5 External Sector

5.1 Overview

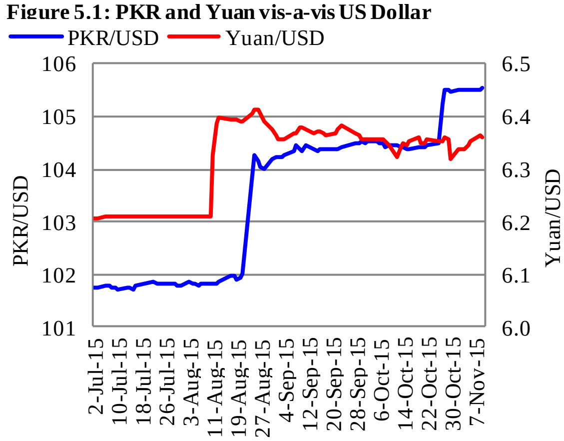
The on-going slump in global commodity prices continued to support Pakistan's external sector. Oil prices posted a fresh decline of 25 percent during Jul-Sep 2015, and averaged 51 percent lower than the same period last year. This not only helped reduce the country's import bill, but also contributed to a much smaller deficit in the services account (**Table 5.1**). As a result, the current account posted a lower deficit than last year, which was comfortably financed via Eurobond issuance; FDI inflows; and commercial borrowings by the government.[1] The release of 8th tranche of the IMF program further strengthened external position. As a result, the country's total FX reserves increased by US$ 1.4 billion during the quarter, to surpass US $20 billion – first time ever, at end-September 2015.

Table 5.1: Summary of Pakistan's External Sector
million US$

	Q1-FY15	Q1-FY16	*Abs change*
Current account balance	-1,631	-351	1,280
Trade balance	-6,054	-4,700	1,354
Exports	5,959	5,321	-638
Imports	12,013	10,021	-1,992
Oil imports	4,476	2,582	-1,894
Services balance	-658	-177	481
CSF	735	713	-22
Freight deficit	-766	-395	370
Worker remittances	4,775	4,967	192
FDI in Pakistan	201	248	47
Portfolio inv. in Pakistan	133	390	257
Euro bond	0	500	500
FX reserves (end-period)	13,511	20,074	6,563

Source: State Bank of Pakistan

Figure 5.1: PKR and Yuan vis-a-vis US Dollar

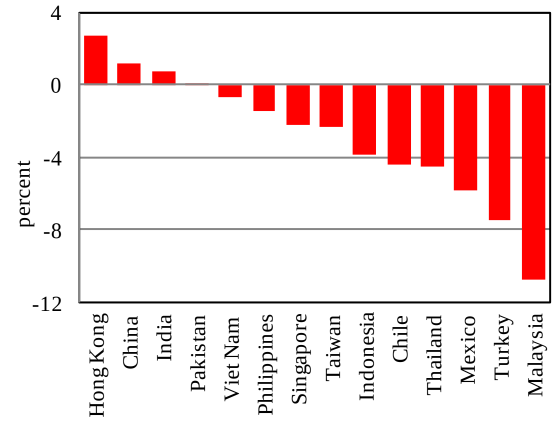


Source: State Bank of Pakistan

[1] Due to delays in budgeted disbursements of project and program loans, the government borrowed US$ 513 million short-term commercial loans from private lenders during Q1-FY16.

The PKR depreciated by 2.6 percent against the US Dollar during Q1-FY16. This depreciation mainly represents turmoil in Asian stocks and currency markets during August: Yuan's reference rate was reduced by 2.7 percent (**Figure 5.1**). In relative terms, the PKR depreciated marginally as currencies of our major trading partners like the EU, Japan and the UK, weakened vis-à-vis the US Dollar during the quarter.

Figure 5.2: Change in REER during Jul-Sep FY16



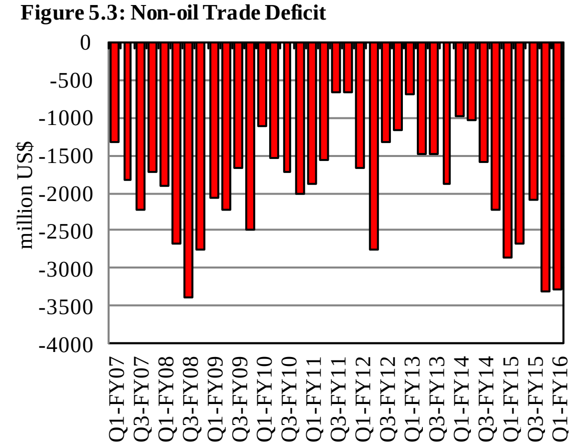
Source: Haver Analytics

More importantly, most Asian currencies have plummeted in real terms that may pose concern for Pakistan's trade competitiveness (**Figure 5.2**).

