5 External Sector

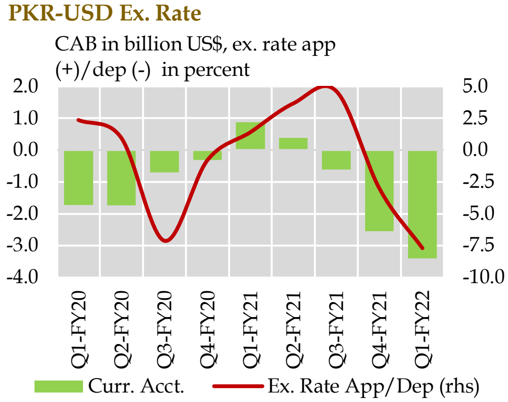
The substantial increase in global commodity prices strained Pakistan's external sector position during Jul-Sep 2021, by pushing goods import payments to an all-time quarterly high of US$ 17.5 billion. Demand-side pressures emanating from strong industrial output added onto the import burden. Exports, especially of textiles, also benefitted from the higher cotton prices; however, the rise in export earnings was outstripped by the higher import payments. Resultantly, the merchandize trade deficit widened to its highest quarterly level on record. This imbalance was partially offset by workers' remittances, which continued on their upward trajectory and crossed US$ 8 billion for the first time in a quarter. Nevertheless, the current account deficit rose to US$ 3.4 billion during the period. The resulting payments gap reflected in the market-determined exchange rate, which depreciated 7.7 percent during the quarter. Nonetheless, the availability of considerable external financing, including under the additional SDR allocation and tap bond issuance, resulted in the SBP's FX reserves rising to US$ 19.3 billion by end-September 2021.

5.1 External Sector Developments

The surge in global commodity prices proved challenging for Pakistan's external sector during the first quarter of FY22. The higher prices significantly added to the country's import burden, which was already elevated in the wake of the policy-induced uptick in demand in some import-dependent sectors (especially automobiles and construction); capex imports; and the need to import Covid-19 vaccines. The resultant payment pressures – which could not be completely offset by the rising receipts under both exports and workers' remittances – manifested in the interbank FX market, where the PKR depreciated 7.7 percent against the US Dollar during the quarter (**Figure 5.1**). Nonetheless, the country's external buffers remained intact, as SBP's FX reserves rose by US$ 2.0 billion to US$ 19.3 billion by end-September 2021 (**Table 5.1**).

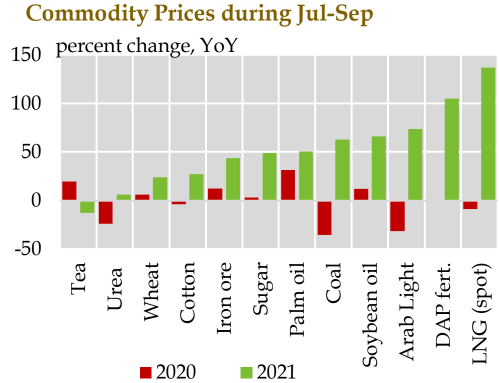
The broad and significant spike in international commodity prices (**Figure 5.2**), along with the unprecedented uptick in global shipping and logistics costs, is having spillover effects across both developed and developing economies. First, the resultant uptick in CPI inflation is leading to central banks reevaluating their accommodative post-Covid policy stances, and market participants to price in future rate hikes into

Curr. Acct. Balance & Change in PKR-USD Ex. Rate — **Figure 5.1**



Source: State Bank of Pakistan

Growth in Major Global Commodity Prices during Jul-Sep — **Figure 5.2**



Source: World Bank & Bloomberg

Pakistan's Balance of Payments during Jul-Sep **Table 5.1**

billion US Dollars

	FY20	FY21	FY22	Change in FY22
Current account balance^	-1.7	0.9	-3.4	-4.3
Trade balance	-5.3	-5.3	-10.2	-4.9
Exports	6.0	5.4	7.2	1.9
Imports	11.3	10.6	17.5	6.8
Energy	2.9	2.1	4.0	1.9
Non-energy	8.4	8.6	13.5	4.9
Services balance	-1.2	-0.5	-0.8	-0.2
Primary income balance	-1.4	-1.5	-1.0	0.5
Secondary income balance	6.1	8.2	8.5	0.3
Workers' remittances	5.5	7.1	8.0	0.9
Capital account balance	0.1	0.1	0.1	0.0
Financial account balance*^	-2.5	0.6	-5.9	6.5
FDI into Pakistan	0.5	0.5	0.4	-0.1
FPI into Pakistan	0.3	-0.1	0.9	1.0
o/w Eurobonds/Sukuk	-	-	1.0	1.0
FX Loans & Liabilities (net)*	1.0	-0.2	4.3	4.5
o/w SDR allocation	-	-	2.8	2.8
SBP's FX reserves (end-period)**	7.9	12.2	19.3	2.0
PKR app(+)/dep(-) in percent**	2.4	1.4	-7.7	-

^Negative change shows worsening & vice versa *Including below-the-line IMF repayments **Change during quarter
Note: negative sign with financial account balance means FX inflow into Pakistan and vice versa
Source: State Bank of Pakistan

current bond yields.[1] Second, for multiple commodity-importing developing economies, the sharply rising commodity prices and shipping costs are generally worsening their trade balances and subsequently leading to currency depreciations (**Section 5.4**).

In Pakistan's case, the impact of the commodity price surge was much more pronounced on imports than on exports, and contributed to the trade deficit rising to a quarterly record high of US$ 10.2 billion during Jul-Sep 2021. That said, some demand-side pressures were also evident. In the midst of the continued accommodative policy stance, strong industrial activity translated into higher demand for imported inputs.

Here, it is worth noting that the rise in global prices also benefitted Pakistan's goods exports, especially high value-added items, which crossed the US$ 7 billion-mark during the quarter. However, the magnitude of this benefit was capped by the country's limited export base. With the current account in deficit, the substantially higher financial flows during the quarter played a crucial role in consolidating the official FX reserves position. The earlier decision in March-April

[1] For instance, the yield on the benchmark 10-year US Treasury bonds averaged 1.3 percent during Jul-Sep 2021, almost double the average of 0.7 percent in the same period last year. Meanwhile, the US Dollar Index appreciated 1.9 percent during the quarter, whereas it had depreciated 3.6 percent in the same period last year (source: US Federal Reserve and Bloomberg).

2021 to opt for a Medium-Term Note Program when issuing sovereign debt also proved helpful, as the country was able to raise a further US$ 1.0 billion via tap bond issuance from foreign investors in July 2021.[2] The continued inflows from mostly non-resident Pakistanis into the Naya Pakistan Certificates via the Roshan Digital Accounts, also provided an important source of official external financing during the period.[3]

While the financial inflows were important in stabilizing the reserves position, it is important for the country to generate non-debt creating FX earnings to ensure the sustainability of the external account. In this regard, some encouraging developments include the continued uptick in informational and communications technology (ICT) exports, as well as the foreign direct investment inflows into technology start-ups in Pakistan.

5.2 Current Account

The current account recorded a deficit of US$ 3.4 billion during Jul-Sep 2021, against a surplus of US$ 0.9 billion in the same period last year. The major reason for the widening current account gap is the 93.7 percent uptick in the merchandize trade deficit, which reached US$ 10.2 billion during the quarter. While goods exports recorded broad-based growth, the sharper uptick in import payments resulted in a significantly higher merchandize trade deficit. The services trade deficit also widened considerably on YoY basis, mainly due to a more than doubling of net freight payments, though the continued growth in ICT exports partially offset some of the higher payment pressures. Meanwhile, a reduction in the primary income deficit and continued increase in workers' remittances partially offset the higher trade deficit.

Workers' remittances maintain their upward trajectory

Workers' remittances rose 12.5 percent to US$ 8.0 billion during Jul-Sep 2021, after increasing 31 percent in the same period last year. Corridor-wise data indicates that inflows from the advanced economies as well as five out of six Gulf Cooperation Council (GCC) countries rose during the quarter (**Table 5.2**).

Multiple factors that have been driving the remittance growth since the Covid-19 outbreak and discussed in the SBP's *State of the Economy Reports* over the past year – such as the adoption of digital channels for funds transfer and the formalization of inflows, incentives in Pakistan for banks and money transfer operators (MTOs) to channelize higher inflows, and fiscal support in the advanced economies – continued to be in play during Jul-Sep 2021, and contributed to the sustained increase in remittances from most of the major corridors.

[2] Under the Medium-Term Note Program, an issuer is able to raise financing from capital market investors from time to time, including at short notice, without undergoing the extensive legal and regulatory processes every time. Instead, the underlying documents are prepared and filed once at the start of the program, and are then only updated in the future when the issuer goes for a tap issuance.
[3] Of the US$ 849 million gross inflows received in RDAs during Jul-Sep 2021, US$ 610 million went into NPCs. From their launch in September 2020, the cumulative inflows into RDAs reached US$ 2.4 billion by end-September 2021, of which US$ 1.6 billion had been invested in NPCs.

Corridor-wise Remittances Received Pakistan during Jul-Sep **Table 5.2**

million US$

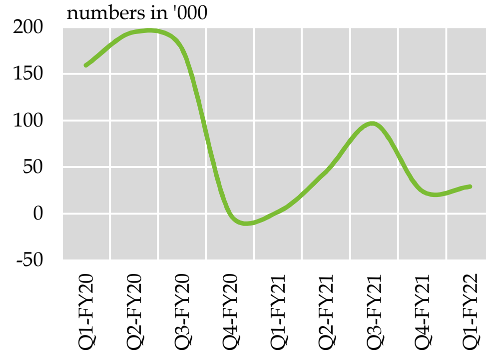
	2020	2021	Abs. Change
US	632.8	836.1	203.3
UK	985.5	1,115.9	130.4
GCC	4,286.9	4,451.5	166.9
KSA	2,080.5	2,025.9	-54.6
UAE	1,420.8	1,544.9	124.1
Other GCC	784.4	880.7	96.2
Germany	93.7	130.8	37.1
France	90.0	130.4	40.4
Italy	137.4	228.7	91.3
Australia	141.2	181.6	40.4
Canada	117.2	162.5	45.3
Others	659.8	797.0	137.2
Total	**7,144.5**	**8,034.4**	**832.3**

Source: State Bank of Pakistan

Furthermore, the employment dynamics for foreign workers in the Middle East are also improving, as air travel restrictions are eased and economic activity picks up. Changes over the past year to the *Kafala* systems in both Saudi Arabia and Qatar would also make it slightly easier for workers to switch jobs, and therefore not tie the workers' employment to one firm's business circumstances.[4]

To some extent, these evolving changes in the labor markets of the GCC are also reflected in the data of Pakistanis who are going to the region for work. After an initial uptick in the number of workers that went to the GCC after some ease in air travel restrictions during October 2020-March 2021, the trend in work-related migration appears to have recovered from the sharp Delta variant-induced drop (**Figure 5.3**),

No. of Pakistanis Going to the GCC for Work **Figure 5.3**



Source: Bureau of Emigration & Overseas Employment

contributing to the healthy outlook for remittances.

