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PRIME
Policy Research Institute of Market Economy
آزادمعیشت۔خوشحال پاکستان

Prime Buzz

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Weekly roundup on the business climate and economic development in Pakistan including growth drivers, risk factors and policy signals.

Growth Drivers | Risk Factors | Policy Signals

01 Key Messages

Every Monday, we bring you this independent report on Pakistan's business climate by providing concise comments. The selection of news follows our unique analytical framework which brings together growth drivers, risk factors, and policy signals worth your attention. In 20 minutes, you get a well-rounded review of Pakistan's business outlook.

GROWTH DRIVERS

- Commercial activity reviving, foreseeing economic recovery post-COVID
- 8 new **CPEC energy projects** connected to the national electricity grid
- USD 1.1 billion loan alleviating concerns of **energy security**
- Local brands offered protection by **Madrid system**
- Tackling climate change through **green bonds**

RISK FACTORS

- Government's liabilities exceeding current repayment capacity
- **Distortionary subsidies** in the agriculture sector
- **Farmers** on the verge of breaking out into protests
- Pakistan's energy market – overproduction meets undersupply
- Conflicting **electricity policies** eventually curbing export profits

POLICY SIGNALS

- SBP initiatives along 3 fronts:

1. **Financial inclusion** for gender marginalized labor force
2. Boost to cost competitiveness of **export industries**
3. Support to **fintech & startups** of Pakistan

Growth Drivers 02

Growth drivers encompass recent developments that show promising potential for economic and business growth in Pakistan.

- Pakistan seems to be on a path of **post-COVID economic recovery**. The dampened market forces, demand, and supply are picking up. This is reflected in the surge of private-sector borrowing and consumer morale. These coupled with **National Command and Operation Centre (NCOC)** easing and lifting the embargo on multiple commercial activities signal growth in Pakistan's business and economic climate.
- The rise in private businesses and investors borrowing is established by the State Bank of Pakistan, quoting PKR 315 billion borrowings in the first seven months of FY 2021, a growth of 109% over the same last FY. This growth can be attributed to **Temporary Economic Refinance Facility (TERF)** by SBP and availability of loans at a low-interest rate. The latter, consumer morale, is captured by a recent survey study conducted by Dun and Bradstreet and Gallup, Pakistan. **The consumer confidence index (CCI)** witnessed a growth in the last quarter of 2020. These forces, hand in hand, have the potential for recovery of economic activity post-COVID slump.
- Moving on to the energy domain, a couple of recent developments present a green signal for growth. Under the game-changer project, **CPEC**, 8 out of 22 **energy projects** are near completion. These 8 have successfully added 4,470 MW of electricity to the national grid. This boost to electricity can complement the increased business activity if incorporated properly.
- Further, the **International Islamic Trade Finance Corporation (ITFC)** has extended a loan of USD 1.1 billion to Pakistan to meet its demand for oil and LNG through imports. This inflow of funds can ensure Pakistan's energy security for the year 2021 and boost foreign exchange reserves.
- Among growth drivers, a glad tiding for the domestic and local brands of Pakistan is its joining of the **Madrid System**. Entrepreneurs and SME brands will be provided branding protection, securing their trademark property rights in international markets.
- **Climate change** is a reality, catching up to economies across the world. Pakistan's public policy is planning to adapt accordingly. In the coming month, Pakistan is all set to issue **green bonds** of USD 500 million. These bonds are expected to boost hydro energy production in the country as per PTI's mandate. Pakistan's ambitious goals of a sustainable green economy are being recognized and praised globally.

