4 Fiscal Policy and Public Debt

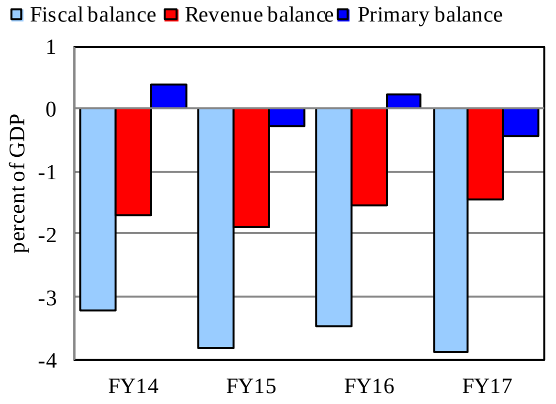
4.1 Overview

Fiscal deficit during Jul-Mar FY17 was 3.9 percent of GDP, which was higher than the full year target of 3.8 percent. While overall expenditures were managed well, the revenue collection could not accelerate. As a result, it became challenging to sustain the fiscal consolidation observed during the past few years, which is also evident from a large primary deficit during Jul-Mar FY17 against a surplus last year (**Figure 4.1**).

On a positive note, the revenue deficit improved slightly with restrained current expenditures. Despite an increase in defense and security related spending, the growth in current expenditures slowed down in Jul-Mar FY17 compared to the same period last year. This slowdown, in fact, was due to interest payments, which remained close to the last year's level. Contained interest expense, in the prevailing low interest rate environment, has provided fiscal space for development expenditures (**Figure 4.2**).

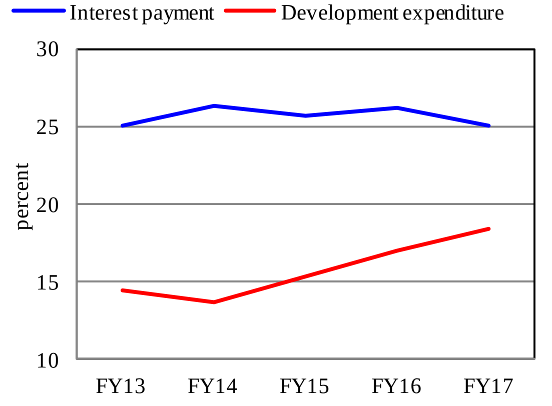
Meanwhile, the growth in total revenues decelerated significantly during Jul-Mar FY17 as compared to the last year. This was due to a considerable slowdown in tax collection, which was partly the result of fiscal relief measures and tax incentives provided to support investment

Figure 4.1: Fiscal Indicators (Jul-Mar)



Data source: Ministry of Finance and SBP's calculations

Figure 4.2: Share in Total Expenditures (Jul-Mar)



Data source: Ministry of Finance and SBP's calculations and growth in the economy.[1] The non-tax revenue also declined on account of lower receipts under Coalition Support Fund (CSF), SBP profit, and dividend income.[2]

Despite an increase in fiscal deficit, the debt accumulation was significantly lower during Jul-Mar FY17 as compared to the last year. This improvement took place on the back of revaluation gains accrued on external debt, along with the government's utilization of deposits held with the banking system (especially SBP).

4.2 Revenues

Total revenues grew by 6.2 percent during Jul-Mar FY17 as compared to 10.4 percent increase realized in the same period last year. As mentioned earlier, this slowdown was brought about by: (i) a 6.2 percent decline in non-tax revenues; and (ii) deceleration in growth of tax revenue to 8.6 percent in July-Mar FY17 from 20.3 percent realized last year (**Table 4.1**). The sluggish growth in overall tax revenues, despite a robust growth in provincial tax collection, largely came from a lower than targeted growth in FBR tax collection.

<u>FBR taxes</u>

As per the past pattern, the revenue collection gathered some pace in second and third quarters of FY17; yet, the growth momentum remained weak as compared to the last year despite a steady improvement in the economic activity. FBR tax collection grew by 8.2 percent during Jul-Mar FY17 as compared to an impressive 17.7 percent increase witnessed in the same period last year. Lower collection from both direct and indirect taxes contributed to this slowdown **(Table 4.2)**. This partly reflects the impact of fiscal relief measures and tax incentives to support investment, exports, and domestic production. Further, a divergence between tax collection and steadily improving economic activity highlights issues in the taxation system, which needs further efforts for improvements.

[1] For instance, government allowed sales tax exemptions/concessions on agriculture inputs (fertilizer and pesticides) to reduce the cost of production for farmers. Similarly, government announced incentives like zero-rating, exemptions of sales tax on import of new machinery and raw material for textiles and duty drawback to registered exporters to revive exports. Moreover, the government offered tax incentives to firms investing in energy projects.

[2] Pakistan received US$ 550 million under CSF during Jul-Mar FY17 against US$ 713 million in the same period last year.