Additional challenges to external sector include the following:

(i) Non-oil trade deficit has reached 7-year high of over $3 billion in the first quarter (**Figure 5.3**). Last time this deficit touched $3 billion a quarter, was early 2008 when global prices were booming and our importers hurried purchases in an anticipation of further increase in prices. This time, however, the reason is different: it is the decline in non-oil exports (6th quarter in a row) that has caused non-oil deficit to touch this level.

Figure 5.3: Non-oil Trade Deficit



Source: Pakistan Bureau of Statistics

Non-oil imports have posted a YoY decline of 1.7 percent over last year;

(ii) FDI inflows, though remained higher than last year, are still low in volume (**Table 5.2**). Bulk of the investment during Q1-FY16 came from China; power projects were prime recipients. FDI in other sectors have dried up, as the slump in commodity prices and global economic uncertainty, has put many investment projects on hold. A related concern arises from the fact that FDI from other countries have remained low. While the US, Saudi Arabia and Sweden have divested from Pakistan during the quarter, inflows from Japan, the UK and UAE remained lower than last year; and

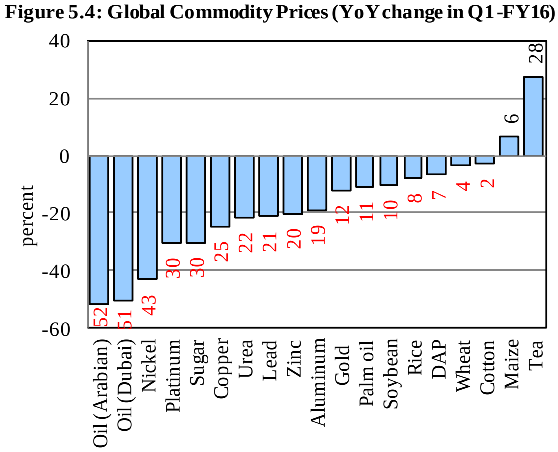
Table 5.2: FDI Inflows
million US$

	Q1-FY15	Q1-FY16
Total FDI inflows	201	248
FDI from China	2	186
FDI excl. China	199	62

Source: State Bank of Pakistan

(iii) Gulf countries that constitute nearly 61 percent of total worker remittances to Pakistan, rely heavily on oil revenues to finance infrastructure spending; if prices fail to recover, governments in this region may need to cut back their spending. Saudi Arabia seems particularly vulnerable: since January 2015, its FX reserves have been depleted by almost US$ 80 billion, to finance oil-led fiscal deficit.[2] IMF estimates the Kingdom's breakeven oil price to be much higher than the prevailing one; the Fund has recently cautioned Saudi Arabia against risk of reserves depletion within 5 years, if current level of deficit is sustained.[3,4]

Figure 5.4: Global Commodity Prices (YoY change in Q1-FY16)



Source: Bloomberg

[2] Saudi Arab's FX reserves (including FX, reserves position in the Fund and the US$ value of SDR holdings by Saudi Arabian Monetary Agency) have been reduced from US$ 764 billion in January 2015, to US$ 654 billion at end-September 2015 (Source: Haver Analytics).
[3] IMF defines fiscal breakeven oil price as, "the oil price that balances the government budget".
[4] Source: "Middle East and Central Asia", IMF's Regional Economic Outlook, October 2015.

5.2 Current account: *Commodity prices weigh in*

The current account benefited from the fact that price of commodities which Pakistan imports (like oil, metals, fertilizers and palm oil) fell much steeply than the price of commodities which Pakistan exports (like rice and cotton) (**Figure 5.4**). Therefore, the decline in imports was much stronger than the decline in exports during Q1-FY16. What concerns us is the fact that while the decline in imports is explained almost *entirely* by price effect, the decline in exports was caused by *both* lower prices and quantum (**Section 5.4**).

Worker remittances

Worker remittances posted a growth of only 4 percent YoY during Q1-FY16, compared to 22 percent growth during the same period of FY15. This slowdown basically represents seasonal factor (high base effect): expat Pakistanis typically send higher remittances during the early days of Ramadan for Eid related expenses and Zakat payments; in CY14, most of these disbursements were realized in the month of July (included in FY15), whereas in CY15, these fell in the month of June (also included in FY15).[5] Therefore, remittance inflow posted a YoY decline in July 2015, causing an overall slowdown during Q1-FY16.

