2 Real Sector

2.1 Agriculture

The prospects of meeting the FY05 agri-sector growth targets have improved significantly in recent months. Firstly, the value-addition by the *kharif* FY05 crops is now considerably higher than the initial estimates, with the revised cotton production figure exceeded 14.0 million bales (as compared to the earlier estimate of 11.6 million bales and the FY05 target of 10.7 million bales). Secondly, fears of a serious water shortage for the *rabi* FY05 season have abated significantly following timely rains as well as heavy snowfalls. The improved water availability has given rise to hopes that the wheat harvest will be at least close to the FY05 target.

In fact, the revised *Kharif* crops production figures, together with the improved prospects for the wheat harvest suggest that the growth in aggregate crop sector could exceed 8 percent during FY05, well above the 3.5 percent target for the year. This expectation is also bolstered by the sustained high prices for agricultural produce, and the ample availability of credit (implying improved access to inputs). However, it should be kept in mind that the sector is uniquely vulnerable to natural vagaries and that the final growth number will depend heavily on the eventual outcome of the standing wheat crop. In particular, continued heavy rain and snowfall may damage the standing wheat crop and some minor crops as well.

Since, the crop sub-sector comprises approximately 46.0 percent of the agriculture sector, the improved crops scenario would also have a beneficial effect on the overall agriculture sector performance. The prospects for a better outturn by the livestock sub-sector also appear promising at this stage. Unlike the preceding year,[1] there are no evident problems so far, and the extensive promotion of credit availability for livestock under special scheme of small loans is likely to support a higher pace of growth.

2.1.1 Crop Sub-sector Performance

The large upward revision of the cotton production figure has substantially improved the value-addition growth by the FY05 *kharif* crop,[2] in real terms, from initially estimated 5.3 percent YoY to a much more robust 15.7 percent YoY (see **Table 2.1**).

[1] e.g., bird flu virus infected poultry in FY04.
[2] *Kharif* season is from April to September and *rabi* season is from October to March.

Specifically, the cotton crop is now provisionally estimated at 14.2 million bales in FY05, which is not only far above the 10.7 million bales annual production target, but is also the record highest cotton output in Pakistan.

This has comfortably offset the impact of the relatively disappointing rice and sugarcane harvests.[3] Therefore it is now increasingly likely that the crop sub-sector performance will substantially be above the target in FY05. In fact, a sensitivity analysis, varying the potential wheat production during *rabi* FY05, suggests that the overall growth in the crop sub-sector will be quite significantly above target even in the unlikely event that the wheat harvest is 1.8 million tonnes below target, and could ever be over twice the target rate if the more optimistic scenarios materialize (see **Table 2.2**).

Table 2.1: Production of Important Crops

cotton million' bales; other crops 000' tonnes

Crops	FY04	FY05		percent change Over	
		Target	Prel.	FY04	Target
Cotton	10.0	10.7	14.2	40.9	32.0
Sugarcane	52,600	50,875	47,938	-8.9	-5.8
Rice	4,871	5,114	4,977	2.2	-2.7
Wheat	19.5	20.8	N.A.	N.A.	N.A.

Area under important crops

thousand hectares

Crops	FY04	FY05		percent change Over	
		Target	Sown	FY04	Target
Cotton	2,989	3,140	3,210	7.4	2.2
Sugarcane	1,050	1,000	958	-8.8	-4.2
Rice	2,451	2,586	2,507	2.3	-3.0
Wheat	8,195	8,290	N.A.	N.A.	N.A.

Source: Ministry of Food, Agriculture and Livestock
N-A=Wheat provisional estimates for area and production are yet to come

Table 2.2: Value Addition by Major Crops

million Rupees

	Real value addition		Percent growth
	FY04	FY05	
Rice	55,970.1	57,459.4	2.7
Cotton	72,886.9	103,025.2	17.0
Sugarcane	42,952.3	38,289.3	-10.9
***Kharif* sub-total**	171,809.0	198,773.9	15.7

Assumed wheat harvest (million tonnes)	Value addition by wheat FY05	Total value addition by major crops FY05	Overall crop sector growth
19.0	127,323.4	326,097.2	7.8
20.2	135,364.9	334,138.7	10.5
21.0	140,725.8	339,499.7	12.2

[3] The estimates for the other two important kharif crops, rice and sugarcane remained unchanged. Though, rice output is below target for *kharif* FY05, it saw an increase of 2.2 percent over the actual rice production during *kharif* FY04. A decline in the production of sugarcane crop was envisaged as its targeted production level was set at lower than the actual FY04 production. However, problems with marketing the produce during last two years and realized prices below the announced procurement created strong disincentives for the farmers. This situation resulted in a larger than anticipated[3] decline of 8.9 percent in sugarcane output during FY05.

Initially, there had been considerable concern over the prospects of the FY05 *rabi* crops due to a severe water shortage that was expected to worsen later in the season. In the event, timely rains significantly diluted immediate concerns at sowing times (not only did the wheat crop benefit directly from the rains, the water stocks also improved). These rains were probably beneficial to the *barani* (non-canal fed) districts of Attock, Chakwal, Jehlum and Rawalpindi, (which account for a significant part of total wheat production) and probably encouraged some additional late sowing of wheat as well.[4]

The heavy rains have probably also had some adverse impacts, particularly on some of the less important major crops (e.g. gram) as well as some minor crops (e.g. chillies, pulses). However, since these less important crops contribute less than 10 percent of the crop sub-sector and since, on aggregate these crops depict a mixed performance, the negative impact of the rains on the aggregate crops sub-sector in unlikely to be significant.

