2 Real Sector

As the government eased mobility restrictions following a significant reduction in domestic Covid cases, activity started to pick up in all sectors of the economy during Q1-FY21. Fiscal and monetary incentives had been offered to multiple sectors and the results of these measures became evident in Q1-FY21. The industrial sector showed a robust growth during the period, while preliminary estimates of important crops suggested an overall improvement in the agriculture sector as well. Buoyancy in the commodity-producing sector, in turn, trickled down to the services sector, with an improvement in wholesale and retail trade, transport, and financial sector indicators. The positive sentiment was further substantiated by a significant improvement in the SBP Business Confidence Index from July 2020 to August 2020. Commensurate with the increase in overall output, indicators of the labor market such as industrial employment, Business Confidence Survey-based employment index and wages in the construction sector, all suggested pick-up in employment.

2.1 Economic Growth

Prospects of economic growth showed visible signs of improvement during Q1-FY21. After a turbulent Q4-FY20 in which industrial and services sector activity remained largely subdued due to Covid induced mobility restrictions, Q1-FY21 started on a promising note for these sectors. Industrial sector activities proxied by Large Scale Manufacturing (LSM) posted an encouraging recovery. Pickup in petroleum and automobile industries indicated a normalization in transport activity, whereas expansion in cement and long steel production pointed towards growth in the labor-intensive construction sector.

With the exception of the cotton crop, the agriculture sector's performance during the *Kharif* season was also broadly encouraging. Estimates of sugarcane and rice production indicated a noteworthy improvement from last year. However, the cotton crop suffered due to exceptionally heavy monsoon rains and pest attacks.

The indicators for the services sector also pointed to a recovery, especially in the wholesale and retail trade, transportation, and general government services segments. Gauging from mobility data, activity in a number of related segments reverted back to pre-Covid levels by end-September 2020.

The labor market, in line with improvements in the LSM and services sector, also portrayed positive trends in the period. Indicators of employment suggested recovery during Q1-FY21. This was evident in the Punjab and Sindh manufacturing sector index of employment, Business Confidence Survey and positive growth in wages of both rural and urban construction sector. However, the labor market could not yet reach pre-Covid employment levels in these sectors during the review period.

Judging from the first quarter's performance, the economy appears to be on track to achieve the real GDP growth target of just over 2 percent (**Table 2.1**). In fact, in the Annual Plan for FY21, the government had expected the decline in the LSM to continue. Hence, the bright start made by the LSM during Q1-FY21 bodes well for the economy's full-year prospects. For agriculture as well, the output of major crops, such as rice, sugarcane and maize, surpassed the respective targets during the *Kharif* season. The upward revision of wheat support price and subsidies on fertilizer and pesticides are likely to aid recovery despite a

Growth Targets in Annual Plan FY21 Table 2.1

percent

	FY19	FY20	FY21T
Agriculture	0.6	2.7	2.8
Important crops	-7.7	2.9	1.9
Livestock	3.8	2.6	3.5
Industry	-2.3	-2.6	0.1
LSM	-2.6	-7.8	-2.5
Construction	-16.8	8.1	3.5
Electricity & gas	14.5	17.7	1.4
Services	3.8	-0.6	2.6
Wholesale & retail	1.1	-3.4	1.1
Transport & comm.	4.6	-7.1	0.9
Finance & insurance	5	0.8	3
Housing	4	4	4
General government	5.2	3.9	4.6
GDP	1.9	-0.4	2.1

T: target

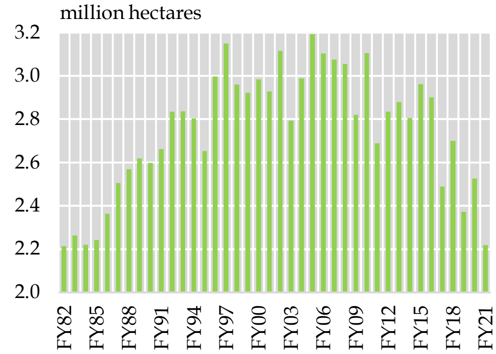
Source: Annual Plan 2020-21, Ministry of Planning, Development & Special Initiatives

shortfall in cotton production. Given its interlinkages with industry and agriculture, the services sector's annual target also appears to be attainable as long as the pace set during Q1-FY21 is maintained.

2.2 Agriculture

Among major crops, rice and sugarcane crops performed well during *Kharif* FY21. Estimated production for both crops was higher compared to last season as well as their annual targets. To some extent though, this came at the expense of a decline in area dedicated to the competing cotton crop. The area under cotton, at a little over 2.2 million hectares, was the lowest on record since FY82 (**Figure 2.1**).

Area under Cotton in Pakistan Figure 2.1



Source: Pakistan Bureau of Statistics; Ministry of National Food Security & Research

As reported previously in the SBP's FY20 Annual Report, overall crop production in the agriculture sector was relatively less affected by Covid during FY20, since the harvest of most of the major crops had already been completed before the lockdowns came into effect. Similarly, while locusts had appeared to pose a considerable threat in H2-FY20, continuous survey and control operations enabled the country to contain a major fallout on crop output.[1,2]

Nonetheless, the outlook for agriculture remained subject to certain risks. In surveys conducted by the Asian Development Bank (ADB) with farmers to gauge the dual impact of locusts and Covid lockdowns on agriculture, several respondents – more so in Sindh, and to a lesser extent in Punjab –

[1] As of 10th November, 2020, the area surveyed amounted to around 62.3 million hectares, and control operations had been conducted over an area spanning 1.1 million hectares. Source: National Locust Control Centre, Government of Islamic Republic of Pakistan.

[2] Initial estimates suggest that crops in Balochistan incurred damages amounting to Rs 4 billion, while other provinces are still in process of assessment. Source: Minutes of the 15th Meeting of the Federal Committee on Agriculture for *Rabi* season .

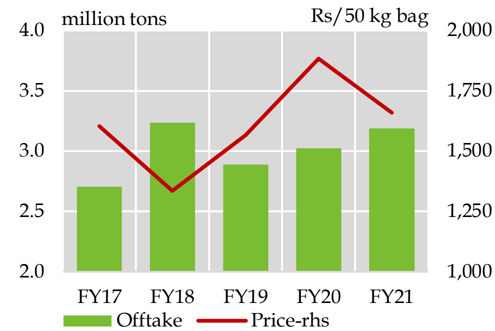
reported seeing locust swarms.[3] In addition, while farmers in Punjab did not report a major impact of the Covid lockdown on the wheat harvest, survey respondents in lower Sindh in particular cited labor shortages and Covid disruption as a factor that delayed their wheat harvest and marketing efforts. Moreover, growers of minor crops (including vegetable and fruit) and milk producers in both provinces reported difficulties in marketing their produce due to Covid-related restrictions. For perishables like tomatoes, supply-side disruptions contributed to an increase in prices of such items during Q1-FY21 (details in **Chapter 3**). Given the findings of the ADB surveys, official assessment of the province- and crop-wise impact of locusts and Covid lockdowns on agriculture is awaited for a more in-depth analysis.

Inputs

From a policy perspective, the government formulated an agriculture package as part of its broader Rs 1.2 trillion Covid relief package. This agriculture package, amounting to Rs 50 billion, had four main focus areas: fertilizers; agriculture loans, tractors, and cotton seeds. It was approved by the ECC in May 2020 and had a bearing on the *Kharif* FY21 season.

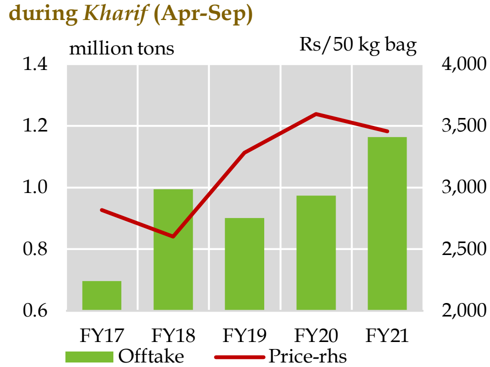
The bulk of the package was earmarked for subsidies on fertilizer purchase. The rationale was that fertilizers account for nearly 10 to 15 percent of the cost of production for major crops, and the subsidy would make this input more affordable for farmers. Enhanced application of fertilizer could, in turn, boost crop yields. The subsidy had a notable impact, as fertilizer prices for urea and DAP fell by 12 percent and 4 percent YoY, respectively, during the *Kharif* season and played a part in increasing their respective offtake (**Figure 2.2a, Figure 2.2b**).[4]

Urea Offtake and Price during *Kharif* (Apr-Sep) **Figure 2.2a**



Source: National Fertilizer Development Centre

DAP Offtake and Price during *Kharif* (Apr-Sep) **Figure 2.2b**



Source: National Fertilizer Development Centre

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[3] Source: ADB (2020). *COVID-19 Impact on Farm Households in Punjab, Pakistan: Analysis of Data from a Cross-Sectional Survey*. ABD Briefs No. 149. Mandaluyong: Asian Development Bank; ADB (2020). *COVID-19 Impact of COVID-19 and Locust Swarms on Farm Households in Sindh, Pakistan: Analysis of Data from a Cross-Sectional Survey*. ABD Briefs No. 149. Mandaluyong: Asian Development Bank.

[4] The proposed subsidy for urea and DAP amounted to Rs 243 and Rs 925 per bag, respectively.

