2 Real Sector

2.1 Overview

Continuing on its growth momentum, Pakistan's real GDP grew by 5.3 percent in FY17, compared to 4.5 percent last year. This was the highest growth achieved over the last decade. A sharp recovery in agriculture sector, healthy performance by services, and an uptick in the large scale manufacturing output contributed towards this encouraging performance.

Table 2.1: GDP and its Components

Share and growth in percent; contribution in percentage points

	Share FY17	Growth			Contri. to growth
		FY16^{R}	FY17^{P}	FY17^{T}	
Agriculture	**19.5**	**0.3**	**3.5**	**3.5**	**0.7**
Of which					
Important crops	4.7	-5.5	4.1	2.5	0.2
Livestock	11.4	3.4	3.4	4.0	0.4
Industry	**20.9**	**5.8**	**5.0**	**7.7**	**1.1**
Of which					
Mining and Quarrying	2.9	6.9	1.3	7.4	0.04
LSM	10.7	2.9	4.9	5.9	0.5
Electricity gen. & dist. and gas dist.	1.8	8.4	3.4	12.5	0.1
Construction	2.7	14.6	9.0	13.2	0.2
Services	**59.6**	**5.5**	**6.0**	**5.7**	**3.5**
Of which					
Wholesale & retail trade	18.5	4.3	6.8	5.5	1.2
Finance & insurance	3.4	6.1	10.8	7.2	0.3
General govt.	7.6	9.7	6.9	7.0	0.5
GDP	**100**	**4.5**	**5.3**	**5.7**	**5.3**
Memorandum item					
Investment-GDP ratio		15.6	15.8	17.7	

R: Revised; P: Provisional; T: Target

Data source: Pakistan Bureau of Statistics

The key factors enabling this performance include improved supply of energy, increased developmental spending, supportive monetary policy, and a better law and order situation.

The agriculture sector was able to achieve its targeted growth rate of 3.5 percent during FY17, with a broad-based improvement in the production of important crops. Price subsidy on fertilizer, and affordable access to credit facilities (owing to decades low policy rate), resulted in the important crops segment posting a growth of 4.1 percent against a contraction of 5.5 percent experienced last year.

The services sector – benefitting from a recovery in the agriculture sector, an increase in manufacturing, and a rise in trade activities – contributed around two-thirds of the growth witnessed during FY17, with *wholesale and retail trade* growth rising from 4.3 percent last year to 6.8 percent in FY17.[1] In addition,

[1] Manufacturing activities contribute more than half of the value addition in wholesale & retail trade. In comparison, share of the agriculture trade is around 18 percent.

finance and insurance posted a recovery on account of healthy deposit and advances of the banking sector.

The performance of the industrial sector, meanwhile, remained constrained as growth stayed below last year's level. This was the major reason GDP growth could not reach its targeted figure, as the agriculture and services sectors performed at and above the expected rates, respectively (**Table 2.1**). A decline in the growth rate of *electricity generation and distribution, mining and quarrying,* and *construction* constrained the industrial growth. On the other hand, large scale manufacturing (LSM) fared better than last year.

From demand-side perspective, the support to GDP growth mainly came from increased domestic consumption. Subdued inflation, growing income levels, improved liquidity among farmers (through roll-out of subsidy package), and higher demand from expanding middle class population bolstered consumer spending in the economy. Further support to domestic demand came from the investment on account of increased focus on CPEC and public infrastructure development projects during the year.

2.2 Agriculture

Agriculture sector was able to achieve its growth target envisaged in the Annual Plan for FY17, primarily due to better-than-expected performance of important crops which posted a growth of 4.1 percent in FY17 compared to a decline of 5.5 percent in FY16 (**Table 2.2**). The recovery is broad-based, as maize and sugarcane posted double-digit growth, while the rest of the important crops also contributed positively albeit with lower growth rates (**Table 2.3**). The improvement in crop sector could have been even better, had the country not faced a decline in area under cotton and dry weather during Rabi season. Finally, the livestock subsector, which contributes more than half of agriculture output, maintained its pace during the period under review.

Table 2.2: Value Addition by Agriculture
Share and growth in percent; contribution in percentage points

	Share	Growth			Contribution to growth	
	FY17	**FY16^R**	**FY17^T**	**FY17^P**	**FY16^R**	**FY17^P**
Crop sector	37.2	-5.0	-	3.0	-2.0	1.1
Important crops	*23.9*	*-5.5*	*2.5*	*4.1*	*-1.4*	*1.0*
Other crops	*11.0*	*0.6*	*3.2*	*0.2*	*0.1*	*0.0*
Cotton ginning	*2.3*	*-22.1*	*2.5*	*5.6*	*-0.7*	*0.1*
Livestock	58.3	3.4	4.0	3.4	1.9	2.0
Forestry	2.3	14.3	3.0	14.5	0.3	0.3
Fishing	2.1	3.2	3.0	1.2	0.1	0.0
Overall	**100.0**	**0.3**	**3.5**	**3.5**		

R: Revised; P: Provisional; T: Target

Data source: Pakistan Bureau of Statistics

Input Situation

The input situation remained comfortable during Jul-Mar FY17. Fertilizer and credit off-take posted steady gains, while shortfall in water availability during Rabi 2016-17 was the only impeding factor that emerged during this period.