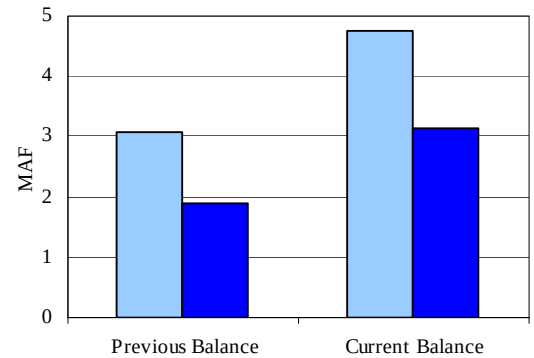
2.1.2 Water

The aggregate canal water shortage for Sindh and the Punjab during the *rabi* FY05 season had initially been estimated at a crop-threatening 47.0 percent of normal requirements, raising concerns that the FY05 agri-growth target could be missed by a wide margin. Fortunately, the unexpectedly heavy (and timely) winter rains and snowfall substantially alleviated this risk.

Not only did the precipitation improve water availability prospects, the timings of the rains probably also allowed farmers to increase areas under cultivation, particularly in rain-fed areas.

In fact, as a result of the rains by end-January 2005 the water balance for the remaining period of *rabi* FY05 i.e., February-March FY05 has significantly increased; with a 54.2 percent and 67.1 percent increase in

Figure 2.1: Improved Water Balance for Rabi FY05 (Feb-Mar)



[4] The actual overall impact of these rains on wheat sowing patterns is not yet available.

the water balances for Punjab and Sindh respectively from the pre-rainfall levels (see **Figure 2.1**). Moreover, the snowmelt from the heavy snowfall is also expected to ensure good water availability in the subsequent *kharif* FY06, season. [5]

As a result of this improvement in prospective water availability, IRSA has lowered the average carryover level in the water reservoirs, down by 82.1 percent from 2.8 MAF (determined at the beginning of the rabi season) to 0.5 MAF, compared with the average maintained level of 1.2 MAF.

Table 2.3: Anticipated Water Availability-Rabi FY05 Season

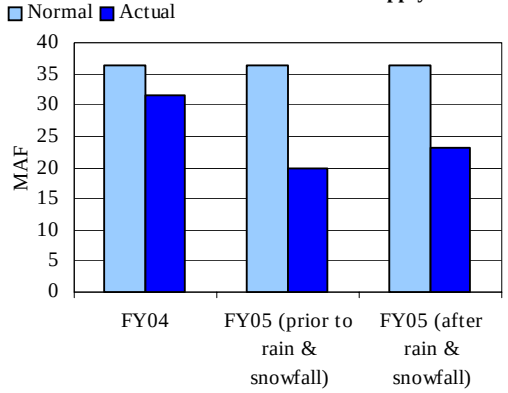
million acre feet (MAF)

Availability for canals	8.7
Less NWFP & Balochistan	0.8
Balance for Punjab & Sindh	7.9
Utilization Oct-Jan, 05 (Punjab & Sindh)	16.5
Seasonal availability (Punjab & Sindh)	21.4
Share	34.7
Shortage	38

Source: IRSA

The water shortage has improved from 47.0 percent in the case of Sindh and Punjab during *rabi* FY05 to 38.0 percent[6] (see **Table 2.3 & Figure 2.2**). This is because of zero water shortage for the balance period of *rabi* i.e. February-March 2005.

Figure 2.2: Impact of Recent Winter Rain & Snowfall on Rabi Water Supply



2.1.3 Fertilizer Offtake

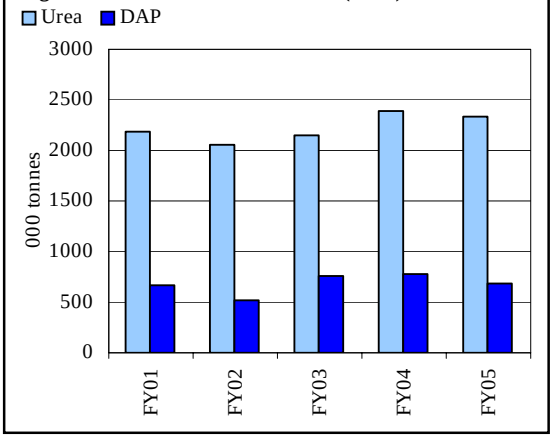
Fertilizer offtake during the first half of *rabi* FY05, i.e. Oct-Dec, remained below that in the corresponding period of *rabi* FY04 (see **Figure 2.3**), although the credit disbursement for fertilizer was 29.1 percent higher during H1-FY05 as compared

[5] The MET department predicts a rise in temperature after March 15, 2005. Thus, if this forecast holds, there will probably be no water shortage during early *kharif* FY06, as compared with a water shortage of 11.9 percent during *kharif* FY05.

[6] The overall water shortage has reduced to 36.4 percent from for rabi FY05 against initial estimate of 44.6 percent.

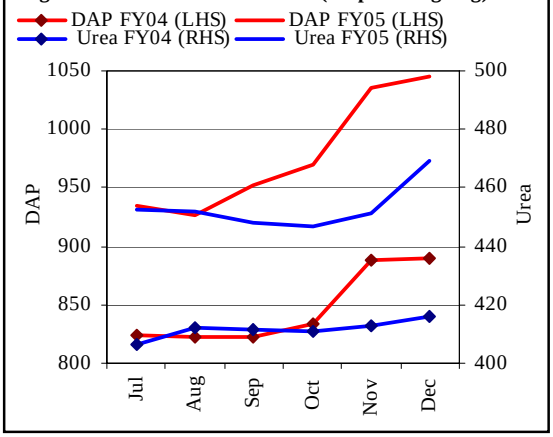
to H1-FY04.[7]
The offtake of urea was down by 5.8 percent YoY, while that of DAP declined by 14.5 percent YoY during Oct-Dec FY05. As a result, it is estimated that the overall fertilizer offtake for the whole of *rabi* FY05 is likely to be down by about 3.0 percent for urea and 11.8 percent for DAP compared to the preceding *rabi* season.

