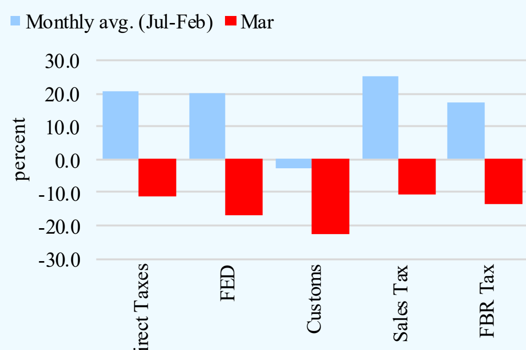
4 Fiscal Policy and Public Debt

The overall fiscal position during Jul-Mar FY20 showed considerable improvement over the corresponding period of last year. Fiscal deficit declined to 4.0 percent from 5.1 percent; while revenue deficit contracted, primary balance recorded a surplus. The improvement is primarily attributed to a strong growth in non-tax revenues and higher tax rates, along with curbs on expenditures in Q1. Within expenditures, current spending recorded a marginal deceleration while spending on social fronts notably increased in Q2 and Q3. However, the arrival of COVID-19 pandemic towards the end of Q3 has challenged an otherwise encouraging trend in Pakistan's fiscal accounts. While remaining largely within the contours of IMF agreed fiscal targets, primary surplus seen in the first two quarters transformed into a deficit in Q3; fiscal and revenue deficits also deteriorated. In March 2020, all categories of FBR taxes recorded a negative growth and PSDP releases shrank. In effect, the pressures on public finances are quite significant both because of the contraction in economic activity and additional spending requirements especially on health and cash transfers. As for the financing of the budget deficit is concerned, the burden fell on both domestic and external sources. Resultantly, public debt increased during the period under review; however, pace of debt accumulation was slower as compared to last year due to lower financing needs.

4.1 Revenues

Before COVID-19 pandemic, the growth in tax revenues was on track during Jul-Feb FY20 with expectations of meeting the revised FBR tax revenue target. However, as the COVID-19 pandemic worsened in the world and started to interrupt the normal functioning of the economy by mid-March 2020 in Pakistan, FBR tax collection deteriorated sharply on account of the large shock to activity, thus disrupting the pace of revenue

Figure 4.1: Growth (YoY) in FBR Taxes (FY20)



Data source: Federal Board of Revenue

growth by the end of Q3 **(Figure 4.1)**.[1] The impact was more pronounced as bulk of tax collection is concentrated at quarter and year ends. Yet, the cumulative growth in revenues during Jul-Mar FY20, both in tax and non-tax revenue remained in double digit.

Table 4.1: FBR Tax Collection during Jul-Mar
billion rupees, growth in percent

	Budget FY20*	Collection			Growth		
		FY18	FY19	FY20	FY18	FY19	FY20
Direct taxes	2,081.9	1,001.4	993.2	1,142.3	12.2	-0.8	15.0
Indirect taxes	3,473.0	1,626.4	1,709.1	1,918.2	18.9	5.1	12.2
Customs duty	1,000.5	428.4	506.5	481.5	24.8	18.2	-4.9
Sales tax	2,107.7	1,053.7	1,039.7	1,250.2	17.4	-1.3	20.2
FED	364.8	144.3	162.9	186.5	13.5	12.9	14.4
Total taxes	**5,555.0**	**2,627.8**	**2,702.4**	**3,060.5**	**16.2**	**2.8**	**13.3**

* Budget in Brief, Ministry of Finance
Data source: Federal Board of Revenue

FBR Taxes

Overall FBR tax collection reached Rs 3,060.5 billion during Jul-Mar FY20, a growth of 13.3 percent compared to 2.8 percent growth in the same period last year **(Table 4.1)**. It is important to note that the steps taken in Q1-FY20 remains the main drivers in FBR revenue growth. Accordingly, main impetus came from higher sales tax rates on various POL products, abolishment of zero-rating regime for export-oriented sectors, upward revision of income tax rates on various salary slabs, re-enactment of WHT on telecom services, and higher FED rates. Relatively higher inflation during Jul-Mar FY20 may also have contributed to revenue growth. Moreover, import-related taxes, constituting more than 40 percent FBR taxes, continued to remain under stress due to the declining trend in imports.[2]

Direct Taxes

Direct taxes that constitute one-third of the overall FBR taxes, rose by 15.0 percent in Jul-Mar FY20 in contrast to a decline of 0.8 percent in the corresponding period last year. Breakup of direct taxes shows that collection from withholding taxes (WHT) had the largest contribution. Within this

[1] The growth in FBR taxes declined sharply by 13.2 percent (YoY) in March 2020.
[2] The FBR tax collection target for FY20 has been revised further down from Rs. 4803.0 billion to Rs 3,908.0 billion to incorporate COVID-19 impact.

category, taxes on salaries, bank interest and securities, and telephone together contributed 13.0 percentage points to the overall growth in direct taxes **(Table 4.2)**.

