Chapter 1

GROWTH AND INVESTMENT

COVID-19 is having a devastating impact on Pakistan's economy; however, to ascertain the true extent, it is important to take stock of economic performance of Pre-COVID-19, essentially for two reasons; to explore economic outcomes in relation to the policy environment adopted and second, what trajectory of economic recovery we expect post COVID-19 and will it take the "V shape" for recovery as most of the economic experts claim. The COVID-19 was declared a pandemic by WHO on March 11, 2020. The first case of the novel Coronavirus in Pakistan was confirmed on February 26, 2020. On March 13, the government started to move towards the closure of certain economic and social activities. Both the national and international economic scenarios have flagged by then. Thus, for true description of the performance of the economy, we need to compare the performance of economy pre COVID-19 and Post COVID-19.

Pre-COVID-19, FY2020 showed dedicated efforts of the government for addressing structural issues that caused macroeconomic imbalances, the result of which was also seen in the latest macro-economic indicators. The government not only took some immediate steps on the fiscal, monetary and exchange rate side for stabilization but also implemented long-run measures for sustainable and inclusive growth in the future. Economic reforms program and implementation was acknowledged by the IFIs. In December 2019, a successful IMF review was completed, declaring that Pakistan's program was on track and bearing fruit. IMF was of the view that decisive policy implementation by the Pakistani authorities is helping to preserve economic stability which would put the economy on the path of sustainable growth. Empirical literature shows, stabilization is considered as a pre-step towards long-run sustainable growth. International rating agencies S & P and Fitch appreciated government efforts and predicted Stable Outlook while Moody's Investor Services upgraded Pakistan's sovereign outlook to Stable, mainly due to improvement in the balance of payments dynamics hence supported policy adjustments.

The pre-COVID-19 economic recovery was also supported by macroeconomic indicators. On the external side, the decline in current account deficit, buildup of foreign reserves, stable exchange rate, etc., were the gains of prudent policy measures. From July-Apr FY2020, Current Account Deficit reduced by 70.8 percent to \$ 3.3 billion (1.5 percent of GDP) against \$ 11.4 billion (4.8 percent of GDP) in the corresponding period last year. It was mainly due to a 29.5 percent contraction in the trade deficit and 5.5 percent growth in workers' remittances. On the capital account side, FDI is considered as a means of complementing domestic investment, and to get external benefits, FDI is mostly dependent on the country's ease of doing business. Pakistan was among 'top ten best improvers' in World Bank's Ease of Doing Business Index 2020, jumping up 28 places on the index and clinching the 108th position, out of total 190 economies. This helped in attracting foreign investors, during Jul-March FY2020 where Foreign direct investment increased by 137.3 percent and reached $ 2.1 billion as compared to $ 0.9 billion last year. Government plans to improve the policy environment further besides working on "ease of doing business" to attract more potential FDI.

On the fiscal side, there were significant improvements in all major fiscal indicators and the trend continued till March 2020, implying that the fiscal consolidation was on track. During July-March, FY2020, fiscal deficit reduced to 4.0 percent of GDP against the deficit of 5.1 percent in the same period of FY2019. Primary balance has witnessed a remarkable turnaround as it has posted a surplus of Rs 193.5 billion during July-March, FY2020 against the deficit of Rs 463.3 billion last year. Improved performance is largely attributable to a significant increase in provincial surplus and non-tax revenues. On the flip side, although the FBR tax collection remained lower than the target, however, 13.3 percent growth was recorded during July-March FY2020 as compared to the same period last year. The FBR's less than target revenue collection is still defendable as it occurred mainly due to significant contraction in imports thereby decreasing collection of customs duties and other taxes at the import stage by a significant amount.

Stock market performance is a reflection of the state of the economy. After witnessing a dip in the first quarter of FY2020, the KSE-100 index was on a recovery path. The index closed at 40,735 on 31st December by gaining 6,739 points in the first six months of CFY. The bullish trend can be attributed to various factors like improvement in ease of doing business ranking, timely release of PSDP funds, stable exchange rate, and improvement both in political outlook and macro indicators. It is worth mentioning that in December 2019, the overall business confidence[1] turned positive (after remaining in the negative zone for the last four waves (surveys) to 52 from 48 in October 2019, which implied that pessimistic views of the business community about the economy were improving.

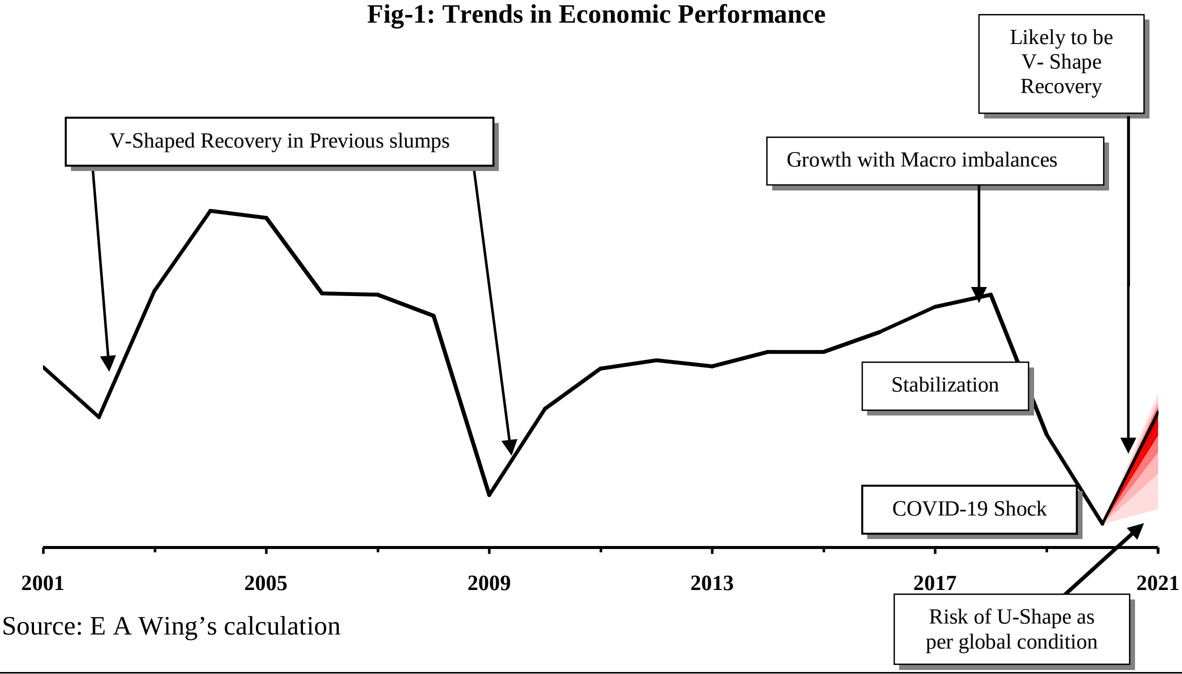
Inflation remained worrisome area as moving towards market value-based exchange rate adjustments and energy prices adjustments led to a rising trend on YoY basis even till January 2020. The government vigilantly took not only policy and administrative measures to decelerate inflation but also provided relief measures to facilitate consumers. The government ensured smooth supply especially for food items and legalized punishment and fine imposition against hoarding. The efforts of government started materializing with decline in national CPI in February 2020.