Figure 2.3: Urea & DAP Off take (Rabi)



The major reasons for the lower fertilizer offtake during the first half[8] of FY05 include water shortages (that discouraged farmers' usage of inputs), higher fertilizer prices (see **Figure 2.4**) and supply shortages. The impact of these factors was further aggravated by the disruption of gas supply[9] to the fertilizer plants at the start of second half of *rabi*.

Figure 2.4: Urea & DAP Prices (Rs per 50kg bag)



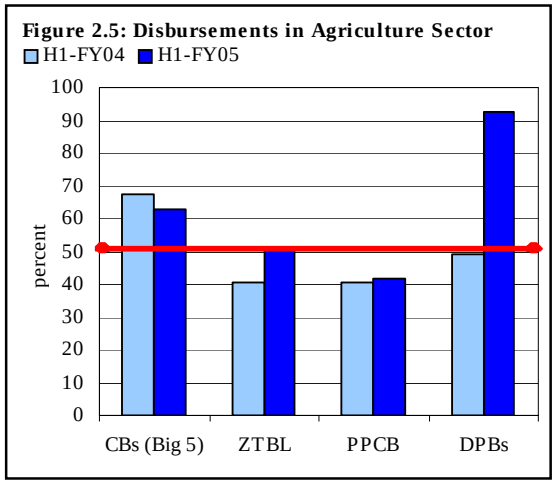
Thus, it would be difficult to compensate for the decline in fertilizer usage during the second half of *rabi*, as immediate import of urea is not possible. The increased international prices of

[7] As a result of a higher expansion in overall credit disbursement, the share of credit disbursement for fertilizer as a percent of total credit disbursement also witnessed a fall from 49.1 percent in FY04 to 42.4 percent in FY05.
[8] The general ratio of fertilizer offtake between the first and second halves of *rabi* is 60:40.
[9] The daily loss due to this disruption was 4000 tonnes lower production of urea. The production was stopped since January 12, 2005, and according to initial reports the gas was restored on January 25, 2005. It therefore implies that the total loss would be around 60,000 tonnes. Similarly, estimated losses were 19,000 tonnes for CAN, 19,000 tonnes for NP and 21,000 tonnes for DAP. Furthermore, the DAP availability remained lower for *rabi* FY05 due to closure of DAP Bin Qasim plant.

fertilizer coupled with domestic supply shortages are likely to adversely affect the fertilizer offtake in the next cropping season (*kharif* FY06) as well.

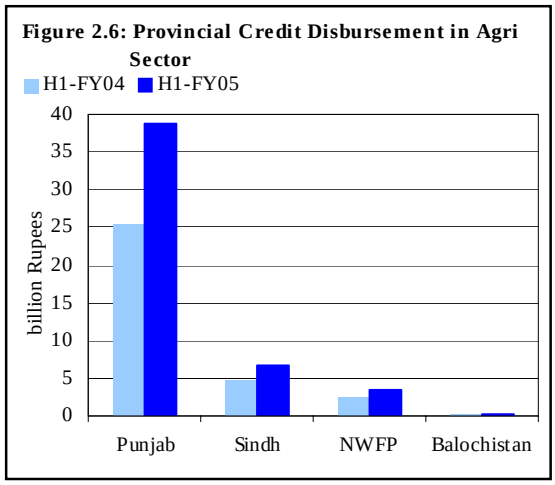
2.1.4 Agricultural Credit

The ambitious agri-credit disbursement target of Rs 85 billion for FY05 (up 15.6 percent YoY from the disbursement seen in FY04) is likely to be comfortably exceeded.



Disbursement

The amount disbursed (Rs 49.1 billion) during H1-FY05 is an impressive 49.4 percent higher than that in the corresponding period of H1-FY04, and 57.8 percent of the FY05 annual target. To put the latter in perspective, it should be noted that: (1) disbursements had never before crossed 51 percent of the target, and that (2) this was achieved despite a large increase in the target.



The credit for this extraordinary performance is shared by almost all of the banking groups (see **Figure 2.5**) but the biggest improvement in the disbursements was by Domestic Private Banks (DPBs). While these have only recently entered this market segment, their performance is remarkable, they achieved 93 percent of their annual disbursement

target during H1-FY05 compared with 49 percent in H1-FY04.[10] Almost 85.0 percent of this disbursement was to the crop sub-sector.
Furthermore, a break-up of the credit data by province shows that disbursements rose substantially for all provinces except Balochistan. The highest YoY increase of 52.0 percent was witnessed in the Punjab followed by 48.2 percent for NWFP and 41.5 percent for Sindh. Agri credit disbursement for Balochistan fell by 27.0 percent YoY during this period (see **Figure 2.6**).

Purpose-Wise Credit Disbursement

The analysis of agriculture credit disbursement by usage during H1-FY05 reveals that not only did *farm* and *non-farm* credit disbursements increase, for the first time, this period also saw significant disbursement of loans for corporate farming.

The lending to corporate farm was solely by DPBs. These loans rose from an insignificant Rs 12.4 million in H1-FY04 to Rs 593.9 million in H1-FY05 (see **Figure 2.7**).

The share of *non-farm* sector increased from 13.4 percent in H1-FY04 to 15.4 percent in H1-FY05. This is probably due to the increasing credit extension to the livestock sub-sector.