The agriculture package also had a provision for a reduction in the mark-up on agriculture loans, which could potentially drive up agriculture credit. However, while the weighted average lending rate (WALR) on agriculture loans fell subsequently, the disbursement of agriculture credit during Q1-FY21 remained lower than the comparable quarter last year (**Table 2.2**).[5] From a sectoral perspective, the drag emanated from the non-farm sector, as disbursements to the livestock, dairy, and poultry segments declined. This could be reconciled with the Covid related restrictions on marriage halls and restaurants, which continued to suppress the demand for segments like poultry during Q1-FY21.[6,7]

Agriculture Credit Disbursements (Q1) **Table 2.2**

billion Rupees

	FY20	FY21p
Farm sector		
A. Production	103.8	113.9
B. Development	9.3	5.6
Tractor	0.7	0.6
C. Total farm sector (A+B)	113.1	119.5
Non-farm sector		
Livestock/dairy	77.8	71.2
Poultry	64.3	49.5
Other	8.1	14.4
D. Total non-farm sector	150.2	135.1
Total agri (C+D)	263.3	254.7
p=provisional		

Source: State Bank of Pakistan

Meanwhile, within the farm sector credit, disbursement of development loans remained subdued. In particular, disbursements for tractor purchases were lower compared to the same period last year, despite an extension of subsidy on sales tax of locally manufactured tractors for a period of one year. While tractor production and sales rose during Q1-FY21 (as indicated by the LSM and PAMA data), bank financing did not pick up in a commensurate manner. There is a possibility that higher remittance inflows during Q1-FY21 relative to the comparable quarter last year facilitated a greater amount of cash purchases of tractors during the review period. By contrast, production-related borrowing in the farm sector was on the higher side during Q1-FY21 compared to the same period last year, suggesting that better crop outcomes created demand for working capital loans.

Furthermore, up until end-September 2020, the government had budgeted Rs 1.5 billion to tackle the locust situation.[8] Owing to the priority focus and concerted survey and control operations, the impact of locusts on *Kharif* FY21 crop output was limited. Moreover, by October 2020, the locust prone area in Pakistan had largely been cleared of the threat, though the Food and Agriculture Organization (FAO) recommended that surveys be kept ongoing in Cholistan,

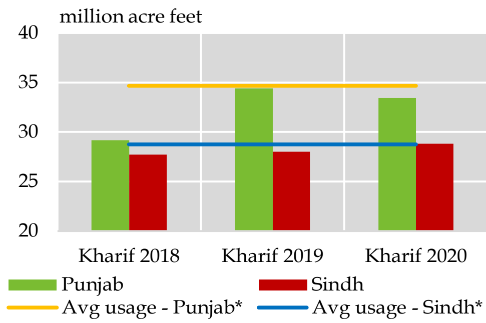
[5] The weighted average lending rate (WALR) for the agriculture sector fell to 11.8 percent by end-June 2020, compared to 13.7 percent as of end-June 2019.

[6] While the government issued guidelines for the reopening of food establishments and restaurants on 8th August, 2020, a number of restrictions – particularly on indoor dining – remained in place. Similarly, marriage halls remained closed till mid-September 2020.

[7] The poultry segment experienced a YoY deflation of 14.5 percent during Q1-FY21, compared to a 44.4 percent inflation during Q1-FY20.

[8] Source: Federal Budget 2020-2021, Details of Demands for Grants and Appropriations, Volume 3, Current Expenditure, Government of Pakistan, Finance Division, Islamabad.

Irrigation Water Releases **Figure 2.3**



* Ten-year average system usage

Source: Indus River System Authority

Tharparkar and Lasbella, and surveillance be continued till at least end-November 2020.[9]

In terms of water availability, irrigation water releases in Sindh were marginally higher compared to the same period last year, and at par with the ten-year *Kharif* season average system usage (**Figure 2.3**). Irrigation water released in Punjab was also broadly in line with the long-term average. However, heavy and untimely rains, especially in Sindh, damaged the cotton crop.

Output

Cotton

Cotton production fell for the third consecutive year, as area under production declined while yields failed to reach targeted levels. Specifically, cotton production declined by 7.7 percent to 8.4 million bales, according to provisional estimates (**Table 2.3**). Recall that, last year, the area dedicated to the crop had grown (by 6.1 percent), but the production had been undermined by low yield. However, in the *Kharif* FY21 season, the prospects of higher cotton production were slim from the outset, given that the area dedicated to the crop, recorded at 2.2 million hectares, is the lowest since FY82 **(**as depicted in **Figure 2.1** earlier).[10]

Cotton Crop Estimates **Table 2.3**

		FY21		Growth (percent)	
	FY20	**Target**	**FY21 P**	**FY20**	**FY21**
Area ('000 hectares)					
Punjab	1,879.6	1,600.0	1,546.0	-0.4	-17.7
Sindh	598.7	640	615	33.6	2.7
Pakistan	2,517.0	2,310.0	2,217.9	6.1	-11.9
Production ('000 bales)					
Punjab	6,306.6	6,000.0	5,300.0	-7.6	-16
Sindh	2,746.0	4,600.0	3,000.0	-6.5	9.2
Pakistan	9,149.0	10,897.5	8,442.7	-7.2	-7.7
Yield (kg/hectares)					
Punjab	570.7	637.8	583.1	-7.2	2.2
Sindh	780.1	1222.5	829.7	-30	6.4
Pakistan	617.8	802.4	647.5	-12.6	4.8

P: provisional

Source: Ministry of National Food Security and Research

[9] Source: 27th Commission for Controlling the Desert Locust in South-West Asia (SWAC)- Technical and Operational Coordination (TOC) Virtual Meeting on Locust Surveillance and Control for Pakistan, held on 12th October, 2020.

[10] Specifically, the area under cotton in FY82 was 2,214.1 thousand hectares, marginally lower than the 2,217.9 thousand hectares registered in FY21.

The area under cotton has witnessed a secular decline in the past decade: it averaged 2.7 million hectares during FY12 to FY21, compared to nearly 3 million hectares between FY92 to FY11. The crop has lost its competitiveness relative to other major crops, in particular sugarcane.[11]

Being a tradable commodity, there is higher competition in the cotton market, which effectively puts a ceiling on its price growth. Meanwhile, sugarcane is generally non-tradable, and the market structure does not allow it to be traded across borders. Moreover, the minimum support price for sugarcane also gives comfort to growers. Therefore, the pricing dynamics have tended to give sugarcane an edge over cotton, which has manifested in the switching of area away from the latter in favor of the former.[12]

In terms of yield, the cotton yield in Sindh in *Kharif* FY21 was affected by severe monsoon rains. The rainfall received by the province during August 2020 was a staggering 363 percent above the normal average for this month, making it the wettest August observed in the past sixty years.[13] Among the more prominent cotton-growing regions, Mirpurkhas and Dadu received 348 mm and 180 mm of rain during August 2020, compared to the normal levels of 76.5 mm and 29.9 mm, respectively. This caused widespread damages to the standing crops in Sindh. Specifically, the rains and flash floods completely damaged around 27 percent of the cotton crop grown in Sindh. At the district level, as much as 80 percent of the crop in Mirpurkhas and Umerkot was affected. In Punjab, also, around 8,034 acres (or 3,251 hectares) of crop area was badly affected by excess rain. [14] As a result, the provisional cotton yield was estimated to be 47.3 percent short of the FY21 target in Sindh, and 9.4 percent shy of the annual target for Punjab.

While heavy rains played an outsized role in depressing the cotton yields during *Kharif* FY21, the yields have been erratic over the past decade on the whole. This can primarily be traced to the gaps in cotton seed quality, which leave the crop susceptible to weather-induced damages and attacks by pests like the pink bollworm and whitefly.[15,16] Thus, research and development of high-yielding varieties of cotton seed, along with improved availability of certified cotton seeds, needs priority focus.

[11] For details, see the SBP Annual Report on The State of Pakistan's Economy for FY20.

[12] The switching towards the water-intensive sugarcane crop appears to be more prominent in Punjab, where groundwater of adequate quality is more widely available in addition to canal water, compared to the relatively saline groundwater available in many districts of Sindh.

[13] Source: Pakistan Meteorological Department (2020). *Pakistan's Monthly Climate Summary, August 2020*. Karachi: Pakistan Meteorological Department

[14] Source: Pakistan Cotton Grower, 2020, Central Cotton Research Institute Multan, Vol.3, No. 3.

[15] Regarding seed quality, anecdotal evidence suggests that the downward relaxation of germination standard, from 70 percent in *Kharif* FY20 to 50 percent in *Kharif* FY21, may have contributed to the relatively low yield during the latest season relative to the annual target.

[16] The government had provided a subsidy on imported PB Ropes to combat pests like the pink bollworm. Even so, some cotton farmers could not afford the technology, and their cropped area fell prey to pink bollworm attacks.