Table 2.3: Production of Major Crops

millions tons; cotton in million bales; growth in percent

				Growth	
	FY16	**FY17^T**	**FY17**	**FY16**	**FY17**
Cotton	9.9	14.1	10.7	-28.8	7.6
Rice	6.8	6.8	6.8	-2.9	0.7
Sugarcane	65.5	67.5	73.6	4.2	12.4
Wheat	25.6	27.4	25.8	2.2	0.5
Maize	5.3	4.6	6.1	6.8	16.3

Data source: Pakistan Bureau of Statistics; T: Target

Irrigation data showed a 10.0 percent drop in water availability in Rabi 2016-17, broadly in line with Indus River System Authority's projections.[2] Not only was there a shortfall in canal flows, prolonged dry weather during Oct-Dec cast a shadow on the prospects of wheat crop.[3] Wheat growers in the rain dependent areas of Potohar region suffered due to lack of moisture, however, growers elsewhere were able to draw groundwater to compensate for the surface water deficit.

A combination of cash subsidy, reduction in sales tax and voluntary reduction in prices by manufacturers consolidated the recovery in fertilizer off-take in FY17. Urea and DAP sales surged by 18.8 and 11.1 percent in Rabi 2016-17 compared to the corresponding period last year. Significant drop in fertilizer prices benefited the farmers (**Box 2.1**).

Box 2.1: Impact of Reduction in Urea and DAP Prices on Important Crops

According to our estimates, a typical grower involved in cultivation of important crops saved Rs 2,485 per hectare on urea in Jul-Mar FY17 compared to previous year (**Table 2.1.1**). The same

Table 2.1.1: Estimated Savings from Reduction in Fertilizer Prices (Jul-Mar)

	DAP		**Urea**	
	FY16	**FY17**	**FY16**	**FY17**
Quantity of fertilizer (# of 50 kg bag per hectare)[1] (a)	3.8	3.8	5.0	5.0
Price of fertilizer (Rupees per 50 kg bag)[2] (b)	3,494.8	2,589.0	1,903.4	1,392.8
Cost of fertilizer (Rupees per hectare) (a*b)	13,361.8	9,924.8	9,482.6	6,997.8
Savings per hectare (FY16-FY17)		**3,437.0**		**2,484.9**
Total savings -DAP + Urea (Rupees per hectare)				5,921.9
Area under important crops FY17 (million hectares)				16.8
Total benefit (billion Rupees)				**99.6**

[1] This is the average use of fertilizer for important crops weighted by area under these crops (Data source: Pakistan Bureau of Statistics, and State Bank of Pakistan)

[2] This is the weighted average price of fertilizer for Jul-Mar period (source: NFDC)

[2] Source: SUPARCO

[3] The country received 40 percent less precipitation during this year's Rabi season compared to the previous one.

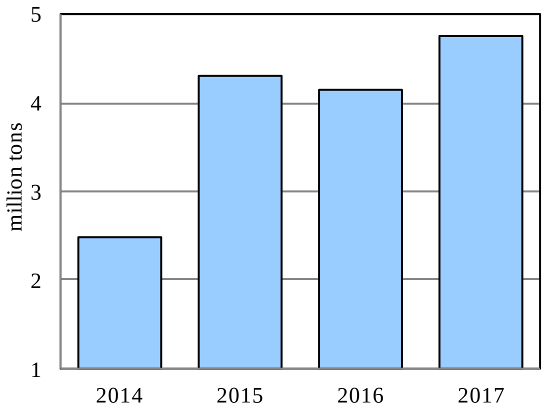
grower saved Rs 3,437 per hectare in case of DAP during this time. Adding these savings for total area under important crops in FY17, reveals that these growers were better off to the tune of Rs 100 billion in Jul-Mar FY17 compared to the same period last year.

Agriculture credit demand remained strong during the period. Gross agriculture sector disbursements witnessed an upsurge of 22.7 percent during Jul-Mar FY17 compared to the same period last year. Both production and development loans registered impressive growth of 23.5 and 14.2 percent respectively during the period. Agriculture finance received added impetus this year due to: (a) stable interest rates; and (b) inclusion of Micro Financial Institutions (MFIs) in agri financing for the first time.

Wheat

Wheat output of 25.8 million tons in FY17 was 0.5 percent higher than the last year. This performance was appreciable in the aftermath of dry weather that prevailed during the crucial sowing and germination period. As mentioned earlier, the rain-fed wheat cultivation areas in particular suffered losses. However, these losses were offset by rise in production from the irrigated areas which can be attributed to increased use of fertilizer and groundwater withdrawals.

Figure 2.1: Wheat Stocks - April



Data source: Provincial Food Departments

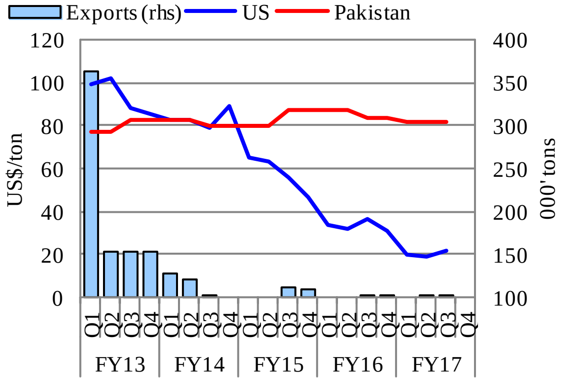
As has been the trend in the recent past, high procurement price kept wheat crop highly profitable, which, in turn has resulted in production surpluses. With domestic consumption averaging around 24.5 million tons each year,[4] there would be an excess of 1.3 million tons of wheat at home. On the other hand, unsold wheat stocks from previous harvests had increased to 4.8 million tons by April FY17; these were 15.7 percent more than last year's April figure (**Figure 2.1**).