The disbursement for tractor financing witnessed a marginal

Figure 2.7: Purpose-Wise Disbursement of Agriculture Credit

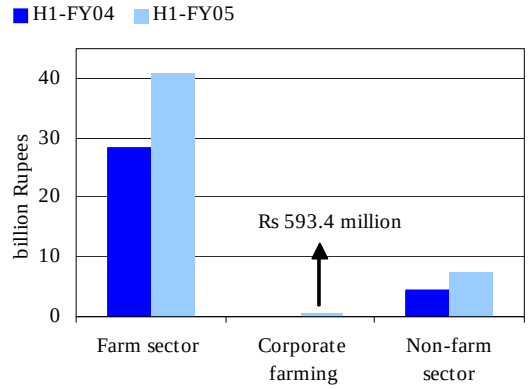
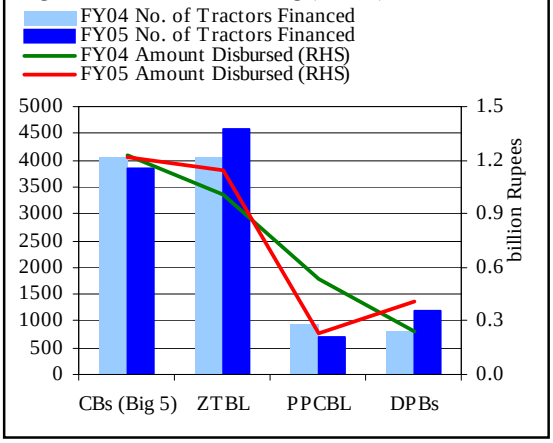


Figure 2.8: Tractor Financing (H1-FY)



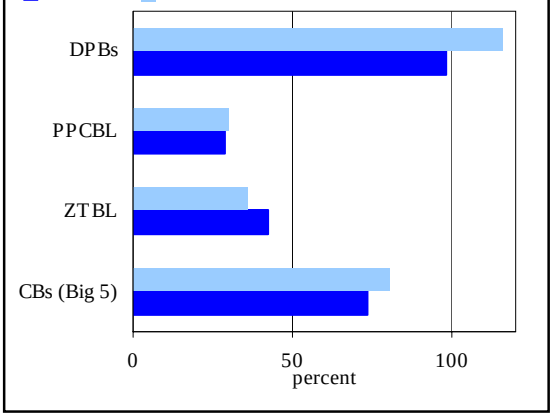
[10] Actual disbursement as a percent of Agri-credit target was witnessed at 229 percent for Bank Al-Falah Ltd, 178 percent for Bank of Punjab, 59 percent for Prime Commercial Bank Ltd & Askari Commercial Bank Ltd and 53 percent for Faysal Bank Ltd during H1-FY05.

decline of 0.5 percent during H1-FY05. This was because a significant rise in the disbursements by DPBs and ZTBL (70.7 percent YoY and 12.8 percent YoY respectively), was offset by decline of 56.4 percent YoY and 0.6 percent YoY in disbursements by PPCBL and CBs respectively (see **Figure 2.8**). However, the number of tractors financed by the banks actually rose by 4.5 percent YoY.

Recovery

H1-FY05 witnessed an improvement in the recovery ratios for all banks excluding PPCBL (see **Figure 2.9**) and consequently the aggregate recovery rate[11] increased from 38.8 percent in H1-FY04 to 43.8 percent during H1-FY05.

Figure 2.9: Bank Wise Recovery Ratios



The most pronounced improvement was seen in the case of DPBs, which registered a recovery rate of 115.6 percent (due to pre-mature loan repayments) during H1-FY05 as against an already high recovery ratio of 98.4 percent in H1-FY04. An improvement in DPBs recovery ratio, is not surprising as these institutions need to be more careful given their relatively smaller capital. Another important development in agriculture recovery profile was the improvement in recovery ratio of ZTBL, which rose by one percentage point to 29.8 percent in the first half of FY05. Given the largest share of ZTBL in the amount recoverable (68.2 percent), there is a need to improve its recovery ratio further to make ZTBL a more competitive and viable institution.

2.2 Industrial Production[12]

Industrial production, as measured by the Index of Industrial Production (IIP), recorded a robust growth of 15.4 percent YoY during H1-FY05, significantly higher than the 9.8 percent annual growth target. While the growth is certainly slower than the 21.0 percent seen in H1-FY04, it is nonetheless impressive given

[11] Amount recovered as percent of the total amount recoverable.

[12] Industrial Production is measured by IIP and it includes sub-sectors of LSM, *mining & quarrying*, and *electricity generation*. Due to data constraint on *mining & electricity*, estimated production figures, extrapolated using the available data (for July-August 2004) were used for the months of September-December 2004.

the strong performance in almost all the months of H1-FY05 (see **Figure 2.10**).[13]

The deceleration in the H1-FY05 growth rate relative to the preceding year is evident in all components of IIP except *electricity generation.* However, despite the decelerated growth rate, LSM continued to dominate the industrial growth profile, contributing approximately two-thirds of the overall industrial growth during the period (see **Figure 2.11)**.

Figure 2.10: Changes in IIP

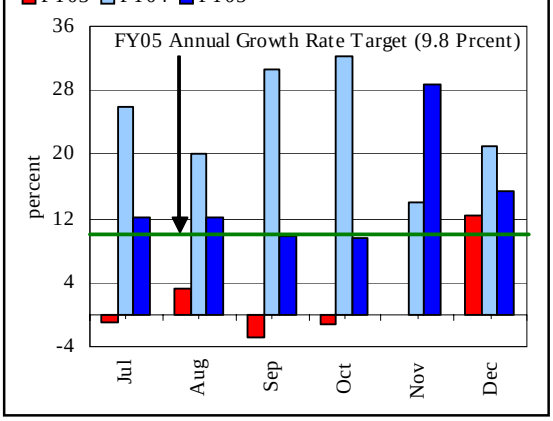
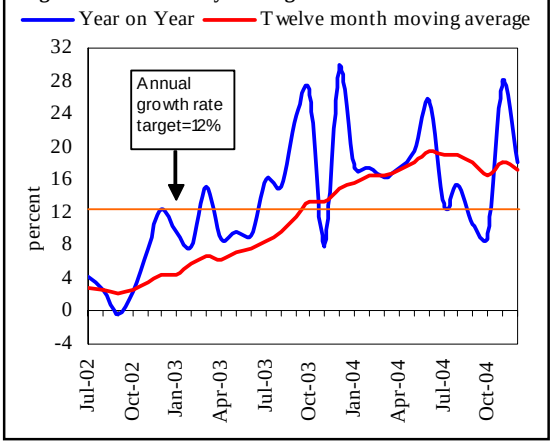


Figure 2.11: Monthly Change in LSM Index



2.2.1 Large Scale Manufacturing (LSM)

Provisional data shows that LSM growth during H1-FY05 remained comfortably above the 12 percent annual target. While this suggests that the annual growth target will very likely be surpassed, the growth *momentum* clearly seems to have weakened somewhat as evident in **Figure 2.12 & Table 2.4**. This deceleration appears to be largely attributable to both, capacity constraints as well as a high base effect.

