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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.

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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

- **CPEC** keeping **FDI** afloat in hard economic times
- Potentially, **Gwadar** can be the future oil city
- **LNG** deal with **Qatar** may lead to energy security, affordability, and price stability
- Pakistan's **communication network** set for an upgrade
- PM's **housing scheme** – back from break after COVID

RISK FACTORS

- A blow to FBR - number of **taxpayers** take a massive dip
- Pakistan to remain on **FATF's grey list**, costing billions and risking its international business
- Government's inability to eradicate inefficiencies in the food and power market fanning **inflation**
- Pakistan's trade suffering due to **anti-export biases** and **mercantilist policies**

POLICY SIGNALS

- **Privatization** the way to cut fiscal losses
- SBP introduces **End-to-End Digitization** on FX proceeds
- FBR adds a special chapter of **custom laws** to realize gains from **CPEC**

Growth Drivers 02

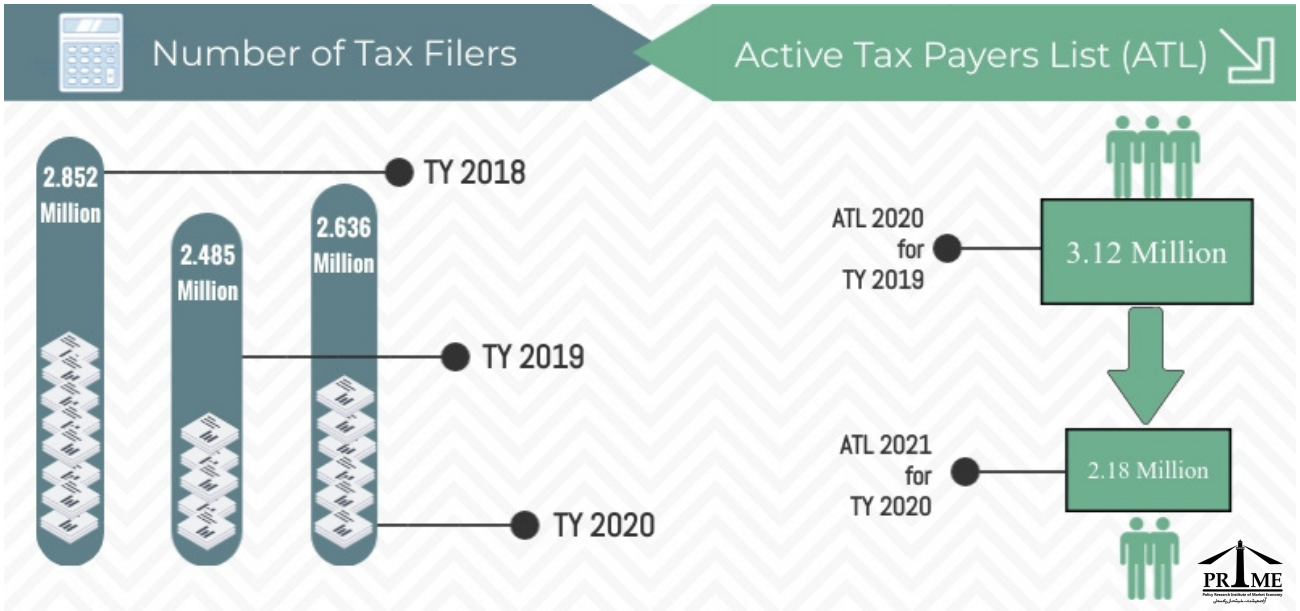
Growth drivers encompass recent developments that show promising potential for economic and business growth in Pakistan.

- Multiple developments in the last week, promise to be conducive to Pakistan's business outlook. Pakistan seems to be on a path of post-COVID economic recovery. The dampened **market forces**, demand, and supply are picking up. These coupled with National Command and Operation Centre (NCOC) easing and lifting the embargo on multiple commercial activities are positive drivers for Pakistan's economic climate. This is in line with the latest **Pakistan Prosperity Index (PPI)** report published by PRIME.
- China-Pakistan Economic Corridor (CPEC) has been projected as a game-changer and it has been playing a role in increasing economic growth since its inception in 2014. When **FDI** from most of the countries took a dip in the first seven months of FY 21, Chinese FDI went up to USD 402.8 Million, owing to Belt and Road Initiative's (BRI) central CPEC project. The extent of CPEC's impact on the Pakistani economy hinges on Gwadar city. Moving forward, **Gwadar** has the potential to attract foreign inflows, not only from China but the rest of the world as well. This has been realized upon mending of Pak-Saudi ties, as the world's largest **Saudi-based oil company Aramco** plans an investment worth USD 10 billion in the future oil city Gwadar.
- Further, in the energy domain, a new deal with **Qatar** has been brokered to ensure energy security, affordability, and price stability for Pakistan. Qatar will supply **Liquefied Natural Gas (LNG)**, at a rate of 10.2pc of Brent. The rate has been revised downward from 13.37pc of Brent, as stipulated in the previous 15-year contract.
- Pakistan's **communication network** is in line for a boost as three **airlines**, Q-Airlines, Fly Jinnah, and Jet Green are set to launch operations. Moreover, on land, a **freight train** connecting Islamabad to Istanbul, inactive for the last nine years, is also resuming operations.
- PM's **housing scheme** is also reviving post-COVID slump. State Bank of Pakistan (SBP) is working to ensure disbursement of finances towards housing scheme for low-income groups, by commercial banks (target is set at 5% of their portfolio by December 2021). Similar credit lines are expected from World Bank and Asian Development Bank (ADB) as well. Housing and construction industries will benefit from these measures, leading to economic growth.