This year's bumper crop will add to the already substantial stockpile with no bright prospects for exports. Wheat exports seem implausible without adequate

[4] Source: Foreign Agriculture Service, United States Department of Agriculture- (FAS-USDA)

export subsidy, as the price differential between domestic and international market is unfavorable at this stage (**Figure 2.2**).

Figure 2.2: Wheat Price and Exports



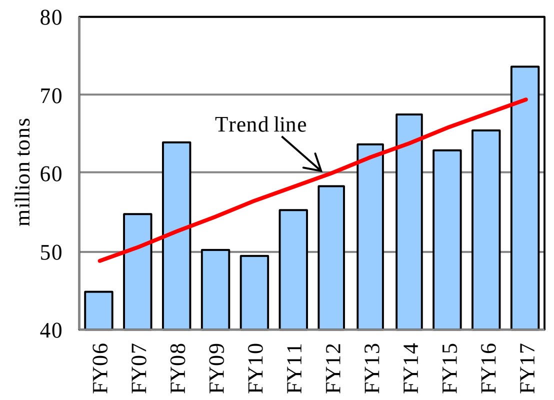
Data source: Pakistan Bureau of Statistics; World Bank; State Bank of Pakistan

<u>Sugarcane</u>

The country produced record sugarcane in FY17. The output of 73.6 million tons markedly exceeded both, the target of 67.4 million tons for the year, and 65.5 million tons realized in the previous year (**Figure 2.3**).

Profitability and resistance (to pest and weather related shocks) has placed sugarcane in an advantageous position over cotton crop in recent years. This has led to increase in area under sugarcane crop at the expense of cotton. Area under sugarcane grew by 7.6 percent from the previous season, while area under cotton contracted by 14.2 percent. A 4.5 percent increase in the sugarcane yield in FY17 also contributed to the record output.

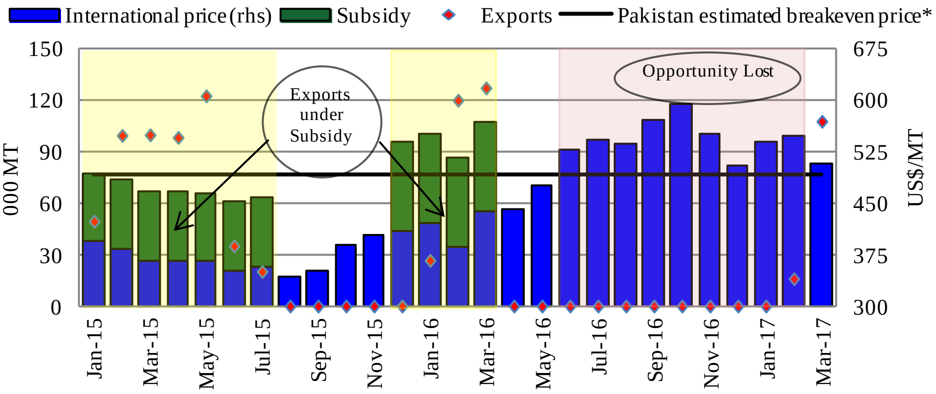
Figure2.3: Sugar Production



Data source: Pakistan Bureau of Statistics

This growth in sugarcane production has direct implications for the sugar industry. For example, the reserves of sugar in the country have increased substantially to 5 million tons in April FY17, compared with 3.7 million tons last year.

Figure 2.4: Sugar Exports - Opportunity Lost



*10% sugar recovery rate, cost of sugarcane at indicative price and 15% overheads are assumed for calculation of break-even price

Data source: MNFSR; USDA; PBS and SBP's calculations

However, despite excess stock in hand, the sugar industry could not exploit export opportunities (**Figure 2.4**). Price of sugar in the international market remained high between June 2016 and March 2017. The country was not able to register worthwhile sugar exports during that time due to quantity restrictions and short time limit, despite possessing ample carryover stocks and record production. Recently, news about healthy sugarcane crop has led to a fall in international sugar price. This has reduced the profitability margins of Pakistani exporters substantially compared to a few months back.

