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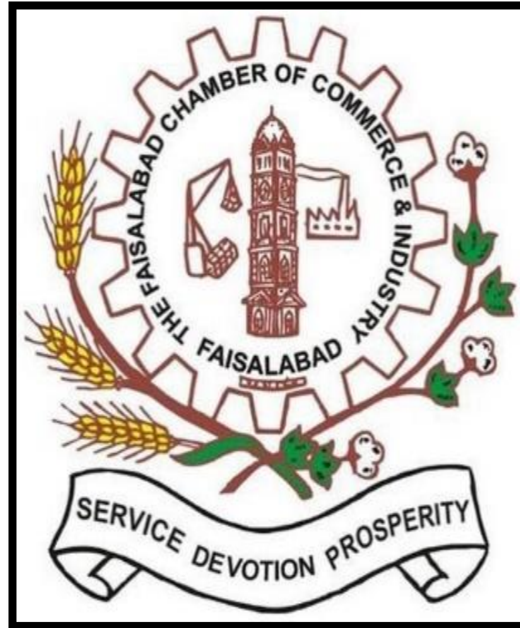

Title

In Pakistan, The World Bank

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In Pakistan, The World Bank

Update on the economy and the prospects

Pakistan has been efficiently deploying localized lockdowns to restrict the spread of COVID-19 since imposing a countrywide lockdown in response to the initial COVID-19 wave, enabling economic activity to mostly continue. The expansion of the national cash transfer program, a mass vaccination drive, accommodating macroeconomic policies, and banking sector support all served to alleviate the pandemic's negative impacts. As a result, after contracting by 1.0 percentage point in FY20, real GDP growth at constant factor prices rebounded to 5.6 percentage points in FY21.

Nonetheless, the economy's long-standing structural difficulties and poor productivity growth pose a threat to a long-term recovery. Strong aggregate demand pressures, owing in part to previously accommodative fiscal and monetary policies, combined with a persistently less favorable external environment for exports, have resulted in a record-high trade deficit, putting pressure on the rupee and the country's limited external buffers.

Indicators have mainly shown favorable economic momentum from July to December 2021 (H1 FY22). Private spending is expected to have improved as community mobility improves and official remittance inflows remain strong. Similarly, with high growth in machinery imports and government development spending, investment is likely to have grown. With the purchase of vaccines, government consumption increased significantly. Agricultural output, mostly rice and sugarcane, increased because of improved meteorological conditions. Similarly, growth in large-scale manufacturing increased to 7.5 percent year on year in H1 FY22, from 1.5 percent in H1 FY21., business and consumer confidence have been declining since June 2021 because of fears about rising inflation and interest rates.

Headline inflation increased to 9.8% y-o-y in H1 FY22, up from 8.6% in H1 FY21, thanks to higher global commodity prices and a weaker currency rate. Similarly, since September 2021, core inflation has been rising. As a result, the State Bank of Pakistan has been gradually unwinding

its expansionary monetary policy since September 2021, boosting the policy rate by 275 basis points (bps) and the cash reserve requirement for banks by 100 bps.

The current account deficit (CAD) increased to $9.0 billion in H1 FY22, up from $1.2 billion in H1 FY21, as imports increased by 54.4 percent, more than twice as much as exports increased by 27.3 percent. Remittances grew by double digits in H1 FY22, helping to finance the country's record-high trade imbalance. The financial account had net inflows of US $10.1 billion, fueled by the new IMF SDR allocation, Saudi Arabian short-term government deposits, and a July 2021 Eurobond issue. The government received US $2.1 billion in January and February through international sukuks and the IMF Extended Fund Facility (EFF). Despite these inflows, by March 25, 2022, foreign exchange reserves had decreased to US $13.5 billion, equivalent to 2.0 months of imports of goods and services. In the meantime, the rupee has devalued.

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Despite higher tax revenue due to higher imports, the budget deficit increased by 20.6 percent in the first half of FY22 due to increased spending on vaccine procurement, power sector arrears, and development projects. At the end of December 2021, public debt, including guaranteed debt, was 70.7 percent of GDP, up from 72.0 percent at the end of December 2020. To go along with the tighter monetary policy, the government passed a Supplementary Finance Bill in January 2022, eliminating tax exemptions and reducing federal development expenditure while maintaining social spending.

Because of the economic recovery and improving labour market conditions, poverty at the lower middle-income class poverty level of $3.20 PPP per day is expected to fall from 37.0 percent in FY20 to 34.0 percent in FY21. Inflationary pressures on food and energy are likely to erode households' actual buying power, disproportionately hurting poor and vulnerable households that

spend a larger percentage of their budget on these commodities. In February 2022, the government responded by introducing a targeted food subsidy program (Ehsaas Rashan Riyat).

Due to a large base effect, recent macroeconomic adjustment measures, and higher inflation, real GDP growth is expected to fall to 4.3 percent in FY22 and 4.0 percent in FY23. that, economic growth is expected to rebound to 4.2 percent in FY24, aided by structural changes to promote macroeconomic stability and the dissipation of global inflationary pressures. Inflation is expected to grow to 10.7% in FY22, but then decline over the next few years. Due to an increase in imports in FY22, the CAD is expected to rise to 4.4 percent of GDP in FY22. Imports are likely to be tamed largely in FY23 due to macroeconomic adjustment efforts and a weaker currency.