Tax measures such as upward revision in tax rates on various salary slabs, increase in tax rates on profit on debt, and the re-enactment of WHT on mobile phone top-ups helped in higher collection in these categories. With the abolishment of advance tax on banking transaction for filers in Finance Supplementary (Second Amendment) Bill, 2019, the collection from cash withdrawal declined by 52.5 percent during Jul-Mar FY20 as compared to a rise of 7.8 percent in the review period. The import compression suppressed the WHT on imports that declined by 7.9 percent in Jul-Mar FY20 compared to growth of 5.3 percent.[3]

Collection from contracts grew by 5.5 percent during Jul-Mar FY20 in contrast to a decline of 15.3 percent in the corresponding period last year. This is largely due to higher PSDP releases during the period under review.

Table 4.2: Major Revenue Drivers of Direct Taxes - Jul-Mar
billion rupees; growth in percent

	FY18	FY19	FY20	Growth	
				FY19	FY20
Withholding taxes	**749.7**	**684.5**	**827.2**	**-8.7**	**20.8**
Imports	159.8	168.2	155.0	5.3	-7.9
Salaries	95.2	53.5	89.7	-43.8	67.6
Dividends	38.7	33.6	38.5	-13.2	14.4
Bank interest & securities	34.5	43.7	100.8	26.8	130.4
Contracts	194.6	164.9	173.9	-15.3	5.5
Exports	20.2	24.2	29.7	19.8	22.5
Cash withdrawal	24.8	26.8	12.7	7.8	-52.5
Electricity bills	23.3	26.7	35.8	14.9	33.8
Telephone	38.0	5.3	41.3	-86.1	680.8
Collection on demand	**68.4**	**74.4**	**41.5**	**8.8**	**-44.3**
Voluntary payments	**240.0**	**308.6**	**324.7**	**28.6**	**5.2**
Miscellaneous	4.0	-14.8	2.5	-470.7	-116.7
Gross income tax	1,062.1	1,052.7	1,195.9	-0.9	13.6
Net direct tax	**1,001.4**	**993.2**	**1142.3**	**-0.8**	**15.0**

Data source: Federal Board of Revenue

Table 4.3: Major Revenue Spinners of Sales Tax during Jul-Mar
billion rupees; growth in percent

	FY19	FY20	Growth
Sales tax	**1,039.7**	**1,250.2**	**20.2**
POL	193.9	209.0	7.8
Electrical energy (DISCOS)	37.6	73.9	96.6
Textile sector	5.9	54.1	812.3
Sugar	16.9	26.8	58.9
Iron and steel	14.5	13.0	-10.2
Plastics	4.4	4.6	4.7
Photosensitive semiconductor devices	4.9	4.0	-19.5
Indirect taxes	**1,709.1**	**1,918.2**	**12.2**

Data source: Federal Board of Revenue

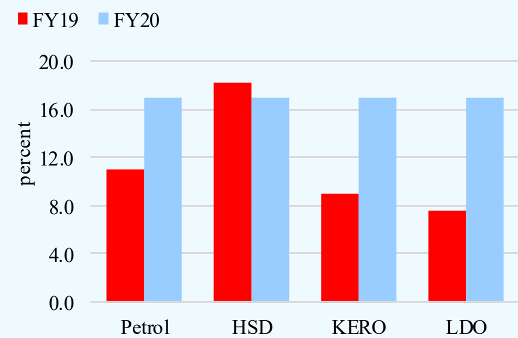
[3] Overall imports in value terms declined by 14.4 percent during Jul-Mar compared to a decline of 8.1 percent in same period last year.

Indirect Taxes

Indirect taxes grew by 12.2 percent during Jul-Mar FY20 against a subdued growth of 5.1 percent in the corresponding period last year **(Table 4.3)**.[4] The rise in collection of indirect taxes is primarily due to upward revision of sales tax rate and federal excise duty.