2.3 Industry

The industrial growth remained short of both the target as well as last year's performance, mainly due to a drag from *mining and quarrying* (on the back of decline in natural gas, which has a weight of about 66 percent in the mining sector) and *electricity generation & distribution and gas distribution* subsectors. These subsectors, which contributed almost one-third of the industrial growth last year, could not maintain their momentum (**Table 2.4**). Similarly, the growth in *construction* moderated, but this was expected as this

Table 2.4: Growth in Industry

Share and growth in percent; contribution in percentage points

	Share in GDP	Growth			Contri. to industry growth	
		FY16	FY17	FY17[T]	FY16	FY17
Mining & quarrying	2.9	6.9	1.3	7.4	1.0	0.2
Manufacturing	13.4	3.7	5.3	6.1	2.4	3.4
Large-scale	10.7	2.9	4.9	5.9	1.6	2.5
Small-scale	1.8	8.2	8.2	8.2	0.7	0.7
Slaughtering	0.9	3.6	3.6	3.7	0.2	0.2
Electricity gene & distt and gas distt	1.8	8.4	3.4	12.5	0.7	0.3
Construction	2.7	14.6	9.0	13.2	1.7	1.1
Industry	**20.9**	**5.8**	**5.0**	**6.4**	**5.8**	**5.0**

T: Target; Data source: Pakistan Bureau of Statistics subsector had recorded a very strong growth of 14.6 percent last year. In contrast, *manufacturing* experienced a significant improvement over last year, stemming mainly from higher sugar production.[5]

Large-scale Manufacturing

LSM improved on a YoY basis, growing by 5.1 percent during Jul-Mar FY17, compared to 4.6 percent in the previous corresponding period (**Table 2.5**)[6]. Although, as mentioned earlier, the contribution of food industry (especially sugar) was the major growth stimulant, various industries such as pharmaceuticals, electronics, and steel also witnessed marked improvement. Increased energy supplies (bolstering efficiency), historically low policy rate (facilitating cheaper credit availability), better security situation, and widespread construction activities (stimulating associated industries) helped LSM step-up its growth momentum.

Table 2.5: YoY Growth in LSM Jul-Mar FY17

growth in percent; contribution to growth in percentage points

		Growth		Contribution to growth	
	wt.	FY16	FY17	FY16	FY17
LSM	**70.3**	**4.6**	**5.1**		
Textile	20.9	0.7	0.8	0.19	0.22
Cotton yarn	13	1.5	0.8	0.29	0.14
Cotton cloth	7.2	0.4	0.5	0.04	0.05
Jute goods	0.3	-36.7	-7.9	-0.12	-0.02
Food	12.4	3.2	9.6	0.72	2.1
Sugar	3.5	2.9	29.3	0.24	2.46
Cigarettes	2.1	-8.3	-42.5	-0.19	-0.86
Vegetable ghee	1.1	6.1	2.7	0.08	0.04
Cooking oil	2.2	6.1	2.0	0.21	0.07
Soft drinks	0.9	5.0	18.1	0.12	0.45
POL	5.5	2.4	-0.3	0.15	-0.02
Steel	5.4	-7.5	16.6	-0.28	0.56
Non-metallic minerals	5.4	10.3	7.1	1.03	0.75
Cement	5.3	10.5	7.2	1.04	0.75
Automobile	4.6	23.5	11.3	1.27	0.72
Jeeps and cars	2.8	29.7	4.7	0.81	0.16
Fertilizer	4.4	16	1.3	0.87	0.08
Pharmaceutical	3.6	6.8	8.7	0.54	0.71
Paper	2.3	-2.9	5.1	-0.1	0.17
Electronics	2	-5.3	15.3	-0.09	0.23
Chemicals	1.7	10.2	-2.2	0.24	-0.05
Leather products	0.9	10.1	-18	0.19	-0.35
LSM Excl. Sugar	**66.8**	**4.8**	**2.8**	**--**	**--**

Data source: Pakistan Bureau of Statistics

The improvement in LSM growth came despite some sector specific and regulatory challenges. For instance: (a) cigarettes industry suffered further contraction following the increase in the federal excise duty on sales announced in the FY17 budget; (b) the automobile industry (especially LCVs segment in which the production declined) experienced a slower growth than last year following the

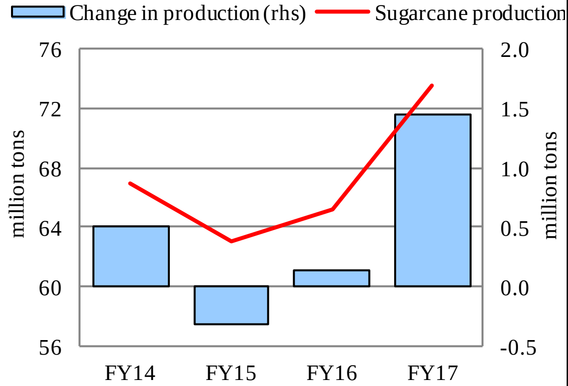
[5] Excluding sugar, the LSM grew by 2.8 percent during FY17, compared to 4.8 percent in FY16.
[6] According to National Income Accounts, LSM growth for FY17 is 4.9 percent (compared to 2.9 percent last year).

conclusion of the Apna Rozgar Scheme; (c) high inventory stocks, uncertainty over the subsidy program at the start of the year, coupled with a delayed export,[7] constrained growth in the fertilizer industry; (d) introduction of the regulation to sell higher quality (RON 92) fuel in the domestic market negatively impacted the production of refineries, as majority of the players faced capacity and technology constraints; and (e) inventory pressures (accumulated since last year) alongside international market price fluctuations of palm oil limited the output of vegetable ghee and edible oil sector. A detailed industry wise analysis follows:

Food

The performance of food sector recorded substantial improvement during Jul-Mar FY17 by growing at a rate of 9.6 percent against 3.2 percent during the same period last year. This growth was led by a surge in sugar production (**Figure 2.5**).