Going forward, we expect remittances to comfortably surpass the target set in the Annual Plan for FY16.[6] However, the pace of increase is likely to be much modest compared to last year.[7] Besides seasonal factor, we believe that some slowdown may be driven by the government's decision to cut effective rebate on remittances with effect from July 1, 2015.[8]

Another factor that might weaken remittance inflow is the possible decline in public spending in the GCC that constituted the bulk of increase in remittances last

[5] In 2015, 1st Ramadan fell on 19th June, whereas last year it had fallen on 30th June 2014.
[6] The government has envisaged remittance inflow of US$ 19 billion for the full-year FY16 (Source: Planning Commission). This represents growth rate of only 1.4 percent over FY15.
[7] In FY15, remittances had grown by 18.2 percent. As mentioned earlier, this extraordinary growth stemmed mainly from seasonal effects.
[8] SBP vide *EPD Circular Letter No. 12 of 2015,* announced a cut in rebate from 25 SAR (Saudi riyal) to 20 SAR per transaction. Furthermore, the minimum amount of remittance to qualify for reimbursement of T.T. Charges has been increased from equivalent of USD 100 to USD 200. This rebate effectively works as reimbursement of telegraphic transfer (TT) charges that banks incur for funds transfer. Banks are also allowed to share this rebate with partner exchange companies and/or money transfer organizations, to encourage them mobilize more customers.

year.[9] In the oil and gas sector, some impact of oil slump is already visible in layoffs and salary cuts. Up till now, Pakistanis are largely unaffected, since most of them work in construction and services sectors; number of Pakistani migrants into this region is still following an upward trend.[10] This is because GCC governments have been able to sustain their fiscal spending with the help of FX reserves and funds mobilized via bond issuances.[11] However, a persistent weakness in oil prices would necessitate heavy fiscal adjustments, especially in those countries where breakeven oil price is much high (like Bahrain, Saudi Arabia, Oman and Yemen).

5.3 Financial account

Foreign direct investments

Net FDI posted an increase of US$ 47 million YoY during the first quarter of FY16. This increase was primarily on account of inflows from China in coal-based power projects, under the China-Pakistan Economic Corridor (CPEC). Excluding this, the overall FDI has actually dropped by US$ 137 million YoY (**Table 5.2**).[12]

The decline in FDI was attributed to divestment from Pakistan's petro-chemical sector.[13] This divestment mainly represents the decision of California-based Chevron Corporation, to dispose-off its downstream petroleum assets (like lubricants, fuel stations, etc.) from Pakistan, Egypt and Australia.[14] With 538 retail fuel outlets across Pakistan, and a market size of 5 percent, Chevron Pakistan (Caltex) will now be operated by Total Parco.

For the remaining year, more FDI is expected from China under the CPEC: the government has estimated disbursements of Rs 207 billion (around US$ 2.1

---

[9] GCC countries contributed 81 percent of the *increase* in worker remittances in FY15.

[10] Number of Pakistanis migrating to GCC countries has increased by 23 percent during January to September 2015, over the same period last year. Here it is important to mention that there is no data available on number of Pakistanis returning from abroad.

[11] Saudi Arabia issued sovereign bonds, first time after 2007, amounting SAR 15 billion (or US$ 4 billion) in July 2015, for deficit financing. Source: http://www.reuters.com/article/2015/07/10/saudi-bond-idUSL8N0ZQ03F20150710#Fcoh8Sx64YPHigz5.97

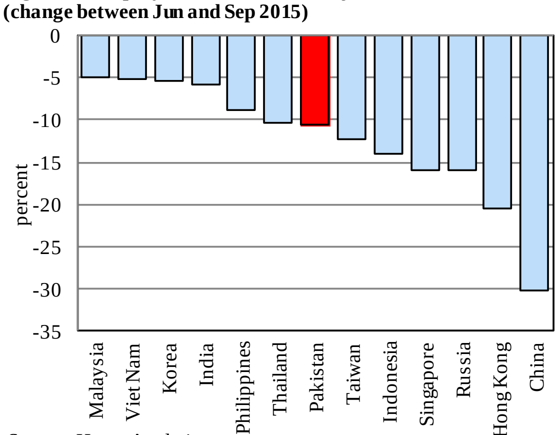
[12] China's FDI ($186 million) constituted 75 percent of total net FDI inflows during the period.

[13] Petro chemicals sector recorded huge outflow of $135.8 million during the quarter.

[14] Due to a sharp decline in oil price in the international market, Chevron has already pulled out of shale exploration in countries like Romania, Lithuania and Poland.

billion) from China in 2015-16 budget;[15] power and construction would be the prime recipients. Other than CPEC, no major activity is in pipeline: uncertainty in the international oil market, and the squeeze in institutional liquidity, has stalled growth in global FDI. Only if the government expedites its privatization process – and offer its stakes to foreign investors, we should expect more FDI inflows before June.[16]

Figure 5.5: Equity Performances in Major Asian Markets (change between Jun and Sep 2015)



Source: Haver Analytics

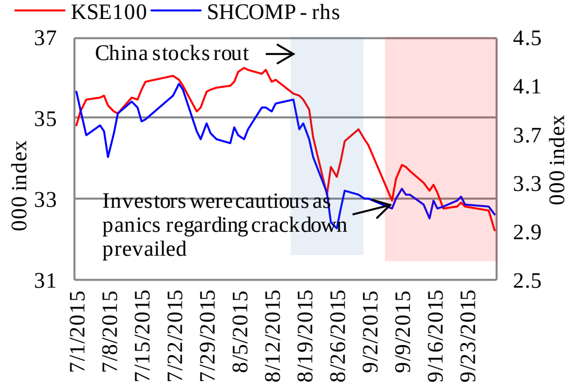
Portfolio investment

Portfolio investments in Pakistan posted an increase of US$ 257 million YoY during the first quarter of FY16. Most of the activity was seen in the public sector, as the government rolled out a 10-year Eurobond in the international market during the last week of September 2015. This was the third sovereign issue in past 17 months; similar to previous two instances, this was also oversubscribed. However, this time the government preferred to stick to its target of US$ 500 million, as coupons offered were quite above expectations. A significant improvement in Pakistan's credit worthiness could not trim the spread, as global bond market was facing tight conditions on account of a massive institutional sell-off (**Chapter 4**).