Early Estimates of Sugarcane Crop Performance **Table 2.4**

		FY21		Growth (percent)	
	FY20	Target	FY21P	FY20	FY21
Area ('000 hectares)					
Punjab	643	752.7	776	-9.5	20.7
Sindh	286.1	310	288.8	2.4	1
Pakistan	1,039.3	1,180.60	1,174.2	-5.7	13
Production ('000 tons)					
Punjab	43,346.6	44,906.0	52,528.6	-3.5	21.2
Sindh	17,233.8	19,000.0	17,325.2	3.3	0.5
Pakistan	66,379.6	69,801.5	75,646.7	-1.2	14
Yield (kg/hectare)					
Punjab	67,413.0	59,659.9	67,691.5	6.7	0.4
Sindh	60,239.2	61,290.3	59,982.1	0.9	-0.4
Pakistan	63,867.0	59,123.8	64,426.2	4.8	0.9

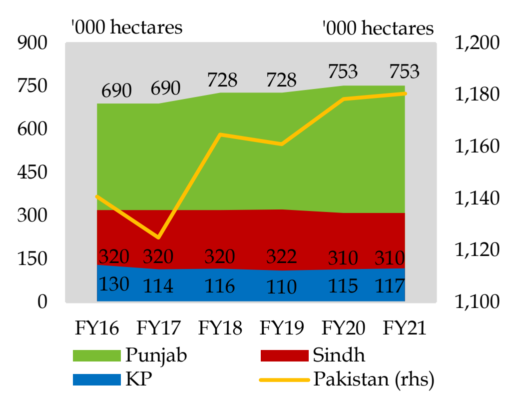
P= provisional

Source: Ministry of National Food Security and Research

Sugarcane

The sugarcane crop experienced an increase in area under cultivation, while yields remained more or less unchanged compared to last year **(Table 2.4**). The crop has generally given attractive returns to growers in the recent past compared especially with the cotton crop; estimates suggest that this relative profitability of sugarcane was maintained in FY21.[17]

Target area for Sugarcane **Figure 2.4**



Source: Ministry of National Food Security & Research

It is worth recalling that back in April 2018, the Federal Committee on Agriculture (FCA) had advised the provinces to develop strategies that encouraged a shift away from sugarcane production towards lower delta crops, with an eye towards mitigating water scarcity. However, sugarcane continued to be a favored crop for growers, contradicting the expected shift. The FCA recommendation can possibly be implemented through targeted area and support price signals (**Figure 2.4**).

[17] From a profitability angle, the grower's *ex-ante* anticipation of better returns from sugarcane this season (reflected in greater area under cultivation) were validated *ex-post*. For Punjab, the profit at farm gate was estimated to be Rs 22,993 per acre for sugarcane, compared to Rs 9,051 per acre for cotton (both estimates are based on weighted average cost of production, for growers paying land rent). Source: Crop Reporting Service, Government of the Punjab.

Rice Crop Performance **Table 2.5**

		FY21		Growth (percent)	
	FY20	Target	FY21^P	FY20	FY21
Area ('000 hectares)					
Punjab	2,029.0	1,900.0	2,441.0	6.6	20.3
Sindh	775.9	800.0	707.7	12.4	-8.8
Pakistan	3,034.0	2,957.0	3,380.80	8	11.4
Production ('000 tons)					
Punjab	4,144.0	4,200.0	4,984.00	4.1	20.3
Sindh	2,576.5	3,000.0	2,493.00	0.2	-3.2
Pakistan	7,414.0	7,990.0	8,184.30	2.9	10.4
Yield (kg/hectare)					
Punjab	2,042.4	2,210.5	2,041.8	-2.3	-0.03
Sindh	3,320.8	3,750	3,522.8	-10.9	6.1
Pakistan	2,443.6	2,702.1	2,420.8	-4.7	-0.9

P= provisional

Source: Ministry of National Food Security and Research

Rice

Building on the previous season, the overall cultivated area for rice grew by 11.4 percent during *Kharif* FY21 (**Table 2.5**). Rising unit prices and upbeat demand for the country's rice in export markets have made the rice crop a profitable investment for growers.

That said, on a provincial basis, there was some decline in the area under the rice crop in Sindh. This may have been a reaction to the last season's unfavorable experience, when above normal temperatures in rice-growing districts like Larkana, Jacobabad, Thatta and Badin during September 2019 contributed to a double-digit decline in yields in Sindh.

2.3 Large Scale Manufacturing

The output of the LSM sector expanded during Q1-FY21 compared to Q4-FY20 and Q1-FY20 (**Table 2.6**). Analyzed in context to the preceding quarter, when the economy was hamstrung by the Covid shock, the recovery in the review period was expected on the back of resumption of production activities. However, compared to Q1-FY20, when the LSM sector was in the middle of a sustained downturn, the performance in Q1-FY21 was noteworthy (**Figure 2.5**).

The blow to the industrial sector was mitigated by well-coordinated fiscal and monetary stimulus. The government announced incentive packages focusing primarily on the construction and export-oriented sectors.[18, 19] In addition, the SBP lowered its policy from 13.25 percent to 7 percent, and initiated several facilitative schemes to speed-up the recovery. While the incentives were largely implemented in the preceding period, the positive impact of these measures became more prominent in Q1-FY21.

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[18] Source: Ministry of Finance (2020). *Monthly Economic Update, April 2020*. Islamabad: Economic Advisor's Wing, Ministry of Finance.

[19] Source: The Tax Laws (Amendment) No. 1 of 2020, Law and Justice Division Letter F.No.1(1)/2020, dated April 19, 2020, Federal Board of Revenue.

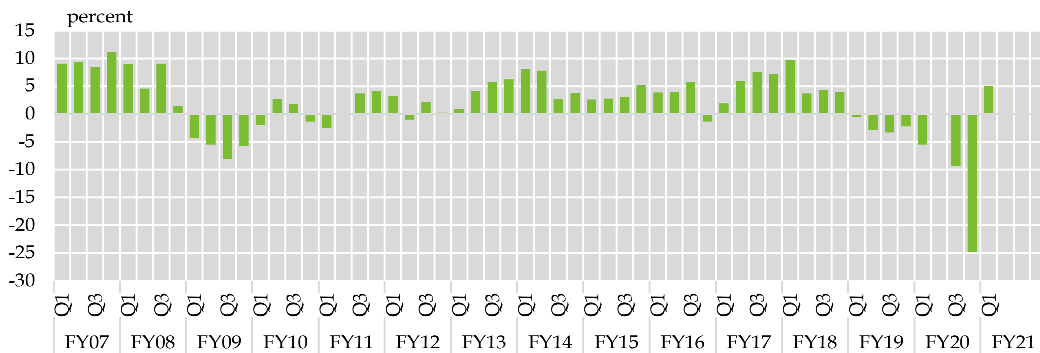
LSM Growth (Q1) **Table 2.6**

percent, YoY

	wt.	Growth					Contribution in growth				
		FY20				FY21	FY20				FY21
		Q1	Q2	Q3	Q4	Q1	Q1	Q2	Q3	Q4	Q1
LSM	**70.3**	**-5.5**	**0.2**	**-9.4**	**-24.8**	**5.0**					
Textile	20.9	0.2	0.5	-8.3	-33.9	2.2	0.0	0.1	-1.9	-9.2	0.6
Cotton yarn	13	0.2	0.0	-9.0	-34.5	0.1	0.0	0.0	-1.4	-6.2	0.0
Cotton cloth	7.2	0.1	0.3	-8.8	-34.3	-0.1	0.0	0.0	-0.6	-2.9	0.0
Jute goods	0.3	-14.8	3.5	37.6	-31.3	10.7	0.0	0.0	0.1	-0.1	0.0
Food	12.4	-9.0	15.8	-7.6	-4.0	13.4	-1.4	2.6	-2.3	-0.6	2.0
Cigarettes	2.1	-34.5	-24.3	-35.2	6.6	31.2	-0.7	-0.5	-0.7	0.1	0.5
Vegetable ghee	1.1	2.0	8.4	6.4	-1.5	-5.6	0.0	0.1	0.1	0.0	-0.1
Cooking oil	2.2	0.0	13.7	14.0	7.3	3.2	0.0	0.5	0.4	0.3	0.1
Soft drinks	0.9	-14.1	-6.5	-10.7	-10.3	7.6	-0.5	-0.1	-0.2	-0.4	0.3
POL	5.5	-14.5	-5.9	-32.0	-27.8	2.7	-1.0	-0.4	-1.7	-1.7	0.2
Steel	5.4	-17.0	-6.8	2.0	-47.1	-8.1	-0.8	-0.3	0.1	-1.9	-0.4
Non-Metallic minerals	5.4	-0.9	6.3	-0.2	-13.6	22.2	-0.1	0.8	0.0	-1.7	2.6
Cement	5.3	-1.4	6.3	0.0	-12.8	22.8	-0.2	0.8	0.0	-1.6	2.7
Automobile	4.6	-34.6	-39.5	-37.7	-70.1	-5.7	-2.8	-2.9	-2.3	-4.3	-0.3
Jeeps and cars	2.8	-38.6	-54.6	-50.4	-85.4	-21.1	-1.7	-2.2	-1.8	-2.5	-0.6
Fertilizer	4.4	15.9	-5.1	7.9	0.4	2.0	0.9	-0.3	0.3	0.0	0.1
Pharmaceutical	3.6	-11.9	-0.7	-3.6	5.6	14.4	-1.0	-0.1	-0.3	0.4	1.1
Paper	2.3	-1.3	16.0	-1.2	-4.2	11.0	-0.1	0.6	0.0	-0.1	0.4
Electronics	2	11.0	-6.1	-34.1	-72.8	-20.4	0.4	-0.2	-1.4	-4.1	-0.9
Chemicals	1.7	4.9	4.7	4.2	-24.1	10.5	0.1	0.1	0.1	-0.5	0.3
Caustic soda	0.4	35.0	15.7	-4.5	-25.8	2.5	0.2	0.1	0.0	-0.1	0.0
Leather products	0.9	6.3	16.0	-2.1	-55.4	-44.5	0.1	0.2	0.0	-0.8	-0.7

Source: Pakistan Bureau of Statistics

LSM Growth YoY **Figure 2.5**



Source: Pakistan Bureau of Statistics

The industry-wise analysis of the LSM sector suggests that cement and food processing segments were the key drivers of growth during Q1-FY21. On the other hand, major drag came from the electronics and leather industries.