[13] Only in September and October did industrial growth drop below the FY05 target. It is no coincidence that in the corresponding months of FY04 industrial growth had been well above 30 percent, setting a high base for FY05 growth.

Expectations of a small deceleration in LSM growth in H2-FY05 seem to be supported by a cursory look at the distribution of the H1-FY05 growth performance of the various LSM components (see **Table 2.4**). In H1-FY05, not only are there three sub-sectors depicting negative growth, the number of sectors witnessing growth rates of over 10 percent have also declined. Also, the impact of capacity constraints in particular, could potentially be significant on the growth in some of the high-growth sectors, such as *electronics*, *automobiles* and *fertilizers* (see **Table 2.5**). To put this in perspective, these three sectors contributed approximately 6.0 percentage points to the H1-FY05 LSM growth (as compared to 5.2 percentage points during H1-FY04). In addition, a decline in FY05 sugarcane crop would lead to a fall in *sugar* production. SBP forecasts indicate that LSM growth during FY05 is likely to range between 12 to 16 percent.

The most notable feature of the current fiscal year's LSM performance is that large investment in the textile industry along with high cotton output is beginning to

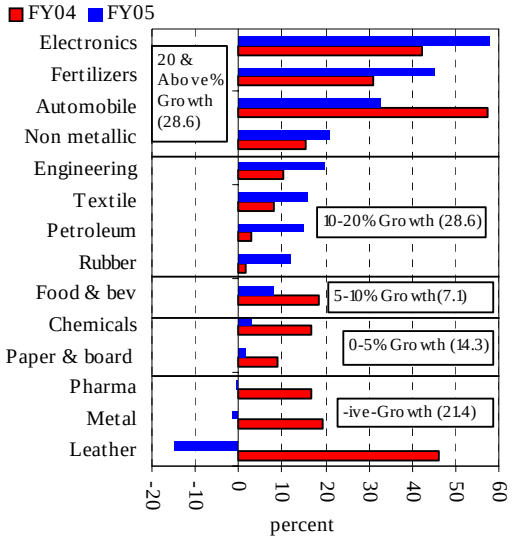
Table 2.4: Distribution of Sub-sector Growth Rates-H1

numbers

	FY04 [1]	FY05
Negative	0	3
0-5%	2	2
5-10%	2	1
10-20%	6	4
20% and above	4	4

[1] Excluded sub-group of wood products

Figure 2.12 Growth in LSM Sub-sector during



Note: Figures in parenthesis show group's share in LSM

Table 2.5: LSM Growth Rate H1-FY05

percent

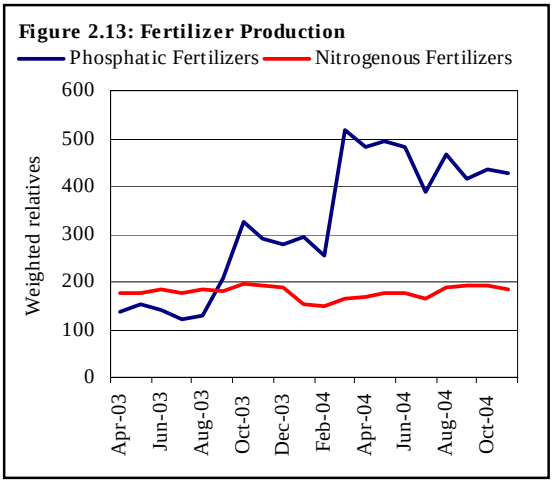
	FY03	FY04	FY05
Overall	4.8	17.9	16.1
Excluding fertilizer	6.1	17.4	14.8
Excluding automobile	2.8	14.9	14.4
Excluding electronics	3.1	16.8	13.8
Excl. automobile & electronics	2.8	14.9	11.8
Excl. automobile, electronics & fertilizer	2.2	12.7	10.1

Source: Federal Bureau of Statistics

appear in the form of higher production in this sub-sector. During H1-FY05 textiles sector almost doubled its growth rate to 15.9 percent although it was disconcerting that the production of large units in value added items recorded a negative growth. Considering that almost one-third of LSM value added originates from textiles, the impact of this robust growth on exports and employment is likely to be favorable. The rise in textile production during H1-FY05, despite weaknesses in external demand is indeed an encouraging development. This substantial growth was supported by the various textile sub-sectors such as cotton ginned, cotton cloth and cotton yarn, which recorded strong growth rates of 39.4 percent, 21.8 percent and 7.5 percent respectively in H1-FY05.

One of the strongest growth rates amongst LSM sub-groups during H1-FY05 was seen by *fertilizers*, where production rose by more than 45.4 percent YoY (even over the 31.1 percent rise in the corresponding period of FY04). This owed principally to the re-commencement of production by the phosphatic unit of a large domestic producer (see **Figure 2.13**). However, despite this increase, domestic production was still unable to meet demand, necessitating a 7 percent YoY rise in imports during the period. The production shortfall, together with rising international prices, was reflected in higher domestic prices for both urea (up 35.8 percent YoY) and DAP (up 26.6 percent YoY).