The situation in global equity market was not helpful either. Many emerging economies struggled with turbulent capital markets during the period, as investors turned wary of a slowdown in China and a possible hike in Federal funds rate (**Figure 5.5**). August was particularly painful, when Chinese stocks tumbled by 13 percent; Hong Kong by 12 percent; and Singapore and Vietnam by 9 percent each.

[15] Budget documents for 2015-16.
[16] Privatization of Heavy Electrical Complex (HEC), and Pakistan Steel Mills (PSM), is on cards.

Figure 5.6: Performance of KSE vis-a-vis Chinese Stocks*



* Measured by Shanghai Composite Index - SHCOMP
Source: Karachi Stock Exchange and Bloomberg

Although Pakistan's largest bourse had, for long, been insulated from developments in global markets, this time it could not resist the shock: KSE lost nearly 3 percent during the month of August. Both local and foreign investors cut their positions in response to a near-crash in Chinese stocks (**Figure 5.6**). In dollar terms, there was a net outflow of US$ 85 million in SCRA during the month of August.[17]

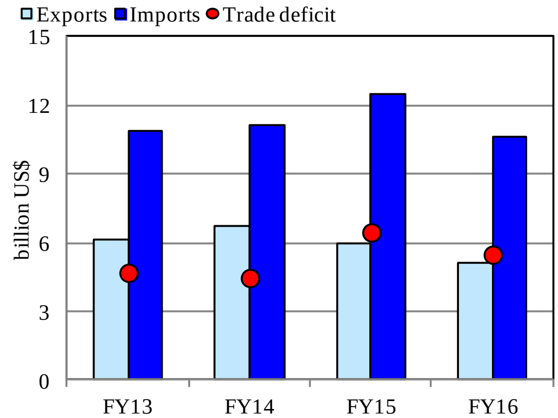
September turned out to be a better month for most Asian markets, but in case of Pakistan, it was no good. In fact, KSE was the worst-performing market in Asia during the month with nearly 9 percent decline in valuations. This was an outcome of rumors prevailing in the market regarding anti-corruption crackdown on major stock brokers. Investors were particularly flustered with regulatory action against certain brokers for not maintaining a clear segregation of own and clients' accounts. Foreign investors pulled away nearly US$ 46.7 million (or Rs 4.9 billion) from KSE during the month. It was only after the clarification from SECP in the last week of September (strongly dismissing reference of certain cases to NAB) that bulls returned to KSE: the market gained 6.1 percent in the subsequent month.[18]

Going forward, inflows under the portfolio investment would be influenced primarily by developments in the global bond and stocks markets. For instance, we expect the government to wait for better spreads, before it could mobilize another US$ 500 million via sovereign issuance to meet budgetary targets. On a positive note, Morgan Stanley Capital International (MSCI) has put Pakistan in its

[17] Foreign investors can invest in Pakistan's stock and bond markets via special convertible rupee accounts (SCRA).
[18] On 29th September 2015, SECP clarified that NAB was approached to take punitive action exclusively against those brokers who embezzled shareholders' assets and have fled the country; no other case against brokerage houses has been referred to NAB for any regulatory violations.

review list for reclassification under 'Emerging Markets'.[19] However, this process will not be completed before June 2016, which means gains from this reclassification would be realized from FY17 onwards.

Figure 5.7: Trade Account (Jul-Sep)

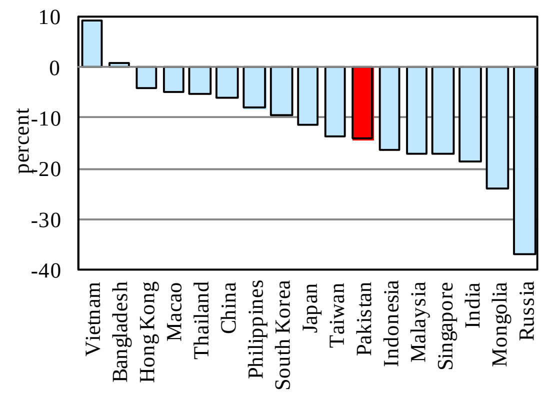


Source: Pakistan Bureau of Statistics

5.4 Trade account[20]

The country's trade deficit shrank during Q1-FY16 (**Figure 5.7**).[21] Both imports and exports posted a decline, but the fall in exports was more than offset by a sharp decline in imports: global commodity prices, which had been softening since July 2014, led to a greater contraction in the import bill.