Petroleum

The petroleum industry's production expanded by 2.7 percent during Q1-FY21 against a decline of 14.5 percent during Q1-FY20. The increase in output of petrol and diesel led to an overall improvement, which more than compensated for the decline in the production of other products, such as jet fuel. A couple of factors also facilitated growth in petrol and diesel production. Resumption of activities in the transport sector drove public and private sector demand for petroleum products. Stricter border controls also deterred illicit smuggling of diesel to Pakistan which led to increase in demand for products produced locally.[20]

The output of the high sulfur furnace oil (HSFO) remained at almost the same level despite an increase in electricity generated from HSFO-based power plants. The higher demand for the commodity was met primarily by imports. In the past few years, the government had focused on reducing its reliance on HSFO for electricity generation in favor of cheaper alternatives, such as gas.

In addition to restrictions on HSFO, the government has now set its target to move to the *Euro-5* standard compliant fuels. Whereas it is a step in the right direction, there are certain ramifications of this measure on the petroleum and automobile industries (**Box 2.1**).

Box 2.1: Introduction of Ultra-Low-Sulfur-Fuel (ULSF) and its Implications for Domestic Automotive and Petroleum Industries

The decision by the government to move to a new emission standard is expected to affect domestic automobile and crude oil refining industries in the short- to medium-term, whereas in the long-term the measure will improve urban air quality and modernize these industries. This transition is in line with the steps being taken around the world to cut down air pollution caused by certain gases and airborne particles.[21] Air pollution is one of the major causes of breathing, cardiovascular, mental, and reproductive health issues around the world and is responsible for around 7 million deaths worldwide, with the majority of these deaths reported in Asia. Air pollution accounted for 9 percent of deaths in Pakistan in 2017.[22] Moreover, according to IQAir, Pakistan was one of the most polluted country in the world in 2019.[23]

The advanced economies are dealing with air pollution in urban areas through regulatory measures, such as vehicle emission and fuel quality standards, since road transport is one of the major sources of air pollution.[24] For the vehicle emissions, *Euro* has become the global benchmark. At present, countries are

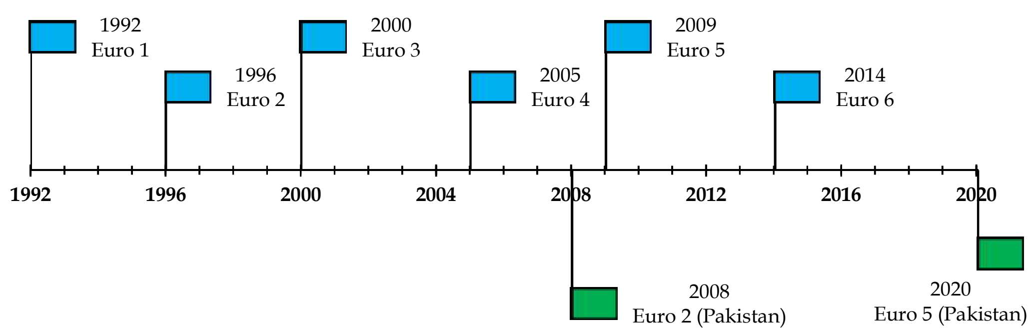
[20] Source: Federal Board of Revenue (source: fbr.gov.pk/pr/smuggled-items-worth-3800-millionconfiscated/152389).
[21] Source: National Aeronautics and Space Administration (climatekids.nasa.gov/air-pollution/).
[22] Source: World Health Organization.
[23] Source: iqair.com/us/world-most-polluted-countries.
[24] EU, US, China, India, Japan and South Korea consume more than 80 percent of global oil exports.

moving towards the *Euro-6* standard that was introduced in 2014. The fuel standard is also a necessary component of the global drive to reduce pollution. Sulfur content in petroleum products, a major health hazard, has witnessed a sharp reduction over the years due to improvements in the refining technology. Driven by regulatory measures in advanced economies, almost all the major oil exporting countries have switched to ultra-low-sulfur fuels (ULSFs). The interplay between major oil importers and exporters meant that the developing economies had to adapt to these standards as well. In Pakistan also, the government has outlined its plan to shift to *Euro-5* compliant fuels in FY21.

At the global level, the requirements on emissions and fuel quality had been based on the available technology and institutional capacity at the time of implementation. On the technology side, these industries were given realistic timelines to comply with the new parameters. Concurrently, the respective governments set up enforcement mechanisms to ensure adherence to the standards. The transition from one standard to the other was therefore carefully managed. From this perspective, Pakistan's jump from *Euro-2* standards to *Euro-5* may seem rather abrupt and is expected to create some frictions in the local automobile and petroleum industries. As the country lagged behind other nations for a long time with regards to transitioning towards improved standards, a relatively longer adjustment period may now be required to achieve full compliance (see **Figure 2.1.1**). That said, a few other countries have also leapfrogged to higher standards (for instance, India has jumped from *Euro-4* to *Euro-6*).

The implications of this measure on the automobile industry in Pakistan are straightforward. The assemblers would be required to install specialized equipment to meet the emission standards. These emission control components are standard in countries that have upgraded to *Euro-5/6* standards. However, it may be noticed that equipping domestic cars with *Euro-5* compliant parts is likely to increase the cost and, subsequently, the retail price of the vehicles. Another potential bottleneck is the rerouting of imports away from non-compliant countries such as Thailand and Indonesia and towards compliant countries like Japan (*Euro-6* equivalent), which may further escalate costs.[25]

Timeline - Euro Emission Standards and Adoption in Pakistan **Figure 2.1.1**



Source: DieselNet

[25] Thailand and Indonesia, still following *Euro-4*, account for around 40 percent of Pakistan's CKD vehicle imports. Source: Pakistan Bureau of Statistics.

The impact on the petroleum refining industry is expected to be more acute. The largely outdated petroleum industry was already feeling the strain in the face of an earlier measure that had curtailed demand for high-sulfur-furnace-oil (HSFO) which made up around a quarter of the industry's output (**Table 2.1.1**). The latest regulatory decision to move to *Euro-5* compliant fuel would make their task even more daunting, further necessitating the need to upgrade. It will also be a massive financial undertaking. For instance, the planned upgrade of the 47,000-bpd plant of Pakistan Refinery Limited to produce *Euro-2* compliant fuel was expected to cost around US$ 1 billion.[26] Compliance with *Euro-5* can possibly cost even more.

Refinery Production by Product 2019-20 **Table 2.1.1**

percent of total

	Pakistan	US	EU
Petrol	22	49	18
Diesel	37	25	40
HSFO	20	2	13*
Others	21	24	29

*Ultra-low sulfur furnace oil

Source: PBS, EIA, OECD

On the flip side, for a developing country coping with high public and foreign debt, the challenges in the implementation of the standards are substantial given the lack of resources. In particular, the lack of institutional capacity can hamper the efforts of the state for a trouble-free convergence to Euro-5 standards.[27] Necessary incentives can be provided to the automobile and the petroleum industry for a smooth transition. Here, Pakistan can learn from experiences of other countries that have made that transition. For instance, differential tax structure was imposed at pumps in Hong Kong, the United Kingdom and Germany. Meanwhile, the United States and Japan allowed tax incentives for refiners and, in some regions, also provided direct subsidies.28 Another option is to give tax-breaks to refineries and auto-assemblers that comply with new standards. A well-managed switchover may spur investment, create employment and build capacities in both the industries.

Automobile

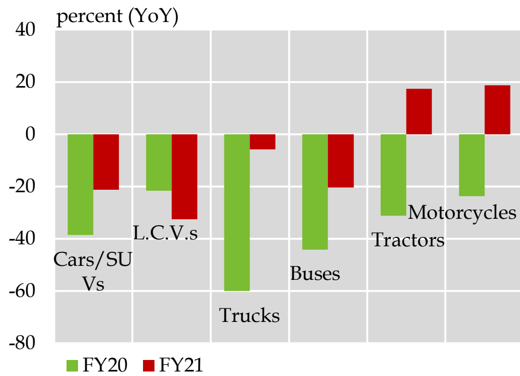
Production activities in the automobile sector contracted by 5.7 percent in Q1-FY21 compared to the same period last year. The car and jeep segment, in particular the compact car segment, was again the major contributor towards this below-par performance. On the contrary, tractors and motorcycles production expanded relative to the same period last year and offset some of the drag from the other categories. Overall, the severity of contraction markedly decreased during Q1-FY21 (**Figure 2.6a, Figure 2.6b**).

The output of car and jeep segment declined to its lowest level in the review period since FY09 with exception of Covid-hit-Q4-FY20. Within this segment, there were contrasting results for compact hatchbacks and for sedan and jeeps. The former witnessed a sharp contraction, whereas the latter two observed production growth due to robust demand for new variants.

The downtrend in the compact car segment may be attributed to some demand-side factors; such as lack of demand from ride hailing services for hatchbacks in the

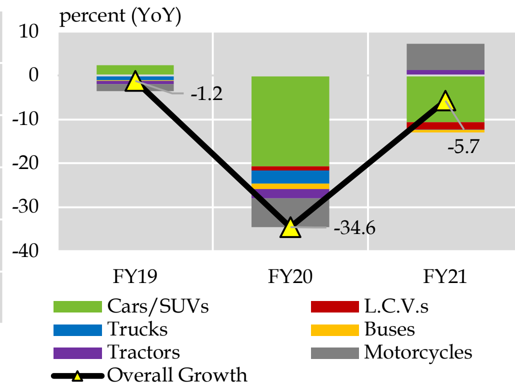
[26] Source: Radio Pakistan (radio.gov.pk/05-11-2019/govt-to-upgrade-pakistan-refinery-limited-with-1b-cost)
[27] Source: Timilsina, G. R. and H.B. Dulal (2009). "Regulatory Instruments to Control Environmental Transport Sector,"*European Transport \ trasporti europei, 41:80-112.*
[28] Source: The International Council for Clean Transportation (theicct.org/sites/default/files/publications/ICCT_LSF-fiscalpolicy_June2013.pdf).