In brief, the economy of Pakistan was moving towards stabilization. Business confidence was recovering and prices have started settling down, twin deficits were under control and economy was gradually moving towards sustainable growth when the shock of the COVID-19 outbreak hit the economy. And suddenly, the whole paradigm of Pakistan's economy changed in most unexpected ways, which no one could have anticipated. COVID-19 challenged the political, social, economic, and financial structures of the whole world including developing countries like Pakistan. Data shows (Fig.1) that Pakistan's

[1]SBP is conducting Business Confidence Survey in collaboration with Institute of Business Administration which is considered as leading indicator for economic activity as these surveys are particularly suitable for monitoring and forecasting the short term changes in the economy.

economy bounces back quickly after recessions and there is a strong likelihood of a fast V-type recovery given the strong and timely policy measures taken by the Government. Further with temporary shutdown, it is expected that will be no or little loss of real capacity. Thus, keeping in view the productive, economic and financial structures of the economy, it is expected that both consumer and business confidence will recover soon.

Fig-1: Trends in Economic Performance



Source: E A Wing's calculation

COVID-19: The Global Perspective

The COVID-19 has been termed as a severe acute respiratory syndrome. The outbreak originated in Wuhan, Hubei, China, in December 2019 and spread throughout the globe, affecting 213 countries and territories by this time. Till the writing of this report, about 5 million individuals have tested positive worldwide, and around 323,000 have died. In many countries, the infection curve has still not flattened. From December 2019 till May 2020, the world has changed dramatically. COVID-19 became a real disaster as it has caused tragic loss of large number of human lives. Considering its impact on public health, almost all countries implemented necessary quarantines and social distancing practices to contain the pandemic. Thus, the world has been put in an Extensive Lockdown, never seen before in history. The magnitude and speed of collapse in the normal social and economic activities that has followed is unlike anything experienced in our lifetimes. Thus, by this time, a medical crisis has turned into an economic crisis.

In reaction to COVID-19 outbreak, all major economies reacted with flight cancellations, panic buying, and strict quarantine measures. Thus, the immediate effect of lockdown was essentially stopping activities in contact-intensive businesses like restaurants, gyms, hotels, etc. A negative supply shock happened due to disruption in supply chains globally. But this supply shock is of a special nature as it affected different sectors asymmetrically. From a spending perspective, consumers redirected their spending towards substitutes for the goods and services. However, it is argued that if the majority of consumers start decreasing their overall spending, recession can spread widely. Thus, a demand-driven recession can be expected if there is a massive fall in spending or there is a persistent drop in productivity, growth expectations for the future will be greatly compromised.

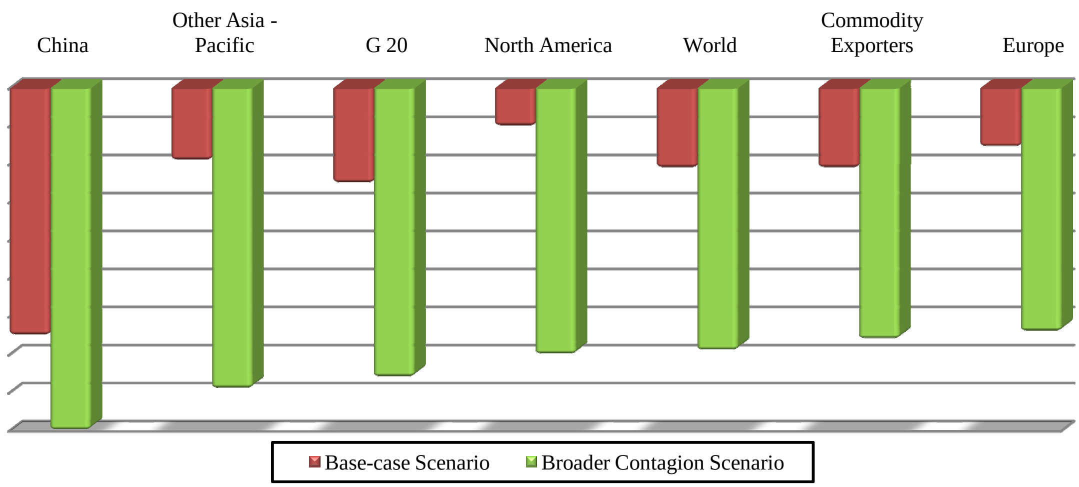
Thus, IFIs as well as rating agencies have downgraded their global growth forecasts. On the other hand, based on epidemiological predictions in April 2020, the IMF has predicted a V-Shaped recovery in 2021 on the back of the structures which are still in place and it is considered a temporary halt in economic activities. Table-1 presents the comparison of the forecast made by IMF in Oct 2019 (Pre COVID-19) and in April 2020 (COVID-19)