Figure 5.8: Export Growth (YoY) in Asian Economies in Jul-Sep FY16



Source: Haver Analytics

Exports

Exports declined by 14.1 percent in Q1-FY16, compared to a fall of 10.4 percent in the same period last year. The decline was broad-based, but most prominent in rice, cotton yarn, fabric, bed-wear, leather

[19] Pakistan was part of the MSCI Emerging Markets between 1994 and 2008. However, the temporary closure of the Karachi Stock Exchange in 2008 led MSCI to remove it from the Emerging Markets and classify it as a "standalone country index". MSCI made Pakistan a part of the Frontier Markets Index in May 2009, and it has remained as such since then.

[20] This analysis is based on provisional data provided by the Pakistan Bureau of Statistics, which is subject to revision. This data may not tally with the exchange record numbers posted in Section 5.2.

[21] This improvement was expected, as imports were exceptionally high last year when prices began to fall and importers were panicked anticipating price reversals.

and cement. Both lower prices and quantum contributed to this trend (**Table 5.3**).

Table 5.3: Change in Export Values – Quantum and Price Impact

million US$

	Percent Share in Exports *	Q1-FY15			Q1-FY16		
		Quantity	Price	Value	Quantity	Price	Value
Basmati rice	2.8	-21.2	20.6	-0.6	-23.0	-12.0	-35.1
Non-basmati rice	5.8	-31.3	-10.0	-41.3	59.0	-49.7	9.3
Fish	1.5	-12.6	6.1	-6.5	-8.2	-5.4	-13.6
Fruits	1.8	-22.1	4.5	-17.6	-21.3	8.0	-13.3
Sugar	1.3	41.8	-1.1	40.8	-60.5	-0.4	-60.9
Meat	1.0	-15.4	0.8	-14.6	13.1	8.7	21.7
Raw cotton	0.7	-14.2	-1.5	-15.7	17.2	-11.7	5.5
Cotton yarn	7.9	-98.2	-26.2	-124.4	-71.9	-13.2	-85.2
Cotton fabric	10.7	-177.3	80.5	-96.7	-45.1	-24.6	-69.7
Knitwear	9.7	-9.1	70.0	60.9	23.5	-21.7	1.8
Bed-wear	8.7	-4.4	-13.2	-17.7	-44.2	1.4	-42.8
Towels	3.2	0.4	7.6	8.0	28.6	-4.8	23.8
Garments	8.2	22.4	-15.6	6.9	-27.5	55.0	27.4
Synthetic textiles	1.5	-19.8	25.2	5.3	-10.8	-6.9	-17.7
POL	2.7	-7.7	0.4	-7.2	-0.6	-8.7	-9.3
Footballs	0.7	1.3	3.5	4.9	4.5	-5.2	-0.7
Leather	2.1	-20.4	14.8	-5.6	-39.5	13.0	-26.5
Leather garments	1.6	-21.3	14.6	-6.8	-16.3	-4.0	-20.2
Plastic	1.3	-18.9	-3.7	-22.7	-9.1	0.3	-8.9
Cement	1.9	-6.4	1.6	-4.8	-52.4	-2.6	-55.0

*Average share in total exports during FY14 and FY15.
Source: Pakistan Bureau of Statistics

In our view, exports fell primarily because of global factors: exports of most emerging economies posted YoY declines in Jul-Sep 2015. More importantly, Pakistan has been able to increase its share in EU and US markets (**Figure 5.8**).[22]

[22] Share of Pakistan in the EU and US import markets (total) has increased to 0.37 and 0.17 percent, respectively during Jul-Sep FY16, compared to 0.34 and 0.16 percent same period last year. In the US market, the decline in Pakistan's share in apparel imports was entirely offset by better performance of other commodities like cereals, surgical instruments, raw cotton, etc.

Table 5.4: EU Import of Clothing from Major Countries (Jul-Sep)
value in billion US$; growth and share in percent

	Value		Growth		Share	
	FY15	**FY16**	**FY15**	**FY16**	**FY15**	**FY16**
China	13.42	11.47	6.3	-14.5	45.3	43.0
Bangladesh	3.99	4.10	5.5	2.6	13.5	15.3
Indonesia	0.47	0.39	3.3	-15.7	1.6	1.5
India	1.55	1.39	11.7	-10.7	5.2	5.2
Pakistan	0.66	0.69	30.2	4.1	2.2	2.6
Vietnam	0.99	0.98	28.9	-0.7	3.3	3.7
Turkey	3.23	2.86	6.2	-11.5	10.9	10.7
Total	**29.60**	**26.71**	**8.5**	**-9.8**	**82.1**	**81.9**

