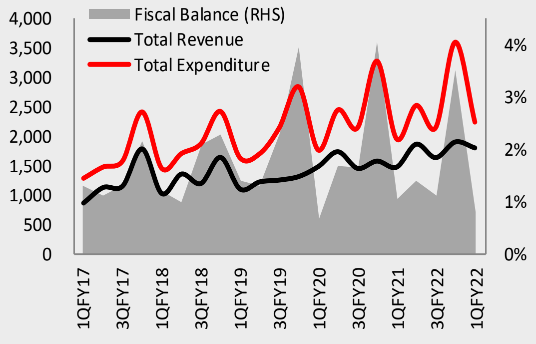
PAKISTAN

Proposed schedule of reviews & purchases after rephasing

Date	Amount of Purchase SDR mn	% of Quota	Conditions
3-Jul-19	716	35	Approval
6-Dec-19	328	16	1st review
5-Mar-21	350	17	2nd-5th reviews
3-Sep-21	750	37	6th review
4-Mar-22	687	34	7th review
3-Jun-22	687	34	8th review
2-Sep-22	750	37	9th review
Total	**4,268**	**210**	

Source: IMF, FSL Research, February, 2022

IMF sets fiscal balance target of 5.6% for FY22



Source: MoF, Foundation Research, Feb 2022

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Monday, February 7, 2022

Pakistan Economy

IMF revival strives for further reforms

Pakistan at a crossroads

IMF aims to conclude the 3yr, US$6bn EFF program as originally planned by Sep'22 with disbursement of the un-utilized US$3bn in 3 approximately equal tranches in Mar'22, Jun'22 and Sep'22. Despite significant efforts to bring the program back on track post COVID in Apr'21, Government efforts shifted toward expansionary macroeconomic policies and reversed some earlier reforms in an attempt to spur growth. IMF has introduced new structural benchmarks which support current efforts to (1) strengthen revenue mobilization, (2) public financial management, (3) energy sector viability, (4) governance/anti-corruption, and (5) AML/CFT framework.

Tax reforms will remain center of FY23 budget

In order to comply with broadening of tax base, reducing informality, and simplifying and modernizing the tax system, fund is planning to introduce reforms in Personal Income tax (PIT) and General Sales tax (GST). New structural benchmark of PIT reforms will focus on reducing number of rates and income tax brackets, reduce tax credits and allowances, introduce special tax procedures for very small taxpayers and bring additional taxpayers into the tax net. GST reforms will aim to harmonize GST on services across provinces and unify the current fragmentation with services. Strengthening of tax administration, enhancing Public Financial Management in particular improving debt management and safeguarding the transparency of COVID spending are among other key measures to improve tax collection.

SBP refinance facilities to move to new DFI

New structural benchmark envisages preparation of a plan to establish an appropriate Development Finance Institution by end-April 2022 as a basis for a plan to transfer the SBP refinancing schemes to the government. Fund also advised Govt to unwind measures of (1) mandatory bank lending to housing and construction sectors and (2) lower risk weight of REIT for banks/DFIs.

Structural benchmark was also introduced for 1st stage recapitalization of two private sector banks that are undercapitalized. Fund also set new deadline for adaptation of measures to strengthen effectiveness of AML/CFT framework to support efforts to exit the FATF grey list.

Sustained reforms required to turn around energy sector

New structural benchmark seeks a decision from the cabinet on the 2nd step of the energy subsidy reform for residential consumers. Fund also set a new date for the parliamentary adoption of the OGRA Act by end-June 2022 to support regular and full cost recovery going forward.

Enhanced monitoring of Govt officials and contracts

Fund called on the authorities to accelerate the legal, regulatory and policy framework update of the State Owned Enterprises (SOE) sector. A key element remains the parliamentary approval of the SOE law which is a new structural benchmark.