Figure 2.5: Sugar Production during Jul-Mar



Data source: Pakistan Bureau of Statistics

Bumper sugarcane crop, increased domestic prices (in tandem with international sugar prices), favorable weather, and timely commencement of crushing activities by millers helped the sugar industry record an impressive growth of 29.3 percent in Jul-Mar FY17 compared to 2.9 percent in the corresponding period last year. Permission to generate electricity via by-products not only incentivized the players to boost production but also resulted in the industry borrowing heavily from the commercial banks (for detail see **Chapter 3**).[8]

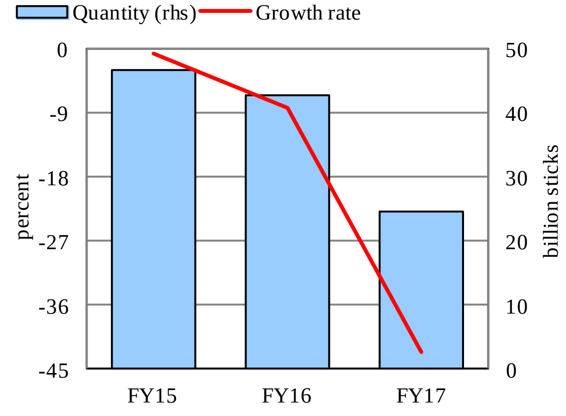
The cigarette production, on the other hand continued its declining trend on the back of an increase in federal excise duty in the FY17 budget and smuggling of competitive products. These factors forced the documented production to register a steep decline of 42.5 percent during Jul-Mar FY17 on top of 8.3 percent decline observed during same period in FY16 (**Figure 2.6**).

[7] Although the government allowed the export of 0.3 million tons of urea in H2-FY17 for a limited time, unavailability of logistic infrastructure for exports coupled with its higher domestic production cost makes exports challenging.

[8] In tandem with production figures of sugar in the Jul-Mar FY17 period, the energy generation through its by-products (baggasse) rose 63.4 percent on annual basis (from 359 GWh to 586 GWh).

Vegetable ghee and edible oil manufacturing also could not match their last year's pace, as the recent volatility in international prices of palm oil (a key input for the industry) enhanced uncertainty regarding the production decisions. Furthermore, regulatory restrictions on quality grounds caused a number of oil and ghee production units to suspend their operations.[9]

Figure 2.6: Trend in Cigarette Production (Jul-Mar)

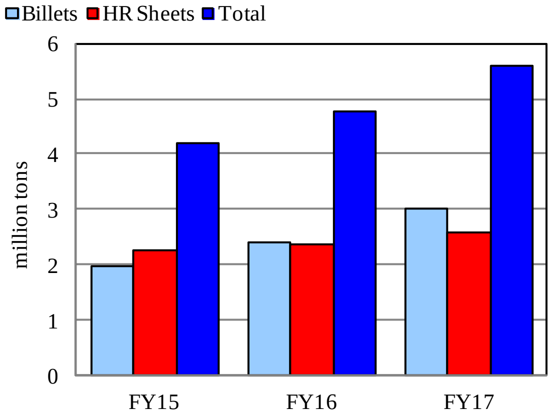


Data source: Pakistan Bureau of Statistics

Steel

The robust growth in construction activities also helped the steel sector to record a notable turnaround by growing 16.6 percent during Jul-Mar FY17, compared to a contraction of 7.5 percent in the corresponding period last year (**Table 2.5** and **Figure 2.7**). Stagnation in the imports of cheap Chinese steel products also helped, as the effect of anti-dumping duties started to materialize.[10]

Figure 2.7: Trend in Private Steeel Production



Data source: Pakistan Bureau of Statistics

Further support to industry came from improved energy supplies and some recovery in international steel prices.[11] These positive developments allowed the industry to

[9] During November, 2016, the Punjab Food Authority (PFA) declared various cooking oil and *ghee* brands unfit for human consumption due to rancidity (unpleasant odour), absence of Vitamin A, and inclusion of artificial flavor and other acid values.

[10] In early February 2017, the National Tariff Commission (NTC) imposed anti-dumping duties on imports of steel products (e.g., galvanized steel coils and sheets), in the range of 6 percent to 40.5 percent.

[11] International steel prices have rebounded by more than 27 percent at end March 2017, compared to end September 2016 (source: Bloomberg).

enhance economies of scale, earn higher margins,[12] and undertake expansionary plans.[13] Going forward, industry's efforts to reduce its dependence on imported raw materials and investment in cost efficient technology would provide basis for sustainable growth of the industry.

Electronics

The electronics sector was able to record a turnaround as it grew by 15.3 percent in Jul-Mar FY17, in a sharp contrast to a contraction of 5.3 percent witnessed during the same period last year. Consumer durables e.g., refrigerators, deep freezers and electric fans mainly contributed towards the sector's improved performance.

Better availability of electricity, coupled with increased levels of consumer financing, helped spur the demand for electronics in the urban areas.[14] Meanwhile, improved purchasing powers of farmers bolstered sales in rural areas as well. In the coming months, ongoing capacity expansions are expected to further boost the growth potential of the sector.[15]

Pharmaceutical

A number of factors explain the continued strong performance of the industry: for instance, the increased focus of the government on health;[16] the launch of new products (such as the introduction of Rotavirus vaccine in Punjab);[17] and the recently announced drug pricing policy (that aimed to address the counterfeiting trends and improve the transparency of the businesses). Resultantly, the industry built on its last year's healthy performance (6.8 percent) by growing 8.7 percent during Jul-Mar FY17.