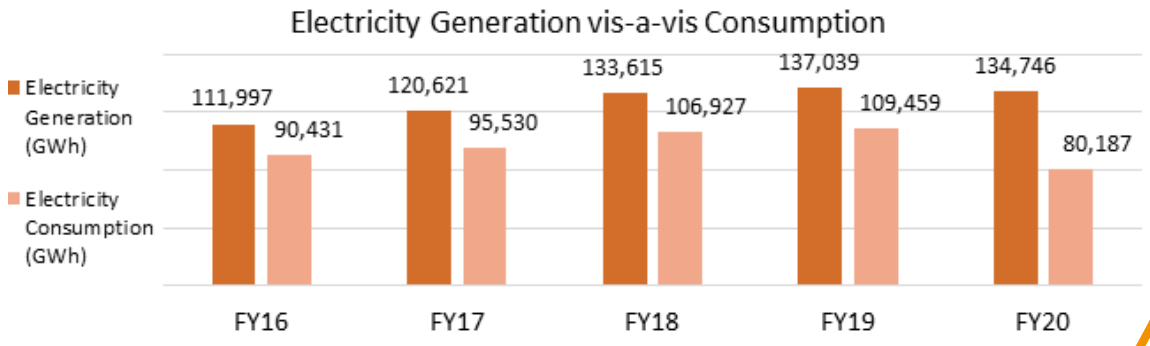
03 Risk Factors

Risk factors are identified threats and pitfalls that can potentially limit and constrain economic and business development in Pakistan.

Loans are **sustainable** as long as they are invested wisely, yielding more return than the cost of borrowing. To have a high debt to GDP ratio is only bad as long as the debt servicing capabilities are growing at a less than complimentary rate. For Pakistan, we notice that this is not the case. Yet the **foreign debt** is mounting, it has risen by **USD 6.7 billion**, in only the first seven months of FY 2021, registering a rise of 6%. An agreement has been reached for an additional loan of USD 1.1 billion. These inevitable liabilities pose a serious threat to the economy of Pakistan by reducing fiscal space.

Subsidies lead to market distortion and inefficiencies, which are aggravated in the absence of a uniform distribution mechanism. The PM had announced a PKR 50 billion relief package for the agriculture sector. It was to be allocated among **Kharif and Rabi** crops as subsidies. Inadequate and skewed transfer of agriculture subsidies carries the potential of harming the free market transactions. Due to problems in delivery mechanism and funds transfer among federation, provinces, and crops, the set target has not been achieved. The farmers are growing relentless, and there exists some risk of lashing out in protests like their counterparts in India.

Pakistan's **electricity market** is marked by overproduction and undersupply of electricity. The newly active **CPEC projects** have added energy to an already overproducing national grid, yet electricity is inaccessible to more than 50 million people around the country. The government continues its support to the introduction of renewables in the energy mix, which is still in the pipeline, as the share of renewables in the generation of electricity has fallen in the PTI regime. The fixed **capacity charges** are continuously adding to the circular debt and will continue to do so at an even higher rate with the incorporation of new power plants in the main grid. All this eventually translates into high energy tariffs, power outages, and cut off the gas supply to industrial sectors in hope of increasing electricity demand, which curbs the **competitiveness** of our **export products** in the global competitive market.



Policy Signals 04

Key policy actions and signals shape the business environment, directly and indirectly affecting all stakeholders.

- The **State Bank of Pakistan (SBP)** in the last week, has taken some promising initiatives for the business environment of Pakistan. First is aimed at the **financial inclusion of women** into the economic world. Women constitute about 49% of Pakistan's population, yet their labor force participation is limited at 22%. SBP is working on a policy draft in close coordination and counsel of experts from across the world to remedy this. SBP aspires to sensitize financial services for women through gender-based product diversification. The inclusion of women in the financial world is the right step towards their ultimate participation and mainstreaming in industry and business.
- Additionally, SBP has made special provisions for exporters regarding their **Special Foreign Currency Accounts (SFCA)**. SBP has increased the utility of SFCAs by adding to their payment purposes several new avenues. This step can help exporters in building their foothold in the ever-competitive international markets by better campaigning and marketing their products, liaison with global supply chains, and investment networking.
- Another move in the right direction by SBP is the **revised foreign exchange policy** as it will now allow financial technology and startup companies of Pakistan to set up a holding company abroad in exchange for remittance of up to USD 10,000 and other specified provisions. The subsidiaries of Pakistani companies will allow exporters to tap into unconventional and new markets in foreign countries.

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This report keeps CEOs, entrepreneurs, professionals, bankers, investors, diplomats, and other interested individuals and organizations informed and updated about the business climate in Pakistan through concise comments on growth drivers, risk factors, and policy signals. For subscription, please visit this link:
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