IMF advised the establishment of an asset declaration system with a focus on high-level public officials to strengthen effectiveness of anti-corruption institutions. New structural benchmark was set for the issuance of regulations to collect and be able to publish beneficial ownership information of companies awarded Rs50mn and above public procurement contracts.

Table 1: Gross Financing Requirements and Sources, FY20-FY26 (US$ mn)

	FY20	FY21	FY22	FY23	FY24	FY25	FY26
		Est.			Proj.		
Gross External Financing Requirements (A)	**23,430**	**21,551**	**30,417**	**35,068**	**41,882**	**39,123**	**36,600**
(In percent of GDP)	9	7	10	10	11	10	8
Current account deficit	4,449	1,916	12,994	12,163	12,363	12,230	11,789
(In percent of GDP)	2	1	4	4	3	3	3
Amortization	18,236	18,555	16,416	21,798	27,707	25,204	24,185
Public Sector	12,799	13,943	11,658	16,977	22,957	20,360	19,292
Short-term Borrowing	1,182	784	2,715	3,100	4,000	4,900	4,000
Long-term Borrowing (non-IMF)	10,617	13,159	7,942	12,877	17,957	15,460	13,492
Bonds	1,000	-	1,000	1,000	1,000	-	1,800
Private Sector	5,437	4,612	4,758	4,821	4,750	4,844	4,893
Short-term Borrowing	3,610	3,365	3,514	3,381	3,414	3,471	3,520
Long-term Borrowing	1,827	1,247	1,244	1,440	1,336	1,373	1,373
IMF Repurchases	745	1,080	1,007	1,107	1,812	1,689	626
Available Financing (B)	**25,497**	**26,174**	**31,275**	**33,450**	**41,335**	**39,848**	**38,808**
Foreign Direct Investment (net)	2,652	1,786	2,350	3,063	3,690	4,201	4,478
Disbursement	22,418	25,144	26,120	30,259	37,532	35,527	34,292
From private creditors	15,430	11,508	13,899	17,794	20,929	24,594	24,594
Disbursement to Private Sector	12,052	4,221	5,317	8,394	10,329	8,912	10,303
Disbursement to Public Sector	3,377	7,287	8,582	9,400	10,600	15,682	14,291
From official creditors (non-IMF)	6,989	13,636	12,222	12,465	16,603	10,934	9,697
o/w Project Loans	1,588	1,876	1,647	1,770	2,416	2,378	2,042
o/w China	487	204	63	100	127	127	-
o/w Program Loans	3,666	2,120	2,479	2,182	2,093	1,974	2,144
o/w WB	729	1,009	1,379	1,182	1,093	974	1,144
o/w ADB	2,347	858	738	1,000	1,000	1,000	1,000
o/w Rollover of short-term debt	12,631	8,945	10,567	10,014	10,043	10,395	9,703
o/w Public Sector	4,627	5,245	7,100	7,100	7,100	7,100	7,100
o/w Private Sector	8,004	3,700	3,467	2,914	2,943	3,295	2,603
Other Net Capital Inflows (net)	427	(756)	38	127	113	120	39
IMF SDR allocation	-	-	2,767	-	-	-	-
Remaining Financing Needs (C=A-B)	**(2,067)**	**(4,623)**	**(858)**	**1,618**	**546**	**(725)**	**(2,208)**
Borrowing from IMF (D)	**2,834**	**499**	**3,056**	**1,085**	**-**	**-**	**-**
Reserve Assets (decrease = +) (E=C-D)	(4,901)	(5,122)	(3,914)	533	546	(725)	(2,208)