Higher freight costs widen the services trade deficit

The services trade deficit widened to US$ 760.1 million in Jul-Sep 2021, up from US$ 533.1 million in the same period last year (**Table 5.3**). Unlike last year, when sizable reductions in the travel and transport services deficit had curtailed the overall services deficit, the trend reversal in these two segments contributed to the higher services deficit this year.

Net freight payments more than doubled to US$ 827.4 million during the quarter. Freight imports during a period partially depend on the magnitude of the goods imports during the same period; the substantial percent rise in goods imports during Jul-Sep 2021 therefore contributed to the higher freight

[4] In Qatar, after the changes to the Kafala system, workers can switch jobs after giving a one-month notice to their current employer; previously, they had to obtain a no objection certificate from their employer to switch jobs. In Saudi Arabia, workers can now switch their jobs after the end of their current contract, though after obtaining the consent of their current employer.

Breakdown of Services Balance during Jul-Sep* **Table 5.3**
million US$

	2020	2021	Change**
Transport	-395.0	-850.0	-455.0
o/w Air passengers	22.7	10.5	-12.2
Freight	-398.0	-827.4	-429.5
Travel	-97.9	-113.0	-15.1
o/w Education exp.	-28.5	-56.7	-28.2
ICT Services	307.1	498.0	190.8
Exports	445.1	635.0	189.9
Imports	137.9	137.0	-0.9
Financial Services	-16.1	-21.0	-4.9
Other Services	-331.3	-274.1	57.2
Services Balance (net)	**-533.1**	**-760.1**	**-227.0**

*Negative balance means deficit and a positive sign means surplus.
**Positive sign shows YoY improvement in services account & vice versa
Source: State Bank of Pakistan

deficit in the quarter as well.[5] Moreover, the global freight costs, including the cost of containers, have spiraled quite substantially since the Covid outbreak, as global supply chains have been stretched due to a myriad of localized and global factors.[6]

Meanwhile, net travel services deficit grew 15.4 percent YoY to US$ 113 million during the quarter. The data breakdown indicates that higher FX payments for educational expenses were the primary drivers of the higher travel imports during the quarter.[7]

Last year during Jul-Sep, based on numerous anecdotes, many students pursuing higher education abroad had either postponed their studies till they could attend in-person classes, or they attended classes virtually and saved on traveling and living expenses. In both these cases, the FX payments for education-related purposes were lower as compared to the year earlier. During Jul-Sep in 2021, the ease in international air travel amidst the vaccine rollout, provided opportunities for students to go abroad for in-person studies. In line with this trend, the education-related FX payments also increased.

Lastly, the country's net exports of information and communications technology (ICT) services continued to rise, growing 62.1 percent YoY to US$ 498.0 million; to put this FX earning into perspective, the country earned a lower US$ 437.1 million from the export of one of its traditional items – rice – during the same period. ICT exports have been rising consistently since the Covid-19 outbreak, as Pakistani firms and freelancers capture the surge in global demand for tech-related services in the wake of remote working and e-learning arrangements. Within ICT, exports increased across almost all segments, including software consultancy, call centers, and telecom services, during the

[5] Freight imports are estimated by the SBP using a freight factor, which is applied to the goods import payments during a month. The higher the goods imports in a period, the higher will be the freight import payments. From July 2015 to June 2018, the freight factor was 3.5; it was reduced to 2.7 during July 2018 to August 2021; and then increased to 3.17 in September 2021. The factor is periodically derived from a survey of various logistics firms in airlines, shipping and related industries.
[6] Global shipping costs, as captured by the Baltic Dry Index, more than doubled during Jul-Sep 2021 on YoY basis (from an average of 1,526 index points last year to 3,727 points). The average cost of a 40 MT shipping container box, as per World Container Index's (WCI) Composite Container freight benchmark, more than tripled in Jul-Sep 2021 on YoY basis, to US$ 9,836 from US$ 2,297 (source: Bloomberg).
[7] On net basis, FX payments for educational expenses rose to US$ 56.7 million during Jul-Sep 2021, from US$ 28.5 million in the same quarter last year. Before the Covid-19 outbreak, in Jul-Sep 2019, these FX payments had amounted to US$ 22.9 million.

period. The government as well as the SBP are actively working to promote this rapidly growing services segment, including via facilitating receipt of export earnings and tax rebates and incentives.

5.3 Financial Account

The net financial flows into the country amounted to US$ 5.9 billion during July to September FY22, in contrast to an outflow of US$ 600 million during FY21; after accounting for below-the-line IMF repayments. The largest inflow was due to the Special Drawing Rights (SDR) allocation by the IMF in August of 2021 (US$ 2.8 billion), followed by the tap issuance of Eurobonds in July 2021 (around US$1.0 billion. Furthermore, the country also received significantly higher external financing from mainly multilateral and commercial sources, as opposed to making net retirements last year. The inflows from these sources more than offset a 4.1 percent reduction in net foreign direct investment during the period.

Sector-wise Net FDI inflow in Jul-Sep **Table 5.4**

million US dollar

	FY21	FY22	Abs.
Food*	4.0	3.1	-0.9
Chemicals	-0.4	-5.5	-5.1
Trade	26.4	10.1	-16.3
Oil & gas**	58.3	47.9	-10.4
Electronics	-2.6	-0.2	2.4
Electrical machinery	36.8	4.5	-32.3
Transport	-6.2	-17.9	-11.7
Power	198.1	131.1	-67
o/w Coal	106.4	59.8	-46.6
Hydel	45.0	25.5	-19.5
ICT	-2.1	88.4	90.5
o/w Telecom	-12.8	24.2	37
IT	10.8	64.2	53.4
Financial firms	98.0	100.5	2.5
Others	-102.2	-96.7	5.5
Total	**457.6**	**439.1**	**-18.5**

*includes food packaging **exploration & refining

Source: State Bank of Pakistan

Foreign direct investment

Net FDI inflows into Pakistan fell by 4 percent to US$ 439.1 million in the first quarter of FY22, from US$ 457.6 million last year **(Table 5.4)**. The decline was relatively broad-based across sectors, though the power sector – which has had the dominant share in net FDI over the past few years – accounted for most of this drop.

FDI into the power sector declined 33.9 percent to US$ 131.1 million. Within power, FDI into both coal and hydropower segments fell during the quarter. Here, two major factors stand out. First, most of the investments into the country's power sector had been arriving under the first phase of CPEC. As most of these projects have been completed and become operational, fresh investments into the sector from China has correspondingly diminished. Second, another possible factor could be the active global policy focus on reducing the usage of coal (including in power generation) over environmental sustainability concerns. This has discouraged investments into coal-fired power projects globally, including possibly in Pakistan as well.[8]

[8] A report from the Center for Research on Energy and Clean Air points out that "In June 2021, the G7 countries announced that they would stop all new financing for overseas coal projects by the end of this year, as well as a 'Clean Green Initiative' to support sustainable development in developing countries at

In contrast to the power sector, FDI into the information communications technology (ICT) sector increased by US$ 90.5 million YoY to US$ 88.4 million, against a marginal net outflow last year. Within ICT, FDI into IT services firms registered a sizable increase, with higher investments coming from China, Germany and the UAE. Within the IT sector, investments came into a tech incubator from Germany; a major telecom services operator with majority ownership stakes in the UAE; and into a Chinese manufacturer of telecom equipment and consumer electronics.

In this regard, it is encouraging to note that Pakistan's digital services firms and tech entrepreneurs, are consistently increasing their exports and are now also benefitting from the sharp increase in global investments flowing into tech start-ups. Especially since the outbreak of Covid-19, foreign investors are looking to invest into Pakistan's communications sector, largely because of the consistently rising telecom connectivity, along with the increased demand for digital services amidst the pandemic.[9] Recent FX regulatory changes in Pakistan are also aimed at facilitating these services-oriented firms and start-ups to scale-up their operations and to increase their global footprint. **Box 5.1** below discusses some recent developments in this regard.

Box 5.1: Start-up Firms in Pakistan –Attracting Foreign Investment [10]

One of the major outcomes of the Covid-19 outbreak and the resultant social distancing and containment measures is the acceleration in the trend of digitization. According to a study, an estimated 70 million *additional* people became digital consumers only in the Southeast Asia region after the beginning of the pandemic.[11] While e-commerce and distant learning platforms were among the major avenues for internet usage, the pandemic also stimulated a drive to digitize a wide range of other services, including financial technology (fintech) and logistics companies. Many of these services attempt to address structural imbalances in developing countries, in areas like financial inclusion, gender disparity in financial access, and efficiency-lags in the retail sector and in logistical connectivity. As such, firms offering digital solutions in these areas have become highly sought-after by global investors, and have managed to raise significant amount of external financing. Investments are flowing into start-ups at

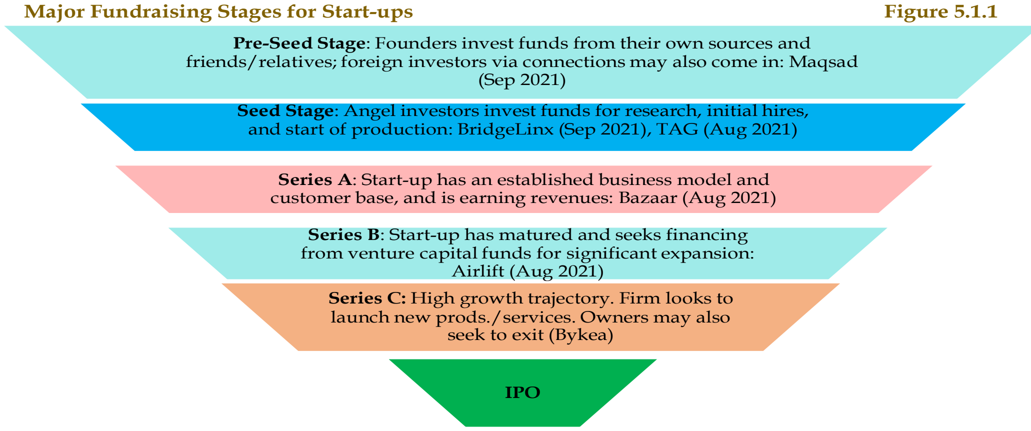
the US Climate Summit in April 2021, [China] re-iterated a commitment to green the BRI. Source: Overseas Coal Briefing; Centre for Research on Energy and Clean Air (2021).