Source: Eurostat

Table 5.5: EU Import of Home Textile from Major Countries (Jul-Sep)
value in million US$; growth and share in percent

	Value		Growth		Share	
	FY15	**FY16**	**FY15**	**FY16**	**FY15**	**FY16**
China	1,228.0	1,137.4	15.5	-7.4	41.5	42.5
Bangladesh	107.2	84.1	-10.3	-21.5	3.6	3.1
Indonesia	16.0	10.4	4.8	-34.8	0.5	0.4
India	345.1	304.4	6.9	-11.8	11.7	11.4
Pakistan	431.4	409.4	25.2	-5.1	14.6	15.3
Vietnam	62.9	56.3	16.6	-10.5	2.1	2.1
Turkey	369.7	316.9	2.2	-14.3	12.5	11.8
Total	**2,957.0**	**2,674.8**	**11.9**	**-9.5**	**86.6**	**86.7**

Source: Eurostat

Table 5.6: US import of Non-Apparel from Major Countries (Jul-Sep)
value in million US$; growth and share in percent

	Value		Growth		Share	
	FY15	**FY16**	**FY15**	**FY16**	**FY15**	**FY16**
China	3,271.4	3,568.8	-2.5	9.1	48.5	49.7
Bangladesh	35.1	43.1	-0.2	22.7	0.5	0.6
India	857.2	951.6	12.0	11.0	12.7	13.3
Indonesia	52.2	57.1	-14.9	9.4	0.8	0.8
Pakistan	379.6	396.6	-2.1	4.5	5.6	5.5
Vietnam	173.5	185.0	12.8	6.7	2.6	2.6
Cambodia	7.1	17.0	-17.0	140.8	0.1	0.2
Total	**6,740.9**	**7,178.3**	**1.5**	**6.5**	**70.8**	**72.7**

Source: OTEXA

Most of the decline was seen in case of textiles, where exports fell by 5.6 percent YoY during Q1-FY16. As mentioned before, shrinking global demand has hurt exports. More specifically, EU's overall import of textile and clothing declined sharply during Jul-Sep FY16. In case of clothing, all major countries faced export declines in the EU market, except Pakistan and Bangladesh (**Table 5.4** and **5.5**). These two countries enjoy duty-free access to this market: Pakistan via GSP+ and Bangladesh via Everything-But-Arms (EBA). Indonesia, China and Turkey suffered the most, with notable declines in their respective shares, whereas, India maintained its contribution in the market. However, in case of home textiles, export of Pakistan and Bangladesh also suffered setbacks.

Table 5.7: US Import of Apparel from Major Countries (Jul-Sep)
value in billion US$; growth and share in percent

	Value		Growth		Share	
	FY15	**FY16**	**FY15**	**FY16**	**FY15**	**FY16**
China	10.0	10.7	-0.1	6.3	41.0	41.3
Bangladesh	1.3	1.5	-3.4	10.0	5.4	5.7
India	0.8	0.9	5.1	5.6	3.4	3.4
Indonesia	1.3	1.3	-0.7	1.3	5.1	4.9
Pakistan	0.4	0.4	-4.2	-3.8	1.7	1.5
Vietnam	2.7	3.1	15.9	14.3	11.1	12.0
Cambodia	0.7	0.7	-6.1	7.6	2.7	2.8
Total	**24.4**	**25.8**	**2.7**	**5.6**	**70.4**	**71.6**

Source: OTEXA

Table 5.8: US Import of Cotton Apparel from Major Countries (Jul-Sep)
value in billion US$; growth and share in percent

	Value		Growth		Share	
	FY15	**FY16**	**FY15**	**FY16**	**FY15**	**FY16**
China	3.9	3.8	-10.0	-0.7	33.2	33.1
Bangladesh	1.0	1.1	-5.0	7.5	8.7	9.4
India	0.6	0.6	2.3	6.0	4.9	5.2
Indonesia	0.6	0.6	-6.1	-6.4	5.5	5.2
Pakistan	0.4	0.4	-6.4	-4.4	3.2	3.1
Vietnam	1.2	1.2	10.1	2.7	10.3	10.7
Cambodia	0.4	0.4	-5.8	-6.2	3.6	3.4
Total	**11.6**	**11.6**	**-3.5**	**-0.3**	**69.4**	**70.1**

Source: OTEXA

In the US market, the overall import demand for textile and apparel increased during Jul-Sep 2015; however, Pakistan has not been able to firm up its exports (**Table 5.6** and **5.7**). Following the trend in previous few years, the demand for cotton textile, which constitutes the bulk of Pakistan's exports, continued to decline in the US market. The market for man-made fiber products is expanding at a fast pace, but Pakistan has failed to diversify its product range accordingly.[23] Worryingly, Pakistan has now begun to lose its share even in the *cotton* apparel market of the US (**Table 5.8**).