Table-1: World Economic Outlook Growth Projection

Real GDP Growth Rates (%)	**WEO, Oct 2019**			**WEO, April 2020**			
	Pre-COVID-19			**COVID-19**			
Group / Country Name	**2019**	**2020**	**Expectation**	**2019**	**2020**	**2021**	**Expectation**
World	3.0	3.4		2.9	-3.0	5.8	
Euro area	1.2	1.4		1.2	-7.5	4.7	
United States	2.4	2.1		2.3	-5.9	4.7	
Japan	0.9	0.5		0.7	-5.2	3	
Other Advanced Economies	1.5	1.8		1.6	-5.2	4.4	
Emerging Market and Developing Economies	3.9	4.6		3.7	-1	6.6	
ASEAN							
Indonesia	5.0	5.1		5.0	0.5	8.2	
Thailand	2.9	3.0		2.4	-6.7	6.1	
Malaysia	4.5	4.4		4.3	-1.7	9.0	
Philippines	5.7	6.2		5.9	0.6	7.6	
SOUTH ASIA							
India	6.1	7.0		4.2	1.9	7.4	
Bangladesh	7.8	7.4		7.9	2.0	9.5	
Sri Lanka	2.7	3.5		2.3	-0.5	4.2	
Pakistan	3.3	2.4		3.3	-1.5	2	
MIDDLE EAST							
Saudi Arabia	0.2	2.2		0.3	-2.3	2.9	
Kuwait	0.6	3.1		0.7	-1.1	3.4	
Islamic Republic of Iran	-9.5	0.0		-7.6	-6.0	3.1	
United Arab Emirates	1.6	2.5		1.3	-3.5	3.3	
Turkey	0.2	3.0		0.9	-5.0	5.0	
AFRICA							
Morocco	2.7	3.7		2.2	-3.7	4.8	
South Africa	0.7	1.1		0.2	-5.8	4	
Kenya	5.6	6.0		5.6	1.0	6.1	
Tanzania	5.2	5.7		6.3	2.0	4.6	
Source: International Monetary Fund, World Economic Outlook Database, Oct 2019 & April 2020							

However, major uncertainties still surround almost every aspect. Starting from the uncertainties of prevalence and the capacity of healthcare systems to meet this extraordinary challenge. There is also uncertainty about the duration and effectiveness of social distancing, market lockdowns, and other mitigation and containment strategies. Keeping this in view, IMF is expecting that the global economic outlook will worsen compared to its forecasts made in April 2020. According to the United Nations Conference on Trade and Development press released in March 2020, "COVID-19" shock will cause a recession in some countries and depress global annual growth this year to below 2.5 percent, the recessionary threshold for the world economy. OECD Interim Economic Assessment indicates that growth prospects are very uncertain and with the recent marked deterioration in global financial conditions and heightened uncertainty, this will depress global GDP growth (Fig-2)

Fig-2: Change in GDP growth



Source: OECD Interim Economic Assessment, Coronavirus: The world economy at risk, 2 March 2020

On May 15, 2020, the Asian Development Bank (ADB) released the report which highlighted that the global economy could suffer between $5.8 trillion and $8.8 trillion in losses—equivalent to 6.4 percent to 9.7 percent of global GDP—as a result of the COVID-19 pandemic.

Governments and central banks around the world are showing clear intentions of doing everything possible to mitigate adverse economic effects. The immediate concern of economic policy is to protect the livelihood of the people working in sectors which were significantly immediately affected by lockdown. But there is no doubt, that COVID-19 will raise unemployment and poverty regardless of the policy responses. As an example, in the US, the unemployment rate stood at 3.5 percent in February 2020, lowest rate in the past 67 years, the latest figures of the Bureau of Labor Statistics USA showed it has risen to 14.7 percent in the span of few months, the highest since the Great Depression. A recent fall in oil prices will further add pressure on global growth and may lead to more people losing jobs in oil-producing countries as well. The UN's work agency warns that hundreds of millions of people could be left without work due to the impact of COVID-19. Thus, the growth in the global remittances flows is expected to fall.

In the context of Pakistan, COVID-19 may have a double-edged impact; through the trade channel and through the remittances. Remittances may fall significantly due to lay-offs of Pakistani workers abroad due to economic slowdown internationally. Although there was a 1 percent increase in workers remittances on a YoY basis in April 2020 and for July-April FY2020, there is a 5.5 percent growth compared to the same period last year. But there is not only a risk of decrease in workers' remittances in the future but also more challenging will be the influx of returning migrant workers due to job losses. Similar to global conditions, within Pakistan increase in unemployment is inevitable. According to the report prepared by Sub-committee of the National Coordination Committee for COVID-19 on Economic Analysis, 72 percent of Pakistan's non-agriculture workforce is engaged in the informal sector, with no social security or insurance cover and it may take a major hit. The estimated size of informal employment in non-agriculture sector is around 27 million, with only food, pharmaceuticals, and few services still functional, these employees will be worst affected. As out of 27 million, around 86 percent are engaged in wholesale and retail trade, transport, construction, manufacturing, hotels & restaurants sector which are severely crippled due to the lockdown situation. According to HIES 2015-16, Pakistan has 1.93 average earners per household. With, these breadwinners of their household out of job or at risk of losing one and with an average household size of 6.7 persons, total affected people will be over 81 million people out of a total population of 220 million, through this channel only.

World trade has dipped into negative territory only three times between WWII to 2008. However, in 2008, the steepest drop in world trade was observed since the Great Depression. There is no doubt that global trade is facilitated through worldwide transport networks and historically these were also responsible for the transmission of diseases. Thus, recognizing transportation being an important vector of transmission, the sector was one of the first to face significant restrictions due to COVID-19 hit. The restrictions have been extended to seaborne transportation also, which carries 80 percent of world merchandise trade. These disruptions will damage vital supply chains and add to further disruptions that the manufacturing sector is already experiencing. Thus, the outlook for international trade is becoming bleak. Further due to the closure of businesses, the depressed demand for fresh imports is also a major reason besides less transportation of goods. Due to COVID-19, the 2020 trade collapse will be big, sudden, synchronized, and broad. In 2008, there was a demand-side shock but now on top of that, we have massive, supply-side shocks across most sectors of major economies. Taking just the US, China, Japan, Germany, Britain, France, and Italy, the stricken economies account for 60 percent of world 'supply and demand' and 65 percent of world manufacturing. Global supply chain disruption has further exacerbated the economic woes across the globe.

Pakistan also started experiencing this trade shock. According to Pakistan Bureau of Statistics, exports remained $ 957 million in April 2020 which in dollar terms has declined by 54 percent compared to April 2019 and declined by 47 percent compared to March 2020. Likewise, imports also declined by 32 percent compared to April 2019 and declined by 3 percent compared to March 2020. The decline of import bill is related to fall in international oil prices, however, a decrease in capital goods, which constitute a major portion in imports, will add to disruptions in the supply chain of manufacturing both for exports and domestic production. If the situation persists, then, there is a high risk of a substantial reduction in trade volumes in the coming months.

The most important and massive uncertainty created by COVID-19 is regarding global capital flows. Within fifteen days, the United Nations Conference on Trade and Development (UNCTAD) revised its forecasts about the effects of COVID-19 on global FDI flows. On March 8, 2020, there was a conservative drop from -5 to -15 percent but on March 26, 2020, expected a contraction from -30 to -40 percent in global FDI.