Within indirect taxes, sales tax grew by 20.2 percent during Jul-Mar FY20 in contrast to a decline of 1.3 percent during the review period of last year. This rise in sales tax was mainly derived from the collection on POL and Electrical energy (DISCOS) **(Figure 4.2)**. Having the second largest share in sales tax, the collection from electrical energy surged to Rs 73.9 billion in Jul-Mar FY20 against Rs 37.6 billion in the same period last year. This rise is explained by the upward price adjustments in power tariffs.[5] Lastly, taxes from textile sector recorded an exponential increase on account of the abolishment of zero-rating regime for export-oriented sector. Collection from textile sector increased by Rs 48.2 billion to Rs 54.1 billion during Jul-Mar FY20 against Rs 5.9billion in the same period of last year. Meanwhile, an upward revision in sales tax rates on sugar also contributed to higher revenue collection.[6]

Figure 4.2: Sales Tax Rates on POL in Jul-Mar*



*Effective tax rates are calculated on the basis of weighted average formula
Data source: Federal Board of Revenue and SBP calculations

[4] However, the growth would have been even higher if we take out the sharp decline of 14.6 percent in March 2020.
[5] Now variable charges are collected, i.e. on peak (Rs 20.7 per unit) and off peak (Rs 14.4 per unit) instead of previously consumption slabs-based tariff.
Source: https://nepra.org.pk/tariff/Tariff/KESC/2019/SRO%20575%20I%202019%2022-05-2019.PDF
[6] Sales tax collection from sugar increased to Rs 26.8 billion in Jul-Mar FY20 against Rs 16.9 billion during Jul-Mar FY19.

Collection from FED grew by 14.4 percent in Jul-Mar FY20 compared with 12.9 percent growth in Jul-Mar FY19.[7] The rise in FED collection was explained by an upward revision in FED rates.[8] Cement and beverages together contributed almost 9 percentage points to the overall growth in FED during the review period.

Having a share of around 25 percent in indirect taxes, collection from custom duty declined by 4.9 percent in Jul-Mar FY20, compared to 18.2 percent growth in the corresponding period of last year **(Table 4.4)**.[9] With the exception of POL and photosensitive semiconductor devices, the collection from other major heads of custom duty declined during Jul-Mar FY20, mainly in collection from vehicles.

Table 4.4: Major Revenue Spinners of Excise and Custom Duties in Jul-Mar
billion rupees; growth in percent

	FY19	FY20	Growth
Custom Duty	**506.5**	**481.5**	**-4.9**
Mineral fuel, oil, and products.	59.2	68.1	15.0
Vehicles	66.1	43.6	-34.0
Iron and steel	35.5	35.1	-1.0
Other	345.7	334.6	-3.2
FED	**162.9**	**186.5**	**14.4**
Cement	42.6	53.3	25.0
Cigarettes & Tobacco	58.2	58.2	0.0
Concentrate/ aerated Water/beverage	13.7	18.6	35.1
Indirect tax	**1709.1**	**1918.2**	**12.2**

Data source: Federal Board of Revenue

Non-tax Revenues

Non-tax revenues rose significantly by Rs 673.9 billion during Jul-Mar FY20, compared to a decline of Rs 84.6 billion in the corresponding period last year **(Table 4.5)**. The rise is largely attributed to higher SBP profits and revenues received through GSM license renewal fee. The renewal fee of GSM license was realized in Q1 and Q2 of FY20. SBP profits

Table 4.5: Non-tax Revenues during Jul-Mar (consolidated)
billion rupees

			Abs. change	
	FY19	**FY20**	**FY19**	**FY20**
SBP profits	138.2	635.5	-5.0	497.3
Profits (post office/PTA)	16.2	113.2	7.3	97.0
Mark-up (PSEs & others)	14.4	70.0	-7.3	55.7
Royalties on gas & oil	61.8	65.6	19.4	3.8
Dividends	32.2	26.6	-1.4	-5.6
Passport & other fees	16.3	16.3	4.4	0.0
Defense	10.7	10.8	1.4	0.1
Discount retained (crude oil)	10.4	10.5	3.9	0.1
Others	121.4	147.0	-107.4	25.6
Total	**421.6**	**1,095.6**	**-84.6**	**673.9**

Data source: Ministry of Finance

[7] The growth in FED collection during Jul-Mar FY20 is higher than the 5-year average of the same period.
[8] The FED rate for beverages was increased to 13.0 percent from 11.5 percent. While FED on cigarettes and cement was increased by Rs 700 per 1000 sticks and Rs 0.5 per kg, respectively.
[9] Overall, the import related collection constitutes more than 40 percent share in the overall FBR taxes.

increased by Rs 497.3 billion compared to a decline of Rs 5.0 billion during the same period of last year. This sharp increase in profits is largely attributed to higher interest rates, and revaluation gains.