Rice exports fell by 7.1 percent YoY in Q1-FY16 – entirely due to a decline in sales of basmati. This is because of the penetration of Indian basmati into major markets like UAE and other GCC countries, due to better marketing and branding strategies. On the contrary, the demand for non-basmati rice from Pakistan remained strong, as unit values of Pakistani varieties declined much sharply compared to the declines in unit prices of Thailand and India.[24] Going forward, we expect some recovery in global prices due to subdued production in major exporting countries.[25] In case of Pakistan also, production is expected to decline, but carryover stocks would not allow prices of Pakistan's variety to increase much.

As far as *cement* is concerned, some decline in exports was expected. South Africa – the 2nd largest buyer of Pakistani cement, had imposed anti-dumping duty on different Pakistani cement companies (ranging from 14.3 percent to 77.1 percent) in May 2015.[26] This decision was taken at a time when Afghanistan, our largest buyer, had already lowered the overall demand for cement because of political instability and deteriorating law and order condition. Imports

[23] Overall import of non cotton apparel by the US increased by 6.1 percent during Q1-FY16, compared to a fall of 3.5 percent in the same period last year.
[24] According to FAO, the price of Pakistan's 25 percent broken rice variety witnessed the fall of 16.0 percent YoY during Q1-FY16 over the last year. It is larger than the fall in price of Indian as well as Thailand's broken rice.
[25] The overall paddy production was declined by 2.6 percent in 2015, compared to a fall of 0.4 percent in 2014. Specifically, Thailand and Vietnam are expecting to cut their rice production due to drought like weather conditions. Thailand government has even banned rice plantings for off-season crop, which typically account for nearly 30 percent of national production. Similarly in India, poor monsoon rains may curtail production for the second consecutive year.
[26] This decision of International Trade Administration Commission of South Africa, has been challenged by Pakistan's largest cement exporter (Lucky Cement). Ministry of commerce has also decided to challenge this decision in WTO.

from Pakistan in this market suffered also because of influx of cheaper imports from Iran (especially in Kandahar region near the Iranian border). Iran enjoys a much lower production cost than Pakistan, and also benefits from proximity to many western and southern parts of Afghanistan.[27,28]

Imports

Imports have declined by 14.7 percent in Jul-Sep 2015, compared to a sharp rise of 11.6 percent during the same period last year. This decline is primarily attributed to lower unit prices, as quantum import of most products has increased. As mentioned before, a slump in global prices, particularly POL and palm oil, has helped reduce import values (**Table 5.9**).

Table 5.9: Import Performance during Jul-Sep
value in million US$; growth in percent

	Value			YoY Growth	
	FY14	**FY15**	**FY16**	**FY15**	**FY16**
Food	1,042.0	1,430.1	1,198.9	37.2	-16.2
Machinery	1,434.5	1,765.0	1,707.0	23.0	-3.3
Transport	625.4	619.3	637.7	-1.0	3.0
Petroleum	3,984.5	3,927.8	2,251.1	-1.4	-42.7
Textile	524.2	635.5	628.3	21.2	-1.1
Chemical	1,556.6	1,860.4	1,781.2	19.5	-4.3
Metal	742.3	905.9	896.3	22.0	-1.1
Rubber	92.7	118.1	127.3	27.5	7.7
Paper	86.9	126.5	121.3	45.6	-4.2
Other items	1,088.3	1,085.2	1,285.1	-0.3	18.4
Totals	**11,177.4**	**12,473.8**	**10,634.4**	**11.6**	**-14.7**

Source: Pakistan Bureau of Statistics

A rise in quantum imports for most products was observed along with a decline in prices, e.g., palm oil, petroleum products, crude oil, steel, paper, tyers, pulses, fertilizer, and polyester fiber (quadrant A of **Figure 5.9**). Similarly, the increase in price of milk, rubber, plastic, dry fruits, steel scrap and pharmaceuticals resulted in lower quantum import of these products (quadrant D). Pesticides and tea were few exceptions to this trend: both unit prices and quantum import of these commodities, posted a YoY increase during the quarter (quadrant B).

The demand for *petroleum* remained strong in the first quarter, as evident in higher sales of POL products in Jul-Sep 2015 (up 2.7 percent YoY). Within petroleum products, the demand for petrol was the strongest: according to Oil Companies Advisory Council (OCAC), petrol sales showed a 13-year high YoY growth of 38.7 percent in Jul-Sep 2015. This increase can be traced to two factors: first,

---

[27] Iran is the 4th largest producer of cement in the world with an installed capacity of nearly 80 million MT. Pakistan's capacity is only 46 million MT.