Table 4.1: Summary of Fiscal Operations (Jul-Mar)
billion Rupees

	FY17 Budget	Actual		% of GDP	
		FY16	**FY17**	**FY16**	**FY17**
A. Total revenue	**5347.0**	**2,961.9**	**3,145.5**	**10.2**	**9.9**
Tax revenue	4,306.0	2,481.0	2,694.3	8.5	8.5
Non-tax revenue	1,041.0	480.9	451.2	1.7	1.4
B. Total expenditure	**6,623.0**	**3,971.3**	**4,383.6**	**13.6**	**13.8**
Current	5,198.0	3,407.0	3,605.1	11.7	11.3
Interest payments	*1,360.0*	*1,079.4*	*1,094.5*	3.7	3.4
Defence	*860.2*	*482.9*	*535.7*	1.7	1.7
Development	1,435.0	699.4	803.9	2.4	2.5
Net lending	-10	10.8	-34.2	0.0	-0.1
C. Statistical discrepancy	0.0	-145.8	8.8	-0.5	0.0
Fiscal balance (A-B-C)	**-1,276.0**	**-1,009.4**	**-1,238.1**	**-3.5**	**-3.9**
Revenue balance	149.0	-445.1	-459.6	-1.5	-1.4
Primary balance	84.0	70.0	-143.6	0.2	-0.5
Financing	1,276.0	1,009.4	1,238.0	3.5	3.9
External sources	234.0	222.9	220.2	0.8	0.7
Domestic sources	1,042.0	786.5	1,017.9	2.7	3.2
Banks	453.0	538.0	694.7	1.8	2.2
Non-bank	539.0	248.4	323.2	0.9	1.0
Privatization	50.0	0.0	0.0	0.0	0.0
% Growth					
Total Revenue		10.4	6.2		
Tax revenue		20.3	8.6		
Non-tax revenue		-22.4	-6.2		
Total Expenditure*		8.5	6.3		
Current		6.5	5.8		
Development		20.7	14.9		

*Excluding statistical discrepancy; Data source: Ministry of Finance and SBP's calculations

Table 4.2: FBR Tax Collection (Jul-Mar)
billion Rupees

	FY17 Budget	Collections		% Growth	
		FY16	**FY17**	**FY16**	**FY17**
Direct taxes	1,558.0	809.8	892.3	15.4	10.2
Indirect taxes	2,063.0	1,279.2	1,368.2	19.2	7.0
Customs duty	413.0	276.1	343.4	32.2	24.4
Sales tax	1,437.0	886.0	897.7	16.5	1.3
Federal excise duty	213.0	117.1	127.2	12.3	8.6
Total Taxes	**3,621.0**	**2,089.0**	**2,260.5**	**17.7**	**8.2**

Data source: Federal Board of Revenue and SBP's calculations

Direct taxes

Direct tax collection grew by 10.2 percent during Jul-Mar FY17 compared to 15.4 percent growth recorded in the corresponding period last year. This slowdown can be traced to reduction in corporate tax rate amid slower pace of increase in corporate profitability.[3] Banks' profits, in particular, declined by 40 percent during Jul-Mar FY17.[4]

Within the direct taxes, the growth in withholding tax (WHT) decelerated to 12.2 percent in Jul-Mar FY17 from 19.6 percent increase in the last year. However, WHT collection from dividend income registered a 24.3 percent increase in Jul-Mar FY17. This higher collection from dividend income can be traced to increase in WHT rates for both filers and non-filers.[5]

Similar to WHT, growth in voluntary tax payments (with a 26 percent share) fell to 7.3 percent in Jul-Mar FY17 from 25.0 percent last year. Collection on demand was the only component that rebounded with an increase of 10.0 percent from a 30.6 percent decline recorded in last year (**Table 4.3**).[6]

Table 4.3: Break-up of Withholding Taxes (Jul-Mar)
billion Rupees

	FY16	FY17	% Growth
I. Voluntary payments	230.9	247.7	7.3
II. Collection on demand	47.2	51.9	10.0
III. Withholding taxes	575.4	645.7	12.2
Imports	130.1	142.1	9.2
Salary	63.0	75.2	19.3
Dividends	24.9	31.0	24.3
Bank Interest	36.8	32.3	-12.3
Contracts	144.6	165.2	14.3
Cash withdrawals	21.0	21.6	3.0
Electricity	18.5	17.9	-3.0
Telephone	33.8	36.8	8.9
Others	102.8	123.7	20.3
IV. Miscellaneous	7.4	3.8	-48.4
Total	**860.9**	**949.1**	**10.2**

Data source: Federal Board of Revenue and SBP's calculations

Indirect taxes

The impact of fiscal relief measures and tax incentives was particularly reflected in lower collection from indirect taxes. The growth in indirect tax collection decelerated to 7.0 percent during Jul-Mar FY17 from 19.2 percent recorded in the last year.

[3] As explained in previous reports, direct taxes were also lower due to tax credits for employment generation/and new industrial undertakings and tax exemptions/relaxations given to companies working on CPEC related projects.