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[12] On average, gross profit margins of steel manufacturers increased from 15 percent to 20 percent (source: Company financials).

[13] Private steel manufacturers are investing heavily in increasing production capacities. In next 2 to 3 years production capacity would increase by about 50 percent (source: company financials).

[14] Electricity generation increased by 4.4 percent during Jul-Mar FY17 on YoY basis.

[15] In November, 2016, Turkish company Arçelik A.S. acquired home appliances brand Dawlance for US$243 million and is planning to invest about US$ 50 million in capacity expansion.

[16] By the end of third quarter, the funding released by NHSRC (National Health Services, Regulations, and Coordination Division) stood at Rs 21 billion as compared to Rs 13.5 billion during the Jul-Mar period of FY16. Furthermore, till Q3 FY16, the government had spent about 65 percent of the allocated amount (Rs 20.7 billion) on health related services. This year, the allocated amount (Rs 25.0 billion) is not only higher but is being spent faster as well. At the end of third quarter, around 84 percent of the allocated amount has been spent.

[17] In January 2017, the Punjab government introduced the Rotavirus Vaccine in the routine immunization schedule of the Expanded Program on Immunization.

Automobile

The automobile industry grew by 11.3 percent on top of 23.4 percent growth observed last year. While a deceleration in growth rate was expected following the conclusion of Apna Rozgar Scheme, a number of factors helped keep the momentum strong.

Foremost, an increase in the number of infrastructure related projects under CPEC (and construction activities due to urbanization trends) resulted in a higher growth in production of trucks and buses by 39.3 percent and 19.7 percent year-on-year respectively (**Table 2.6**).

Table 2.6: Vehicles Production and Sales

	Jul-Mar-FY16		Jul-Mar -FY17		Growth %	
Units	**Production**	**Sales**	**Production**	**Sales**	**Production**	**Sales**
Passenger Cars	**137,067**	**137,206**	**143,317**	**139,300**	**4.6**	**1.5**
Exc. Apna Rozgar Scheme	111,830	111,858	127,893	124,362	14.4	11.2
Trucks	**3,940**	**3,751**	**5,489**	**5,321**	**39.3**	**41.9**
Buses	**746**	**700**	**893**	**853**	**19.7**	**21.9**
LCVs, Vans & Jeeps	**30,150**	**29,692**	**19,449**	**19,038**	**-35.5**	**-35.9**
Exc. Apna Rozgar Scheme	4,813	4,344	5,237	5,050	8.8	16.3
Farm Tractors	**21,942**	**22,169**	**37,938**	**38,620**	**72.9**	**74.2**
Motorcycles & Three-Wheelers	**998,040**	**993,336**	**1,211,454**	**1,207,988**	**21.4**	**21.6**

Data source: Pakistan Automobiles Manufactures Association

Secondly, higher purchasing power of farmers (owing to improved commodity prices, better yields and assistance programs such as the Kissan Package) and a reduction in sales tax on tractors led to a surge in the demand of tractors as shown by 74.2 percent increase in sales during Jul-Mar FY17.[18] Encouragingly, domestic manufacturers have also started to exhibit inclination towards exports.[19] While the magnitude is nominal at the moment, the development marks a welcome change in their long-term strategy to diversify their serving markets.

Going forward, a comparatively low motorization rate,[20] rising consumption levels (backed by growing real incomes), increasing volume of auto financing (aided by

[18] Sales tax on tractors was reduced to 5 percent from 10 percent in the Federal Budget FY17.

[19] Millat tractors have started exports to Africa and Middle East, where the product is very well received due to its competitive price and quality.

[20] Motorization rate (cars/1000 inhabitants) stands at 16 in Pakistan in comparison with India (22), Afghanistan (47), Sri Lanka (50), Indonesia (83) and China (102) (source: International Organization of Motor Vehicle Manufacturers).

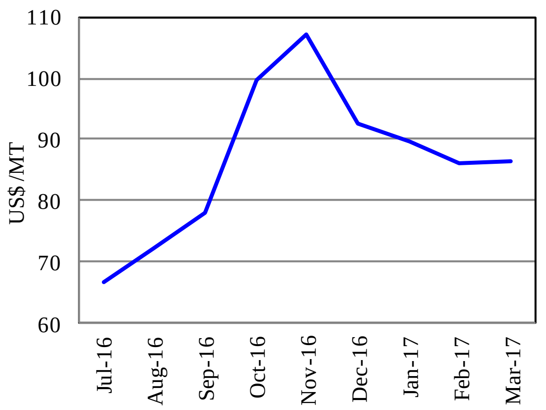
the historical low interest rates),[21] and anticipated entrance of new players through incentives offered in the Automotive Development Policy 2016-21, suggest the industry would be able to maintain its growing momentum.