In Pakistan, FDI volume has persisted between $ 2 – 2.5 billion for the last several years. Realizing the importance of FDI, the government had made all efforts to attract FDI. Till March 2020, data on FDI was encouraging. During Jul-March FY2020, Foreign direct investment increased by 137.3 percent and reached $ 2.1 billion compared to $ 0.9 billion last year. However, the risk of drying up of foreign investment hangs heavy but with the silver lining that the measures taken by the government to attract foreign investment and providing a business-friendly environment especially in SEZs may help in building foreign investors' confidence. Further, Pakistan has also made significant strides on “Ease of Doing Business” which would also bring in the positive results. Having said that, still, the policy environment needs to improve for realizing these goals.

Global financial markets were the first to indicate the adverse impact of COVID-19. Further, in comparison with other contagious outbreaks since 1985 (like Ebola, SARS, H1N1), COVID-19 hit the stock market the hardest. It also put immense pressure on Pakistan’s financial markets. Between February 26th (the date when first COVID-19 case was reported in Pakistan) and March 25th, Pakistan’s KSE-100 index benchmark dived 30.33 percent and Rs 1,913.89 billion were wiped out of the Market Capitalization. Rupee depreciated by 7.5 percent against a strengthened dollar between February 26 (Rs 154.25=1$) and Mar 31 (Rs 166.71=1$), which severely constrained spending power. In the debt market, foreign investors took out over US$ 1.7 billion from T-bill investments in March 2020.

To facilitate the capital markets, the SECP introduced a number of measures (for e.g. increasing the duration of index-based market halts etc.). These measures, along with government’s stimulus package and 525 basis points cut in the SBP’s policy rate, helped the stock market to regain most of its lost value.

On 21st May, 2020, KSE-100 closed at 33,836.6 (up by 24.2 percent compared to March 25th value) and market capitalization closed at Rs 6,471.6 billion, gaining Rs 1,091.4 billion since March 25th.

The stock market has shown stability in April & May. In May 2020, the KSE-100 index oscillated around 34000 points and is predicted to improve further in the coming months. The exchange rate has also stabilized and it is expected that Pakistan’s stock and debt market will witness an inflow of foreign investments, again.

Affected countries, both developed and developing, have taken swift fiscal measures for dampening the shock to the most exposed households and businesses, including cash transfers, wage subsidies, tax relief, and extension or postponements of debt servicing payments. These fiscal measures are largely, targeted to the most vulnerable sectors of the economy, and are designed to be temporary.

Policy Response in Pakistan

To prevent the negative supply shock on the economy triggered by the COVID-19 and severely affecting employment and productivity, drastic policy interventions for both monetary and fiscal policies were needed. On the fiscal side, the government announced a fiscal stimulus package of Rs 1.24 trillion while the State Bank of Pakistan provided liquidity support to households and businesses to help them through the ensuing temporary phase of economic disruption. Further, the policy rate was cut by 525 basis point in total till May 15, 2020, bringing it down to 8 percent from a peak of more than 13 percent.

Box-I: Fiscal & Monetary Stimulus

Following the lockdown in several economic activities, workers and small business suffered from severe income losses. This resulted in both supply side and consequently fall in aggregate demand as well. Both monetary and fiscal policies response were needed to mitigate this economic fallout and to support economic system as a whole.

Fiscal Stimulus

The government undertook immediate measures as soon as the threats of pandemic became evident. The main aim was a speedy response while remaining flexible and being prepared for adjustments.

- On 24th March, the Prime Minister announced a fiscal stimulus package of Rs 1.24 trillion (around $8 billion) for emergency response, relief to citizens, and support to businesses and economy. This historic relief package was subsequently supplemented by a package for construction sector with the aim to boost business activity to generate employment.
- For emergency health response, Rs 75 billion were made available for procurement of medical supplies, equipment, incentives to medical workers and provision of quarantine facilities. In addition, the government established a Rs 100 billion emergency fund to cater for any eventuality. Taxes were also waived on import of related medical supplies. Withholding taxes and custom duties were waived on certain food items and reduced on food items supplied through Utility Stores Corporation.
- As the pandemic is projected to result in increased unemployment due to either closure of businesses or reduced business activity, Rs 200 billion are earmarked for daily wage workers and employees who have lost their jobs. A registration portal has been developed to screen laid off workers and employees. In addition, Rs 12000 are being distributed to around 12 million families all over Pakistan through *Ehsaas* program. For this purpose, Rs 150 billion (Rs 144 billion for Ehsaas Emergency Cash Program & Rs 6 billion for Panagahs) have been provided. As on 03-06-2020, Rs 117.0 billion have been disbursed to 9.6 million beneficiaries under Ehsaas Emergency Cash Program.
- To provide relief to general public, prices of petrol were reduced. This is an ongoing policy initiative under which the government will continue to pass on reduction in international oil prices to the general public. Rs 70 billion have been provided for this purpose.
- As unemployment and poverty are seen to increase due to the pandemic, the government provided a support package to lower prices of essential food items available through Utility Stores. Every day consumable items are now available at a much cheaper rate than in the markets.
- In order to support low income families, the government announced relief in payment of electricity and gas bills. All low-income electricity and gas consumers have been allowed to pay their bills after three months. Rs 100 billion have been earmarked for this purpose.
- To facilitate farmers, the government announced immediate procurement of wheat at prescribed support prices. Rs 280 billion have been provided for this purpose. Procurement of wheat across Pakistan is on-going and its target of 8.2 million tons will soon be met.
- Exporters in the country faced financial issues due to tax-refund claims. The government has released Rs 20 billion against duty drawback of taxes and drawback of local taxes and levies to exporters. In addition,

Rs 70 billion of tax refunds through Federal Board of Revenue have been cleared.

- For small and medium sized businesses and industries, which are most hit by the pandemic, the government announced a package in the last week of April 2020 that included payment of electricity bills. Small businesses having a commercial connection of less than five kilowatt and industrial consumers less than 70 kilowatts can benefit from the initiative, under which the government will pay electricity bills for the months of May, June and, July. Besides, some 3.5 million people running small businesses i.e. tailor shops, small markets, and industrial units will take advantage of this initiative. Rs 100 billion have been allocated for this purpose.