[4] The provisional numbers reported by banks show that banking sector profitability declined to Rs 137.8 billion in Jul-Mar FY17 from Rs 231.7 billion during previous year.

[5] The WHT rate on dividend income was increased to 12.5 percent from 10.0 percent for filers; and 20 percent from 17.5 percent for non-filers. In particular, dividend rate on mutual funds for individuals/associate of persons was increased to 15.0 percent from 10.0 percent for non-filers.

[6] This can be attributed to better handling of audit cases through introduction of risk-based audit.

This deceleration was broad-based. The major drag, however, came from decline in domestic sales tax and lower than expected FED collection.

The total sales tax collection, which accounts for two thirds of indirect taxes, grew by merely 1.3 percent during Jul-Mar FY17 as compared to 16.5 percent growth last year. This sluggish growth was primarily due to a 3.9 percent decline in domestic sales tax collection, as that from imports increased by 5.8 percent. Within domestic sales tax, collection from POL, fertilizer, cigarettes, and natural gas fell sharply; this more than offset the increase in sales tax collection from other sectors (**Table 4.4**).[7]

Table 4.4: Break-up of Sales Tax Collection (Jul-Mar)

billion Rupees

	FY16	FY17	% Growth
Domestic			
POL products	193.5	145.4	-24.9
Electrical energy	22.9	32.4	41.9
Cement	19.8	21.0	6.3
Cigarettes	12.1	9.7	-19.7
Fertilizer	15.0	2.9	-80.7
Natural gas	12.1	5.8	-52.0
Other	142.8	184.8	29.4
Total	***418.1***	***402.0***	***-3.9***
Imports			
POL products	142.8	145.8	2.1
Iron and steel	37.9	43.7	15.4
Machinery & mech. appliances	34.8	46.1	32.7
Electrical machinery	31.4	37.7	20.4
Vehicles (non-railway)	30.4	37.7	24.0
Other	190.7	96.1	-49.6
Total	***467.9***	***495.3***	***5.8***
Grand Total	**886.0**	**897.3**	**1.3**

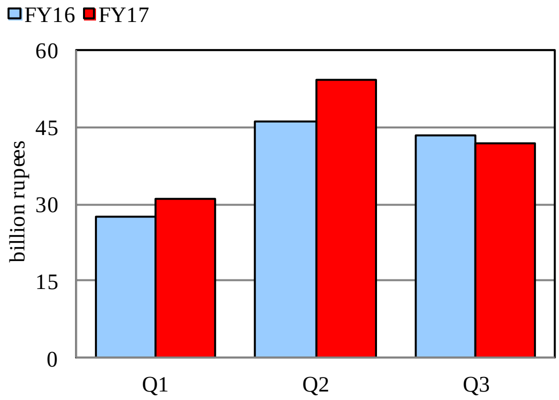
Data source: Federal Board of Revenue and SBP's calculations

FED collection grew by 8.6 percent during Jul-Mar FY17, against 12.3 percent growth witnessed in the last year, as the momentum gained in the second quarter could not be maintained in Q3-FY17 (**Figure 4.3**). This was mainly due to a 24 percent decline in collection from cigarettes (which accounts for one third of total FED collection) due to fall in its production following increase in the FED rate. Encouragingly, a significant increase in FED from booming cement and beverage industries, along with air travel services, more than offset the decline in FED on cigarettes.

[7] As explained in previous SBP reports, decline in sales tax collection from petroleum can be traced to the government's decision to absorb the increase in international prices of petroleum products in the start of the fiscal year and reduction in sales tax rates on petroleum products. Similarly, decline in sales tax collection from fertilizer was on account of reduction in GST rates from 17 to 5 percent under the Prime Minister's Kissan package coupled with reduction in feedstock prices to lower the per bag cost of fertilizer. Lower sales tax collection from cigarettes was due to decline in demand for locally manufactured cigarettes following the increase in FED rate on cigarettes. Cigarette consumers switched to low price black market alternatives.

Collection from customs duty grew by 24.4 percent during Jul-Mar FY17 compared to the 32.2 percent increase realized in the previous year. This steady growth in customs duty collection, despite reduction in rate of duty (on selected items) under the fiscal relief measures and tax incentives, can be attributed to a phenomenal increase in overall imports, especially those of raw material and machinery.[8,9]

Figure 4.3 : Quarterly Trend in FED Collection



Data source: Federal Board of Revenue

Non-tax revenues

The non-tax revenues declined by 6.2 percent during Jul-Mar FY17 compared with a decline of 18.8 percent in the corresponding period last year. This contraction was broad-based except for an uptick in mark-up income and passport fee collection, which have very small share in overall non-tax revenues. Lower CSF receipts, together with decline in SBP profit and dividend income, mainly led to contraction in non-tax revenues (**Table 4.5**).