Table 4.6: Analysis of Fiscal Spending
billion rupees; growth in percent

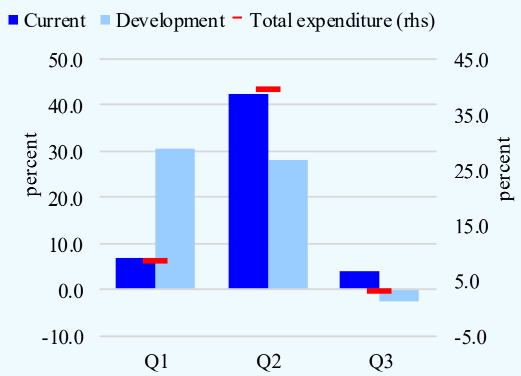
	Jul-Mar		Abs. change		Growth	
	FY19	FY20	FY19	FY20	FY19	FY20
Current expenditures	**4,798.4**	**5,611.6**	**722.9**	**813.2**	**17.7**	**16.9**
Federal	3,180.9	3,887.7	527.6	706.8	19.9	22.2
of which						
Interest payments	1,459.2	1879.7	286.3	420.5	24.4	28.8
Domestic	1,276.8	1645.6	205.4	368.9	19.2	28.9
Foreign	182.4	234.1	81.0	51.6	79.8	28.3
Grants	227.1	363.1	-6.5	136.0	-2.8	59.9
Defense	774.7	802.4	150.9	27.7	24.2	3.6
Public order and safety	106.1	111.2	12.2	5.1	12.9	4.8
Others	840.9	1,094.3	311.8	253.5	58.9	30.1
Provincial	1,617.4	1723.9	195.3	106.4	13.7	6.6
Development expenditures	**655.9**	**751.7**	**-337.4**	**95.9**	**-34.0**	**14.6**
PSDP	578.5	722.5	-352.9	144.0	-37.9	24.9
Federal	302.4	340.5	-51.1	38.0	-14.5	12.6
Provincial	276.0	382.0	-301.8	106.0	-52.2	38.4
Others	77.4	29.2	15.5	-48.2	25.0	-62.2
Net lending	**28.3**	**29.7**	19.1	**1.4**	**208.0**	**4.9**
Total expenditure*	**5,482.5**	**6,393.0**	**404.6**	**910.5**	**8.0**	**16.6**

* Excluding Statistical discrepancy
Data Source: Ministry of Finance

4.2 Expenditures

Total expenditures grew by 16.6 percent during Jul-Mar FY20 as compared to 8.0 percent during the same period last year. A broad-based increase in current and development expenditure at both federal and provincial fronts, contributed to this growth **(Table 4.6)**.

Figure 4.3: YoY Growth of Fiscal Spending during FY20



Data source: Ministry of Finance

However, the quarter-wise analysis reveals that the total expenditure actually decelerated in Q3-FY20 after a sharp growth reported in the second quarter. Moreover, the development expenditure declined along with the slowdown in current expenditure in Q3-FY20 **(Figure 4.3)**.

Major contribution in current spending came from the interest payments (mainly on the back of domestic debt) and the government's concern to support social spending (*Ehsaas* Program). Towards the end of Q3-FY20, the COVID-19 pandemic necessitated the need for fiscal stimulus package and accordingly the government announced one **(Table 4.7)**.

Table 4.7: Government's Stimulus Package amid COVID-19
(billion rupees)

Emergency measures	**190**
Emergency funds	100
Tax relief on food and health items	15
Incentive for workers/ medical equipment	50
National Disaster Management Authority (NDMA)	25
Support to business and economy	**480**
Relief to SMEs and Agriculture	100
Relief to Exporters	100
Payment to farmers (wheat)	280
Relief to citizens	**570**
Relief to poor and *Panahgahs*	150
Funding to Utility stores	50
Power and gas subsidy/payment deferrals	100
Support to daily wage workers	200
Relief to petrol/diesel	70
Total funding	**1,240**

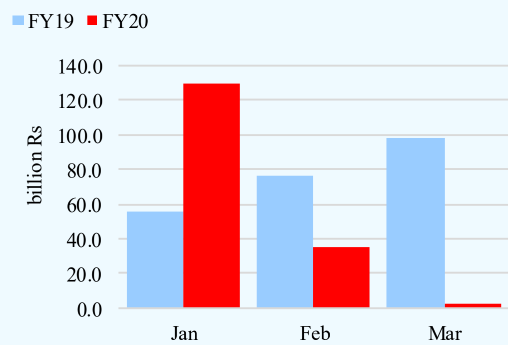
Data source: Ministry of Finance

The dynamics of interest payments and grants for social spending were noteworthy in Q3-FY20. On one side, the interest payments grew by only 2.7 percent in Q3-FY20 as compared to 38.2 percent during Q3-FY19. On the other side, the grants with a continued increasing trend for the last two quarters, further grew significantly by 25.9 percent in Q3-FY20 against a decline of 5.4 percent in the corresponding period of last year.

Despite a relatively higher growth in development expenditures during Jul-Mar FY20 than the corresponding period of last year, Q3-FY20 witnessed a YoY decline, which can be explained by a decline in federal PSDP spending during the quarter. In contrast, provincial PSDP grew sharply by 50.2 percent in Q3-FY20.