Source: IMF, Foundation Research February, 2022

Table 2: Pakistan: Decomposition of Public Debt and Debt Service by Creditor

	Debt Stock (end of period)			Debt Service					
	FY21			FY21	FY22	FY23	FY21	FY22	FY23
	(US$ mn)	(% total debt)	(% GDP)	(In US$ million)			(Percent GDP)		
Total	268,410	100.0	88.6	71,830	83,868	40,549	24.0	26.3	11.7
External	91,766	34.2	30.3	11,578	16,899	15,579	3.9	5.3	4.5
Multilateral creditors	41,726	15.5	13.8	4,057	3,896	3,497	1.4	1.2	1.0
IMF	7,384	2.8	2.4						
World Bank	18,135	6.8	6.0						
ADB/AfDB/IADB	13,423	5.0	4.4						
Other Multilaterals	2,783	1.0	0.9						
o/w: IsDB	1,512	0.6	0.5						
AIIB	835	0.3	0.3						
Bilateral Creditors	30,307	11.3	10.0	3,325	5,227	6,954	1.1	1.6	2.0
Paris Club	10,726	4.0	3.5	10	584	1,175	-	0.2	0.3
o/w: Japan	5,427	2.0	1.8						
France	1,725	0.6	0.6						
Non-Paris Club	19,581	7.3	6.5	3,314	4,643	5,779	1.1	1.5	1.7
o/w: China	18,434	6.9	6.1						
Saudi Arabia	961	0.4	0.3						
Bonds	8,615	3.2	2.8	362	1,516	1,460	0.1	0.5	0.4
Commercial creditors	10,287	3.8	3.4	3,834	6,260	3,668	1.3	2.0	1.1
o/w: Chinese commercial banks	6,735	2.5	2.2						
Other	3,552	1.3	1.2						
Other international creditors	831	0.3	0.3						
o/w: NPC/NBP/BOC deposits/PBC	831	0.3	0.3						
Domestic	176,644	65.8	58.3	60,251	66,969	24,971	20.2	21.0	7.2
T-Bills	42,404	15.8	14.0	34,958	40,939		11.7	12.8	
Held by: local banks	37,975	14.1	12.5						
local non-banks	4,429	1.7	1.5						
Bonds	98,108	36.6	32.4	14,755	18,848	19,288	4.9	5.9	5.6
Held by: central bank	42,025	15.7	13.9						
local banks	42,901	16.0	14.2						
local non-banks	13,182	4.9	4.4						
NSS/Other	26,163	9.7	8.6	10,539	7,182	5,683	3.5	2.2	1.6
Held by: local non-banks	26,163	9.7	8.6						
Memo items:									
Public guarantees	15,278	5.7	5.0						
Central bank deposit liabilities	2,700	1.0	0.9						
Central bank bilateral SWAP liabilities	4,650	1.7	1.5						
Nominal GDP	298,994								

Source: IMF, FSL Research, February, 2022

Table 3: FY21 Quantitative Performance Criteria and Indicative Targets (Rs bn)

	FY21 end-March				FY21 end-June			
	Program (PC)	Adjusted Proj.	Actual	Status	Program (PC)	Adjusted Proj.	Actual	Status
Performance Criteria								
Floor on net international reserves of the SBP (US$ mn)	(10,238)	(10,198)	(7,836)	Met	(8,676)	(8,041)	(4,434)	Met
Ceiling on net domestic assets of the SBP (Rs bn)	9,655	9,650	9,044	Met	10,173	10,083	9,290	Met
Ceiling on SBP's stock of net foreign currency swaps/forward position (US$ mn)	5,200	...	4,285	Met	5,200	...	4,870	Met
Ceiling on general government primary budget deficit (Rs bn)	(230)	(350)	(505)	Met	246	412	462	Not met
Ceiling on net government budgetary borrowing from the SBP (Rs bn)	6,908	...	5,127	Met	6,618	...	5,274	Met
Ceiling on the amount of government guarantees (Rs bn)	2,715	...	2,682	Met	2,715	...	2,626	Met
Continuous Performance Criteria								
Zero new flow of SBP's credit to general government	-	...	-	Met	-	...	475	Not met
Zero ceiling on accumulation of external public payment arrears by the general government	-	...	-	Met	-	...	-	Met
Indicative Targets								
Cumulative floor on Targeted Cash Transfers Spending (BISP) (Rs bn)	114	...	76	Not met	199	...	194	Not Met
Cumulative floor on general government budgetary health and education spending (Rs bn)	975	...	1,006	Met	1,567	...	1,583	Met
Floor on net tax revenues collected by the FBR (Rs bn)	3,394	...	3,395	Met	4,691	...	4,764	Met
Ceiling on net accumulation of tax refund arrears (Rs bn)	65	...	112	Not met	65	...	(30)	Met
Ceiling on power sector payment arrears (Rs bn)	319	...	269	Met	354	...	297	Met
Gross issuance of PIBs, Sukuks, and Eurobonds (Rs bn)	2,850	...	2,341	Not met	4,250	...	3,496	Not met