Table 4.5: Non-tax Revenues (Jul-Mar)
billion Rupees

	FY17	Actual	
	Budget	FY16	FY17
Mark-up (PSEs and others)	81.1	11.1	12.1
Dividends	85.0	35.8	22.1
SBP profits	280.0	177.6	144.8
Defense (including CSF)	171.0	80.6	64.4
Profits from post office/PTA	81.0	5.4	0.7
Royalties on gas and oil	43.0	46.3	40.3
Passport and other fees	25.0	8.1	13.6
Discount retained on crude oil	10.0	5.7	5.9
Windfall levy against crude oil	10.0	1.6	1.0
Other	254.9	108.7	146.3
Total non-tax revenue	**1,041.0**	**480.9**	**451.2**

Data source: Ministry of Finance

4.3 Expenditures

The growth in expenditures slowed down for the second consecutive year. The consolidated federal and provincial expenditure grew by 6.3 percent in Jul-Mar

[8] The value of import (PBS) has grown by around 18.7 percent during July-Mar FY17. Specifically, import of machinery increased by 41.9 percent YoY in the same period.

[9] The custom duty on import of machinery and raw materials was reduced from 5 to 3 percent in the federal budget for FY17.

FY17, compared to 8.5 percent growth recorded in the last year. Most of the moderation in total expenditure growth came from a sustained decline in current expenditure growth. The development expenditure, on the other hand, increased by 14.9 percent during Jul-Mar FY17, on top of 20.7 percent increase registered last year.

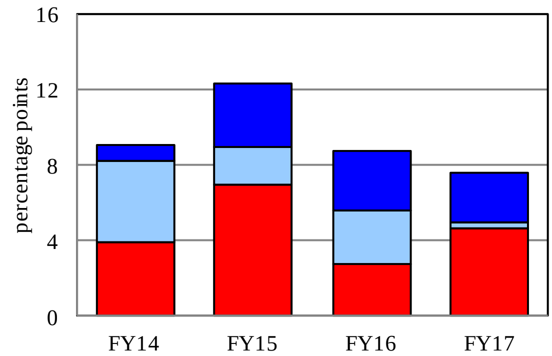
Table 4.6: Analysis of Fiscal Spending (Jul-Mar)
billion Rupees

	Actual		% Growth	
	FY16	**FY17**	**FY16**	**FY17**
Current expenditures	**3,407.0**	**3,605.1**	**6.5**	**5.8**
Federal	2,368.9	2,439.3	5.0	3.0
Interest payment	1,079.4	1,094.5	10.8	1.4
Defense	482.9	535.7	-0.6	10.9
Public order and safety	75.4	81.9	13.5	8.6
Others	731.2	727.2	0.3	-0.5
Provincial	1,038.0	1,165.8	10.1	12.3
Development expenditures	**699.4**	**803.9**	**20.7**	**14.9**
PSDP	623.4	764.6	24.8	22.7
Federal	251.3	324.0	20.8	28.9
Provincial	372.1	422.7	27.7	13.6
Others (incl. BISP)	76.0	57.2	-5.3	-24.7
Net lending	**10.8**	**-34.2**	-24.4	-416.7
Statistical discrepancy	-145.8	8.8	137.4	-106.0
Total Expenditure	**4,117.1**	**4,374.8**	**8.5**	**6.3**

Data source: Ministry of Finance and SBP's calculations

A break-up of the current expenditure, nevertheless, suggests that growth in provincial expenditures still remained strong, i.e., 12.3 percent in Jul-Mar FY17, compared to the 10.1 percent in the same period last year (**Table 4.6**). The spending under General Public Affair (Rs 566 billion), Public Order and Safety Affair (Rs 179.7 billion) and Fuel and Energy (Rs 38.2 billion) mostly contributed to the increase in provincial current expenditure.

Figure 4.4: Contribution to Growth in Expenditures (Jul-Mar)



Data source: Ministry of Finance and SBP's calculations

The federal current expenditure, on the other hand, increased by only 3.0 percent during this period despite a significant increase in defense and security related spending. It was primarily due to restrained interest expense, which rose marginally by 1.4 percent (or Rs 15.1 billion) during Jul-Mar FY17. This has somewhat increased the cushion for maintaining a steady growth in development spending (**Figure 4.4**).

4.4. Provincial fiscal operations

The consolidated provincial surplus reached Rs 227.6 billion in Jul-Mar FY17, about two thirds of the full-year target of Rs 339 billion. Most of the surplus was contributed by Punjab, followed by KP, Sindh, and Balochistan (**Table 4.7**).