9 During Q1-FY22, broadband penetration in Pakistan increased from 46.9 percent to 49.1 percent (source: Pakistan Telecommunications Authority).

10 This Box utilizes data from the Deal Flow Tracker of Invest2Innovate (i2i), a firm deeply involved in promoting start-ups in Pakistan. The i2i data and classifications are as of November 15, 2021. The data essentially captures self-announced investments by the firms. As such, the data does not necessarily imply the actual amount of foreign investment realized in Pakistan during any given time period. This analysis excludes deals for which any of the four major parameters – firm's name, sector of activity, amount of the announced investment, and name of the foreign investor (fund or individual stakeholder) – were not available in the Deal Flow Tracker database as of November 15, 2021. Lastly, given this chapter's focus on the External Sector, the analysis excludes deals involving local venture capital firms and local other investors.

11 The report defines 'digital consumer' as someone who has purchased a product online at least once over the past 12 months. Source: Southeast Asia, the Home for Digital Transformation (2021). Facebook and Bain & Company.

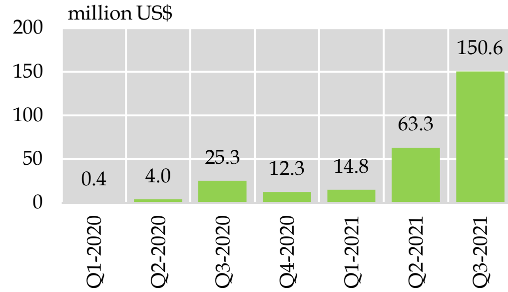
Major Fundraising Stages for Start-ups **Figure 5.1.1**



varying stages of development, including those at the initial stages, to those with established customer bases and revenues, as displayed in **Figure 5.1.1**.

Globally, a major reason for the higher investments into alternative assets, including start-ups, is the substantial monetary easing in the advanced economies, which has led to liquid global capital markets. The venture capital arms of large asset management firms are pouring investments into the technology sector, whereas specialized and tech-focused venture capital firms are now diversifying into new markets and across different sectors.[12] In the finance space, large commercial banks are buying fintech firms outright, instead of pursuing large-scale in-house efforts to come up with digital products.

Announced Foreign Investments in Pakistani Start-ups* **Figure 5.1.2**



*Data extracted on November 15, 2021. Investment announcements by firms.
Source: Invest2Innovate (for data)

It is encouraging to note that many Pakistani start-ups have managed to capitalize on this strong appetite of global venture capital and angel investment funds and raised financing from foreign as well as local investors since the Covid-19 outbreak. Based on analysis of data compiled by Invest2Innovate (i2i), a total of eight Pakistani start-ups announced having raised funds from foreign investors during Jul-Sep 2021, worth over US$ 150 million (**Figure 5.1.2**).[13] Furthermore, these investments have been growing consistently since the Covid-19 outbreak in Q2-2020. Meanwhile, the sectoral breakdown shows that the

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[12] According to data from PitchBook, investments by non-traditional venture funds (such as hedge, mutual and pension funds, and sovereign wealth funds) into American start-ups amounted to US$ 100 billion during the first six months of 2021 (Jan-Jun). That compares with *full-year* investment of US$ 103 billion by these funds into start-ups in 2020, and the previous 5-year (2015-19) average of US$ 57.8 billion.
[13] As mentioned earlier also, data for only foreign investments into start-ups are considered for this analysis, including in **Figure 5.1.2** and **Figure 5.1.3**.

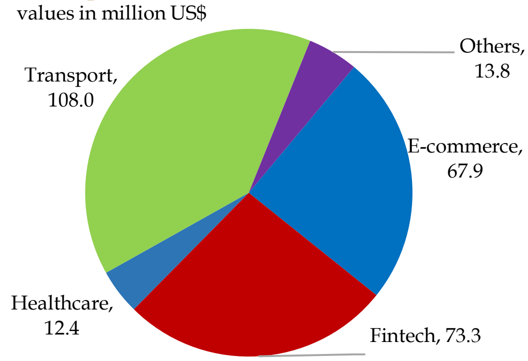
transport sector accounted for the largest share of the announced investments (**Figure 5.1.3**), though this was due to a large-value transaction for one firm; in terms of number of firms attracting foreign investment, the fintech segment dominated, followed by e-commerce.
Multiple factors have played a role in increasing the announced investments into start-ups in Pakistan.

Pakistan-based start-ups are tackling shortcomings across retail, transport & logistics segments: Start-ups that have so far received the greatest amount of foreign interest in Pakistan are mainly offering digital solutions to bring efficiency to the retail shopping experience. Firms in this space can be broadly categorized into two groups: those that offer grocery delivery services directly to consumers; and others that offer digital platforms to facilitate business-to-business (B2B) connections and transactions. The second group appears to have more firms involved. These firms offer a wide range of services, including: connecting small retailers with multiple suppliers (including SMEs) on one platform (instead of the traditional model of arranging inventory from different suppliers); providing warehousing facilities; and providing digital book- and record-keeping products. Some of these firms also arrange delivery services for the products ordered via their platforms.

Closely linked with this space is the transport and logistics segment. Recent investments have been announced by a firm offering freight services that connect manufacturing and industrial firms – such as FMCGs, cement and textile firms – with fleets of truck operators.

Fintech firms are in the spotlight: As indicated in **Figure 5.1.3**, fintech firms have attracted the second-highest interest from foreign investors. These firms are at the early stages of plugging sizable gaps across the country's banking landscape.[14] Multiple start-ups have begun to offer short-term advance (loan) services to customers via digital platforms, in the form of buy now-pay later and early wage access.

Foreign Inv. Announced by Pakistani Start-ups from Q1-2020 to Q3-2021 **Figure 5.1.3**
values in million US$



Source: Invest2Innovate (for data)

Meanwhile, a couple of fintech firms that have attracted foreign interest are offering electronic money (e-money) wallet services to consumers as well as businesses, after obtaining the Electronic Money Institution (EMI) license from the SBP. Other similar firms that have also announced successful fundraising rounds from foreign investors are at the initial development stages, having obtained either in-principal approval or approval to commence pilot projects. These firms have developed digital platforms from where consumers can receive and transfer money and make a wide range of payments. Some of these fintech firms are also offering credit to consumers, including via early wage access facilities.

Regulatory changes to facilitate local IT firms, including start-ups and freelancers**:** With a view to diversify the sources of the country's foreign exchange earnings and to facilitate the ongoing digitization

14 Though financial inclusion in Pakistan has improved, the country still lags regional economies. As of 2017, the percentage of adult population (over 15 years of age) in Pakistan with a bank account was 21.3 percent, significantly lower than the average for low- and middle-income countries (63.0 percent) and South Asia (69.6 percent). Source: Global Financial Inclusion database, World Bank.

drive, the SBP has made multiple changes to foreign exchange regulations. Subject to applicable restrictions, the major regulatory changes allow local firms to:[15]

- Establish their footprint outside the country, by setting up holding companies abroad;
- Remit FX out of Pakistan for necessary operational expenses and initial capital requirements; and
- Remit FX out of Pakistan to undertake equity stake in a foreign company, in order to expand its own business.

Another major regulatory change relates to making it easier for foreign funds to take an equity stake in a start-up. Specifically, in May 2021, the SBP allowed Pakistani start-ups to raise funds from foreign investors via convertible debt instruments, which could be later converted into an equity stake.[16] Such transactions are common across the world, as venture funds initially lend money to a start-up and then convert the loan to an equity stake, in case the start-up matures and is able to generate steady revenues. The regulatory change would help Pakistan-based start-ups to attract investment from foreign investors.

Furthermore, the SBP streamlined regulations for Pakistani businesses so they could acquire the services of major global tech firms, in order to provide seamless services to their clients. The central bank has also made it easier for freelancers to receive payments from abroad via money transfer operators, such as Western Union, MoneyGram and Payoneer.[17]

Foreign Portfolio Investment

Net FPI inflows into Pakistan amounted to US$ 879 million in Jul-Sep 2021, against a net outflow of US$ 145 million last year. The entire inflows this year were received into debt securities, whereas an outflow was recorded from equity securities.

Pakistan raised US$ 1 billion from Eurobonds via a tap issuance under the Global Medium-Term Note Program; the program facilitates debt issuers in accessing international capital markets on relatively short notice. This is because the underlying legal and regulatory documents have to be prepared only once, and these are simply updated ahead of a new debt issuance. In April 2021, the country had realized US$ 2.5 billion in proceeds from Eurobonds that were issued under this note program. In the July 2021 tap issuance, Pakistan raised funds from 5-, 10- and 30-year bonds, while benefitting from the drop in benchmark US Treasury yields relative to March 2021 (**Table 5.5**).

Eurobonds Issued by Pakistan in 2021 **Table 5.5**

Tenor	Coupon (%)	Benchmark (%)*	Amount Raised (bn. US$)
March 2021			
5-year	6.0	0.8	1.0
10-year	7.4	1.6	1.0
30-year	8.0	2.3	0.5
July 2021			
5-year	5.9	0.8	0.3
10-year	7.1	1.3	0.4
30-year	8.5	1.9	0.3

*Average yield on US Treasury bond of same tenor

Source: Economic Affairs Division, Ministry of Finance, US Federal Reserve

[15] The changes were made via FE Circular No. 1 of 2021, in February 2021. The circular also provides the detailed criteria and transaction limits for firms that can utilize these regulatory changes.

[16] The eligibility criteria for start-ups that can issue such convertible limits, along with details on the limits on tenor and cost of financing, are given in FE Circular No. 4 of 2021.

[17] In February 2020 via EPD Circular Letter No. 3 of 2020, the SBP had increased the monthly per-person limit for payments that can be received by Pakistani freelancers via MTOs from US$ 1,500 to US$ 25,000.