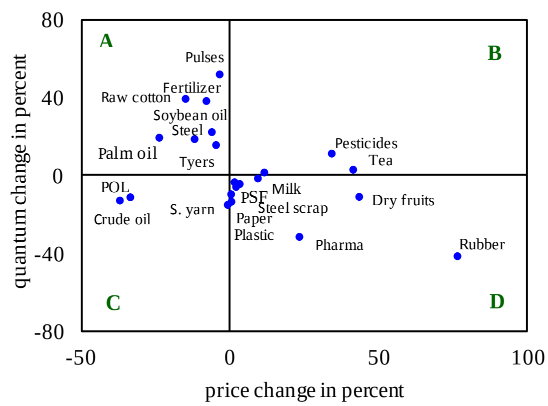
[28] In Afghanistan's north-eastern cities like Kabul and Jalalabad, Pakistani cement is still more competitive.

average petrol prices in Jul-Sep 2015 were nearly 30 percent lower than the average petrol prices during Jul-Sep 2014 (anecdotal evidence suggests that some CNG consumers have also shifted to using petrol due to low prices). And second, car sales were phenomenally higher in Jul-Sep 2015, compared to last year (posting a growth of 61 percent YoY).

Within the metal group, the demand for *steel* increased further on the back of on-going development projects related to power and infrastructure: PSDP outlay has posted a sharp increase of 57.4 percent YoY during Q1-FY16.[29] Private construction activity has also remained vibrant. However, local steel producers claim that a large chunk of imports is unwarranted, as they have the capacity to meet most of the country's steel demand. They particularly blame dumping from China for pricing them out of the market.

Recall here that Pakistan's steel industry is not the only complainant: over the past few months, steel producers all across India, UK, Brazil, Indonesia and Malaysia have been grumbling against dumping from China, which is sitting on massive inventory of raw-material and finished products. Large steel makers in Pakistan have filed petitions with National Tariff Commission (NTC), to impose anti-dumping duty on selected products (e.g., cold rolled coils and galvanized steel sheets). Meanwhile, some firms have also claimed that large quantities of flat steel are being imported into the country under the HS code of *alloy*, which enjoys duty-free status from China under the Free Trade Agreement. The NTC and Customs department are

Figure 5.9: A Cross-section Analysis of Imports in Q1-FY16 over Q1-FY15



Source: Pakistan Bureau of Statistics

[29] Total PSDP spending by federal and provincial governments increased from Rs 93.0 billion in Jul-Sep FY15, to Rs 146.4 billion in Jul-Sep FY16.

looking into these matters, to ensure a level-playing field to local producers, and curb imports.

Within *food*, quantum import of palm oil increased during Jul-Sep 2015. Taking benefit of 80-month low global prices, local traders are importing mostly ready-to-sell edible oil into the country. Local producers also edged up their production levels with the help of inventories built over the past few months. Analysts are divided over the path of palm oil prices in coming months: while some believe softer trend would prevail, others give much weight to possible damage to yields as a result of drought-like conditions in East Asia, and forest fires in Indonesia that have caused massive haze across the region.

Transport sector imports posted a growth of 3.0 percent over last year. Highest growth was seen in car segment (both CKD and CBUs), as domestic sales firmed up. This trend has puzzled many who believed that continuous fall in agriculture commodity prices and incomes would suppress car purchases. Auto assemblers attribute higher sales to low inflation and interest rates, relative improvement in law and order condition, and a pick-up in auto financing by commercial banks.[30] Continuation of Apna Rozgar scheme of Punjab government was another contributing factor in strengthening demand for certain brands.

Import of *fertilizer* posted an increase of 27.2 percent in Q1-FY16, compared with the 33 percent rise in the same period last year. Despite lower off-take and buffer stocks availability, ECC approved the import of 150,000 tons of urea by TCP. This decision was taken to overcome any expected shortage during the *rabi* 2015-16: the domestic industry might be unable to produce sufficient quantities due to possible gas curtailments in winters (for detail see chapter 2).
All other items, which are not classified elsewhere, posted an increase of 18.4 percent YoY (or US$ 199.8 million) in Jul-Sep 2015. This increase was driven by import of LNG worth US$ 121.6 million during the period.[31]

[30] As noted in Chapter 3, car loans increased by Rs 5.9 billion during Jul-Sep 2015, compared to Rs 3.6 billion in the same period last year.
[31] Although detailed data from Pakistan Bureau of Statistics is not available for this category for Jul-Sep, detailed information is available in SBP's payment record data (this data is also showing a sharp increase in 'other items').

For the remaining quarters of the year, we do not expect a major shift in trend in trade values, from what we have seen in the first quarter. Price of oil and other commodities have declined afresh post September 2015, and presently no stability is in sight. Imports have fallen by another 7.4 YoY in October 2015, whereas exports have posted a drop of 11.4 percent. The government has imposed additional regulatory duty on a large number of consumer goods, cotton and cotton yarn, which may further squeeze our import bill. Meanwhile, certain measures have been announced to boost exports, like an increase in credit subsidy for textile sector. Nonetheless, the dominating factor would be how the US economy embraces the increase in federal funds rate (which is due by end-December), and its impact on the global currency market: the demand from EU hinges much on the Dollar-Euro parity. At present, we expect full-year trade values for FY16 to remain less than both the last year, as well as target set for the year (**Chapter 1**).