Table 4.7: Provincial Fiscal Operations (Jul-Mar)
billion Rupees

	Punjab	Sindh	KP	Balochistan	Total	% Growth
FY 17						
A. Total revenue	808.4	500.3	263.1	164.3	1,736.1	13.7
Provincial share in federal revenue	665.6	382.2	224.3	150	1,422.1	13.5
Provincial revenues (I+II)	132.8	107.4	41.3	8.3	289.8	25.2
I. Taxes	112.3	101.7	12.1	4.5	230.5	23.5
II. Non-tax revenues	20.6	5.7	29.2	3.9	59.3	32.6
Fed loans and transfers	10.0	10.7	-2.4	5.9	24.2	-42.4
B. Total expenditure	723	455.5	290.2	129.8	1,598.5	12.6
Current[2]	484	363.4	216.4	112.1	1,175.9	12.3
Development	239.1	92.1	73.8	17.7	422.7	13.6
Gap (A-B)	85.4	44.8	-27.1	34.5	137.6	28.2
Financing[1] (overall balance)	**-82.7**	**-41.9**	**-67.0**	**-36.0**	**-227.6**	**2.9**
FY 16						
A. Total revenue	715.1	430.7	233	147.8	1,526.6	12.2
Provincial share in federal revenue	595.2	329.6	200.6	127.7	1,253.2	13.1
Provincial revenues (I+II)	113.9	87.3	23.4	6.8	231.4	27.1
I. Taxes	91.6	83.0	9.1	2.9	186.7	28.6
II. Non-tax revenues	22.3	4.3	14.3	3.9	44.7	21.1
Fed loans and transfers	6.0	13.7	9.0	13.3	42.0	-41.3
B. Total expenditure	706.6	348.8	231.5	132.4	1,419.3	14.0
Current[2]	484.4	283.1	175.4	104.3	1,047.2	9.9
Development	222.2	65.6	56.1	28.2	372.1	27.7
Gap (A-B)	8.5	81.9	1.5	15.4	107.3	-8.1
Financing[1] (overall balance)	**-57.4**	**-91.0**	**-66.2**	**-6.6**	**-221.2**	**14.0**

[1] Negative sign in financing means surplus; [2] Current expenditure data may not match with those given in Table 4.6 as numbers reported here includes the mark-up payments to federal government.

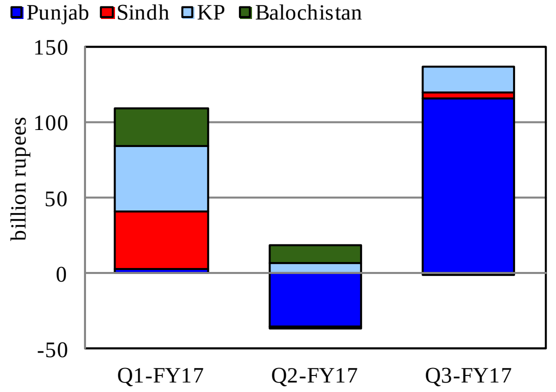
Data source: Ministry of Finance and SBP's calculations

Quarterly data shows that the provincial surplus significantly improved in Q3-FY17 by Rs 137.0 billion as compared to Rs 108.6 billion in Q1-FY17 and a deficit of Rs 18.0 billion in Q2-FY17 (**Figure 4.5**). This was an outcome of both higher revenue and a slower increase in total expenditures.

Besides higher federal transfers, the provinces' own taxation efforts also contributed to 13.7 percent increase in revenues during Jul-Mar FY17, as compared to 12.2 percent increase recorded in the corresponding period last year.

The provinces' revenue efforts are particularly evident from a steady increase in collection from General Sales Tax on Services (GSTS). The higher revenue collection from GSTS is a result of systematic taxation planning by the provinces, especially the establishment of Invoice Monitoring System for effective tax collection on services (**Figure 4.6**).[10]

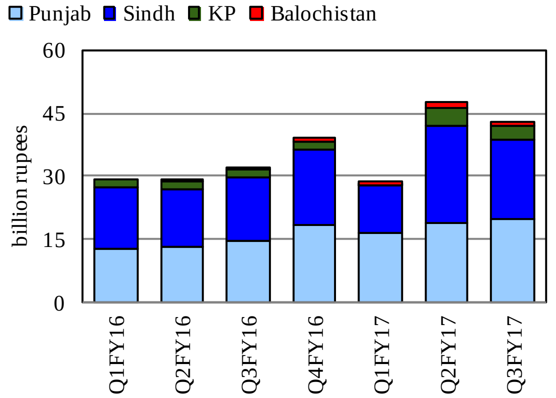
Figure 4.5: Trends in Provincial Surplus



Data source: Ministry of Finance

Besides GSTS, stamp duties and motor vehicle tax also contributed significantly to provincial revenue during Jul-Mar FY17. In particular, property taxes in Sindh grew by 73 percent during this period, which reflects contribution of initiatives regarding property valuation by setting-up automation of land record.[11] Similarly, revenue receipts of Khyber Pakhtunkhwa increased through profits from hydroelectricity under Hydro Power Policy 2016.