Growth in Auto Categories in Q1 **Figure 2.6a**



Source: Pakistan Bureau of Statistics

Growth in Auto Sector & Contribution in Growth in Q1 **Figure 2.6b**



ongoing Covid pandemic. The ride hailing services across the globe are suffering due to a downward shift in demand owing to the mobility restrictions.[29,30]

Contrary to the hatchbacks, significant growth in the sedans category was recorded in Q1-FY21 compared to same period last year, which can be attributed to relatively lower impact of Covid on the demand for sedans from the higher-income group. In particular, robust growth in output of new variants of the category was witnessed during Q1-FY21. The sedan segment was further aided by the low interest rate environment[31] and stable prices, which enhanced the ability of the consumers to buy these cars. However, higher production of sedans could not offset the sharp decline in hatchbacks which meant that overall car production declined during Q1-FY21.

The uncertainty caused by the Covid possibly resulted in a lower demand for commercial vehicles. As a result, production went down by 32.6 percent during Q1-FY21 compared to 28.3 percent contraction observed during the same period last year.

Meanwhile, robust sales in motorcycles and tractors segments reflects that the rural activities remained largely unaffected from the Covid crisis. The increase in tractor sales despite lower credit offtake in that segment can be explained by either lower liquidity constraints in the rural economy or pent-up demand, or both. Meanwhile, the increase in remittance inflows may have facilitated the rise in the share of cash transactions for tractors.

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[29] Ride hailing services suffered a dip in demand across the globe. One of the major players in the Industry, Uber, has reported the number of trips declining by 35 percent YoY during Q1-FY21.
[30] Uber has reduced its global workforce by 25 percent due to the Covid (Source: uber.com/en-PK/newsroom/ubers-2020-people-and-culture-report/).
[31] Consumer financing for car purchases rose by Rs 21.3 billion during Q1-FY21 in stark contrast to the net retirements of Rs 2 billion during the same period last year.

Construction-allied Industry

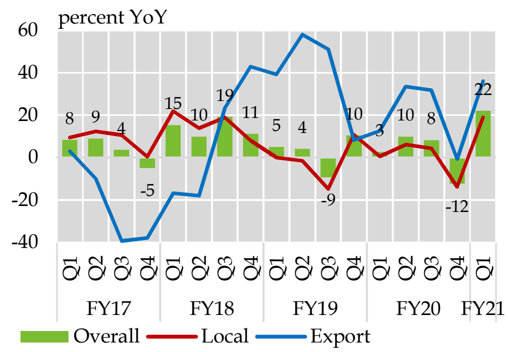
The government had announced an incentive package for the construction industry when some of the mobility restrictions under the lockdowns were lifted and it seems to have kick-started activities in the private sector. Moreover, the construction sector received a boost from the rise in public sector development spending. Specifically, development expenditures rose sharply by 15.4 percent during Q1-FY21 on a YoY basis, with spending on large infrastructure projects such as dams and roads in particular increasing the demand for cement.

Cement

Cement output in Q1-FY21 rose to an all-time high, increasing by 22.8 percent during Q1-FY21 in contrast to a contraction of 1.4 percent recorded during the same period last year. Large-scale infrastructure projects such as Diamer-Bhasha Dam and Burhan-Dera Ismail Khan Motorway gathered pace during Q1-FY21, which increased the demand for cement from the public sector (**Chapter 4**).

In addition to domestic demand, exports of cement registered a decent growth during Q1-FY21 vis-à-vis Q1-FY20 (**Figure 2.7**), contributing more than a quarter to the overall growth during the period. Encouragingly, exports have gained traction in non-traditional destinations such as Bangladesh, China and Sri Lanka, which more than offset the decline in demand from neighboring countries of India and Afghanistan.

Cement Dispatches-Local vs Exports **Figure 2.7**



Source: All Pakistan Cement Manufacturers Association

Steel

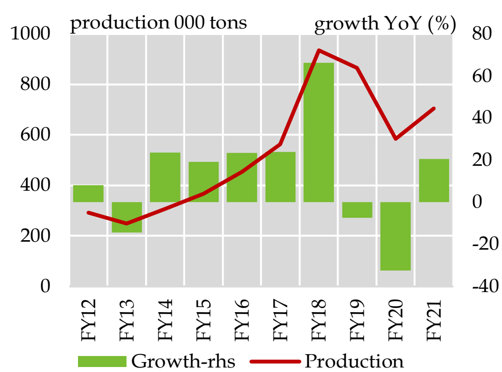
Production in the steel industry declined by 8.1 percent in Q1-FY21 compared to 17.0 percent drop witnessed during the same period last year. While the performance may seem in contrast to that of the cement industry, disaggregate analysis reveals that output of long steel products that are largely used in the construction industry started to show growth during Q1-FY21. In fact, billets production recorded an impressive YoY growth of 26.0 percent during the period (**Figure 2.8a, Figure 2.8b**).

On the other hand, demand for flat steel products is reflective of developments in the automobile and appliances sectors. As the demand from these sectors waned, the flat steel producers saw their capacity utilization levels drop and profit margins squeeze. The impact of lower demand for flat products more than offset the growth witnessed on the long-steel side and resultantly the overall impact was contraction in output.

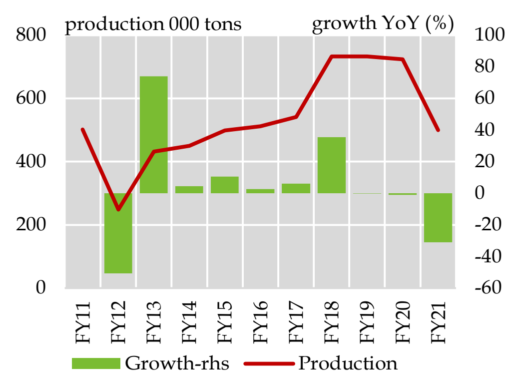
Fertilizer

The fertilizer sector continued to post positive results, with output growing by 2.0 percent in Q1-FY21 on a YoY basis; however, this performance pales in comparison to impressive growth (15.9 percent) recorded

Long Steel Production **Figure 2.8a**

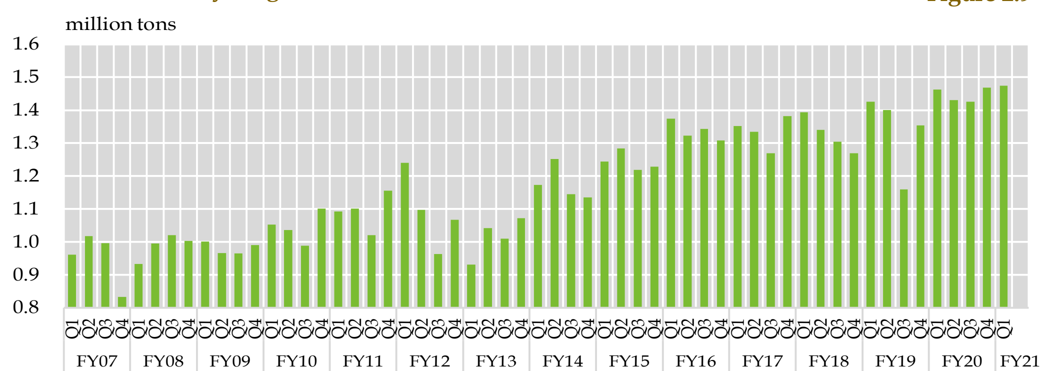


Flat Steel Production **Figure 2.8b**



Source: Pakistan Bureau of Statistics

Urea Production by Large Units **Figure 2.9**



Source: National Fertilizer Development Center

during the same period last year. National Fertilizer Development Center (NFDC) records show that the growth during Q1-FY20 was broad-based, as contributions from both urea and non-urea producing units had increased. In Q1-FY21, however, the urea output declined by 4.2 percent, but was offset by an impressive growth of 19.7 percent in the production of non-urea fertilizer products.

The urea-processing segment in Pakistan is characterized by two types of manufacturing units; large-scale and small-scale. At operational capacity, the production of large-scale units caters to almost 90 percent of the per annum local demand of roughly 6 million tons, whereas the supply from the small-scale units meets the rest. In Q1-FY21, the output of larger units rose by 2.1 percent compared to a decline of 1.3 percent during the same period last year. Incidentally, it was the highest production in any quarter since FY05 (**Figure 2.9**). Financial reports for Q1-FY21 of the large-scale producers point to an enhanced operational efficiency of the plants that resulted in increased output.[32]

On the other hand, small-scale urea producing units remained largely shut during the month of July 2020. In the remaining two months of Q1-FY21, the resumption of gas supplies to these plants kickstarted production activities. Recall that in Q1-FY20, smaller units remained largely operational throughout the period. In overall terms, the impact of significantly lower production in smaller capacity units outweighed the slight increase in production of larger units.