03 Risk Factors

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

The government's chief source of earning is **taxation**. The government's liabilities continue to mount - USD 6.7 billion accumulated in only the first seven months of FY 2021, registering a rise of 6%. Whereas tax collection is dwindling – the **tax to GDP ratio** stands below the average in the last two fiscal years. The situation is further exacerbated by a 30% decrease in the number of active taxpayers. If the situation is not redeemed, Pakistan is likely to miss the stringent tax target set by the **International Monetary Fund (IMF)**, necessary for the release of subsequent Extended Fund Facility (EFF) tranche payment.



To add to the troubles, **Financial Action Task Force (FATF)** has not taken Pakistan out of the **grey list**, despite considerable actions on Pakistan's end to assuage their concerns. Pakistan is to remain on the FATF grey list till June 2021, pending further scrutiny against 3 partially achieved targets out of a total of 27, even though the remaining 23 had been completely achieved. Being on the FATF's grey list can potentially deter FDI, foreign investment inflows, and result in stringent banking sanctions, all limiting Pakistan's access to global capital markets and costing billions in terms of dampened GDP, trade, and FDI.

Risk Factors 04

- The increased **inflation**, 8.7%, is threatening consumer welfare by considerably raising their cost of living. This surge is attributable to increased power tariffs, and raised prices of **food amenities**: wheat, sugar, milk, and wheat flour. The former can be traced to the inefficient and **circular-debt**-ridden electricity market and the latter to shortages due to restricted mobility across the province and country borders, coupled with poor regulations governing domestic markets. Adding to the troubles of the **agriculture sector** is the absence of proper drying and storage facilities for agriculture produce, which leads to post-harvest losses in both quantity and quality, amounting to USD 343 million per year.
- Pakistan has increased **protectionist measures**. Pakistan has been suffering from a **cotton bale production shortage**. Yet no headway to import cotton yarn at lower duties has been made. Restricting free exchange across borders leads to inefficiencies. If this inefficiency remains unaddressed, it will spill over to unfulfilled export orders, severely impacting our chief export industry, textile. **Anti-export sentiment** has severely hampered free trade in Pakistan and will continue to do so unless we do away with qualified policies that foster anti-export biases and favor only a select few exporters and lobbyists.

05 Policy Signals

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

- The government has chalked out a timeline with the aid of the International Monetary Fund's (IMF) "SOEs Triage" to **privatize 44 entities**, including power companies. These entities have been inflicting huge fiscal losses to Pakistan's economy, amounting to PKR 143 billion in FY 2019 only. Privatization of SOEs and **decentralizing power companies** have the potential to eradicate inefficacies, cut losses, generate competition, bring down prices, and cultivate industrial growth.
- After the successful launch of the Roshan Digital Account (RDA), the **State Bank of Pakistan (SBP)**, has taken another promising initiative. SBP is working towards **End-to-End Digitization** on **foreign exchange (FX) proceeds**. The aim is to facilitate the consumer and promote FX, through swift processing of FX transfers, and digitization of service delivery.
- The **Federal Board of Revenue (FBR)** has introduced a new chapter in custom laws dedicated entirely to **China-Pakistan Economic Corridor (CPEC)**. The intended purpose is to attract investment by offering special tax exemptions and concessions so that the positive impact on Pakistan's economic growth is maximized. This move signifies the recognition of CPEC's potential, and a step towards its realization. Additionally, FBR is attempting to pave the way to doing business with ease by offering a **one-window facility** for businesses in Punjab. The facility is aimed at reducing red-tapism to make the environment more conducive to business and investment.

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"Everyday, newspapers, TV channels, portals and social media accounts generate information and comments on Pakistan's economy. The question about the overall direction of our economy remains influenced by what we read and who writes. To help you stay clear of the clutter, Prime Buzz presents you a weekly round up of important news about the business outlook following our daily scanning of a wide spectrum of sources. This is not just aggregation of contents, but a careful selection, with our own short comments. We classify these news as 'growth drivers', 'risk factors' and 'policy signals' and present a cogent summary that you can read in 20 minutes."

- Ali Salman - Executive Director PRIME Institute

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