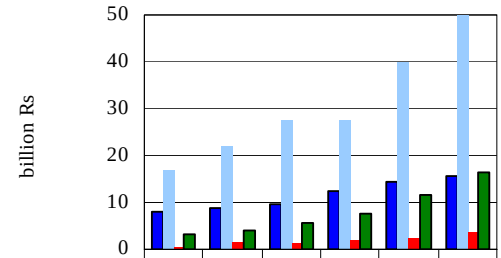
Figure 2.13: Fertilizer Production



Unfortunately, while fertilizer demand is expected to grow strongly, domestic production capacity is not expected to keep pace in the near term. As a result, the contribution of the fertilizer sub-group to overall LSM growth is expected to decline sharply post-February 2005. It is not obvious that the fertilizer industry is gearing itself, like other sub-sectors, to invest in capacity expansion or new capacity addition. This has serious repercussions for the coming years as the demand for fertilizer has already outstripped domestic production. Government and industry should chalk out plans immediately to overcome this emerging problem.

Electronics and *automobiles* sub-sectors witnessed even stronger growth during H1-FY05, benefiting from continued availability of relatively low cost consumer financing and suppliers' credit.[14]

Figure 2.14: Outstanding Position of Consume Loans



	Q1-FY04	Q2-FY04	Q3-FY04	Q4-FY04	Q1-FY05	Q2-FY05
Credit cards	8.0	8.9	9.7	12.3	14.5	15.8
Auto loans	16.9	22.2	27.6	27.8	40.2	49.8
Home appls.	0.6	1.6	1.2	2.2	2.4	3.5
House fin.	3.4	4.1	5.5	7.8	11.5	16.4

Specifically, despite a slower growth in the production of *refrigerators* and *electric transformers*, the *electronics* sector saw growth accelerate to 58.0 percent YoY during H1-FY05 from 42.5 percent YoY rise in the same period of FY04. The major impetus to this was from the big jump in the production of *TV sets, air conditioners* and the inclusion of two new items (*deep freezers* and *electric fans*) in this category. A slowdown in the production of electric transformers is mainly attributed to a sharp decline in its exports (down 78.1 percent YoY during H1-FY05). On the other hand, a rise in the production of TV sets is mainly a function of strong domestic demand on the back of expanding cable TV network and liberal availability of consumer financing.

Consumer financing also continued to play an important role in the expansion of automobile industry. During the H1-FY05, auto loans disbursement by commercial banks increased by Rs 22.0 billion (see **Figure 2.14**), which helped the *automobile* manufacturing sub-sector to record another year of robust growth, production rose 32.9 percent YoY during this period against 57.6 percent growth in H1-FY04.[15] Within the automobile sector, the production of *Light Commercial Vehicles* (*LCVs)* registered the highest growth (62.4 percent) followed by *buses* (40.5 percent) during H1-FY05. This significant rise was due to a low base effect as well as a reflection of increased investment in the transport sector on the back of credit availability for small & medium scale enterprises.

[14] Manufacturers/dealers are offering the consumers durable on easy installments mostly on zero interest rate.
[15] As many as 70 percent of locally assembled cars are being sold through leasing and bank financing schemes while the rest of 30 per cent are being delivered on cash basis.

Similarly, the growth in the production of *cars & jeeps*, though decelerated, was a robust 29.3 percent YoY in H1-FY05. The growth in the production of *motorcycle & auto rickshaw* and *tractors* industry was also strong and recorded at 48.5 percent and 29.7 percent respectively during H1-FY05. However, the growth prospects for these industries are limited without expansion in the production capacity as these are operating at over 100 percent of the installed capacity. The production of trucks registered a single digit growth of 4.9 percent during H1-FY05 against a growth of 13.7 percent during the same period last year. In response of strong growth in automobile industry, *tyres & tubes* industry also witnessed a growth of 12.1 percent during the first six months of FY05 as compared with a weak growth of 1.5 percent during the same period of FY04.

Increased economic activity in the country is also reflected in the rapid growth in the housing and construction sector, which in turn pushed the growth in allied industries such as cement, paints and varnishes, glass sheets, wood etc. Moreover, the robust domestic demand is being boosted by strong external demand; particularly from Afghanistan. The performance of the construction sector can be judged from **Table 2.6**.

Table 2.6: Construction-Performance Indicators

	Unit	FY04				FY05	
		Q1	Q2	Q3	Q4	Q1	Q2
Cement production	000 ton	3,061	3,036	3,180	3,685	3,735	6,190
Iron & steel (Pakistan Steel plus imports) [1]	000 MT	533	5,99	545	612	719	936
Import of construction & mining machinery	million Rupees	1,655	1,306	1,241	1,643	2,122	3,499
Housing finance (outstanding position as on) [2]	million Rupees	14,599	16,141	15,045	18,260	20,816	23,925

[1] Excluding the imports of iron & steel scraps

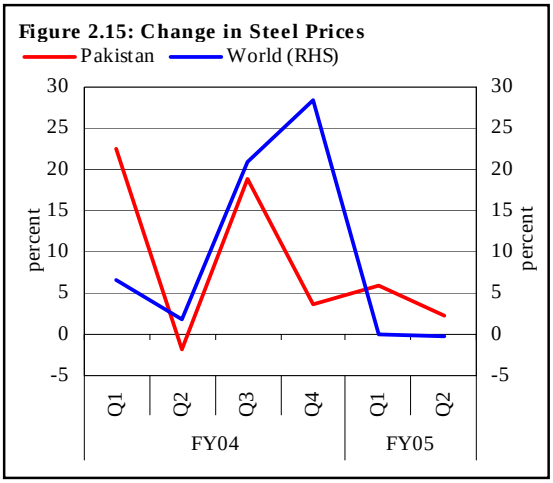
[2] Disbursement for construction

In fact, the cement industry recorded a 21.4 percent rise in production during H1-FY05 over 15.5 percent growth in the corresponding period of last year. While local cement dispatches rose 21.3 percent YoY during H1-FY05 to 7.1 million tons, cement exports in the same period increased by 58.5 percent YoY to 0.8 million tons.