In contrast to debt securities, FPI outflows from equity securities continued, amounting to US$ 100 million in the quarter. A couple of factors explain this ongoing trend. First, expectations of monetary policy normalization in the advanced economies, especially in the US, are triggering capital outflows from some emerging markets that are perceived to be relatively riskier, such as Pakistan.[18] Second, equity markets of some EMs, along with a few advanced economies, performed well during Jul-Sep 2021, thereby providing more attractive investment opportunities for global investors than the Pakistan Stock Exchange (**Figure 5.4**).

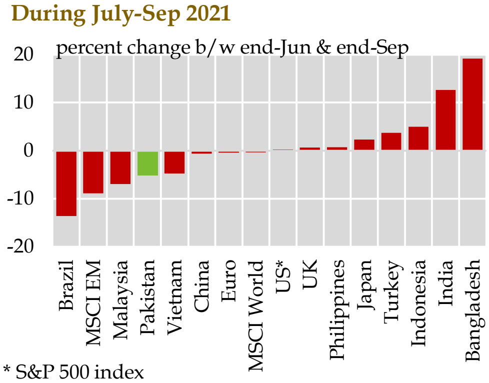
In fact, the Pakistan Stock Exchange had been under pressure during the period, amidst uncertainty related to the resumption of the IMF program and the emerging pressures on the current account and inflation. Furthermore, data from the National Clearing Company of Pakistan indicates that the sell-off from Pakistani equities was noted across multiple major sectors, such as banks, cement and fertilizer (**Figure 5.5**). However, listed ICT firms appeared to attract significant interest from foreign investors during the period.

Net incurrence of liabilities

The net inflow of external loans and liabilities into Pakistan amounted to US$ 4.3 billion in during the first quarter of FY22, net retirements of US$ 0.02 billion in the same period last year; after accounting for below-the-line IMF repayments. During the quarter, significant inflows were realized from multilateral and commercial sources (**Figure 5.6**).

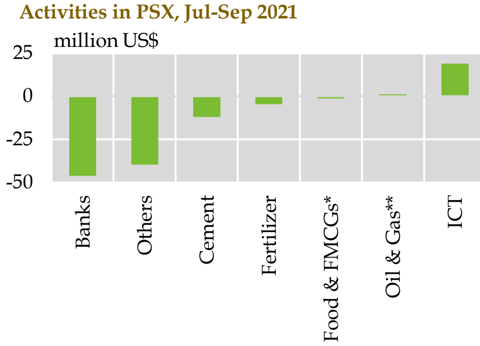
Within the borrowings from multilaterals such as the Asian Development Bank and the World Bank, loans were received to purchase Covid-19 vaccines, and for power and infrastructure development projects. Meanwhile, within bilateral financing, loans from China were mainly for funding an ongoing road infrastructure project. The

Equity Market Performance During July-Sep 2021 **Figure 5.4**



* S&P 500 index
Source: Bloomberg

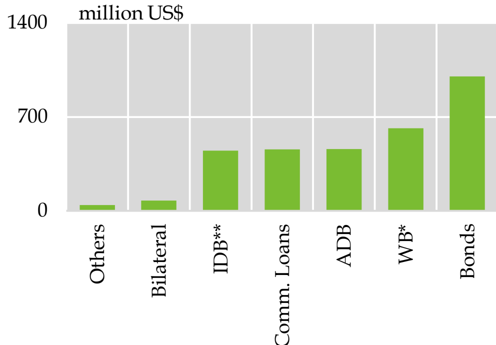
Sectoral Breakdown of Foreign Investors' Buying (+)/Selling (-) Activities in PSX, Jul-Sep 2021 **Figure 5.5**



*incl. personal care items; **OMCs & exploration firms
Source: National Clearing Company of Pakistan Ltd.

[18] For instance, the 5-year credit default swap (CDS) rate for Pakistan averaged 423.8 basis points during Q1-FY22, which was higher than that of Turkey (394.7 bps), China (39.2 bps) and India (80.2 bps) in the same period (source: Bloomberg).

Gross Loan Disbursement (Q1) Figure 5.6



*IDA & IBRD; **including short term

Source: Economic Affairs Division, Ministry of Finance

country also received commercial loans worth US$ 457.5 million (in gross terms) during Q1-FY22, against US$ 335 million in the same quarter last year.

5.4 Reserves and Exchange Rate

In line with the higher financial flows received during the period, the country's overall forex reserves rose US$ 1.6 billion during Jul-Sep 2021 and reached US$ 26.0 billion by end-September. The data breakdown shows that the SBP's FX reserves had risen by US$ 2.0 billion, whereas commercial banks' reserves declined US$ 0.4 billion during the quarter.

The SBP's reserves increased mainly due to cumulative inflows of US$ 3.8 billion from the tap issuance of the Eurobonds and the additional SDR allocations from the IMF. These inflows, coupled with the available multilateral and commercial financing, allowed the SBP to easily make the debt repayments falling due in the period.

On the other hand, the commercial banks' reserves dropped slightly during the quarter. This drop mainly reflected the higher import financing extended by banks from the foreign currency (FE-25) deposits held with them during the period,[19] whereas the level of deposits stayed mostly unchanged between end-June and end-September 2021.[20]

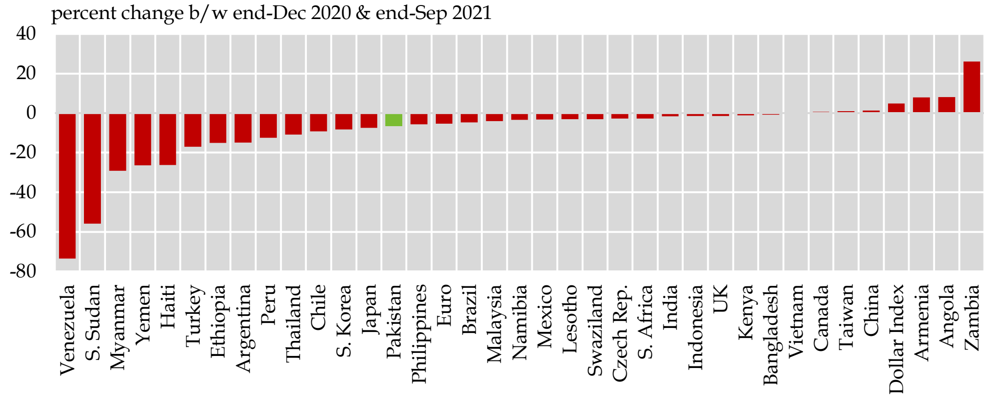
Meanwhile, as discussed earlier, the PKR came under pressure in the interbank market during the quarter, in the wake of the widening current account gap. At the same time, the US Dollar itself has been appreciating against the currencies of multiple emerging market and advanced economies. Expectations of a scaling back of the monetary stimulus by the Federal Reserve in the wake of higher inflation outcomes has contributed to the US Dollar's strengthening against other currencies. When looked over a slightly longer horizon, specifically from the start of CY-21 till end-September, the PKR's depreciation was relatively moderate as compared to other EMs (**Figure 5.7a**). However, it is also worth noting that the average PKR exchange rate during Jan-Sep 2021 had appreciated 1.9 percent against the US Dollar over the average parity in Jan-Sep 2020 (**Figure 5.7b**).

In real effective exchange rate (REER) terms, the emerging markets presented a slightly

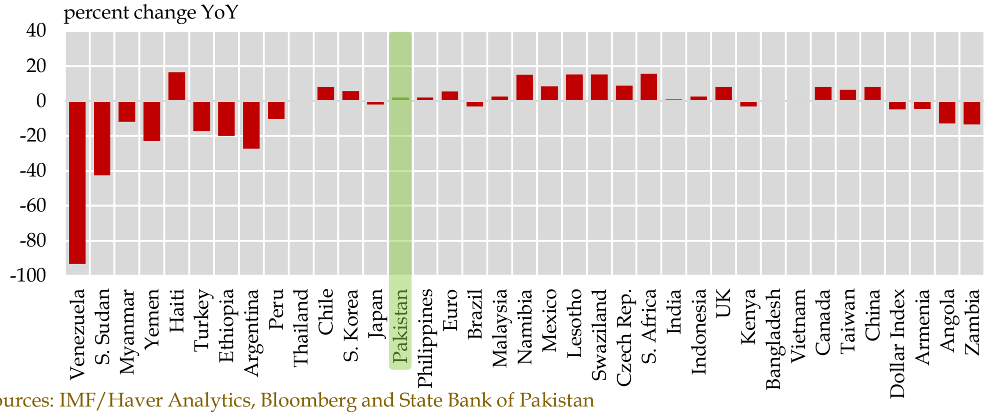
[19] Commercial banks' FX reserves comprise the foreign currency deposits (FE-25 deposits) held with them, excluding any FX-denominated trade financing extended by them to exporters and/or importers.

[20] Between end-June and end-September 2021, banks' liquid FX reserves declined by US$ 369 million. The breakdown shows that FE-25 deposits dropped by US$ 98 million, whereas the trade financing extended by banks rose by US$ 271 million during the period.

Change in Exchange Rates Against US Dollar during Jan-Sep 2021 **Figure 5.7a**

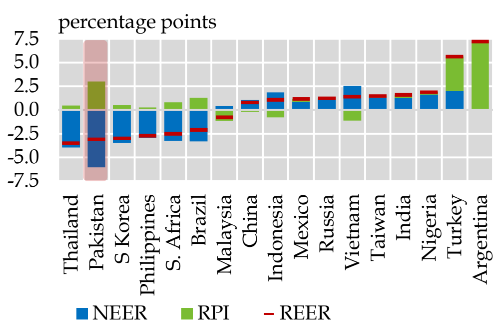


Change in Average Exchange Rates Against US Dollar during Jan-Sep 2021 **Figure 5.7b**



Sources: IMF/Haver Analytics, Bloomberg and State Bank of Pakistan

Breakdown of Change in REER of Major EMs during Jul-Sep 2021* **Figure 5.8**



*JP Morgan Effective Ex. Rate Indices (CPI-deflated)
Source: Haver Analytics

mixed picture, with currencies of some economies appreciating and others depreciating during Jul-Sep 2021 (**Figure 5.8**). Most of the EMs, including Pakistan, witnessed upward price pressures, as captured by the change in the Relative Price Index (RPI) during the period. The nominal effective exchange rate (NEER), however, appeared to play a dominant role in determining the REER movements. In Pakistan's case also, the depreciation in the NEER offset the increasing relative price pressures, and led to a depreciation in the REER during the quarter.