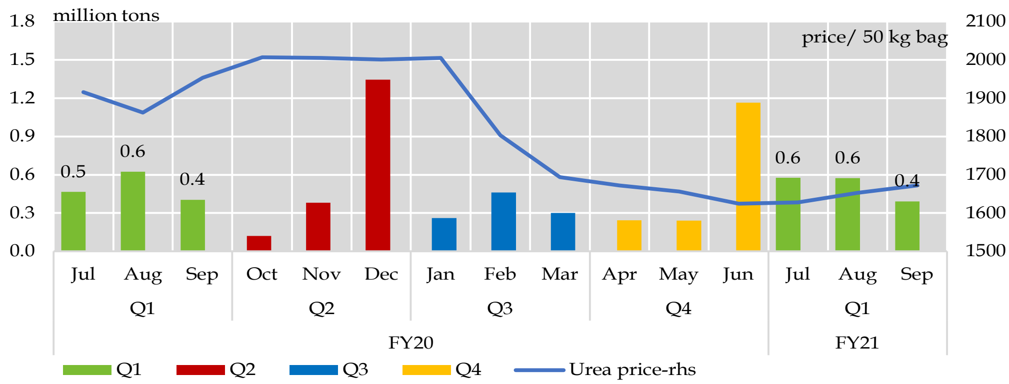
During Q1-FY21, the prices were lower than last year which led to an increased offtake of both urea and DAP fertilizers (**Figure 2.10**). However, the prices started to inch up as the quarter progressed, as uncertainty with regards to payment of Gas Infrastructure Development Cess (GIDC) and its modalities started to affect the market.

Textile

The output of the textile sector increased by 2.2 percent in Q1-FY21 compared to a marginal growth of 0.2 percent during the same period last year. This growth was largely driven by the increase in production of woolen products which can be linked to projections of early onset of winter season by international agencies that prompted millers to start production early.[33] Meanwhile, the cotton-based production of yarn and cloth (having a combined weight of 96.3 percent in textile industry within the LSM index) remained subdued.

The lackluster performance of the cotton textile industry can be attributed to a couple of factors. First, the local raw cotton, which serves as an input for the upstream cotton textile industry, witnessed a below-par harvest. Lower availability of the raw material, in turn, necessitated imports of the commodity to the tune of US$ 208 million,

Urea Offtake and Price **Figure 2.10**



Source: National Fertilizer Development Center

[32] Sources: (1) Engro Fertilizers, Third Quarter Report 2020; (2) Fauji Fertilizer Company Limited, Financial Statements, Third Quarter, September 30, 2020.
[33] Sources: Weather stations issued La Nina watch, which is associated with cooler weather around the globe (1) climate.gov/news-features/blogs/enso/july-2020-enso-update-la-nina-watch (2) iri.columbia.edu/news/july-climate-briefing-la-nina-watch-issued

which was the highest first-quarter import-bill since FY08. Increased reliance on imported cotton also raised costs for the export-oriented industry. The second factor that hampered the growth of cotton textile production was the low international demand for textile products. The exports grew by 2.9 percent in value terms on the back of better prices fetched by textile products, as the demand for cotton apparel has not picked up in major destinations in Europe (**Chapter 5**).

Food

Compared to a decline of 9 percent in Q1-FY20, production activities in the food processing industry rose sharply by 13.4 percent in Q1-FY21. This can be primarily attributed to a sharp increase in the production of tobacco and grain milling industries.[34]

The production of tobacco industry expanded by 31.2 percent compared to a contraction of 34.5 percent last year. The government decided to keep last year's duty structure intact, which was to incentivize the production in the formal industry. In addition, the government intensified its drive against illicit and counterfeit tobacco products by enhancing the monitoring mechanism.[35] These measures helped prop up production in the tobacco industry as demand shifted to locally produced tobacco products (**Chapter 4**).

That said, the duty structure is still incentivizing consumption of informal and illicit variants. A recent study by the Social Policy and Development Centre (SPDC) on the tobacco use in Pakistan states that around 45 percent of households in the country spend around 3 percent of their monthly income on tobacco. Furthermore, the illicit and counterfeit products, which account for around 40 percent of the market share, have an adverse impact on revenue collections. Therefore, there are potential gains for the formal industry and the government if the share of illegal products is reduced.[36]

2.4 Services

Preliminary indicators of the services sectors point to a recovery during Q1-FY21 compared to the same period last year. Growth in the commodity-producing sector, coupled with an increase in imports, suggest that activity in services sector, in particular the wholesale and retail trade segment, picked up during the quarter (**Table 2.7**).

Fast-moving consumer goods (FMCG) recorded a significant growth in Q1-FY21 compared to Q4-FY20, and more importantly against Q1-FY20, which can be traced to pent-up demand. Moreover, anecdotal evidence suggests that strong demand for health and hygiene related products such as sanitizers, soaps and cleansers also played a role in high demand for FMCG.

[34] Increase in wheat production is due to increase in the number of reporting units in the LSM survey.
[35] Source: Federal Board of Revenue - various press releases (1) FBR Seizes Non-Duty Paid Cigarettes - September 17, 2020 (2) Huge Quantity of Counterfeit Cigarettes Seized by I&I-Inland Revenue Peshawar Directorate - September 15, 2020 (3) Smuggled Items worth 3800 Million Confiscated In July - July 30, 2020.
[36] Source: Social Policy and Development Centre (2020). *The Impact of Tobacco Use on Household Consumption Patterns in Pakistan.* Karachi: Social Policy and Development Centre.

Selected Services Sector Indicators **Table 2.7**

	FY20		FY21
	Q1	Q4	Q1
Wholesale and Retail Trade (18.2%)			
Sectoral credit off take*-flow (billion Rs)	-43.8	-0.8	17.8
Petroleum products[1]	0.3	-3.5	17.6
Construction materials[2]	-27.1	-0.1	-0.05
Other	-16.9	2.8	0.25
Imports (billion US$) [a]	11.2	9.8	11.3
LSM (YoY growth)	-5.5	-24.8	5.0
FMCG sales (YoY growth)	1.5	-0.1	17.1
Agriculture credit (disbursements – Rs bln)	263.3	302.5	254.7
Transport, Storage and Communication (12.3%)			
POL sales to transport sector (million MT)	3.4	3.7	3.7
o/w Road Transport	3.3	3.7	3.6
Railways	0.04	0.02	0.03
Commercial vehicle sales (units)	5,000	2,949	6,618
Cellular teledensity (%)	76.8	78.8	79.6^
Broadband users (million)	74	83.1	87^
Finance and Insurance (3.6%)			
Assets (billion Rs)*	21,655	23,705	23,808
Deposits (billion Rs)*	14,945	17,404	17,543
ROA (percent)	0.8	1.1	1.1
ROE (percent)	10.8	14.6	14.8
Profit after tax (billion Rs)	37.3	80	69
Infection ratio	8.9	9.7	9.9
General Government Services (8.6%)			
Expenses on general govt & defense** (billion Rs.)	1,009.3	1,925	1,205

Note: Values in brackets are sectoral shares in GDP, as of FY20.
[1]Solid, liquid, gaseous fuels and related products [2] Construction materials, hardware, plumbing and heating equipment and supplies
* Stocks, as of end-September 2020 **Only federal government ^as of August 2020.
Source: SBP, [a] PBS, OCAC, PAMA, PTA and MoF

Increase in demand for credit from the services industry also suggests recovery in the sector during the review period. Credit offtake witnessed a rise of Rs 17.8 billion compared to net retirements of Rs 43.8 billion during Q1-FY20. The borrowing was largely driven by petroleum products traders. The oil marketing companies (OMCs) borrowed money to meet the rising fuel demand, as economic recovery started to gain momentum following the lifting of Covid-related mobility and production restrictions (**Chapter 3**).

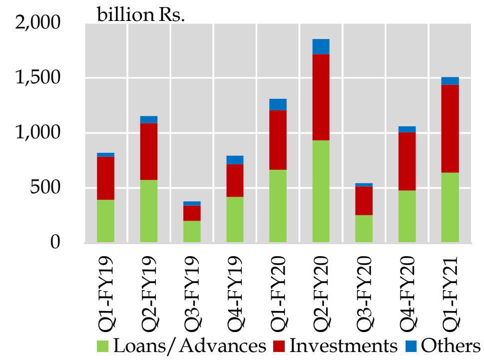
The *transport, storage and communication* segment indicators also showed improvement during Q1-FY21 (**Table 2.7**). The transport sector gained traction with rise in inter-city and inter-provincial travelling and resumption of tourism services after Covid-induced restrictions were lifted. In addition, the increase in sales of commercial vehicles also indicated an uptick in the transport sector.

Meanwhile, in the communication segment, demand for mobile phones and internet services remained strong and was driven by remote-working and online-education arrangements. Consequently, there was a marked increase in cellular teledensity and in the numbers of broadband users in the country. Moreover, a notable rise in the import of cell phones was witnessed during Q1-FY21.[37] This increase can be traced back to reduction of sales tax and advance tax on import of low-end mobile phones and pent-up demand from the lockdown during the previous quarter (**Chapter 5**).

[37] In Q1-FY21, import of cell phones increased by 83.2 percent compared to the corresponding period of last year.

Within *finance and insurance,* the performance of the banking sector showed significant improvement during Q1-FY21. The profit after tax increased to Rs.69 billion, up from Rs.37.3 billion recorded during the same period last year. The profitability indicators, such as return on assets (ROA) and the return on equity (ROE), also improved over the same period (**Table 2.6**). The growth in bank's profits can be traced to higher net interest income mainly from investments. Specifically, the amount of scheduled bank's investments increased to Rs.797.4 billion during Q1-FY21 compared to Rs.541 billion recorded during the same period last year (**Figure 2.11**).