Figure 4.6: Trends in General Sales Tax on Services



Data source: Ministry of Finance

The growth in provincial expenditure, on the other hand, slowed down to 12.6 percent in Jul-Mar FY17 compared to 14.0 percent growth in the same period last year. Importantly, the main focus of provinces remained on infrastructure

[10] The Government of Punjab, in collaboration with Punjab Information Technology Board (PITB), has launched Invoice Monitoring System on various services especially restaurants and beauty parlors (source: Notification No.PRA/Orders.06/2012, Dated January 13th, 2015).
[11] Land Administration and Revenue Management Information System (LARMIS), Board of Revenue, Government of Sindh.

development and energy projects. Punjab spent 33 percent of its total expenditures on development projects with infrastructure and social sectors being priority.[12] Sindh and KP also increased their development spending during Jul-Mar FY17. On the contrary, Baluchistan registered lower development spending during the period under review compared to the last year.

4.5 Public debt

With an addition of Rs 1.2 trillion during Jul-Mar FY17, gross public debt reached Rs 20.9 trillion as of end-March 2017 (**Table 4.8**). More than 90 percent of the rise in public debt came from domestic borrowing, while increase in external debt remained moderate on account of revaluation gains and marginally higher debt repayments during the period.

Table 4.8: Pakistan's Public Debt Profile
billion Rupees

	Stock		Flow				
			Jul-Mar		FY17		
	Jun-16	Mar-17	FY16	FY17	Q1	Q2	Q3
Gross public debt (FRDLA definition)*	**19,676.7**	**20,873.9**	**1,787.7**	**1,197.2**	**866.1**	**-270.6**	**601.7**
Domestic debt	13,625.9	14,746.0	1,205.5	1,120.1	759.8	-193.1	553.5
External debt	5,417.7	5,501.4	415.40	83.8	97.3	-54.4	40.8
Debt from the IMF	633.1	626.4	166.8	-6.7	8.9	-23.0	7.4
External liabilities	377.1	368.1	4.7	-9.0	-1.1	-11.1	3.1
Net public debt**	17,823.2	18,925.4	1,360.2	1,102.1	458.8	103.6	539.7

*Fiscal Responsibility and Debt Limitation Act, 2005 (FRDLA) was amended in June 2016 to define "Total Public Debt" as "The debt of the government serviced out of consolidated fund and debts owed to International Monetary Fund (IMF)".
**Gross public debt minus government deposits with the banking system.
Data source: State Bank of Pakistan

Domestic debt

With higher fiscal deficit and net external financing slightly lower than last year, the burden of deficit financing fell on domestic sources during Jul-Mar FY17. Yet, the pace of domestic debt accumulation decelerated during the period. It grew by 8.2 percent during Jul-Mar FY17 compared to 9.9 percent increase recorded in the last year (**Table 4.9**). Almost entire increase in domestic debt during the period was contributed by short-term debt, as the government retired long-term debt. Quarterly break-up shows that there was a shift in borrowing away from SBP during the second and third quarters of FY17 (**Table 4.10**). In absolute terms, the government retired Rs 177.3 billion to SBP during second and third quarters of

[12] Medium Term Development Framework (MTDF) 2016-19, Government of Punjab.

FY17, after borrowing heavily from SBP in the first quarter. This retirement was made possible through: (i) drawdown in government deposits held with the SBP, and; (ii) increased borrowing from commercial banks.

Table 4.9:Absolute Change in Government Domestic Debt
billion Rupees

	FY16	FY17	FY17		
	Jul-March		Q1	Q2	Q3
Government domestic debt	**1,205.5**	**1,120.1**	**759.8**	**-193.2**	**553.5**
Permanent debt	754.2	-561.8	-746.2	26.0	158.4
Of which					
PIBs	622.6	-644.9	-780.9	0.0	136.0
Prize bond	94.1	83.1	34.8	26.0	22.4
Floating debt	354.9	1,599.9	1,480.0	-243.9	363.8
Of which					
MTBs	540.6	1,077.9	568.1	62.8	447.0
MRTBs	-219.2	734.6	911.9	-94.1	-83.2
Unfunded debt	96.2	82.0	26.0	24.6	31.3
Foreign currency loans	0.1	0.0	0.0	0.0	0.0

Data source: State Bank of Pakistan

Banks' interest in government securities, as evident from the bidding pattern in recent auctions, was also revived in Q3-FY17. Yet, the offer-to-target ratio was much higher in case of T-bill than in PIB auctions. Against a target of Rs 2.5 trillion, commercial banks offered Rs 4.3 trillion in T-bill auctions held during the third quarter. Moreover, most offers were in 3-months and 6-months T-bills (**Table 4.10**). The government accepted significantly higher amount in T-bill auctions compared to targets to facilitate retirement of maturing PIBs in the quarter.