5.5 Trade Account[21]

In Q1-FY22, Pakistan's trade deficit rose by 102.8 percent YoY to US$ 11.8 billion. In the same period last year, the trade gap had reduced to US$ 5.8 billion amid pandemic-related slowdown in trade (**Figure 5.9**). The second lowest trade deficit, since Q3-FY16, achieved in Q1-FY21 was a result of contained growth in imports (0.8 percent) and marginal decline in exports (-0.7 percent) on YoY basis.

In contrast to last year, exports in Q1-FY22 increased by a significant 27.9 percent YoY to US$ 6.9 billion, with both textile and non-textile items registering an increase. The positive price effect amid elevated cotton prices, reinforced the effect of higher volumes in textiles. Moreover, the governments' facilitative policies, to support the manufacturers and exporters, after the pandemic shock also contributed to the overall exports performance in the quarter.

Despite a reasonable improvement in exports, a sharp increase in imports, on the other hand, contributed to the widening of the trade deficit in Q1-FY22. Imports increased by 66.1 percent YoY. Both energy products, and agricultural and chemical product groups (including medicinal products) made a significant contribution to the Q1-FY22 import growth. Besides, imports of machinery, food and transport groups remained at elevated levels.

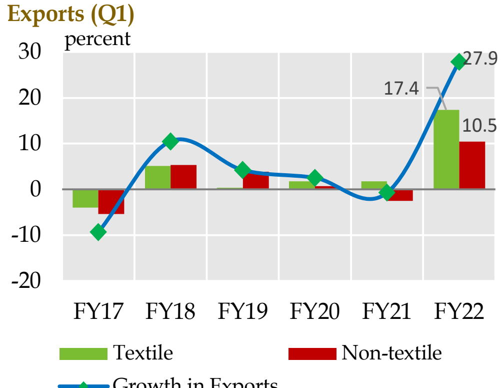
Exports

As per Customs data, exports increased by 27.9 percent YoY to US$ 7.0 billion in Q1-FY22, as opposed to last year when they had slightly declined by 0.7 percent. Historically second-highest in any quarter, these exports were also 31 percent higher than the pre-Covid average (FY18 to FY20) of US$ 5.3 billion.

Growth in exports was broad-based in Q1-FY22, as it was driven from both textile and non-textile products. While growth in textile exports accelerated from 2.9 percent last year to 27.4 percent this year, non-textile exports also made significant contributions towards overall growth vis-a-vis last few comparable quarters (**Figure 5.10**).

Within the textile group, the prominent products included: apparel, home textiles and other textile made-ups, cotton yarn and fabrics, and synthetic textiles. Whereas, in the non-textile category, the major products were: rice; fruits and vegetables; chemicals and pharmaceuticals; oilseeds and nuts.

Breakdown of Growth in Total Exports (Q1) **Figure 5.10**



Source: Pakistan Bureau of Statistics

[21] This section is based on customs data reported by the PBS. The information in this section does not tally with the payments record data, which is reported in **Section 5.1**. To understand the difference between these two data series, see Annexure on data explanatory notes.

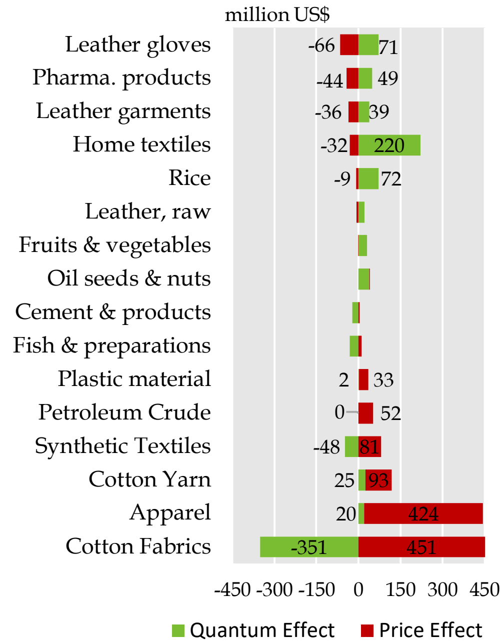
On the aggregate level, this performance in Q1-FY22 came on the back of elevated unit values for some major products in the export basket, especially from the textile sector; however, quantums were also over and above last year for many products (**Figure 5.11**).

For textiles, higher YoY unit values could be attributed to higher input costs, particularly of cotton in the domestic and international market, as well as to the partial knock-on impact of soaring international freight charges on raw material imports. In case of petroleum exports, higher unit values are explained by higher international crude prices. Elevated crude prices also translated into higher unit values fetched by chemicals and plastic materials.

Higher export quantums were realized as a result of capacity expansion in the manufacturing industry, including in textile, chemicals and pharmaceutical industries, partly supported by the SBP's concessionary refinance facilities for fixed investment—Temporary Economic Refinance Scheme (TERF) and Long-Term Financing Facility (LTFF).[22] Whereas, on the demand side, textile exporters were able to secure additional orders from the traditional buyers.

During the quarter, the government also continued the provision of power and gas subsidies to the top five export-oriented sectors, which are designed to make them regionally competitive. Power tariff was set at 9 cents per kWh and gas at US$ 6.5 per mmBtu. This policy contributed to higher quantum exports of many products, with some registering better performances even compared to pre-Covid years (first quarters of FY19 and FY20) (**Figure 5.12**).

Breadkdown of YoY Change in Export Values of Major Products in Q1-FY22 **Figure 5.11**

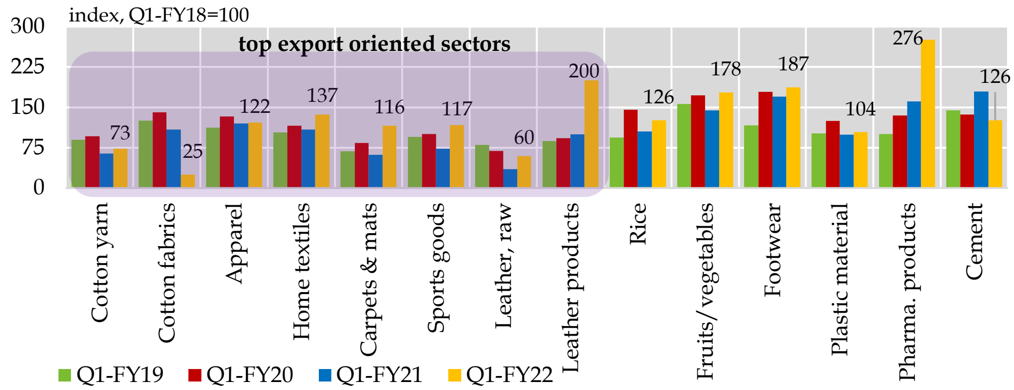


Source: Pakistan Bureau of Statistics

Overall, exporters' liquidity position also improved on the back of higher sales tax refunds. Overall, these refunds amounted to Rs 51.8 billion during Q1-FY22, rising 17.8 percent over last year. It may be noted that in FY21, total sales tax rebates had been Rs 208 billion, which was Rs 116 billion more than the previous year. As a result, exporters' liquidity position had improved, and they were well-placed to fulfill foreign orders.

[22] Total disbursements under TERF, as of end-June 2021, amounted to Rs 139 billion, against a total Rs 435 billion approved financing. The textile sector, which received Rs 69.5 billion in disbursements, was a major beneficiary of this facility. Source: SBP's Annual Report for FY21.

Quantum Exports in Top Five Export Oriented Sectors and Others **Figure 5.12**



Source: Pakistan Bureau of Statistics

Destination-wise, Pakistan's major exports, such as apparel and rice, performed better in traditional markets of the US, EU-27, UK, China, and Africa. However, exports to Afghanistan deteriorated in view of muted cross-border trade due to political uncertainty there.[23] That said, better performance elsewhere supplanted this fall.

Textile Exports

Textile exports grew by 27.4 percent growth to US$ 4.4 billion in Q1-FY22, sharply accelerating from 2.9 percent growth same period last year. Within textiles, exports of knitwear, ready-made garments, bed wear, towels, cotton fabric and yarn, synthetic textiles, and textile made-ups (like dusting or cleaning cloth) performed quite well.

Apparel (knitwear and readymade garments) and home textiles (bed wear and towels) are regarded as high value added products; whereas, cotton fabric and cotton yarn as major low value added products.

In Q1-FY22, apparel registered growth of 28.4 percent to US$ 2.0 billion. Whereas, home textiles exports posted a 22 percent growth to US$ 1.0 billion, which was an acceleration from last year's 9.5 percent growth. Intermediary products, cotton fabric and yarn, together contributed US$ 846 million towards overall exports, which was US$ 218 million over and above last year.

Price effect was positive across apparel, home textiles (towels only) and intermediary products (both cotton yarn and fabric). As far as quantums are concerned, apparel and home textiles shipments increased with intermediary products (cotton fabric) partly offsetting their impact.

Higher unit values bear significantly on textile exports

Higher unit values of Pakistan's major textile products can be traced to the cotton prices trending higher from a year ago in the domestic as well as international market

[23] Pakistan's cumulative exports to the US, UK, EU-27, and China jumped by US$ 1.0 billion to US$ 4.5 billion in Q1-FY22; whereas, exports to Afghanistan declined from US$ 255 million last year to US$ 151 million this year.

(**Figures 13 and 14**). Some competitor countries like Bangladesh have also seen similar surge in export unit values.[24]

In order to fulfill foreign orders and faced with domestic shortage of cotton supplies as the inventories ran out ahead of the fresh harvest, Pakistani textile firms' import demand increased at a time when international prices were also trending higher. Pakistan's raw cotton imports jumped by 65 percent to US$ 343 million in the quarter, keeping the rising momentum from FY21.[25]

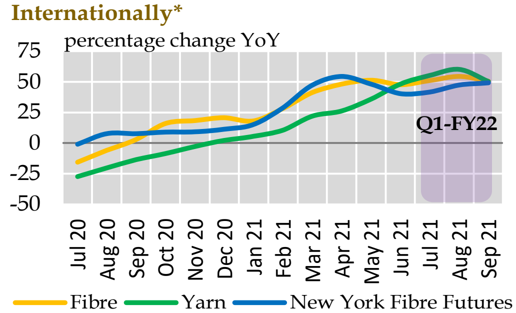
One major reason behind the international price run-up has been strong demand from China, as the country moved to source its cotton supplies from abroad following the US' import ban on Chinese textile products made from Xinjiang cotton in December 2020.[26]

Second, as the global textile industry is making strong post-pandemic recovery, demand for cotton is not only rising, it is outpacing the supplies. This is leading to dwindling global stocks and elevated prices.[27] Besides China, cotton is witnessing vigorous demand from Pakistan, Bangladesh and Vietnam as well.