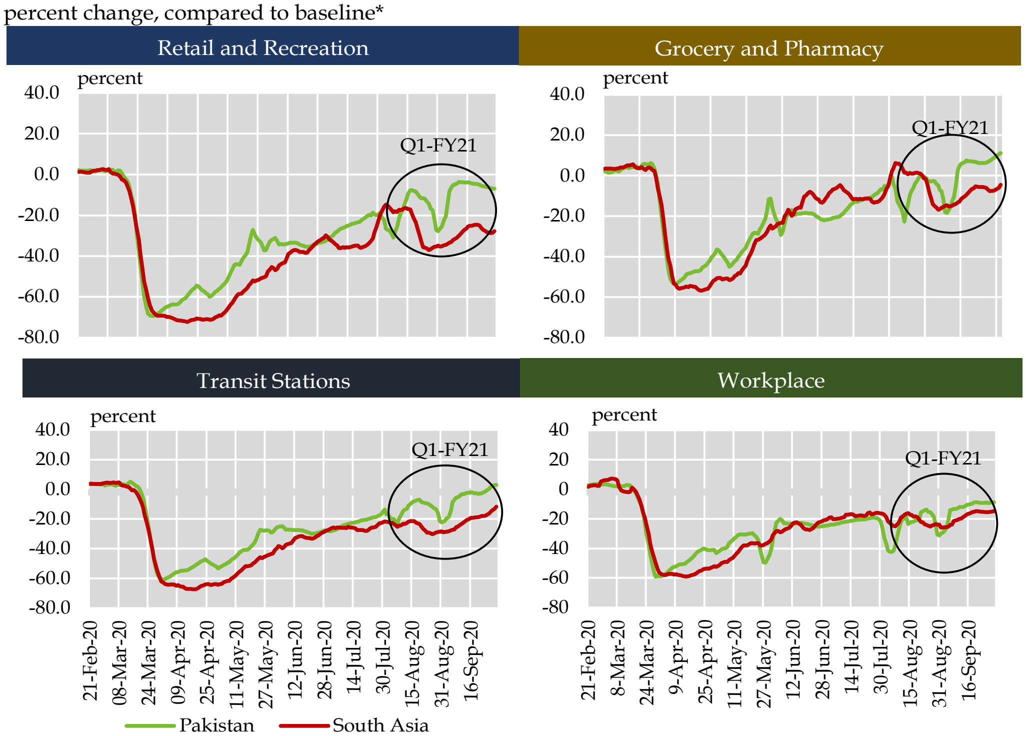
Break-up of Mark-up Earned of Scheduled Banks **Figure 2.11**



Source: State Bank of Pakistan

Google Mobility Changes (7-Days MA): Pakistan vis-a-vis South Asia **Figure 2.12**

percent change, compared to baseline*



*The baseline (pre-Covid) is the median value for the 5- week period (Jan 3–Feb 6, 2020). The negative value represent acitvity is down while positive value represent activity is up from the baseline.

Source: Covid-19 Community Mobility Report

In addition to these indicators, the pickup in services sector activities is evident from the Google mobility data. This dataset covers four segments that are closely associated with the services sector, namely retail and recreation, grocery and pharmacy, transit stations and workplace activities. Analysis of the data shows that in the aftermath of Covid-related restrictions, activities in these sectors had fallen sharply. By the end of March 2020, retail and recreation, grocery and pharmacy, transit stations and workplace declined by 68 percent, 53 percent, 60 percent and 62 percent, respectively, from their baseline (pre-Covid) in Pakistan. In fact, the other South Asian economies excluding Pakistan witnessed a decline of 69 percent in retail and recreation, 57 percent in grocery and pharmacy, 66 percent in transit stations and 63 percent in workplace from the baseline position (**Figure 2.12**).[38] However, as the governments gradually eased the mobility restrictions, the activities started to pick up in all the indicators.

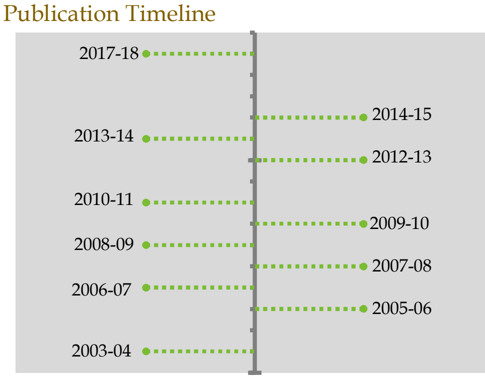
Along with the ease in restrictions, the government authorities also introduced various incentive packages for industries such as construction and small and medium enterprises (SMEs), which aided recovery in the services sector. Cross-country analysis of these indicators in Q1-FY21 highlights that the pace of recovery in Pakistan was higher compared to the rest of South Asia (**Figure 2.12)**. In fact, in Pakistan, visits to grocery stores and pharmacy and transit stations were up 12 percent and 3 percent, respectively, from the baseline position compared to decline of 3 percent and 8 percent, respectively, in South Asia.

2.5 Labor Market

Employment is one of the key indicators of an economy's performance. Therefore, it is important to understand the dynamics of the labor market where various changes in employment, due to structural shifts or different shocks, can be captured. In Pakistan, besides the fact that there are 1.3 million new entrants in the domestic labor force every year, [39] its labor market has had to deal with several shocks, including the recent Covid-related lockdowns.

Labore Force Survery Publication Timeline

Figure 2.13



Source: Pakistan Bureau of Statistics

[38] For the analysis in this section, the 'South Asia' category excludes Pakistan, Bhutan and Maldives. Comparable data for Bhutan and Maldives was not available, whereas date for Pakistan was deliberately excluded to facilitate comparison with the rest of South Asian countries.
[39] Source: World Bank (2018). *South Asia Economic Focus Spring 2018: Jobless Growth?*. Washington DC: World Bank.

However, the analysis of the domestic labor market is challenging due to the limited availability of periodic datasets. For instance, the primary source of information on the labor market for Pakistan is the Labor Force Survey (LFS) which was last published for 2017-18 (**Figure 2.13**).[40] Nonetheless, some useful alternative sources can be utilized to analyze the labor market in Pakistan such as the monthly surveys of industrial performance and employment conducted by provincial statistical bureaus, the employment index from the SBP's Business Confidence Survey, and CPI wage rate data (**Box 2.2**).

Box 2.2: Collating Labor Market Data Sources for Pakistan

To gauge the performance of the labor market key insights can be derived from the Labor Force Survey (LFS). The survey is published by the Pakistan Bureau of Statistics and provides details of socio-demographics, employment status, provincial and sector-wise distribution of the labor market. According to the survey, the agriculture sector contributes 38.5 percent in total employment, followed by service and industry with 37.8 percent and 23.7 percent share, respectively **(Table 2.2.1)**. Note that the services sector makes up the major share of total GDP, while its share in employment is nearly equal to that of agriculture. The LFS also includes data on wages and information on unemployed and employed in the country. However, due to lag in publication, with the latest edition published in 2017-18, it does not cover the current developments in the labor market.

To fill the gaps left by LFS and understand the ongoing trends in the labor market the "Monthly Survey of Industrial Production and Employment", published by the Punjab Bureau of Statistics (BoS) and Sindh

Sector-wise Distribution of Employment **Table 2.2.1**

	GDP Share 2020[41]	Employment Share 2018[42]	Indicators of Employment Trends
Agriculture	19.3	38.5	(1) Labor Force Survey – Pakistan Bureau of Statistics
Industry	19.3	23.7	(1) Labor Force Survey – Pakistan Bureau of Statistics (2) Survey of Monthly Industrial Production and Employment by Punjab and Sindh Bureau of Statistics (3) Construction sector wages from CPI – Pakistan Bureau of Statistics (4) State Bank of Pakistan's Business Confidence Survey
Services	61.4	37.8	(1) Labor Force Survey – Pakistan Bureau of Statistics (2) State Bank of Pakistan's Business Confidence Survey

[40] LFS was published quarterly for 2010-11 and 2012-13

[41] Source: Ministry of Finance (2020). *Pakistan Economic Survey of Pakistan 2019-20*. Islamabad: Ministry of Finance

[42] Source: Pakistan Bureau of Statistics (2019). *Labour Force Survey 2017-18*. Islamabad: Pakistan Bureau of Statistics.

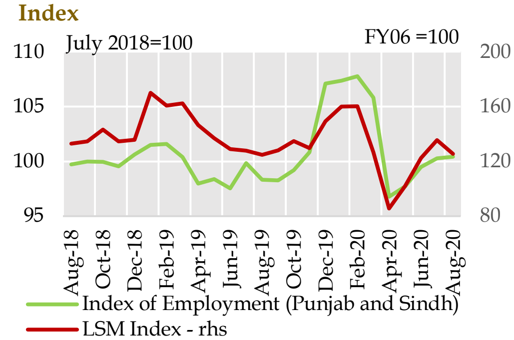
BoS is used.[43] Both provinces can serve as a good proxy to analyze the national trends since they collectively account for 84 percent of the total labor force[44] and 84.1 percent of the total GDP.[45],[46] Punjab BoS collects data from 1,900 industrial units of 45 major industries and Sindh BoS collects data from 535 units of 22 industries. These publications contain pertinent information about workers employed across the industrial sectors. Overall, the industrial sector employs around 24 percent of the labor force, while its share in GDP is around 19.3 percent (**Table 2.2.1**).

Another useful proxy to gauge the recent trends in the labor market is the State Bank of Pakistan's Business Confidence Survey (BCS). The BCS is a bi-monthly telephonic survey in which employers from a sample of 1000 registered firms are asked about their perceptions of the economy, including employment.[47] One advantage of using the BCS-based index is that it is available separately for industrial and services sector in addition to the overall index. A separate metric of the services sector is relevant since the sector contributes more than 60 percent to GDP and employs 38.6 percent of the labor force (**Table 2.2.1)**.

The monthly Consumer Price Index (CPI) data released by the Pakistan Bureau of Statistics also contains information on the wages of the construction related unskilled and skilled workers (painters, carpenters, masons, plumbers). The survey is conducted every month and covers 35 urban and 27 rural centers.