Source: IMF, FSL Research, February, 2022

Table 4: FY22 Quantitative Performance Criteria and Indicative Targets (Rs bn)

	FY22 end-Sept		FY22 end-Dec		FY22 end-Mar	FY22 end-June
	Program (IT)	Est.	Program (IT)	Proposed	Proposed	Proposed
Performance Criteria						
Floor on net international reserves of the SBP (US$ mn)	(8,518)	(2,303)	(7,677)	(5,450)	(6,000)	(5,100)
Ceiling on net domestic assets of the SBP (Rs bn)	9,947	8,793	10,190	9,850	10,233	10,792
Ceiling on SBP's stock of net foreign currency swaps/forward position (US$ mn)	4,900	4,870	4,600	4,900	4,300	4,000
Ceiling on general government primary budget deficit (Rs bn)	(130)	(137)	(96)	(300)	(389)	25
Ceiling on net government budgetary borrowing from the SBP (Rs bn)	6,333	4,973	6,049	6,049	6,049	6,049
Ceiling on the amount of government guarantees (Rs bn)	2,735	2,649	2,765	2,797	2,954	2,956
Continuous Performance Criteria						
Zero new flow of SBP's credit to general government	-	...	-		-	...
Zero ceiling on accumulation of external public payment arrears by the general government	-	...	-		-	...
Indicative Targets						
Cumulative floor on Targeted Cash Transfers Spending (BISP) (Rs bn)	48	6	102	86	199	250
Cumulative floor on general government budgetary health and education spending (Rs bn)	356	336	752	783	1,287	2,014
Floor on net tax revenues collected by the FBR (Rs bn)	1,181	1,397	2,585	2,852	4,343	6,100
Ceiling on net accumulation of tax refund arrears (Rs bn)	-	17	-	11	6	-
Ceiling on power sector payment arrears (Rs bn)	(166)	114	(154)	67	184	166
Gross issuance of PIBs, Sukuks, and Eurobonds (Rs bn)	1,000	1,443	-	-	-	-