Third, global logistical crisis and soaring freight cost further raised the landed cost of imported cotton in Pakistan, which is eventually being factored into export unit

Figure 5.13

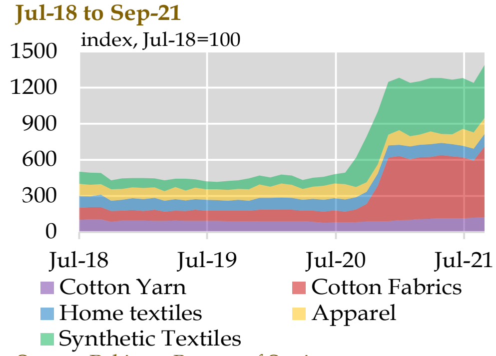
Cotton Fibre and Yarn Prices Trending High in Pakistan and Internationally*



*cotton fibre & yarn prices in US cts/lb & US$/kilo
Source: Emerging Textiles

Figure 5.14

Rising Export Unit Values of Pakistan's Major Textile Products, Jul-18 to Sep-21



Source: Pakistan Bureau of Statists

[24] "The jump in [Bangladesh's] exports in value terms is also due to the rise in prices over a surge in material costs. Cotton fiber and yarn prices have tremendously increased in the past month. Energy prices are also soaring at the same time in Bangladesh like elsewhere." Source: Bangladesh Apparel Exports Quarterly Report, dated November 5, 2021, Emerging Textiles.
[25] Pakistan imported US$ 153 million worth of cotton from the US in Q1-FY22, which was US$ 67 million more than last year.
[26] Source: US Customs and Border Protection press release dated December 2, 2021 (www.cbp.gov/newsroom/national-media-release/cbp-issues-detention-order-cotton-products-made-xinjiang-production).
[27] Source: World Cotton Lint Market Analysis, Forecast, Size, Trends and Insights Update: COVID-19 Impact, Indexbox

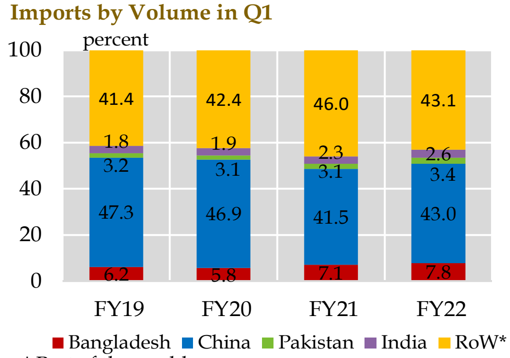
prices of finished goods, like apparel and home textiles.[28, 29]

Quantums also support higher textile exports values

Apparel shipments surpassed last year's level, which can be traced to significantly higher import volumes of the US, EU-27 and UK. Over the last few years, Pakistan's shares in the US and the EU-27 have been inching up, whereas China's share in these markets has been shrinking (**Figures 15a and 15b**).[30] Moreover, the momentum of higher orders received during FY21 has also carried into this year.

At the disaggregate level, shipments of readymade garments, after dipping heavily in Q1-FY21, recovered well in Q1-FY22, pushing up overall apparel volumes. A major factor was the demand for formal wear bouncing back as the Covid-related mobility restrictions generally eased around the globe in 2021, and many workers returned to their workplaces.[31]

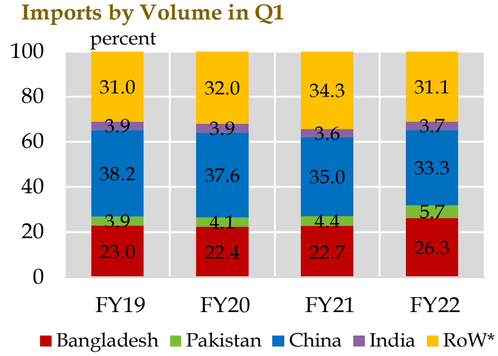
Rising Share of Pakistan in US' Imports by Volume in Q1 — **Figure 5.15a**



* Rest of the world

Source: Office of Textiles & Apparel (US)

Rising Share of Pakistan in EU-27's Imports by Volume in Q1 — **Figure 5.15b**



Source: Eurostat

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28 For instance, between July-2020 and July-2021, global container freight rate index rose about 4 times from US$ 1,762 to US$ 8,848. Source: Statista (www.statista.com/statistics/1250636/global-container-freight-index/#statisticContainer)

29 Nishat Chunian Limited noted in its Financial Report 2021: "Unavailability of local cotton compelled the company to import cotton…. Freight has significantly jumped largely due to two underlying factors; oil prices increasing transportation charges for Karachi bound shipments and the tussle due to container shortage globally causing a hike in ocean freight. However, yarn prices, by virtue of being market driven, have improved significantly, allowing the company to transfer substantial impact of drastic rise in aforementioned input costs, to its customers."

30 "…from 2015 to 2020, China's lost market shares in the world apparel exports (around 7.8 percentage points) were picked up jointly by its competitors in Asia, including ASEAN members (up 4.4 percentage points), Bangladesh (up 1.3 percentage points), and Pakistan (up 0.3 percentage point). Such a trend is most likely to continue in the post-Covid-19 world." Source: www.just-style.com/features/world-textiles-and-apparel-trade-amidst-a-pandemic-statistical-review-2021/

31 This factor has also been mentioned in Nishat Mills Limited's Financial Report 2021: "Sale of workwear cloth also increased because of increase in demand soon after softening of lockdown restrictions world over."

In case of home textiles as well, higher demand originated from the major EU-27 market, which imported 24.4 percent more from Pakistan in Jul-Sep this year, according to Eurostat.

There was vibrancy in the country's entire textile supply chain as higher foreign orders for finished products had also prompted robust demand for textile intermediaries, i.e. cotton fabric and yarn. This phenomenon had necessitated capacity expansion along the value chain. The government's supportive policies in the wake of the pandemic, and the SBP's concessionary refinance schemes (TERF and LTFF) facilitated this capacity expansion.[32] It is evident by the fact that the textile industry took on majority of total fixed investments loans in FY21, with 54 percent higher offtake than the year before.[33]

Among major low value added textile items, cotton yarn shipments recovered in Q1-FY22, mainly owing to low base effect from last year. However, the same cannot be said about the cotton fabric shipments, as their precipitous fall continued from last year. It was mainly due to higher domestic consumption of cotton fabric, leaving lower exportable surplus for the quarter.

Nevertheless, it is pertinent to note here that elevated unit values of cotton fabric supplanted the impact of negative quantum effect, and resulted in 21.9 percent growth in fabric's export values to US$ 557 million.

Rice Exports

Rice exports rose by 17.5 percent to US$ 423 million in Q1-FY22. This growth is partly attributable to low base effect of Q1-FY21, when exports had dropped by almost a quarter. Quantum effect was positive and significant, while the price effect was negative and small.

At the disaggregate level, basmati rice exports were US$ 33 million more than last year, reaching at US$ 154 million. One major contributor to Pakistan's higher basmati shipments was Kazakhstan, which imported 16 times more of this premium grain in this quarter than last year. Besides, there was also higher demand from some African countries, mainly Kenya and Somalia.[34] Price of Pakistan's basmati rice trended lower than last year, making it more competitive in the international market.[35] This reflected in lower export unit values for the premium grain (**Figure 5.16**).

On the other hand, non-basmati rice exports also rose by 12.8 percent to US$ 270 million in the first quarter. Higher shipments could be traced to China, where demand was strong, as underscored by growth in consumption and import of rice amidst Asian origin quotes being lower than the domestic

[32] For instance, as noted by Interloop Limited in its Q1-FY22 financial report: "…. conducive government policies coupled with large export orders have encouraged textile companies to expand their production capacities, which is expected to increase Pakistan's exports in the foreseeable future."

[33] The industry used most of these loans to import textile machinery. In FY21 and Q1-FY22, these machinery imports were 35 percent and 145 percent higher YoY, respectively.

[34] In value terms, Pakistan exported US$ 25 million worth of basmati rice to Kazakhstan, and US$ 29 million to Africa, in the quarter.

[35] Pakistan's average quote for basmati rice during Jul-Sep FY22 was 24 percent lower from a year ago. Source: FAO Rice Price Updates

prices.[36] Besides, Pakistan also shipped higher volumes to African destinations, mainly Madagascar, Kenya and Cote d'Ivoire.

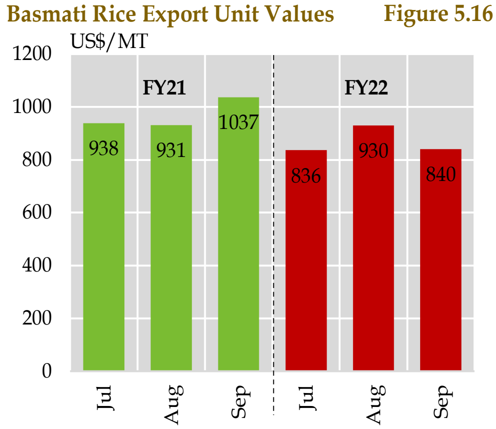
Chemicals and Pharmaceuticals

Exports of chemicals and pharmaceutical products grew by US$ 139 million and clocked in at US$ 363 million in Q1-FY22. Chemicals, other than the ones used in pharmaceutical and plastic products, had the highest share (**Figure 5.17**). Their export values rose significantly to US$ 202 million, showing 94 percent growth YoY. While proceeds from chemical exports received a boost from higher volumes, they were also supported by elevated prices of petroleum crude in the international and domestic market.[37]