Table 4.10: PIB and T-bills Auction Profile*
billion Rupees

	Target	Offer	Accepted	Maturity**
Q1-FY17				
T-bills	1,450.0	3,066.0	1,680.4	1,178.0
PIBs	300	995.4	678.5	1683.9
Total	**1,750.0**	**4,061.2**	**2,358.9**	**2,861.9**
Q2-FY17				
T-bills	1,300.0	1710.6	1,048.4	1,058.4
PIBs	200	234.7	0.0	35.5
Total	**1,500.0**	**1,945.2**	**1,048.4**	**1,093.9**
Q3-FY17				
T-bills	2,550.0	4,319.8	2,888.8	2,522.2
PIBs	150.0	323.6	132.4	207.6
Total	**2,700.0**	**4,643.4**	**3,021.2**	**2,729.8**
Grand total Jul-Mar-FY17	**5,950.0**	**10,649.8**	**6,428.5**	**6,685.6**

* Face value and competitive bids only; ** Principal plus coupon payments for PIBs

Data source: State Bank of Pakistan

PIB auctions depict relatively different picture in Q3-FY17. As a whole, the government did not meet pre-auction targets as banks were bidding for higher rates. With these developments, the composition of Pakistan's domestic debt saw a shift: significant substitution of long-term debt with short-term debt. Thus with an increase of Rs 1.6 trillion in Jul-Mar FY17, the share of floating debt rose to 44.8 percent by end-March FY17 from 36.7 percent as of end June 2016.

While short-term borrowings help curtail the servicing cost, these worsen the maturity profile and increase the government exposure to rollover and re-pricing risks. For instance, the debt re-fixing in one year increased to 53.6 percent in December 2016 from 47.7 in June 2015.[13] Similarly, the average time to maturity (ATM) fell to 2.1 years in December 2016 from 2.3 years in June 2015 (**Table 4.11**).

In terms of ownership, although a part of government securities shifted to non-bank financial institutions through secondary market trading, around eighty percent of the government securities are still held by the commercial banks (**Figure 4.7**). Like commercial banks, non-banks also substituted their investment from PIBs to T-bills during Q1-FY17. However, increased investment in both T-bills and PIBs represent fresh investment during second and third quarter of FY17, which is a healthy development.

Table 4.11: Risk Indicators of Domestic Debt*

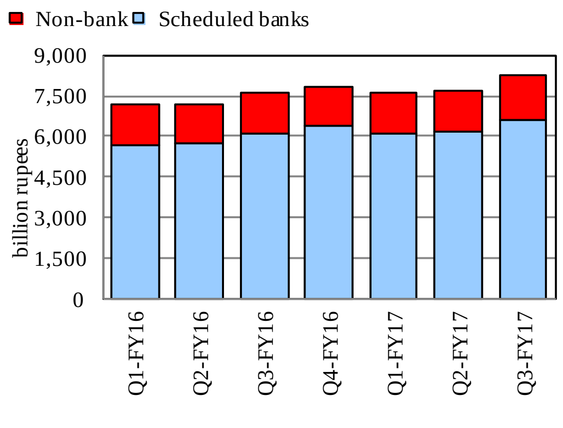
Number of years for ATM and ATR; percent of total otherwise

	2015	Mar-16	Jun-16	Dec-16
Interest Rate Risk				
Debt re-fixing in 1 year	47.7	53.3	52.8	53.6
Fix rate debt	58.9	61.2	61.6	54.3
ATR	2.3	2.0	2.1	2.1
Refinancing Risk				
Debt maturing in 1 year	47.3	52.4	51.9	52.7
ATM	2.3	2.1	2.1	2.1

*Corresponding information for end-March is not yet available
ATR: Average Time to Re-fixing; ATM: Average Time to Maturity

Data source: Debt Policy Coordination Office

Figure 4.7: Holdings of MTBs and PIBs



Unfunded debt

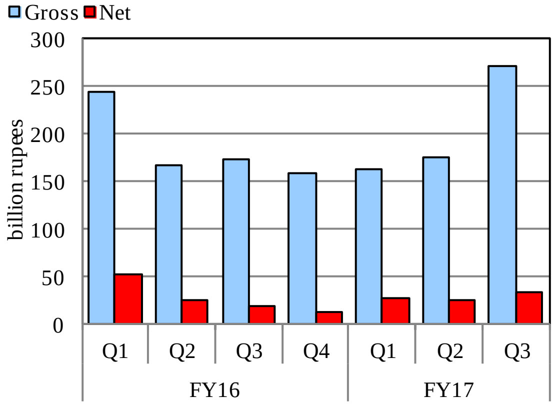
The net flows in National Savings Schemes (NSS) recorded marginal improvement in Q3-FY17 compared to the first half of FY17. This was expected as the impact of an upward revision in the rate of return on

[13] This ratio, nonetheless, is significantly lower than 67.2 percent in 2013.

some schemes during H1 started to become evident during the third quarter.[14] However, net inflows in NSS during Jul-Mar FY17 were still lower than the level observed during the same period last year.