The preferences for PSDP remained towards infrastructure (National Highway Authority), water resources division, security enhancement, programs for special areas (AJK and Gilgit Baltistan), and merged areas 10-year development program[10]. About 60 percent of the budgeted target was spent on PSDP during Jul-Mar FY20 which was below the cumulative 80 percent target of the three quarters of FY20.[11] This is evident from a decline of federal PSDP in Q3-FY20, which slowed down the pace of development expenditures during Jul-Mar FY20. Although already on a decline, PSDP releases fell sharply in March 2020 that may also be on account of disruptions caused by COVID-19 pandemic **(Figure 4.4)**.

Figure 4.4: Federal PSDP Releases in Q3



Data source: Ministry of Planning, Development, and Reform

Table 4.8: Provincial Fiscal Operations during Jul-Mar
billion rupees and percent growth

	Total		Growth	
	FY19	FY20	FY19	FY20
A. Total revenue	2,198.3	2,467.4	1.5	12.2
Provincial share in federal revenue	1,779.1	1,931.6	7.9	8.6
Provincial revenue (I+II)	353.0	400.8	-13.2	13.5
I. Taxes	287.7	321.2	2.8	11.6
II. Non-tax revenue	65.3	79.6	-48.4	21.9
Fed loans and transfers	66.1	134.9	-40.3	104.0
B. Total expenditure	1,906.0	2,123.8	-5.2	11.4
Current**	1,630.0	1,741.8	13.8	6.9
Development	276.0	382.0	-52.2	38.4
Gap (A-B)	292.3	343.1	87.5	17.4
Financing* (overall balance)	**-291.6**	**-394.1**	**52.6**	**35.2**

*Negative sign in financing means surplus. ** Current expenditure data may not match with those given in Table 4.6 as numbers reported here includes the markup payments to federal government.
Data source: Ministry of Finance

[10] This program is for the FATA which was merged with KP under the 25th amendment of the constitution.
[11] Revised Release Strategy for Funds Allocated for the Public Sector Development Program (PSDP) 2019-20

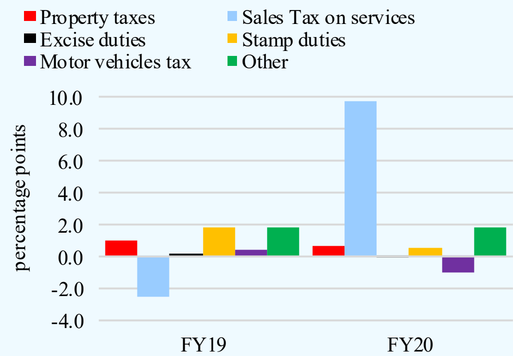
4.3 Provincial Fiscal Operations

Provinces remained committed to the fiscal consolidation and posted a surplus of Rs 394.1 billion during Jul-Mar FY20 which covers around 93 percent of the target envisaged in the budget **(Table 4.8)**. Specifically, Punjab contributed Rs 122.6 billion followed by Rs 106.3 billion, Rs 90.0 billion and Rs 75.2 billion from Balochistan, Sindh and KP respectively.

Total provincial revenue grew by 12.2 percent during Jul-Mar FY20 as compared to 1.5 percent in the corresponding period last year. About 83.8 percent of this came from provincial share (as per NFC award) and *federal loans and transfers*. The remaining 16.2 percent constituted the provincial own revenue collection, which grew by 13.5 percent during Jul-Mar FY20 as compared to a decline of 13.2 percent recorded in last year.

Both tax and non-tax sources contributed to provincial own revenue collection. Provincial tax collection grew sharply during Jul-Mar FY20 compared to last year **(Table 4.8)**. Moreover, the dynamics in provincial tax sources were noteworthy. General sales tax on services (GSTS) continued to be a major revenue spinner that rose by 19.7 percent during Jul-Mar FY20 against a decline in the same period last year.[12]