Not surprisingly, given the strong construction activity, the complimentary demand for steel and iron increased as well (by 46.3 percent YoY) during H1-FY05. This rise was met through a 49.8 percent jump in imports following the fall in the production of Pakistan Steel by 19.6 percent YoY in the same period. The supply shortfall underpinned a rise in domestic prices of iron and steel products in

H1-FY05, despite stable international prices and a reduction in the import tariffs. Specifically, the prices of steel products, as measured in the WPI index, rose by 2.3 percent during H1-FY05[16] as compared with a decline of 1.8 percent during H1-FY04 (see **Figure 2.15**). The contribution of other construction-associated industries such as glass sheets, paints & varnish (solid and liquid), and wood were exceptional with the growth rate of 11.3 percent, 49.8 percent and 185.7 percent respectively during H1-FY05.

Figure 2.15: Change in Steel Prices



The output of food group also witnessed a significant growth on account of higher production of cooking oil, sugar, wheat milling and cigarettes (see **Table 2.7**). The output of cooking oil increased by 25.5 percent in H1-FY05 as compared with a growth of 19.5 percent in the same period of the previous year. The rise in the production of cooking oil is mainly a result of increased margins as international prices of palm oil (and soybean oil) declined sharply, while manufacturers did not pass on this benefit to consumers, possibly anticipating that the decline in international prices would be reversed. While, unanticipated international prices may be a cause of inventory building, strong demand of cooking oil and ghee from Afghanistan is another source of comfort for manufacturers. The sugar industry recorded a growth of 18.6 percent during H1-FY05 as compared with a growth of 23.5 percent in the same period of last year[17]. Finally, the production of cigarettes registered a growth of 7.3 percent YoY in H1-FY05 against a growth of 16.0

[16] Pakistan Steel increased the ex-factory prices of all products. Extra charges for special grades have also been increased. The steel prices have gone up from Rs 38,000 per ton to Rs 43,000 per ton during H1-FY05. The continuing price pressures has prompted the government announce a further 25 percent reduction in the import tariff on steel, on December 10, 2004. Further there have been calls to restrain the alleged smuggling of steel to Afghanistan.

[17] However, it may be noted that given a fall of 5.8 percent in sugarcane production during FY05 crop, it is likely that the growth in the production of refined sugar may decline in the months ahead. According to Pakistan Sugar Mills Association (PSMA) report, as on February 1, 2005 sugar production stood at 1.826 million tons against 1.938 million tons of the corresponding period last year, showing a decline of 5.8 percent in production.

percent YoY in the same period of FY04. This slowdown is largely explainable by a substantial 56 percent YoY decline of cigarette export volumes during this period.

Table 2.7: Growth in the Production of LSM Industries (Jul-December)

		Percentage change				Percentage change	
Items	**Weights**	**FY04**	**FY05**	**Items**	**Weights**	**FY04**	**FY05**
Textile	**32.62**	**8.0**	**15.9**	**Automobile**	**5.27**	**57.6**	**32.9**
Cotton yarn	17.40	1.6	7.5	Cars & jeeps	3.37	70.0	29.3
Cotton cloth	10.06	20.9	21.8	Tractors	0.93	47.7	29.7
Cotton ginned	4.49	-1.6	39.4	LCVs	0.59	4.4	62.4
Other five items	0.68	19.1	-1.4	Motorcycles	0.18	75.4	48.5
Food & tobacco	**19.12**	**18.3**	**8.0**	Buses	0.11	-19.1	40.5
Vegetable ghee	5.65	17.1	-4.9	Trucks	0.08	13.7	4.9
Sugar	5.53	23.5	18.6	**Metal industries**	**4.67**	**19.5**	**-1.4**
Cigarettes	4.07	16.0	7.3	Pig iron	2.15	20.1	1.2
Cooking oil	1.76	19.5	25.5	Coke	1.92	20.2	1.4
Wheat milling	1.32	NA	16.2	Billets	0.45	16.8	-21.1
Tea	0.42	6.1	-3.6	H.R/coils and plates	0.11	11.5	-8.9
Beverages	0.37	19.2	-20.7	C.R coils/plates/sheets	0.04	10.4	-8.5
Petroleum products	**6.97**	**2.8**	**15.0**	**Fertilizers**	**4.51**	**31.1**	**45.4**
Pharmaceuticals	**6.70**	**16.6**	**-0.7**	Phosphatic	2.51	65.4	84.3
Tablets	3.43	16.4	-3.5	Nitrogenous	2.00	5.0	-1.4
Syrup	2.03	23.9	-0.2	**Electronics**	**3.31**	**42.5**	**58.0**
Injections	0.59	14.0	5.3	Electric transformers	0.76	71.3	57.0
Capsules	0.29	29.6	8.4	Refrigerators	0.78	75.4	23.0
Other two items	0.36	-20.2	6.0	Deep freezers	0.53	-	63.2
Chemicals	**6.39**	**16.6**	**3.0**	TV sets	0.30	-2.2	17.5
Caustic soda	0.97	15.0	11.8	Air conditioners	0.10	656.5	776.2
Soda ash	0.12	3.5	3.0	Electric fans	0.02	NA	5.3
Other ten items	5.30	19.1	1.7	Other five items	0.81	43.6	3.5
Non metallic minerals	**5.58**	**15.3**	**21.2**	**Engineering items**	**0.59**	**10.5**	**19.9**
Cement	5.52	15.5	21.4	Safety razor blades	0.35	-1.4	26.0
Glass sheets	0.07	7.0	11.3	Bicycles	0.09	1.4	-6.7
Leather products	**3.03**	**46.3**	**-14.6**	Sewing machines	0.11	27.2	-12.6
Paper & board	**0.80**	**9.1**	**1.5**	Power looms	0.02	49.4	-19.5
Tyres & tubes	**0.40**	**1.5**	**12.1**	Diesel engines	0.01	34.9	43.6
Wood products	**0.04**	NA	**185.7**	Other five items	0.02	-35.0	-0.3

Note: The weights of the LSM industries are adjusted so as the sum of total weights become 100.
NA: Not available.