Cement

Production activities in the cement sector remained buoyant during Jul-Mar FY17 as well and registered a growth of 7.2 percent over a high growth of 10.5 percent during the same period last year. The surge in domestic sales (growing by 10.9 percent YoY), led by the ongoing construction activities in the private sector and public spending on CPEC related (and other) infrastructure projects, more than offset the negative impact of declining exports.[22]

Further relief to the industry came from lower distribution costs, decreasing international coal prices (**Figure 2.8**), and increased electricity generation through waste heat recovery units (WHRU).[23,24] In this backdrop, the proposed capacity expansions signal towards a sustained growing potential of the industry.[25] In order to arrest declining exports and to sustain planned expansion, manufacturers are exploring new markets (such as the Philippines and Sri Lanka).

Figure 2.8: International Australian Coal Prices



Data source: Bloomberg

Textile

The textile sector managed a marginal growth of 0.8 percent during Jul-Mar FY17 as compared to 0.7 percent during the same period last year.

[21] Consumer auto-financing grew by 23.4 percent during Jul-Mar FY17 on top of a growth of 20.4 percent during the previous corresponding period.

[22] Due to implementation of border management system and some other issues, the resultant delays in transportation of cement (which has limited shelf life) has forced Afghan buyers to switch to Indian and Iranian cement. The overall cement exports have declined by 14.8 percent on YoY basis during Jul-Mar FY17.

[23] After accelerating to US$ 107.2 per metric ton in November 2016, the Australian coal prices started decreasing and currently hover around US$ 85.

[24] Manufacturers are investing aggressively on waste heat recovery (WHR) plants; on average WHR reduces fuel cost by about 40 percent (Source: Companies financials).

[25] The industry plans to increase its annual production capacity by 24 million tons (52 percent) during the next three years.

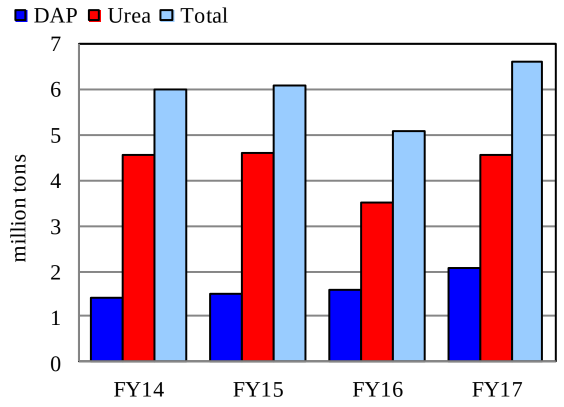
Robust domestic demand continued to compensate for the declining exports.[26] The recently announced export package by the government would take some time before its impact on the performance materializes. Only sufficient investment in BMR, efforts to concentrate on value-added products, and increased focus on improving operational efficiency would broaden the export potential of the products and stimulate the sector.

The jute subsector continued its contraction, as it recorded a negative growth of 7.9 percent during Jul-Mar FY17 compared to a decline of 36.7 percent during the corresponding previous period. The earlier ban on import of raw materials from Bangladesh kept on affecting the production cycle. Worryingly, only five of the ten remaining mills are operational at the moment due to various financial constraints. With the recent lifting of the aforementioned ban, the sector might experience some respite. However, the availability of cheap alternatives, dependence on imported raw material and inefficient technology are hurdles in the recovery of domestic jute industry.[27]

Fertilizer

Despite improved availability of gas to fertilizer companies, production remained subdued during Jul-Mar FY17 (growing 1.3 percent as compared to 16.0 percent last year).[28] Even at discounted prices, the higher off-take could not ease the accumulated supply glut (**Figure 2.9**).[29,30] On the other hand, variations in fertilizer prices in international market, high costs of production, and lack of logistic and infrastructure for exports

Figure 2.9: Fertilizer Off-take during Jul-Mar



Data source: National Fertilizer Development Center

[26] The lack of R&D and reliance on low-value added products has contributed towards decreasing exports and hence stagnancy in the sector.
[27] Jute bags are costlier compared to their substitute (e.g., polypropylene / polyethylene), if a plastic bag is available at Rs 60, the same 100kg capacity jute bag costs more than Rs 100.
[28] On the back of increased LNG imports (increased by 144.0 percent on YoY basis) and continuity of concessional gas supply from domestic sources (source: Pakistan Bureau of Statistics).
[29] The price of urea in the international market is around US$ 250 per ton, which is significantly lower than the price of locally produced urea (i.e., US$ 320 per ton).
[30] Urea stock at end March 2017 stood at around 1.5 million tons (source: NFDC).

constrained manufacturers to avail exporting opportunity provided by the government.[31]

Petroleum Products (POL)

After the imposition of regulation requiring RON 92 grade petroleum to be sold in the domestic market, the *POL industry* witnessed stagnation in growth as the majority of local players do not produce higher quality petroleum products.[32] As a result, the growth rate recorded a marginal decline of 0.3 percent during the Jul-Mar FY17 period compared to a growth of 2.4 percent in the corresponding period last year. Resultantly, import dependence increased to bridge the growing demand-supply gap.[33]

2.4 Services

The services sector continued to consolidate its share in the overall GDP, posting a growth of 6.0 percent in FY17 on top of the 5.5 percent improvement realized last year (**Table 2.1 & Table 2.7**).