At the same time, the gross inflows in these schemes proved to be more resilient to the profit rate changes during FY17, showing significant improvement in the gross inflows during the third quarter (**Figure 4.8**). It seems that investors re-priced their investments to get benefit of higher rates, as net inflows did not increase much.[15]

Figure 4.8: NSS Inflow



Data source: Central Directorate of National Savings

<u>Public external debt</u>

Pakistan's public external debt & liabilities stock increased by US$ 595.6 million during Jul-Mar FY17, reaching US$ 62 billion as of end-March 2017 (**Table 4.12**). Despite substantial disbursements, lower accumulation in external debt reflects US$ 1.5 billion revaluation gain during the period. At the same time, repayment of external debt also increased marginally during the period compared with the same period last year.

Disbursements

Gross external loan disbursements stood at US$ 4.9 billion during Jul-Mar FY17, largely in line with the full year target of US$ 7.6 billion announced at the beginning of FY17 (**Figure 4.9**). In addition to US$ 1.0 billion Sukuk bond proceeds, Pakistan also received substantial inflows from external creditors, especially from ADB, foreign commercial banks, and China.

[14] NSS rates have been revised on three occasions during Jul-Mar FY17 i.e., August 1, 2016; October, 1 2016, and; February 1, 2017.

[15] It is important to note that the number of national saving schemes is exempted from any direct penalty on early encashment that encouraged investors to re-invest their original certificates.

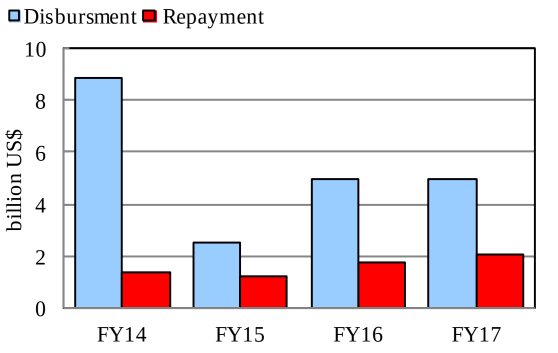
Table 4.12: Public External Debt & Liabilities
billion US$

	Stocks		Flows				
			Jul-Mar		FY17		
	Jun-16	Mar-17	FY16	FY17	Q1	Q2	Q3
Public external debt & liabilities (1+2+3)	61.4	62.0	4.1	0.6	1.0	-0.9	0.5
Public external debt (1+2)	57.7	58.5	4.1	0.9	1.1	-0.8	0.5
1.Government debt	51.7	52.5	2.6	0.8	1.0	-0.6	0.4
Of which							
Paris club	12.7	11.9	0.6	-0.8	0.1	-1.2	0.3
Multilateral	26.4	25.9	0.9	-0.4	-0.2	-0.4	0.2
Other bilateral	4.4	5.2	0.2	0.8	0.3	0.4	0.1
Euro/Sukuk bonds	4.6	5.6	0.0	1.0	0.0	1.0	0.0
Commercial loans	1.5	2.2	1.2	0.7	0.4	0.0	0.4
2.IMF	6.0	6.0	1.5	0.1	0.1	-0.2	0.1
3.Foreign exchange liabilities	3.6	3.5	-0.1	-0.1	0.0	-0.1	0.0

Data source: State Bank of Pakistan

Encouragingly, inflows from the multilateral donors continued, despite conclusion of the IMF program in the beginning of FY17.[16] Specifically, gross disbursement from IFIs stood at US$ 1.2 billion in Jul-Mar FY17. Within the multilateral flows, disbursements from ADB increased, while inflow from the World Bank declined. Another important development is the substantial financing availed from the foreign commercial banks.

Fgure 4.9: Gross Disbusment and Repayment of Government External Debt



Data source: Economic Affairs Division and State Bank of Pakistan

[16] Generally, inflows from multilateral donors (like ADB, World Bank etc) are contingent with the structural reforms under IMF program and usually dry out with the completion of program. However, as inflows remain intact, this shows that government is continuing its reforms program.

These included US$ 700 million from China Development Bank (CDB), US$ 300 million from Industrial and Commercial Bank of China (ICBC) and US$ 315 million from the Noor Bank.

Servicing of external debt
The servicing of public external debt increased by only US$ 40.5 million during Jul-Mar FY17 (**Table 4.13**). This main servicing burden was due to repayment to the multilateral donors that reached around US$ 1.0 billion during Jul-Mar FY17. In addition, the government also repaid China Safe Deposits worth US$ 500 million.

Table 4.13: Servicing of Public External Debt (Jul-Mar)
million US$

	FY16	**FY17**	**Change**
Government debt	2,005.0	2,045.5	40.5
Of which			
Paris club	129.1	153.8	24.7
Multilateral	955.9	999.6	43.8
Other bilateral	200.0	233.4	33.3
Euro/Sukuk bonds	500.0	0.0	-500.0
SAFE China deposits	0.0	500.0	500.0
Commercial loans	200.0	139.8	-61.2
IMF	52.6	0.0	-52.6
External liabilities	0.0	0.0	0.0
Total	**2,057.6**	**2,045.5**	**-12.1**

Data source: State Bank of Pakistan