public external debt servicing includes principal component of long term and short-term government external debt plus debt repayments to the IMF. It does not include foreign exchange liabilities and interest payments.