Table 2.7: Performance of Services

	Share in GDP	Growth			Contri. to growth	
	FY17	FY16	FY17^T	FY17^P	FY16	FY17
Wholesale and retail trade	18.5	4.3	5.5	6.8	1.3	2.1
Trans., storage & communication	13.3	4.8	5.1	3.9	1.1	0.9
Finance and insurance	3.4	6.1	7.2	10.8	0.3	0.6
Housing services	6.6	4.0	4.0	4.0	0.5	0.5
General govt. services	7.6	9.7	7.0	6.9	1.2	0.9
Other private services	10.2	6.8	6.7	6.3	1.1	1.1
Services	**59.6**	**5.5**	**5.7**	**6.0**	**5.5**	**6.0**

Data source: Pakistan Bureau of Statistics

The performance of the largest subsector *wholesale and retail trade* (31 percent share in services) was particularly encouraging, as it built upon last year's growth of 4.3 percent by growing 6.8 percent in FY17. Increase in imports, and growth in both the commodity producing sectors (agriculture and industry) were the major stimulants for the subsector.

The performance of *finance and insurance* also remained remarkable, as it registered a growth of 10.8 percent in FY17 (compared to 6.1 percent in the previous year), mainly due to an encouraging growth in deposits and advances.[34]

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[31] Earlier the government allowed export of 300 thousand tons of urea till end April, 2017, however only 3 thousand tons have been exported so far.

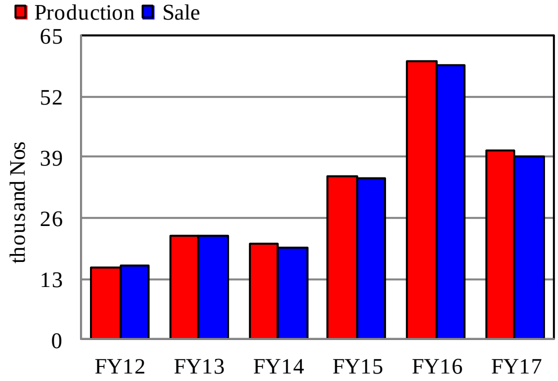
[32] Most of local refineries produce RON 90 Premium Motor Gas (PMG). The conversion to high quality fuel requires a substantial investment to acquire compatible technology.

[33] During Jul-Mar FY17, imports of petroleum products increased by about 29.2 percent compared to same period last year (source: Pakistan Bureau of Statistics).

[34] The banking spread on stocks decreased by 29 bps during Jul-Mar FY17. Advances by commercial banks, on the other hand, recorded a substantial increase (**Chapter 3** on Inflation and Monetary Policy).

Thus, the value addition increased to 9.8 percent in FY17 from 5.9 percent in FY16. Similarly, the growth in *general government services* remained close to the target of 7.0 percent.

Figure 2.10: Production and Sales of Commercial Vehicles (Jul-Mar)

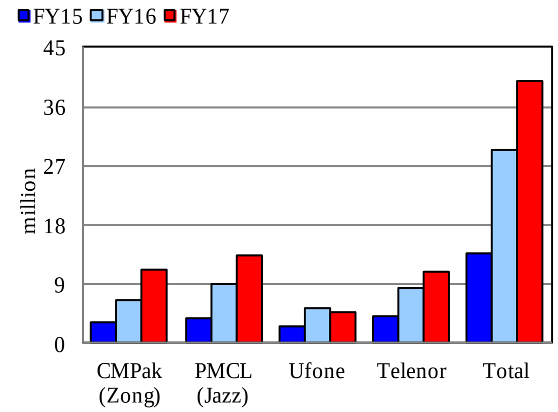


Data source: Pakistan Automotive Manufacturers Association

Slowdown in *transport, storage and communication* continued in FY17, registering a growth of 3.9 percent as compared to 4.8 percent during FY16. Constrained growth of Pakistan Railways, PIA, and lower growth in value addition by the road transport contributed to this slowdown.

The slowdown in road transport was in sharp contrast with improvement in cargo handling activities but broadly in line with decline in sales and production of commercial vehicles during the period under review (**Figure 2.10**).[35] In view of the ongoing expansion in infrastructure, the outlook for the sector remains promising.

Figure 2.11: Trend in 3G/4G Subscriptions



Data source: Pakistan Telecommunication Authority

In the *telecom sector*, total teledensity continued its growth momentum from the last year.[36] On a parallel note, the number of broadband users increased to 42.3 million, up around 10 million over the course of just one year. A healthy growth in 3G/4G subscriptions (35 percent in the period under review) was a major contributor to this increase (**Figure 2.11**).[37]

[35] Although the sales of trucks and buses increased by 41.8 percent and 21.8 percent respectively, they were more than offset by a decline in the sales of LCVs (contracting by 35.9 percent) due to the conclusion of Apna Rozgar Scheme (source: Pakistan Automotive Manufacturers Association).
[36] Total teledensity reached 72.36 percent at the end of March, 2017 compared to 70.81 percent at the end of last fiscal year.

Going forward, recently introduced Digital Pakistan Policy 2017 would provide a platform for sustainable development of the sector, while continuous improvement in voice traffic and broadband is expected to keep augmenting telecom revenues and its contribution to the national exchequer.[38]

[37] After the introduction of Next Generation Mobile Services in the country in 2014, the 3G/4G technologies have been well received by the customers. The growth of 35 percent in Jul-Mar FY17 builds upon the impressive performance experienced in FY16 (when the subscription numbers grew by around a 118 percent).
[38] Ministry of Information Technology and Telecom issued IT Policy "Digital Pakistan Policy 2017"in April 2017.