Figure 4.5: Major Contributors to Provincial Tax Collection during Jul-Mar



Data source: Ministry of Finance and SBP calculations

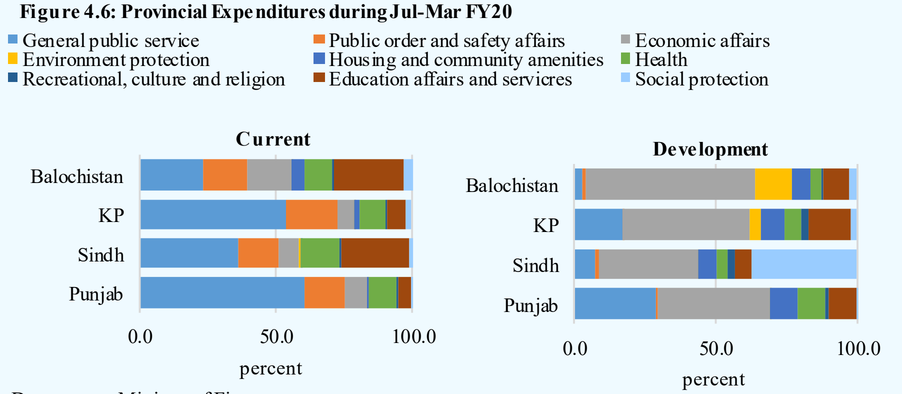
In contrast, motor vehicle tax and excise duties declined during Jul-Mar FY20 against a growth witnessed in last corresponding period **(Figure 4.5)**. This stemmed from a lower growth in the production of cars and motorcycles amid the effects of demand management policies and that was further aggravated due to COVID-19 in the country. Since GSTS and stamp duties are the prominent spinners of the provincial taxes, their growth augmented the provincial own revenue collection during Jul-Mar FY20. Provincial non-tax revenue also surged

[12] As per the Human Rights Case No. 18877 of 2018, there was a ban on collection of sales tax on mobile top-ups that was applicable to all the provinces. Since telecom services make as significant share of taxable services, the collection was lower in H1-FY19. However, the GSTS for provinces increased in H1-FY20 with the revoke of the ban.

mainly on the back of profits from hydroelectricity - KP (Rs 15.6 billion) and Punjab (Rs 6.5 billion) contributed the most.

The total provincial expenditures grew by 11.4 percent during Jul-Mar FY20 against a decline of 5.2 percent in the same period last year. However, provincial current expenditure decelerated during the review period compared to last year. The province-wise breakup shows that Punjab recorded Rs 848.9 billion, Sindh recorded Rs 486.9 billion, KP recorded Rs 254.2 billion, and Balochistan recorded Rs 151.7 billion under current expenditures during the review period. A sharp growth was seen in provincial development spending which has been highest during Jul-Mar since FY16.

Figure 4.6: Provincial Expenditures during Jul-Mar FY20



Data source: Ministry of Finance

The disaggregated analysis shows that the provincial current spending priorities continued to remain towards general public services[13] followed by public order and health. A major portion of development spending was allocated to economic affairs, primarily construction and transport, agriculture and food related spending. **Figure 4.6** elucidates the provincial preferences in the current and development expenditure during Jul-Mar FY20.

[13] General public services include executive, legislative, financial, and fiscal affairs, transfers to districts, administration of general services to public etc.

4.4 Public Debt

Overall lower financing needs helped in containing the pace of public debt accumulation during Jul-Mar FY20 **(Table 4.9)**.[14] Gross public debt increased by Rs 2.5 trillion during the period under review compared to a rise of Rs 3.7 trillion in the corresponding period last year (**Table 4.10**). Two-third of the rise in public debt originated from domestic sources, while the rise in government external debt (in Rupee terms) remained much lower compared to same period last year.

Table 4.9: Sources of Change in Public Debt (Jul-Mar)
trillion rupees

	FY19	FY20
Total change in public debt	**3.7**	**2.5**
Key sources		
1. Deficit financing	1.9	1.7
2. Change in govt. deposits	0.3	0.6
3. Impact of exchange rate movements*	1.3	0.2
4. Others	0.2	-

* Impact of exchange rate movements include the movement of international currencies against the US$ and the movement of PKR against the US$.
Data sources: Ministry of Finance and State Bank of Pakistan

In absolute terms, government external debt (in Rupee terms) increased by Rs 0.6 trillion during Jul-Mar FY20 compared to a rise of Rs 1.8 trillion in the corresponding period last year.[15] Unlike last year when most of the increase in government external debt was due to depreciation of PKR against the US dollar, a

Table 4.10: Pakistan's Public Debt Profile
billion rupees

	Stock		Flow				
			Jul-Mar		FY20		
	Jun-19	Mar-20	FY19	FY20	Q1	Q2	Q3
Gross public debt (1 to 3)	**32,707.9**	**35,207.0**	**3,654.6**	**2,499.2**	**1,532.8**	**-529.0**	**1,495.4**
1. Govt. domestic debt	20,731.8	22,477.7	1,754.3	1,745.9	1,918.1	-973.5	801.3
2. Govt. external debt	11,055.1	11,658.1	1,829.9	602.9	-457.1	395.0	665.1
3. Debt from the IMF	921.0	1,071.3	70.4	150.3	71.7	49.5	29.0
Total debt of government*	29,520.7	31,452.4	3,344.2	1,931.7	-220.6	669.2	1,483.1
Govt. deposits	3,187.2	3,754.6	310.4	567.5	1,753.4	-1,198.2	12.2