Fruits and vegetables

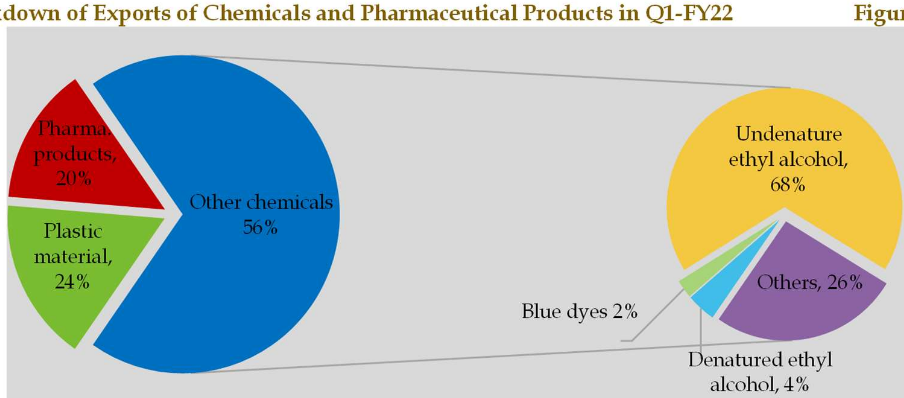
Exports of fruits and vegetables increased by 22 percent to US$ 165 million in Q1-FY22, mainly owing to higher volumes. Major contributions came from fruits—primarily from mangoes, whose exports rose to US$ 87

Basmati Rice Export Unit Values **Figure 5.16**



Source: Pakistan Bureau of Statistics

Breakdown of Exports of Chemicals and Pharmaceutical Products in Q1-FY22 **Figure 5.17**



Source: Pakistan Bureau of Statistics

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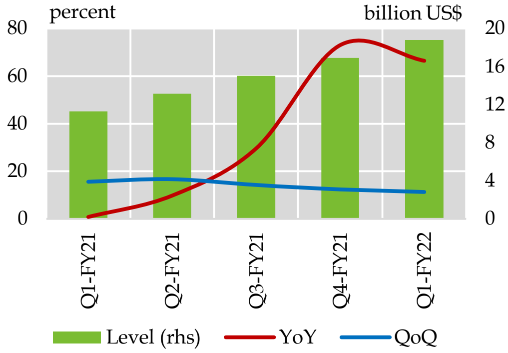
36 Source: USDA 2021. World Agricultural Production Report. July issue. Washington, DC: United States Department of Agriculture

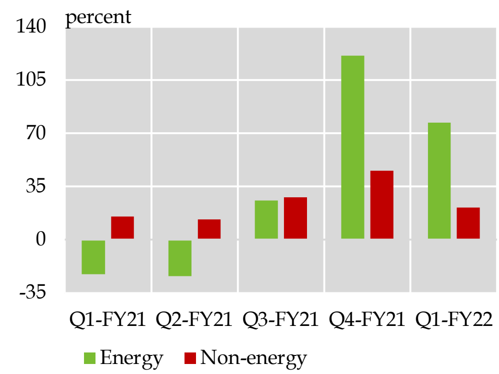
37 Crude and its derivatives are used to make petrochemicals (like ethylene). Rising crude oil prices drive up petrochemical costs as well as market prices for many downstream chemical intermediates and plastics. Source: www.ihsmarkit.com/research-analysis/understanding-how-fluctuating-crude-oil-prices-impact-petrochemical-investment-strategies.html

Pakistan's Recent Quarterly Imports **Figure 5.18**



Source: Pakistan Bureau of Statistics

Growth in Global Energy and Non-Energy Commodity Prices **Figure 5.19**



Source: World Bank

million, about US$ 24 million more than last year. Shipments to the UAE, Kazakstan, and Uzbekistan were quite higher.

Imports

Imports in Q1-FY22 reached US$ 18.7 billion. The increase in imports is recorded in all the major groups. While it is a record high increase in a quarterly imports, there was a deceleration in its growth compared to the preceding quarter (**Figure 5.18**). Multiple factors have contributed to the steep rise in imports in Q1-FY22.

Rising global commodity prices contributed significantly to the increasing import volume

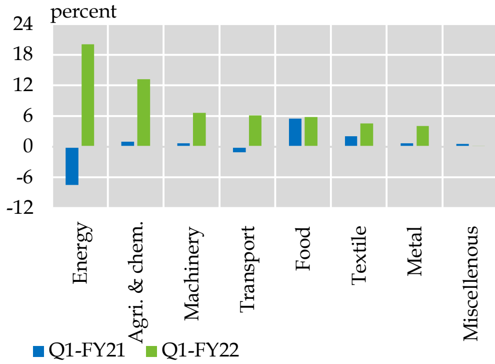
Global commodity prices—both energy and non-energy—remained elevated in 2021. Covid-related disruption in global supply and supply chains, specifically in shipping and allied services, amid recovery in the global demand, created an upward pressure on the commodity prices (**Figure 5.19**).

Category-wise index of non-energy commodity prices increased 31.5 percent on average in first nine months of 2021, and 27.8 and 45.5 percent respectively in Apr-Jun and Jul-Sep 2021 on YoY basis. Index of energy prices, on the other hand, was more volatile; increasing on average by 74.7 percent during Jan-Sep 2021. In Apr-Jun and Jul-Sep of 2021, the energy index rose by 121.1 and 77.1 percent YoY.

Strengthening pace of recovery in the advanced economies, falling global oil inventories, and unanimity maintained by the members of OPEC+ and shale producers in USA in pumping crude oil raised the oil prices to a higher level. At the same time, depletion of the global natural gas stock, adverse weather conditions, and some country-specific shocks, like the decline in Brazilian hydropower output, pushed European natural gas prices to record highs by September 2021.[38]

[38] Source: World Economic Outlook, October 2021. Also, see Box 3.1 in Chapter 3 for more details on rising international commodity prices.

Groupwise Contribution in Q1 Imports **Figure 5.20**



Source: Pakistan Bureau of Statistics

Pakistan also felt the brunt of the increased global commodity prices, especially energy prices. Energy contributed 20.0 percentage points in 66.1 percent growth in imports in Q1-FY22, while contribution of energy was -7.5 percentage points in 0.8 percent import growth in this period of last year (**Figure 5.20**).

Reviving economic activity also strengthened the import demand

The overall policy environment remained accommodative in Q1-FY22 and various economic stimuli continued to support the economic activity, thereby strengthening the import demand. For instance, disbursement against the approved loans under the government's announced housing scheme and erstwhile SBP schemes announced in the wake of the Covid shock continued in Q1-FY22.[39] Furthermore, a continuous increase in workers' remittances might also have added to the purchasing power of the households for imported consumer-durable goods.[40]

Energy Imports

As discussed above, surging global energy prices largely drove the rise in the energy imports in Q1-FY22. Import of crude oil and LNG show the influence of global prices, while higher volume also reinforced the increased imports of petroleum products (**Table 5.6**). Growing economic activity, specifically in transport and power sectors, sustained the demand for HSD and furnace oil despite a significant increase in domestic prices of these products (**Figure 5.21**).[41]

Power generation registered a 6.9 percent increase YoY, despite abated water flow in rivers reducing the hydel generation, and volatile international prices restricting LNG imports (**Figure 5.22**).[42] The shortfall in hydel

Breakdown of Increase in Imports of Major Energy Commodities in Q1-FY22 **Table 5.6**

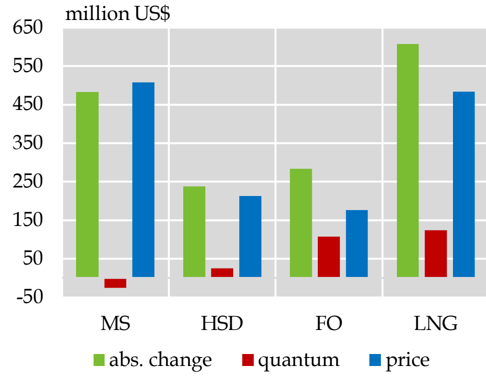
million US$

Items	Change	Quantum impact	Price impact
POL prods.	1049.6	122.7	926.9
Crude oil	562.2	9.1	553.1
LNG	604.7	-16.2	620.9
Coal	365.0	38.7	325.8

Source: Pakistan Bureau of Statistics

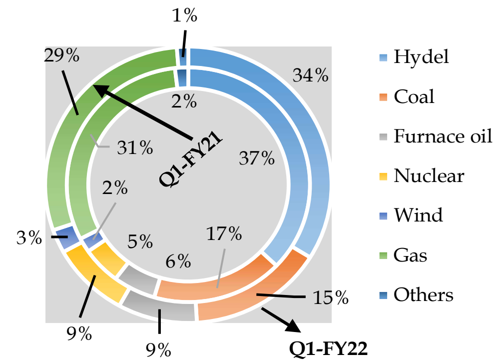
[39] Around Rs 11.7 billion and Rs 60.2 billion were disbursed against approved loans under Mera Pakistan Mera Ghar and TERF schemes in Q1-FY22, while Rs 4.6 billion and Rs 64.6 billion respectively were disbursed in Q4-FY21.
[40] Workers' remittances increased by 12.5 percent YoY in Q1-FY22.
[41] The government transferred the impact of global price increase, albeit partially, to domestic fuel prices, leading to 13.4 percent and 53.6 percent rise in domestic HSD and FO prices respectively during Q1-FY22.
[42] Flows in Jhelum at Mangla and Indus at Tarbela, together, reduced by 4.0 percent YoY in Q1-FY22 (source: WAPDA).

Fuel Imports in Q1 FY22 **Figure 5.21**



Source: Pakistan Bureau of Statistics

Share of Major Fuels in Power Generation **Figure 5.22**



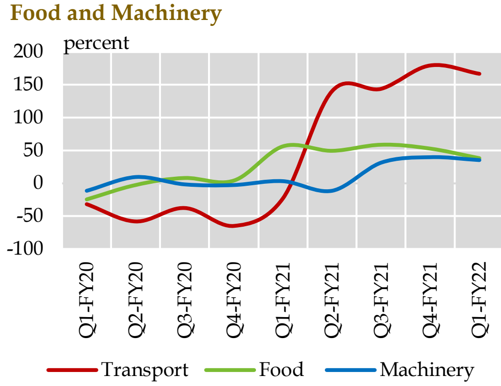
SourceNational Electric Power Regulatory Authority

and reduced LNG supplies to power sector were offset by an increased use of furnace oil and nuclear-based generation.

Non-energy imports

Non-energy imports increased by 58.3 percent YoY to US$ 14.1 billion in Q1-FY22. In terms of contribution, agricultural and chemical group had the largest share. The pandemic-induced import of medicine rose 311 percent YoY to US$ 1.1 billion in Q1-FY22. Moreover, chemical imports due to burgeoning demand in textile sector also increased. Together, the increase in these two categories largely explains the rise in imports of this group in Q1-FY22 (**Table 5.7**). Besides these, imports of transport, food and machinery items contributed significantly to the broad-based increase in the non-energy imports (**Figure 5.23**).