Monetary Stimulus

The recent MPC held on May 15, 2020, highlighted challenges for monetary policy due to disruption of economic activity. Policy rate was reduced further 100 basis points to 8 percent. Besides this there are other relief packages announced by SBP as well.

- In order to support sustainable economic growth especially in the backdrop of challenges being faced by the industry in post-pandemic scenario, SBP has issued **"Temporary Economic Refinance Facility" (TERF)**. All sectors except power sector can avail financing under this facility at a concessionary rate of 7 percent p.a. up to 10 years. Financing can be availed for purchase of new imported and locally manufactured plant & machinery with maximum loan limit of Rs 5 billion per project.
- SBP has launched a **Refinance Facility for Combating COVID-19 (RFCC)** for hospitals & medical centers to develop their capacity for the treatment of infected patients of COVID 19. All hospitals and medical centers registered with respective provincial/federal agencies/commissions engaged in controlling and eradication of COVID-19 will be eligible to avail up to Rs 500 million financing under the facility. Facility will be available at a concessionary rate of 3 percent per annum for 5 years including grace period of up to 6 months. This facility can be used for purchase of imported and locally manufactured medical equipment and creation of isolation wards.
- Moreover, SBP has launched temporary **Refinance Scheme for Payment of Wages and Salaries to the Workers and Employees of the Business Concerns**. Concessional loans at 5 percent per annum will be available to finance 3 months of wages i.e. April to June 2020. Loan tenor is 2 years including six months grace period. The banks have been asked to give preference to businesses that are labor intensive and affected by Corona virus.
- **Regulatory Measures in the wake of COVID-19 Pandemic:** Given the pivotal role of financial sector in providing services to the general public and particularly the businesses, SBP after consultation with stakeholders has instructed banks to take specific measures to provide their services seamlessly taking due care of reducing the risk exposure amid Corona virus. These measures aim at reducing the need for visiting bank branches or the ATMs and to promote use of Digital Payment Services such as internet banking, mobile phone banking etc. These measures include:
    a. **Waiving Charges for Online Fund Transfers**
    b. **Efficient Clearing of Cheques**
    c. **Strengthening Cyber Resilience of Financial Institutions**
- SBP has reduced the capital conservation buffer by 100 basis points to 1.5 percent;
- It has increased the regulatory limit on extension of credit to SMEs by 44 percent from Rs 125 million to Rs 180 million;
- Relaxation of the debt burden ratio for consumer loans from 50 percent to 60 percent will accommodate almost 2.3 million individuals;
- Allowing banks to defer clients' payment of principal on loan obligations by one year; and
- Relaxation of regulatory criteria for restructured/rescheduled loans for borrowers who require relief beyond the extension of principal repayment for one year
- Margin call requirement of 30 percent vis-a-vis banks' financing against listed shares has been

significantly reduced to 10 percent

- Banks/DFIs have been advised to suspend the dividend distribution for the next two quarters which will further increase the resilience of banking sector and improve their ability to provide much needed credit support to the real economy.

As the new fiscal year FY2020 began, the economy started to witness a remarkable turnaround that confirmed that the government had taken appropriate policy action to address the macroeconomic imbalances. However, like the whole world, since March 2020, Pakistan's economy started being affected due to COVID-19 outbreak through various channels like declines in domestic & global demand. Thus, the downturn in economic activities started in March has overshadowed the better performance occurred in the first three quarters of FY2020

Saving – Investment Gap

Historically, saving - investment gap always led to "borrowed growth" as it was consumption-driven growth. Such growth is not sustainable and macro-imbalances recur. The government from its start had taken strict measures to reduce the gap. Table-2 describes the structure of Savings and Investment along with Consumption (As Percent of GDP).

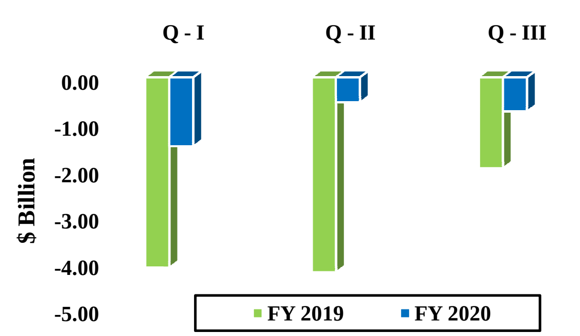
Table 2: Structure of Savings and Investment (As Percent of GDP)

Sectors	2015-16	2016-17	2017-18	2018-19	2019-20
As percent of GDP(mp)			F	R	P
Total Consumption	91.3	93.2	93.8	94.6	91.6
- Private Consumption Expenditure	80.0	81.9	82.0	82.9	78.5
- General Government Expenditure	11.3	11.3	11.7	11.7	13.1
Total Investment	15.7	16.2	17.3	15.6	15.4
Gross Fixed Capital Formation	14.1	14.6	15.7	14.0	13.8
- Private	10.3	10.1	10.5	10.3	10.0
- Public including General Public	3.8	4.5	5.2	3.7	3.8
Change in Inventories	1.6	1.6	1.6	1.6	1.6
National Saving	13.9	12.0	11.3	10.8	13.9
Domestic Saving	7.8	6.5	5.9	4.1	6.8
Foreign Saving	1.7	4.1	6.1	4.8	1.5

Source: EA Wing Calculation, based on PBS data

The decrease in Foreign Saving implies that the impact of the removal of the artificial but costly stability in exchange rates and implementation of the market value-based exchange rate regime became successful. Current Account Deficit was brought down to $ 13.4 billion in FY2019 from $ 19.2 billion in FY2018 and the trend continued in FY2020 as well. Quarter-wise performance is shown in Fig-3.