Source: IMF, FSL Research, February, 2022

Table 5: IMF Structural Conditionality

Action			
Fiscal	**Date**	**Revised Date**	**Status**
1 Commit to not grant further tax amnesties.	Continuous		Met.
2 Avoid the practice of issuing new preferential tax treatments or exemptions.	Continuous		Not met
3 Ministry of Finance will establish and make functional the TSA-1.	end-May 2021		Not met. Implemented with delay in Sept 21
4 Reintroduce and roll out the track-and-trace systems for tobacco products.	end-Jun. 2021		Not met. Reintroduced and rolled out only in one company out of 16 in Oct 21
Social Protection and Gender			
5 Finalize the update of the BISP beneficiaries' database (National Socio-Economic Registry).	end-Jun. 2021		Not met. Implemented with delay in October 2021 with a coverage of 33 million households
Monetary and Financial			
6 Adopt measures to strengthen the effectiveness of the AML/CFT framework to support the country's efforts to exit the Financial Action Task Force list of jurisdictions with serious deficiencies.	end-Jun. 2021	end-Mar. 2022	Not met.
Energy Sector, State-Owned Enterprises, and Governance			
7 Reduction in CPPA-G payables to power producers through a payment up to PRs 180 billion with no more than 1/3 in cash and the remainder in debt instruments.	end-May 2021		Not met. Implemented with delay on June 4 through a payment of PRs 89.9 billion, with 1/3 in cash and the remainder in debt instruments
8 Completion of the FY 2021 annual rebasing (AR).	Jun. 1, 2021		Not met. Implemented with delay on November 5, 2021
9 Notification of FY 2020 Q4 electricity tariff adjustment for capacity payments.	end-Sep. 2021		Not met. Implemented with delay on October 1, 2021
10 Finalization of the energy cross-subsidy reform for the FY 2022 budget.	end-Jun. 2021		Not met. To be implemented through a new SB #4.
11 Adoption by parliament of amendments to the OGRA Act.	end-Jun. 2021	end-Jun. 2022	Not met
12 Conduct and publish external audit of the Utility Stores Corporation (USC) based on FY 2020 financials.	end-Apr. 2021		Not met.
13 Publication of awarded COVID-spending related contracts and beneficial ownership information of bidding and awarded legal persons in a centralized and publicly accessible website.	end-Apr. 2021		Not met. To be partially implemented through PA #4, with beneficial ownership transparency addressed with a delayed but broader reform (new SB#6) that covers all large contracts (not just COVID-related spending).
14 Auditor General of Pakistan will conduct an ex-post audit of the procurement of urgently needed medical supplies related to Covid-19. Audits results will be published on the website of the Ministry of Finance.	end-Apr. 2021		Not met. To be implemented through PA #5
15 Establish a robust asset declaration system with a focus on high-level public officials (including elected and unelected members of the Federal Cabinet).		end-Mar. 2022	Not met.
New Structural Benchmarks			
1 Preparation of draft personal income tax (PIT) legislation.	end-Feb. 2022		
2 Preparation of a plan by Ministry of Finance and State Bank of Pakistan, in consultation with other stakeholders, to establish an appropriate Development Finance Institution to support the eventual phasing out of SBP refinance facilities.	end-Apr. 2022		
3 Completion of the first stage recapitalization of the two private sector banks that are undercapitalized.	end-May 2022		
4 Cabinet decision on the second step of the energy subsidy reform for residential consumers.	end-Jan. 2022		
5 Parliamentary approval of new SOE law in line with staff recommendations.	end-Jun. 2022		
6 Issuance of regulations by the Public Procurement Regulatory Authority to require collection for publication of beneficial ownership information from companies which are awarded public procurement contracts for PRs 50 million and above.	end-Mar. 2022		

Source: IMF, FSL Research, February, 2022

Table 6: Economic Indicators from IMF

	FY19	FY20	FY21 E	FY22 P
Output				
Real GDP at factor cost (% change)	2.1	(0.5)	3.9	4.0
Prices				
Consumer prices, period average (%)	6.7	10.7	8.9	9.4
Consumer prices, end of period (%)	8.0	8.6	9.7	10.2
General government finances				
Revenue and grants (% GDP)	13.0	15.2	14.5	15.9
Expenditure (% GDP)	21.9	23.2	21.6	22.8
Budget balance, including grants (% GDP)	(9.0)	(8.0)	(7.1)	(6.9)
Budget balance, excluding grants (% GDP)	(9.0)	(8.1)	(7.1)	(6.9)
Primary balance, excluding grants (% GDP)	(3.6)	(1.8)	(1.4)	(1.3)
Underlying primary balance (excluding grants)	(3.6)	(1.8)	(0.6)	-
Total general government debt excl. IMF obligations	82.9	84.5	81.1	78.9
External general government debt	28.5	28.4	26.1	27.0
Domestic general government debt	54.4	56.0	55.1	51.9
General government debt incl. IMF obligations (% GDP)	85.3	87.6	83.6	82.0
General government and government guaranteed debt (incl. IMF; % GDP)	90.5	93.2	88.6	86.7
Monetary and credit				
Broad money (% change)	11.3	17.5	16.2	15.8
Private credit (% change)	11.9	3.0	11.5	16.0
Six-month treasury bill rate (%)	10.2	11.9	7.3	-
Balance of Payments				
Current account balance (% GDP)	(4.9)	(1.7)	(0.6)	(4.0)
Foreign Direct Investment (% GDP)	0.5	1.0	0.6	0.8
Gross reserves (in millions of U.S. dollars)	7,274	12,175	17,297	21,211
In months of next year's imports of goods and services	1.7	2.4	2.7	3.2
Total external debt (% GDP)	37.4	41.6	39.1	40.6
Exchange rate				
Real effective exchange rate (% change)	(15.1)	3.4	7.3	-