The employment data for the provinces of Punjab and Sindh suggests that there was an improvement in the manufacturing sector during the Jul-Aug FY21 period when compared to peak-restriction period of mid-March 2020 to April 2020. Note that increase in employment index in the post-lockdown period is in tune with the recovery observed in LSM (**Figure 2.14**). The gradual ease in mobility restrictions since then explains the increase in employment in the industrial sector in these provinces. During the initial phase of the lockdowns, as much as 10 percent of the industrial workers lost their jobs. Gradual ease in restrictions in the

Combined Sindh and Punjab Industrial Employment and LSM Index **Figure 2.14**



Source: Bureau of Statistics, Punjab and Bureau of Statistics, Sindh

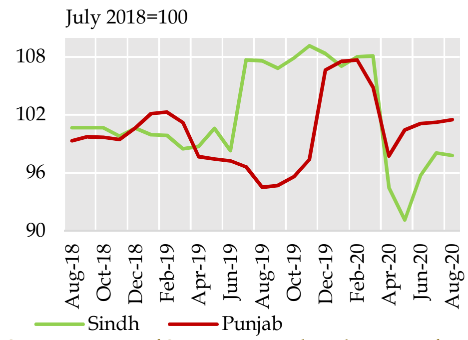
[43] Khyber Pakhtunkhwa Bureau of Statistics also publishes Monthly Survey of Industrial Production but the relevant and latest publications for developments in Q1-FY21 were not available.
[44] Source: Pakistan Bureau of Statistics (2019)
[45] Share of Punjab in GDP was estimated at 54.2 percent (Source: Punjab Growth Strategy 2023, Planning and Development Board, 2018). Share of Sindh in GDP was reported to be 28 percent. Source: Planning and Development Board (2018). *Punjab Growth Strategy 2023.* Lahore: Planning and Development Board. Source: World Bank (2017). *Sindh Public Expenditure Review.* Washington DC: World Bank.
[46] Pakistan Bureau of Statistics (2019).
[47] Questions ask employers, inter alia, about their perception about employment levels in the past 6-months and the expected employment in the next 6-months. Based on the responses, an index reveals positivity in job creation if it is above 50 and pessimism if it is below that mark. For more information visit: sbp.org.pk/research/BCS.asp

following months allowed some recovery; however, the industrial labor market had been unable to regain its pre-Covid level by end-August 2020.

In particular, the province-wise data suggests that job losses in the manufacturing sector in Sindh were higher and the pace of recovery was also slower (**Figure 2.15**). Higher job losses in Sindh can possibly be linked to heavy monsoon downpour and subsequent flooding especially during August 2020 in the industrial hub of Karachi.[48]

From a sectoral perspective, although there were job losses across the board during the peak Covid period, they were more noticeable in sugar and leather industries (**Figure 2.16**).[49] Compared to February 2020 levels, 23.5 percent of the workers lost their jobs during the lockdown period in the sugar industry. Even after the lockdown was lifted, the sugar industry continued to post job losses. The leather industry also saw employments levels drop during the lockdown period; however, unlike sugar, jobs in the leather industry started to inch up in post-lockdown scenario. As the restrictions were gradually eased, a few industries started to hire more workers. For instance, job opportunities in cement and textile industry rose above the pre-Covid levels by August 2020. The positive developments are consistent with growth in output of these industries (**Table 2.6**); output of the cement and textile sector grew by 22.8 and 2.1 percent in Q1-FY21, compared to

Sindh and Punjab Industrial Employment **Figure 2.15**



Source: Bureau of Statistics, Punjab and Bureau of Statistics, Sindh

Employment in Industrial Sector **Figure 2.16**

*Compared to February 2020 level of employment
Source: Bureau of Statistics Punjab, Bureau of Statistics Sindh

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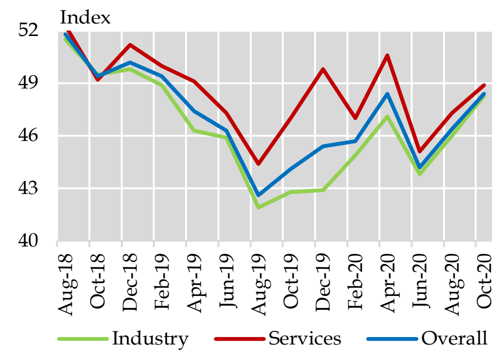
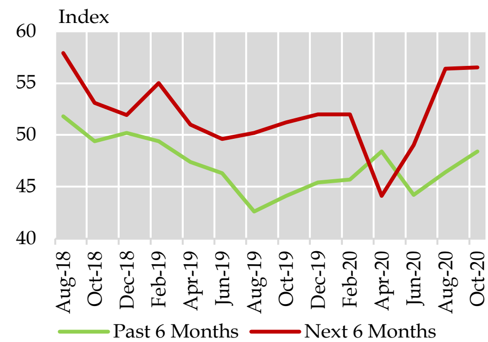
[48] The industrial hub of Karachi accounts for 67.0 percent of the total industrial establishments in Sindh (Source: Sindh Bureau of Statistics). Moreover, according to the Census of Manufacturing Industries 2005-06, Karachi accounted for highest number of total reporting industrial establishments at 17.0 percent while contributing 26 percent overall value of production in the country.

[49] Note, however, that sugar industry also includes non-crushing season job losses.

Business Confidence Survey-Employemnt Indices (Past 6 months) **Figure 2.17a**



Business Confidence Survey-Employment Indices **Figure 2.17b**



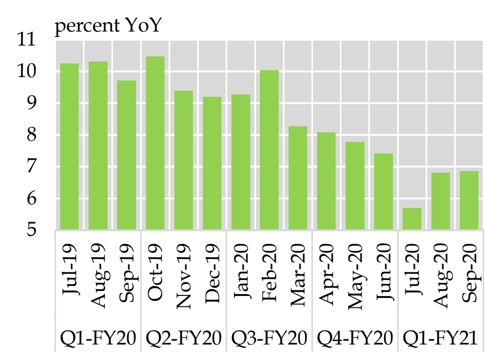
Sources: State Bank of Pakistan

visible contraction of 12.8 and 33.9 percent in Q4-FY20.

The BCS October 2020 wave broadly reflects similar employment trends. Like the industrial sector employment data, a pre-Covid spike, followed by Covid-related job losses during the peak restriction period, and lack of momentum thereafter, are again visible. One advantage of the BCS database is that it provides separate results for the services sector as well. While the employment index follows a similar path for both the categories, the optimism in the services sector is more noticeable (**Figure 2.17**). In conjunction with positive trends witnessed in the Google Mobility statistics, the BCS index lends weight to the recovery in the services sector.
Meanwhile, the construction wage-rate index from the CPI-dataset (another indicator of labor market trends) also depicted growth during Q1-FY21, which highlights the increase in compensation for laborers. The YoY change in the wage-rate index endorses the impact of Covid on the labor market **(Figure 2.18)**.

Further analysis of wage rates points to similar trends within the skilled and unskilled labor force.[50] Unskilled labor wage grew by 7.4 and 6.6 percent in rural and urban areas respectively during Q1-FY21. Similarly, in the skilled labor category, growth of 9.8 and 6.4 percent was recorded for the rural and urban regions, respectively. The noticeably higher growth rate of wages in the country-side areas can partly be attributed to higher rural inflation (10.8

Growth in Construction Sector Wages **Figure 2.18**



Source: Pakistan Bureau of Statistics

[50] Carpenter, mason, plumber and painter are classified as skilled labor.

percent) compared to urban inflation (7.5 percent) during Q1-FY21.

While the improvement in the available employment indicators owes to the resumption of economic activities after the lockdowns, the government and the SBP have also played an important role in restricting job loss through their policies. Accommodative fiscal and monetary measures were geared for retention of employment and recovery of the labor market. In particular, SBP introduced the "Refinance Scheme for Wages to Prevent Layoffs" specifically aimed at cushioning the Covid shock. Latest numbers show that the scheme prevented layoffs of more than 1.6 million workers across Pakistan. By September 2020, 83 percent of the total requested amount under the scheme was approved (**Table 2.8).** Moreover, other SBP initiatives like the Temporary Economic Refinance Facility (TERF) and Debt Relief Scheme also played a role in speeding up the recovery in various sectors, which eventually supported employment in the economy.[51]

SBP Rozgar Scheme **Table 2.8**

	Requested Amount (billion Rs.)	**Approved Amount** (billion Rs.)	**Employees Covered** (millions)
Apr-20	0.1	0.0	0.2
May-20	129.3	89.9	0.6
Jun-20	13.9	29.2	0.3
Jul-20	59.7	28.4	0.1
Aug-20	36.6	42.6	0.2
Sep-20	21.7	26.8	0.1
Total	261.3	216.9	1.6

Source: State Bank of Pakistan

On the fiscal side, the government gave incentives to the construction sector, which is quite labor-intensive. This led to increased economic activity in the construction sector and facilitated its employment generation and retention. Growth in construction-allied manufacturing sectors (such as cement and long steel) and increase in rural and urban construction wages support this. In addition, the government through its Ehsaas Program for social support provided financial assistance to the highly vulnerable daily-wage laborers, the majority of whom lost jobs during the period of economic inactivity.[52]

[51] The SBP initiated several other schemes in the aftermath of Covid shock to support the economy namely *Progress on Loans Deferment and Restructuring*, *Progress on Refinance Scheme for Hospitals to Combat COVID-19* and *Progress on Refinance Scheme for Setting-up New Projects or Expansion/BMR*. (Source: State Bank of Pakistan)

[52] Source: Ministry of Finance, Press Release No. 311 dated May 15, 2020.