As changes to remove import tariffs and trade policy's anti-export bias gain traction, the CAD is forecast to shrink to 3.0% of GDP in FY24. The budget deficit (including grants) is expected to rise slightly to 6.2 percent of GDP in FY22 before gradually shrinking over time as revenue-raising initiatives such as GST harmonization and personal income tax reform take effect. In the short term, public debt as a percentage of GDP is expected to remain high, but gradually decline in the medium term. The projection is based on the IMF-EFF program remaining on track.

The macroeconomic risks are heavily skewed to the negative. They include a faster-than-expected tightening of global financial conditions; higher global energy costs; and the possibility of COVID-19-related travel restrictions being reinstated. Domestically, political squabbles and policy reversals can result in long-term macroeconomic imbalances.

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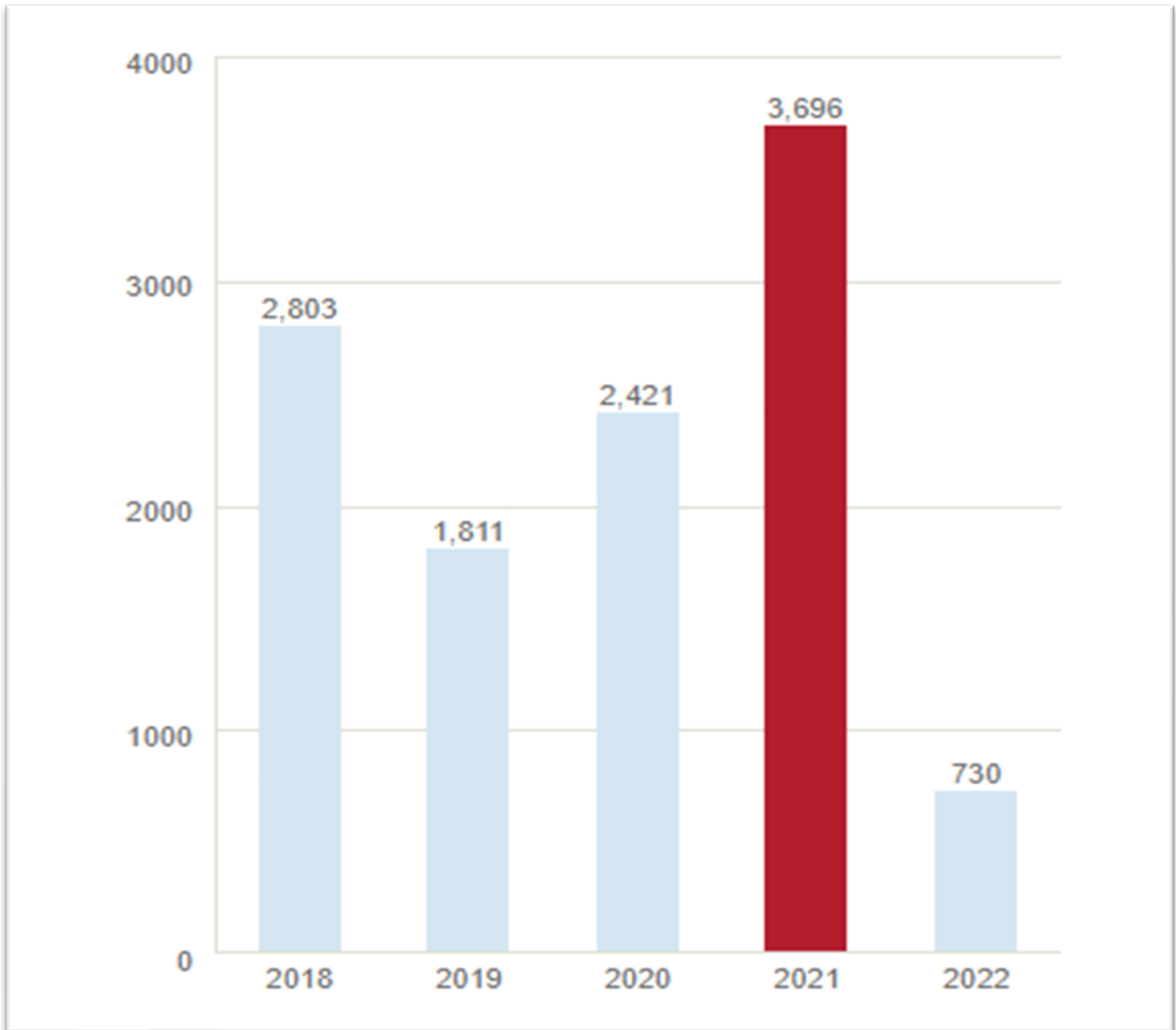
Commitments by Fiscal Year in Pakistan (in millions of dollars)



IBRD and IDA obligations are included in the totals.

Pakistan’s Country Partnership Strategy for Final Years 2015 to 2019 (English)

Pakistan's country partnership strategy (CPS) is designed to assist Pakistan in addressing the most challenging but potentially transformative sectors to achieve the dual goals of poverty reduction and shared prosperity. The CPS's four strategic pillars and results areas are based on the government's 4Es framework: energy, economy, extremism, and education, as well as the proposed Vision 2025 priorities of transforming the energy sector, supporting private sector development, reaching out to the underserved, neglected, and poor, and accelerating service improvements.

This cross-cutting program focuses on energy and trade, including critical building blocks of an integrated regional electricity market in South Asia with power transmission links to Central Asia and India; sub-regional Punjab (Pakistan-India) collaboration; and other opportunities to capture the potential of cross-border trade between Pakistan and its neighboring countries, which are interwoven with the four results areas. Sustained regional cooperation has the potential to add 2% to Pakistan's annual GDP, assist in the development of viable transit routes, and contribute to regional stability.