Fig-3: Quarter-wise performance of Saving-Investment Gap



Source: State Bank of Pakistan

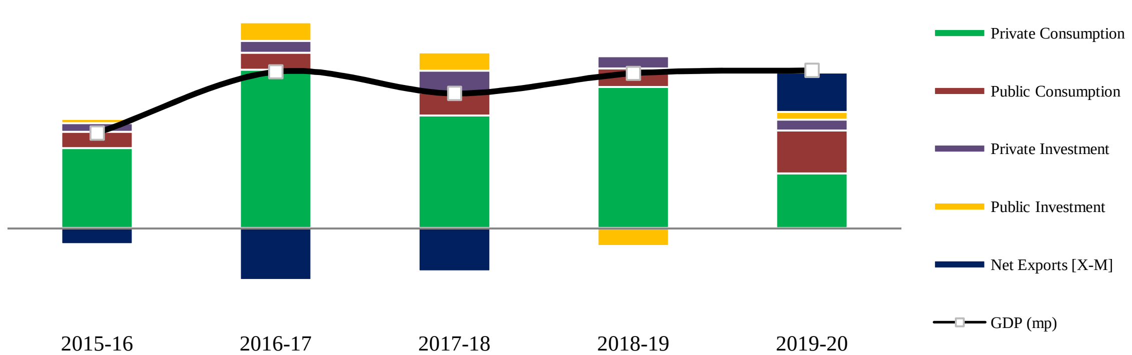
Thus, macroeconomic stabilization measures undertaken by the government over the past year resulted in a significant reduction in Saving-Investment Gap which was mainly driven by a reduction in the trade deficit and an increase in workers 'remittances. A change in any part of the saving and investment identity suggests that if the government budget deficit changes, then either private savings, private investment in physical capital, or the trade balance—or some combination of the three—must change as well. Therefore, it is argued that rising budget deficit may result in a rise in the trade deficit. It is mentionable that owing to government better public finance management the fiscal deficit remained contained in the first three-quarters of FY2020. The fiscal deficit has substantially reduced to 4 percent of GDP during July-March FY2020 compare 5.1 percent of GDP in the same period last year.

Aggregate Demand Analysis

Historically, Private Consumption has significantly contributed to Pakistan's economic growth. In FY2020, nominal private consumption grew by 4.1 percent, compared to 9.9 percent growth in nominal GDP. In percentage of GDP private consumption declined from 82.9 percent in FY2019 to 78.5 percent in FY2020. This was the result of both the stabilization policy and the lockdown. One of the objectives of the stabilization policy was to bring domestic expenditures in line with domestic income creation. The reduction of the share of private consumption has allowed reducing significantly the negative share of net exports, which contributed to the drastic reduction in the trade deficit. This pattern was even enhanced by the lockdown. The reason being that in Pakistan 72 percent of non-agriculture the workforce is engaged in the informal sector. Thus, informal employment is around 27 million. Out of 27 million, around 86 percent are engaged in wholesale and retail trade, transport, construction, manufacturing, hotels & restaurants sector. Air and rail transport remained completely shut. Only food, pharmaceuticals, and a few other services remained functional. Still, the majority of daily wagers suffered.

The government realizing the significance of loss to the vulnerable made provision of cash transfers to the vulnerable section of the society. Rs 200 billion were earmarked for daily wage workers and employees who have lost their jobs. It is expected that the fiscal stimulus package of Rs 1.24 trillion (around $8 billion) will provide relief to citizens, and support the businesses. Further, the relief package for the construction sector will also boost business activity and will generate employment. Government consumption supported GDP growth. Its share in GDP increased to 13.1 percent in FY2020, up from 11.7 percent in the previous year. Figure-4 represent the component-wise point contribution to GDP (MP) growth.

Fig-4: Component-wise Point Contribution to GDP (MP) growth



Source: Pakistan Bureau of Statistics

The trend structure of point contribution of determinants to GDP growth is presented in the Table-3.

Table-3: Point Contribution of Determinants to GDP growth

Flows (Point Contribution)	2015-16	2016-17	2017-18	2018-19	2019-20
			F	R	P
Private Consumption	5.01	9.91	7.05	8.84	3.43
Public Consumption	1.01	1.07	1.43	1.16	2.69
Total Consumption [C]	**6.02**	**10.98**	**8.48**	**10.00**	**6.12**
Gross Fixed Investment	0.82	1.89	2.52	-0.37	1.16
Private Investment	0.56	0.73	1.38	0.75	0.67
Public Investment	0.26	1.15	1.14	-1.12	0.49
Changes in Stock	0.10	0.16	0.14	0.16	0.16
Total Investment [I]	**0.91**	**2.05**	**2.66**	**-0.22**	**1.32**
Exports (Goods & Services) [X]	-0.91	-0.08	1.47	2.13	0.41
Imports (Goods & Services) [M]	0.07	3.16	4.17	2.22	-2.04
Net Exports [X-M]	**-0.99**	**-3.24**	**-2.70**	**-0.09**	**2.45**
Aggregate Demand [C + I + X]	**6.02**	**12.95**	**12.61**	**11.91**	**7.85**
Domestic Demand [C + I]	**6.94**	**13.03**	**11.14**	**9.78**	**7.44**
GDP (mp)	**5.95**	**9.79**	**8.44**	**9.69**	**9.89**

Source: Pakistan Bureau of Statistics

Last year, removing artificial stability in the interest rate and exchange rates for implementing stabilization measures, made contraction to public and private investments. The same trend was seen this year as well. In FY2020, Private Investment as a percentage of GDP dropped to 9.98 percent from 10.29 percent in FY2019 while Public including General Government investment shown improvement as it remained 3.8 percent compared to 3.7 percent last year. In value terms Public including General Government investment grew by 13.2 percent in FY2020, slightly higher than the nominal GDP growth.

According to Pakistan Bureau of Statistics, provisional estimates of Gross Fixed Capital Formation (GFCF) stands at Rs 5,761.0 billion in FY2020 and has increased by 8.3 percent compared to FY2019. In the private sector, during FY2020, GFCF is estimated at Rs 4,162.6 billion as against Rs 3,908.3 billion of FY2019 with an increase of 6.5 percent. There was a decline of 10.9 percent in the Public Sector investments as it is estimated at Rs 458.1 billion against Rs 514.2 billion during FY2019, while, the overall provisional GFCF in the General Government Services for the year FY2020 has been estimated at Rs 1,140.3 billion with increase of 27 percent over the revised estimates of Rs 897.8 billion during FY2019.

In the private sector, the estimates of GFCF in agriculture the sector stands at Rs 1,258.2 billion as against Rs 1,164.5 billion in FY2019 with an increase of 8.0 percent because of an increase in imported agriculture machinery and value of stock in the livestock sub-sector while the GFCF in mining and quarrying industry during FY2020 has been estimated at Rs 55.1 billion as against Rs 35.1 billion in FY2019 registering a growth of 56.8 percent.

According to Pakistan Bureau of Statistics, the GFCF for private large scale manufacturing sector for the year FY2020 is estimated at Rs 569.4 billion against Rs 599.5 billion during FY2019 showing a negative growth of 5.0 percent based on data available from all sources

The conservative reporting of provisional capital formation by private companies in the main the reason behind this decline.