*Gross public debt minus government deposits with the banking system.
Data source: State Bank of Pakistan

[14] Compared to a fiscal deficit of Rs 1.9 trillion during Jul-Mar FY19, the country recorded a fiscal deficit of Rs 1.7 trillion in Jul-Mar FY20. PKR (last day average exchange rate) depreciated by 2.0 percent against the US$ during Jul-Mar FY20 compared to a depreciation of 13.6 percent during the same period last year.
[15] This does not include debt from the IMF.

relatively stable PKR contained revaluation losses during Jul-Mar FY20.[16] It is important to note that movement in the international currencies (in which debt is contracted) and PKR vis-à-vis US$ can change the dollar and PKR value of external debt respectively (for details – see Box 4.1 Second Quarterly Report FY18).[17]

Table 4.11: Absolute Change in Government Domestic Debt

billion rupees

	FY19	FY20	FY20		
	Jul-Mar		Q1	Q2	Q3
Government domestic debt	**1,754.3**	**1,745.9**	**1,918.1**	**-973.5**	**801.3**
Permanent debt	143.6	1,164.3	754.1	327.9	82.3
of which					
PIBs	182.9	1,321.3	906.4	333.4	81.5
Prize bond	97.2	-157.0	-152.3	-5.5	0.8
Floating debt	1,381.5	270.8	1,028.2	-1,429.6	672.2
of which					
MTBs	-2,265.1	555.8	1,028.2	-1,144.6	672.2
MRTBs	3,646.6	-285.0	0.0	-285.0	0.0
Unfunded debt	228.3	310.6	136.0	128.3	46.3
Memorandum Items:					
Internal financing	1,398.0	1,003.8	119.5	361.6	522.7
Govt. deposits	310.4	567.5	1,753.4	-1,198.0	12.2

Data source: State Bank of Pakistan

Domestic Debt

As financing needs of the government remained relatively lower in Jul-Mar FY20, the pace of domestic debt accumulation decelerated during the period. It grew by 8.4 percent during Jul-Mar FY20 compared to a growth of 10.7 percent in the same period last year. Furthermore, the maturity profile of domestic debt improved as almost two-third of the increase in domestic debt during the period was contributed by permanent debt (long-term).[18] This is opposite to last year, in which the government mainly relied on floating debt (short-term) to meet its financing needs (**Table 4.11**).

Quarterly break-up of government domestic debt illustrates that major increase occurred in the first quarter. Apart from deficit financing, the government created cash buffers by further accumulating its deposits with the banking system in Q1, subsequently the government used these cash buffers in the second quarter for debt repayments and deficit financing. However, the pace of domestic debt accumulation accelerated again in Q3 mainly due to higher deficit financing – net

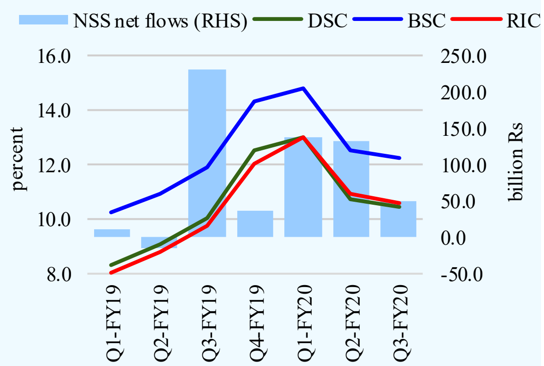
[16]In dollar terms, government external debt stood at US$ 70.0 billion (excluding IMF debt) as of end March 2020, registering a growth of 3.3 percent over June 2019. In Rupee terms, however, the external debt increased by 5.5 percent during the same period. The difference in growth primarily reflects the impact of PKR depreciation during Jul-Mar FY20. The difference in growth was much higher during Jul-Mar FY19 - in dollar terms, government external debt increased by 6.7 percent while in Rupee terms, external debt increased by 23.5 percent.

[17]http://www.sbp.org.pk/reports/quarterly/fy18/Second/Chap-4.pdf

[18] On 29th June 2019, government converted the stock of more than Rs7 trillion MRTBs held by SBP into PIBs.

internal financing increased by Rs 522.7 billion in Q3 compared to an increase of Rs 119.5 and Rs 361.6 billion in Q1 and Q2 respectively **(Table 4.11)**.

Figure 4.7: Profit Rates and Net Inflows in NSS Instruments



Data source: Central Directorate of National Savings

Importantly, the government continued to adhere to its commitment of zero fresh borrowing from the central bank for financing needs during the period under review and relied on non-banks and commercial banks for fund mobilization during Jul-Mar FY20. Both were largely interested in long-term government securities in the first two quarters of FY20 (**Table 4.12**). This is evident by the offered to target ratio, which increased from 1.3 in Q1-FY20 to 3.1 in Q3-FY20 (competitive bids). The offered to target ratio for PIBs (both fixed and floating) decreased from 3.9 in Q1-FY20 to 2.6 in Q3-FY20 (**for details, see Chapter 3**).