Growth in Imports of Transport, Food and Machinery **Figure 5.23**



Source: Pakistan Bureau of Statistics

Transport

The growth spurt experienced by transports in Q2-FY21 onward continued in Q1-FY22, where overall transport imports increased to US$ 1.1 billion; registering a growth of 166.6 percent YoY. Both CBU and CKD transport imports grew sharply. Contrastingly, in the same period of last year, transport imports declined by 23 percent YoY. Persistent increase in demand of motorcycles, motor cars, and heavy vehicles elevated CKD/SKD imports in Q1-FY22 (**Figure 5.24**).

While ongoing economic recovery has increased demand for heavy vehicles, including buses and trucks, the rising income from workers' remittances and inflows in the Roshan Digital Accounts (RDA) may have added to the purchasing power of the households, which resulted in a steep rise in the demand for motor cars and motor cycles.[43] Similar to CKD/SKD imports, the

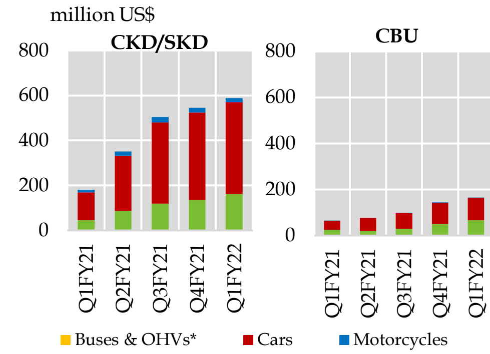
Pakistan's Major Imports (Q1) **Table 5.7**

million US$

Items	FY21	FY22	Change
Energy group	**2,328**	**4,593**	**2,265**
POL prods.	1,126	2,176	1,050
Crude oil	693	1,255	562
LNG	420	1,025	605
Agri and chem	**1,923**	**3,419**	**1,496**
Fertilizer	150	256	106
Plastic Material	519	755	236
Med. Products	279	1148	868
Other chem.	928	1,224	295
Transport group	**414**	**1,105**	**690**
Cars	164	503	339
CBUs	39	96	56
CKDs	125	407	283
Truck & buses	72	230	159
Aircraft & ships	87	205	118
Metals group	**1,084**	**1,542**	**458**
Steel scrap	485	501	16
Iron & steel	375	710	335
Food group	**1,712**	**2,364**	**652**
Wheat Un-milled	102	99	-2
Tea	142	151	9
Palm oil	579	891	312
Sugar	13	91	78
Textile group	**677**	**1189**	**512**
Raw cotton	208	343	135
Syn. yarn	141	226	86
Machinery group	**2,105**	**2,848**	**743**
Power gen	424	530	106
Electrical	324	492	168
Construction	31	39	7
Cell phones	493	495	2
Other machinery	526	747	222
All other items	**772**	**1,387**	**615**
Coal	241	605	365
Total imports	**11,286**	**18,773**	**7,487**

Source: Pakistan Bureau of Statistics

Breakdown of Transport Imports **Figure 5.24**



* Other heavy weight vechiles

Source: Pakistan Bureau of Statistics

CBU imports also witnessed a significant rise in both motor cars and heavy vehicles (**Figure 5.24**).

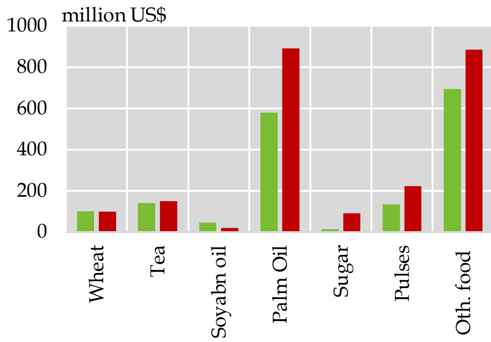
Food

The food imports increased 38.1 percent YoY to US$ 2.4 billion in Q1-FY22 (**Figure 5.25**). In order to contain the prices of essential items, the government continued to import wheat and sugar in Q1-FY22, despite a significant increase in production of wheat in the last crop cycle (ending April) and the forecast of a decent increase in the sugarcane production in this crop cycle (beginning in October).[44] Disruption in the supply chain of sugar, specifically, created upward pressure on the sugar prices prompting the government to import this commodity.

[43] Domestically produced motor car sales increased 80.6 percent, while sales of buses, trucks & light commercial vehicles increased by 93.2 percent in Q1-FY22. Comparatively, the sales of cars and buses trucks & light commercial vehicles increased merely by 2.7 percent and 24.8 percent in Q1-FY21 (**Chapter 2**).

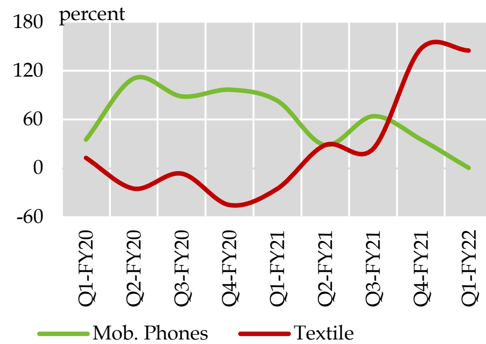
[44] Pakistan produced a record 27.3 million tons of wheat in FY21. However, it was insufficient to cater to the domestic demand of around 29.5 million tons. Moreover, some pressure may be emanating from smuggling of wheat and wheat flour to Afghanistan. Sugarcane production, in contrast, is estimated to increase by 8.2 percent, to 87.6 million tons, due to increase in the crop area (source: MNFSR).

Figure 5.31: Key Components of Food Imports Figure 5.25



Source: Pakistan Bureau of Statistics

Growth in Mobile Phones and Textile Machinery Figure 5.26



Source: Pakistan Bureau of Statistics

Import of palm oil continued to increase in Q1-FY22, with higher prices offsetting the decline in volume (**Table 5.8**). Covid-related supply disruption in Malaysia and Indonesia and increased demand of palm oil from India and China sustained the price of this commodity at elevated level.[45] Moreover, amid increased commodity prices, quantum increase in tea and pulses and some other food items inflated the overall food import bill in Q1-FY22 (**Figure 5.25**).

Breakdown of Imports of Selected Non-Energy Commodities in Q1-FY22 Table 5.8

million US$

Items	Change	Quantum impact	Price impact
Fertilizer	106.0	-1.4	107.5
Plastic Material	236.0	-13.0	249.0
Med. Products	868.0	109.3	759.0
Steel scrap	16.0	-184.1	199.7
Iron & steel	335.0	134.3	200.6
Palm oil	312.0	-85.7	397.9
Raw cotton	135.0	55.7	79.0
Syn. yarn	86.0	24.6	61.3

Source: Pakistan Bureau of Statistics

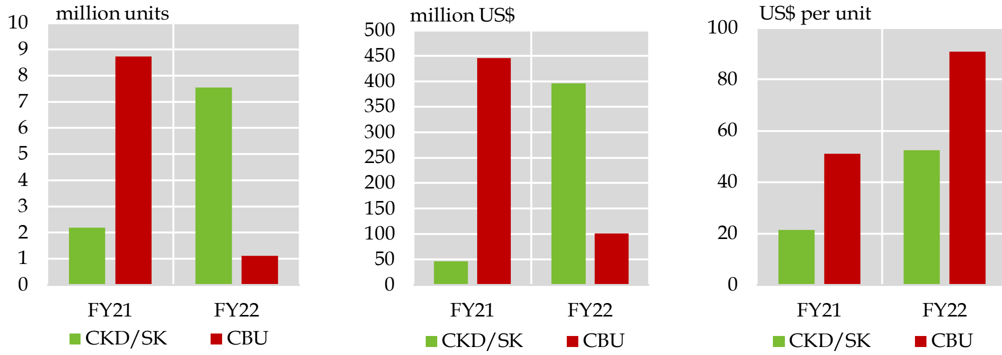
Machinery

Machinery imports climbed to US$ 2.8 billion, with a 35.3 percent YoY broad based rise in Q1-FY22. Nevertheless, two distinct features warrant some deliberation (**Figure 5.26**). First, the pace of increase in mobile phone imports decelerated to a marginal 0.4 percent YoY in Q1-FY22, as improving Covid condition in the country is slowing down the growth in the online activities. This has curtailed some demand of mobile phones.

Importantly, incentivized by Mobile Device Manufacturing Policy (MDMP) 2020, the increase in the CKD/SKD overshadowed the CBU phone imports in both quantity and volume (**Figure 5.27**). Moreover, unit value of these imported mobiles have also increased compared to last year, albeit more sharply for the CKD/SKD mobiles. This suggests that the import of these gadgets is shifting towards the high-end. While CBU imports may be edging towards the costly brands, the local mobile industry is also enhancing their input quality to become

[45] SBP Annual Report on State of Pakistan's Economy FY21.

Breakup of Mobile Imports in Q1 **Figure 5.27**



Source: Pakistan Bureau of Statistics

competitive in the international market. This is evident by the fact that the local industry has started exporting some of their products.[46]

Second, the import of textile machinery increased 144.8 percent YoY to US$ 230.9 million in Q1-FY22. The textile sector, including apparel manufacturers, availed Rs 31.8 billion in approved loans under TERF and LTFF, which may have augmented the demand for textile machinery. This development is in continuation of Q4-FY21, when textile machinery imports had also reached US$ 214.5 million, increasing by 146.6 percent.

Besides mobile phones and textile machinery, the import of power generating machinery corresponded with the continuing power generating projects in the country.[47] Moreover, the ongoing increase in industrial activity, specifically in textile industry and transport sector, raised the demand for switch gears and other electrical equipment leading to the increased demand of electrical machinery.

Apart from the higher demand of machinery, growing demand for the textile exporting sector led to quantum rise in import of raw cotton, despite its higher international prices. The expected increase in cotton production in the country, together with the global commodity price effect, may have restrained some of the imports of cotton in Q1-FY22. Cotton production is estimated to increase by 33.1 percent, to 9.4 million bales.[48] Moreover, despite higher prices, flourishing demand in the transport sector led to significant increase in iron and steel imports, reinforced by the volumetric increase also. However, in case of iron and steel scrap imports, the price led increase more than offset the decline in volume of the commodity’s imports.

[46] Pakistan exported mobiles worth US$ 2.3 million during Jul-Aug FY22.
[47] SBP Annual Report on State of Pakistan’s Economy FY21.
[48] Source: Pakistan Central Cotton Committee (PCCC)