There was an increase of 6.3 percent in GFCF in Electricity Generation & Distribution and Gas Distribution sector in FY2020 compared to FY2019 mainly because of higher expenditure reported by IPPs, while GFCF in construction industry, wholesale & retail trade industry and Transport & Communication sector posted a growth of 20.6 percent, 7.1 and 5.0 percent respectively.

Regarding, Public Sector Enterprises major positive contributors are Manufacturing (from Rs 1.8 billion in 2018-19 to 9.2 billion in 2019-20 owing to Pak Arab Refinery), Construction (40.9 percent), Transport & Communication (increased from Rs 66.8 billion in 2018-19 to 144.5 2019-20 due to higher investment in Post Offices & PTCL, Port Qasim, Civil Aviation, and Highway Authorities) and Finance & Insurance (increased by 37.4 percent from Rs 7.8 billion in 2018-19 to 10.7 billion. in 2019-20 due to E0BI). However, the negative contribution i.e. 34.6 percent has been observed in Electricity Generation & Distribution and Gas Distribution, which has declined from Rs 418.5 billion to Rs 273.7 billion mainly because of WAPDA and Companies (From Rs 391 .5 to 241.3 billion). The GFCF related expenditures in Railways have also declined by 66.7 percent from Rs 14.6 billion to Rs 4.9 billion in FY2020 as compared to FY2019.

Although, estimates of GFCF in the General Government sector are based on budgetary data of federal, provincial, and district governments. The budgeted data is used in the first year of reporting which is subject to changes on the basis of actual and reconciled expenditure by various tiers of government in the subsequent year. GFCF related expenditure for the Federal government has been estimated at Rs 381.4 billion with growth of 7.8 percent over the previous year's estimates of Rs 353.7 billion. Similarly, GFCF related expenditure by Provincial Governments has increased by 32.1 percent from Rs 463.9 billion to Rs 613.0 billion due to an increase in development outlays of Punjab (from Rs 155.5 billion to Rs 209.4 billion), Sindh (from Rs 176.5 billion to Rs 265.0 billion) and Balochistan (from Rs 42.5 billion to Rs 50.6 billion). The estimated development expenditures of Khyber Pakhtunkhwa has declined from Rs 89.4 billion to Rs 88.0 billion (a negative growth of 1.6 percent). Moreover, expenditure on GFCF incurred by district governments has increased by 82.1 percent from Rs 80.2 billion to Rs 146.0 billion. Specifically, provisional GFCF by Tehsil Municipal Administration (TMAs) has doubled from Rs 51.2 billion to Rs 102.5 billion.

Regarding Net Exports, during FY2020, there was a 4.0 percent growth in exports of goods and services while 10.1 percent decline in imports of goods and services as recorded in expenditure on the gross national product at current prices measured in rupees. Thus, there is an improvement of 24 percent in Net Exports as these were recorded negative Rs 2.9 trillion in FY2020, compared to negative Rs 3.9 trillion last year. The main reason is that along with macroeconomic stabilization measures, the import demand for a wide range of non-energy and energy products were significantly curtailed. Further, quantum-led import declines were observed across all product categories and were complemented by lower international prices of most of Pakistan’s principal import commodities.

Sectoral Growth Analysis – Production Side

The provisional GDP growth rate for FY2020 is estimated at a negative growth of 0.38 percent (positive 2.67, negative 2.64 and negative 0.59 percent growth in agricultural, industrial, and services sectors respectively). For FY2020, the negative performance of both Industry and Services overshadowed the growth in the Agriculture which contributed 0.50 percentage points in overall GDP growth (still it has 19.31 percent share in GDP). The share of Industry and Services in GDP for FY2020 remained 19.29 and 61.40 percent respectively. Figure-5 describes the pattern of sectoral share in real GDP.

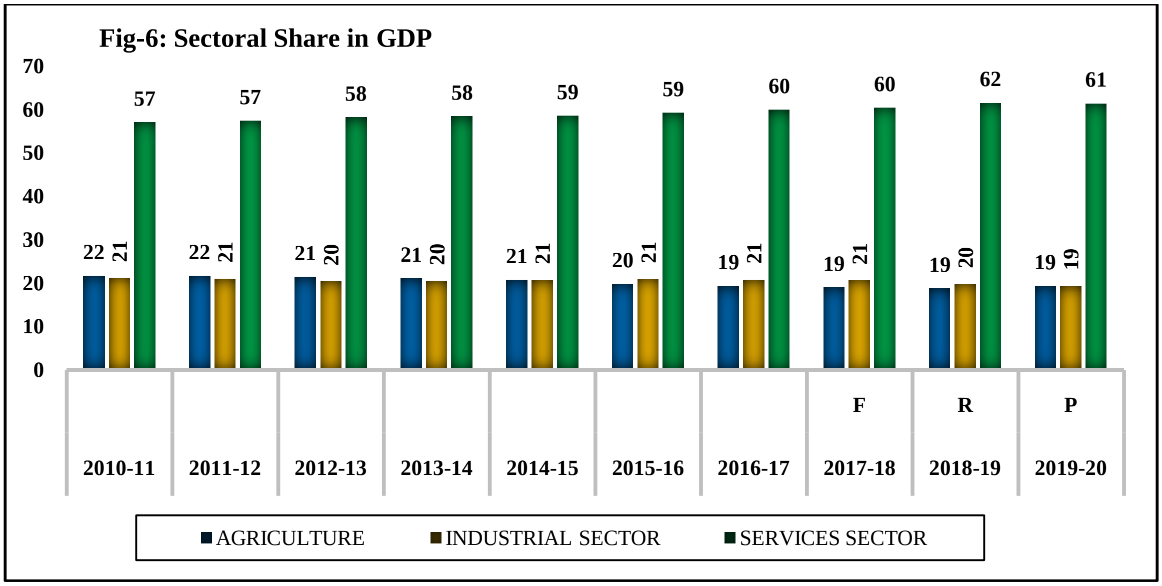


Fig-6: Sectoral Share in GDP

The positive contribution was almost equally reversed by Industry which contributed to GDP by negative 0.52 percentage points. These are mainly due to the COVID-19 a pandemic devastating blow to a low economic base country like Pakistan.