Source: Federal Bureau of Statistics

Strong domestic demand led the acceleration in the growth of petroleum sub-sector, which surged to 15.0 percent YoY in H1-FY05 as compared with a rise of a mere 2.8 percent YoY in the corresponding period of FY04. This is evident from the growing capacity utilization of domestic refineries during this period to cater to rising demand from increased economic activity as well as to greater dependence on thermal power generation.

2.2.2 Growth of User Based Industrial Groups

While *basic* and *capital* goods, (in terms of end-use classification of industrial production) witnessed acceleration in growth during H1-FY05, the production of *consumer* and *intermediate* goods industries recorded a deceleration during the same period.

The major contribution in *capital* goods, in terms of weighted growth, stemmed from a robust 62.4 percent rise in LCV production, 57 percent rise in electric transformers, as well as a rise in the production of tractors, buses, and diesel engines during the first six months of FY05 (see **Table 2.8**).

Table 2.8: Growth of Industrial Production by End Use During July-December

percent

Sectors	Weights	FY03	FY04	FY05
Basic goods	26.6	4.7	2.9	14.7
Intermediate goods	39.9	1.5	16.8	14.9
Consumer goods	31.3	8.2	38.4	16.1
- Non-durables	27.3	0.3	32.3	8.9
- Durables	4.1	61.0	63.7	40.0
Capital goods	2.1	28.5	35.9	45.0

Source: Based on data from FBS

In contrast, the growth in the production of *intermediate* goods declined but nonetheless remained robust. Most of the growth in the production of *intermediate* goods came from higher production of cotton (ginned), natural gas, fertilizer, industrial chemicals, paints, cement etc. The *consumer* goods group grew at a rate of 16.1 percent YoY in H1-FY05 compared with a growth of 38.4 percent YoY during the same period of FY04. A disaggregated analysis suggests that this slowdown is attributable to both *durables* and *non-durables* sub-groups. The slowdown in the growth of *consumer non-durable* sub-group occurred due to significant declines in the production of vegetable ghee, beverages, footwear and some of the pharmaceutical items. Similarly, declines in the production of bicycles and sewing machines slowed the growth of *consumer durables* sub-group.

2.2.3 Capacity Utilization

During H1-FY05, capacity utilization in the selected LSM industries increased in

the range of 1.4 to 33.6 percentage points (see **Table 2.9**). In particular, the *electronics* industry witnessed an impressive 33.6 percent increase in capacity utilization, as production rose by 58 percent YoY during this period. This owed to a substantial rise in the production of both refrigerators and air conditioners.
While substantial idle capacity is still available in the air conditioner industry, there is a need to enhance the installed capacity in refrigerator industry as the capacity utilization has reached 102.5 percent by end of H1-FY05.

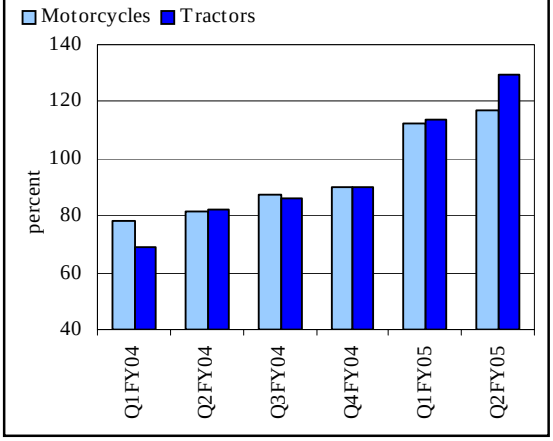
Table 2.9: Capacity Utilization in Selected Industries (Jul-Dec)

percent

	FY04	FY05
Exceeding 100 percent		
Petroleum refining	94.1	108.2
Fertilizer	102.4	105.6
Approaching 100 percent		
Paper & paper board	98.2	99.7
Industrial chemicals	86.6	96.6
Steel (Pak Steel)	94.0	93.0
Between 50 and 90 percent		
Cement	72.0	83.4
Automobile (overall)	59.8	83.2
Electronics (refrigerators and air conditioners)	44.8	78.4
Cars & LCVs	53.8	71.5
Below 50 percent		
Vegetable ghee & cooking oil	40.0	40.0
Trucks & buses	22.1	26.4

Source: EAC- Ministry of Industries & Production

Figure 2.16: Capacity Utilization



Similarly, the *automobile* industry witnessed an increase in capacity utilization during H1-FY05. Within the *automobile* industry, the capacity utilization in tractors witnessed the largest increase of 47 percentage points, followed by motorcycles/ scooters, LCVs and cars & jeeps. Since the capacity utilization in the tractors and motorcycle industries has reached about 129.2 percent and 117.3 percent respectively (see **Figure 2.16**), therefore, to meet the growing domestic demand, manufacturers are planning to expand the production capacity during years ahead.

During the first six month of FY05, capacity utilization in the cement industry increased by 11.4 percentage points to 83.4 percent. As a result of strong growth in the sector, most cement manufacturers have announced expansion plans. However, despite expectations of strong demand growth, it seems likely that the cement industry will see considerable surplus capacity 2007 onwards when large production capacities are expected to begin production.

The petroleum refining industry has also responded to increased demand by increasing capacity utilization by 14.1 percentage points in the first half of FY05. However, it seems insufficient as the capacity utilization in this industry reached to 108.1 percent during Jul-Dec FY05. The capacity constraints suggest that there is a need to expand its capacity in future to meet the rising demand of petroleum products, which was generated by the substantial industrial growth in the economy. Capacity utilization in vegetable ghee & cooking oil has remained low. A probable reason for this under utilization is that unregistered ghee and cooking oil-processing units in the country are filling in the gap.