Source: IMF, Foundation Research, February 2022

Table 7: General Sales Taxation and Competitiveness in Pakistan

The current general sales tax (GST) system, with its cascading effect, undermines competitiveness and ease of doing business, biases production toward simple manufacturing activity, and discriminates against exporters and import-competing industries.

1. Pakistan is a federation with taxation powers shared between federal government and provinces. Under the current system, and as laid out in the Constitution, the sales tax base is fragmented with services subject to taxation at the provincial level, and goods at the federal level. As a result, taxpayers face different taxes across multiple jurisdictions, and in addition to FBR, they need to deal with four separate sales tax administrations—one in each province. The use of multijurisdictional inputs along the value chain means that the federal and provincial revenue authorities are interacting repeatedly in each transaction. For example, a good being sold (sales tax paid federally) can have services input taxes from multiple provinces that need to be credited, as well as sales tax paid on the purchase of any goods inputs. The current system makes this crediting incomplete. It has also led to disputes over base definition and coverage, causing problems of double taxation for businesses, as certain activities are jointly claimed by both the federal authority and provinces.

2. Cascading effect results in high export price. The fragmented GST system as it stands now has a cascading effect since there is no systemic mechanism to ensure that all tax paid on input can be credited against a final sale (the output tax). This results in the cumulative taxation of intermediate inputs of production and distorts the prices that producers face in buying and selling from one another. It therefore causes a significant divergence of nominal and effective tax rates in the price of final goods (Ahmad, 2011). Under the current system it is harder to generate full information on all aspects of the value chain, which is critical to eventually remove all taxation from exports. As a result, Pakistani exports carry unrecovered tax on their input, and exporters' prices are systemically higher than those of exporters in countries without the cascading effect of the GST system. This also contributes to a heavy reliance of the tax revenues on manufacturing, which is the main exporting sector of the economy. Manufacturing, which accounts for only 14 percent of GDP, represents 58 percent of total tax revenue (ADB, 2018).

3. The GST system creates an incentive for low value-added production, and hampers integration in the global value chains (GVC). The cascading GST system hampers the development of sophisticated manufacturing and accentuates incentives for low value-add manufacturing partly as a result of low competitiveness and to limit tax burden. As it gets unclear what the effective rates on inputs and outputs will be, relative prices across the value chain get distorted, which encourages inefficient production choices (e.g., switching from superior to inferior quality inputs). The higher cost of intermediate goods or services due to GST makes more costly to incorporate advanced technology into production and thus affecting productivity and competitiveness, discouraging integration into the global value chains (GVC). The end results of this, is that import competing sectors face a disadvantage with imported final goods. Export oriented industries are also heavily skewed to low value-added products, requiring few manufacturing stages. For example, textile exports (60 percent of total exports) are mainly comprised of simple knitwear, bed wear, cotton cloth, and readymade garments, while food exports (20 percent of total exports) are mostly made up of rice and fish. These low value-added and non-branded goods mean that Pakistani exporters operate in the most competitive segments in the international markets and with limited profitability.

Source: IMF, Foundation Research, Feb 2022

Important disclosures:

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If

Expected return >+10%	Outperform.
Expected return from -10% to +10%	Neutral.
Expected return <-10%	Underperform.