With the objective of reducing the propagation of COVID-19, social distancing was implemented which resulted in lockdown essentially to stop activity in contact-intensive businesses. Thus, spending on restaurant meals, travel, retail, personal services, fuel, and entertainment exhibit pronounced decreases. The negative impact of COVID-19 was so pronounced that the Services posted a negative growth of 0.59 percent. Thus, its contribution to GDP remained a negative 0.36 percentage point, which implies that Services also significantly affected by COVID-19. Table-4 shows sectoral point contribution in GDP

Table 4: Sectoral Point Contribution in GDP

	2015-16	2016-17	2017-18 F	2018-19 R	2019-20 P
A. AGRICULTURE	0.03	0.43	0.77	0.11	0.50
B. INDUSTRIAL SECTOR	1.18	0.95	0.96	-0.47	-0.52
COMMODITY PRODUCING SECTOR (A+B)	1.21	1.38	1.73	-0.36	-0.02
C. SERVICES SECTOR	3.35	3.83	3.81	2.27	-0.36
GDP (fc)	4.56	5.22	5.53	1.91	-0.38

Source: Pakistan Bureau of Statistics

Agricultural Sector: There was no significant impact of COVID-19 on the Agriculture sector. The agriculture sector grew by 2.67 percent.

Positive growth of 2.90 percent in important crops was observed due to an increase in production of wheat, rice, and maize at 2.45 percent, 2.89 percent, and 6.01 percent, respectively. While cotton and sugarcane posted negative growth of 6.92 percent and 0.44 percent respectively. Other crops have shown growth of 4.57 percent mainly because of an increase in the production of pulses, oilseeds, and vegetables. Cotton ginning has declined by 4.61 percent due to a decrease in the production of the cotton crops while the Livestock sector has shown a growth of 2.58 percent. The growth in forestry and Fishing remained 2.29 and 0.60 percent respectively.

Industrial Sector: According to the Pakistan Bureau of Statistics, for FY2020, the industrial sector has been estimated in the light of COVID-19 followed by the partial lockdown of economic activities in the country. Fourth-quarter has been estimated by keeping in view the lockdown situation faced by the industrial sector. Industries were directly contacted to provide the annual estimates of FY2020 by incorporating the impact of COVID-19. A significant impact has been observed in the manufacturing sector, particularly Large-Scale manufacturing and Small-Scale Manufacturing. The provisional growth in the industrial sector has been estimated at a negative 2.64 percent.

The mining and quarrying sector has witnessed a negative growth of 8.82 percent mainly due to natural gas (-6.36 percent), Crude Oil (-10.55 percent) and coal (-6.34 percent) sectors.

The large-scale manufacturing sector has shown the decline of 7.78 percent which is estimated primarily by QIM data (from July 2019 to March 2020) which shows a decline of 5.40 percent. The major decline has been observed in Textile (-2.57 percent), Food, Beverage & Tobacco (-2.33 percent), Coke & Petroleum Products (-17.46 percent), Pharmaceuticals (-5.38 percent), Chemicals (-2.30 percent), Automobiles (-36.50 percent), Iron & Steel products (-7.96 percent), Electronics (-13.54 percent), Engineering Products (-7.05 percent) and Wood Products (-22.11 percent). The increase has been witnessed in Fertilizer (5.81 percent), Leather products (4.96 percent), Rubber products (4.31 percent), Paper & Board (4.23 percent) and Non-metallic mineral products (1.82 percent). The annual estimates of large scale have been estimated on the basis of QIM data for the July-March FY2020. Industry-wise annual estimates have been prepared to keep in view that whether the industry remained functional throughout the year or remained closed for some period in the last quarter of FY2020.

Pakistan Bureau of Statistics has been estimating small scale industry performance on the basis of fixed growth of 8.2 percent since 2005-06. However, while estimating the value addition of small-scale industry in FY2020, this fixed growth has not been used. The detailed industry-wise analysis was conducted and annual estimates have been compiled keeping in view whether the industry remained open throughout the year or remained closed for some period. Due to this special treatment, because of COVID-19 and lockdown situation in the country, the estimates of Small-Scale Industry for FY2020 were reduced to 1.52 percent instead of 8.20 percent.

Electricity and gas sub-sector have grown by 17.70 percent mainly due to the positive growth of Gross Value addition by WAPDA & Companies, however, the performance of the gas sector remained subdued.

The construction activity has increased by 8.06 percent mainly due to an increase in general government expenditure for FY2020.

Services Sector: Similar to the industrial sector, this sector of the economy also witnessed a significant impact of the lockdown the situation in the country due to COVID-19, particularly in Wholesale and Retail Trade and Transport Sectors. The services sector has declined provisionally at 0.59 percent.

Wholesale and Retail Trade sector declined by 3.42 percent. It is dependent on the output of agriculture, manufacturing, and imports. The decline in industry and imported products have pulled growth of this sector downwards overshadowing the positive contribution of agriculture.

Transport, Storage and Communication sector also registered a decline of 7.13 percent due to continuous ban on Railways, Air transport and Road transport particularly public transport during the last two months. There was 45.74 percent decline in Railways and 6.49 percent decline in Air transport while Road Transport declined by 9.58 percent.

Finance and insurance sector witnessed a slight increase of 0.79 percent. Central banking has increased by 1.96 percent and scheduled banks by 0.22 percent and the insurance activities decreased by 2.59 percent.

The Housing Services has contributed positively at 4.02 percent. The General Government Services has grown by 3.92 percent. It is mainly driven by the increase in salaries of Federal, Provincial, and District governments.

Other private services, which is composed of various distinct activities such as computer-related activities, education, health & social work, NGOs, etc. has contributed positively to 5.39 percent.

Way Forward

As economies reopen with expectations that the adverse impact of COVID-19 is bottoming out, there is an on-going debate over the shape of the Recovery. Investors have fears about decline in economic growth and business profits due to a decrease in demand. Further, still, restriction on imports in many countries may dampen demand for Pakistan's exports. Capital flight is also expected with prevailing uncertainty and vulnerabilities, thus putting pressure on the exchange rate. The economic outlook is not very clear as well as doesn't seem promising, however, the fiscal stimulus package of Rs 1.24 trillion along with measures taken by State Bank of Pakistan for providing liquidity support to households and businesses will counteract the current economic downturn. IMFs Rapid Financing Instrument (RFI) amounting to $ 1.386 billion to counter the economic impacts of this novel outbreak will also support government's efforts to mitigate the economic shock, the facility will be used to address declining international reserves and increase social sector spending. Additionally, concessionary lending by IFIs; the World Bank and Asian Development Bank will provide much needed support to the government during this crisis time and help Government of Pakistan to weather the COVID-19 Challenge with minimum affects.