Table 4.12: Institution and Instrument-wise Details of Domestic Debt - Absolute Changes

billion rupees

	Q1-FY20	Q2-FY20	Q3-FY20
Through Scheduled Banks			
Long-term securities	751.6	232.9	29.2
Short-term (T-bills)	880.1	-984.1	544.2
Through Non-Banks			
Long-term securities	157.7	100.5	52.3
Short-term (T-bills)	148.1	-160.5	128.0
NSS (net of prize bonds)	-16.3	122.8	47.1
Through State Bank of Pakistan	0.0	-285.0	0.0

Data source: State Bank of Pakistan

The net flows in National Savings Schemes (NSS) recorded marginal improvement in Jul-Mar FY20 compared to the same period last year. However, quarterly analysis indicates that net flows decelerated in Q3-FY20. This was expected due to downward revision in the profit rates on most of the saving schemes (**Figure 4.7**).

Public External Debt

The pace of accumulation of Pakistan's public external debt & liabilities decelerated during Jul-Mar FY20 – an increase of US$ 2.4 billion compared to a sharp rise of US$ 8.9 billion in the same period last year (**Table 4.13**). One-half of the increase stemmed from foreign investment in local government securities while the remaining expansion in government external debt was sourced through disbursements from multilateral donors and IMF.

Table 4.13: Public External Debt & Liabilities
billion US dollars

	Stocks		Flows				
			Jul-Mar		FY20		
	Jun-19	Mar-20	FY19	FY20	Q1	Q2	Q3
Public external debt & liabilities (1+2+3)	83.9	86.4	8.9	2.4	0.6	3.1	-1.3
Public external debt (1+2)	73.4	76.5	3.9	3.0	0.7	3.6	-1.2
1.Government debt	67.8	70.1	4.3	2.3	0.0	3.2	-0.9
of which							
Paris club	11.2	10.8	-0.4	-0.5	-0.2	-0.2	-0.1
Multilateral	27.8	28.9	-0.7	1.1	0.3	1.3	-0.5
Other bilateral	12.7	13.4	3.8	0.7	0.1	0.4	0.1
Euro/*Sukuk* bonds	6.3	5.3	0.0	-1.0	0.0	-1	0
Commercial loans	8.5	9.0	2.1	0.5	-0.5	1.3	-0.3
Local currency securities	0.0	1.3	0.0	1.3	0.3	1.2	-0.2
2.IMF	5.6	6.4	-0.3	0.8	0.7	0.4	-0.3
3.Foreign exchange liabilities	10.5	9.9	4.9	-0.6	-0.1	-0.4	-0.1

Data source: State Bank of Pakistan

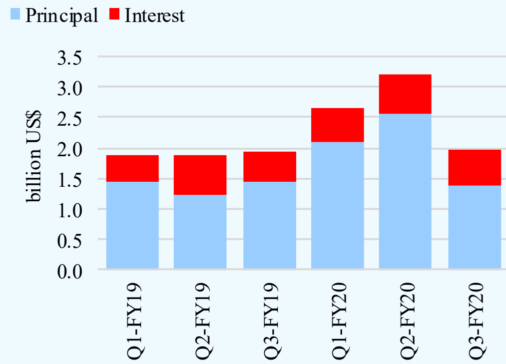
Revaluation gains contributed positively in controlling public external debt

Revaluation gains of US$ 0.7 billion during Jul-Mar FY20 helped in containing the increase in public external debt. Around 94 percent of the revaluation gains is attributed to depreciation of SDR, Euro, Japanese Yen and Chinese Yuan against the US dollar. Quarter-wise breakup reveals that most of the revaluation gains were attained in the first and third quarters.

Debt servicing decelerated in Q3

The servicing of public external debt increased by US$ 2.1 billion during Jul-Mar FY20. Within principal component, *Sukuk* (US$ 1.0 billion in Q2), bilateral and commercial loan repayments recorded a significant increase. Interest payments also increased to US$ 1.8 billion in Jul-Mar FY20, slightly higher than US$ 1.6 billion during the same period last year. This was mainly driven by higher payments on bilateral and commercial loans. Quarterly analysis indicates that after a sharp rise in the first two quarters, public debt servicing decelerated in Q3-FY20 **(Figure 4.8)**. It is important to note that during Q1 and Q2, one-off scheduled payments against central bank liabilities in Q1 and *Sukuk* in Q2 kept debt servicing on higher side.

Figure 4.8: Servicing of Public External Debt



Data source: State Bank of Pakistan