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Today's Daily

■ Economy: Fiscal tweaks pose challenges

Amongst the key challenges facing the newly formed government is an escalating fiscal deficit (6.6% of GDP for FY18 vs. 5.8% in FY17 – marking the highest ever quantum PkR2.26trn). Riding on the populist wave of an election year, spillovers in provincial deficits (PkR22.4bn deficit vs. budgeted surplus of PkR274bn) along with slippages in non-tax revenue (down 21%YoY) paved the way for a massive breach of the GoP's revised target of 5.6% of GDP. For the PTI's economic policy set-up, enacting fiscal consolidation measures with the priorities of enhancing the tax base (currently less than 1%), while enacting austerity measures, limiting subsidies and reviving sick units serve as key tenets to cut back on expenditures. Even so, burdened by inevitable debt servicing (PkR1.7trn in FY19) as well as defense spending (PkR1.1trn), we maintain our fiscal deficit outlook (estimated at 5.4% of GDP vs. GoP target of 4.9%). We highlight possible constraints on development spending as a clear detriment to foreseeable growth prospects, posing headwinds (for construction and allied industries).

KSE100 - Index

Current 42,249.44
Previous 42,544.47
Chg. -0.69%

Mkt Cap. (PkRbn/US\$bn)

Current 8,702 / 70.07
Previous 8,712 / 70.15
Chg. -0.12%

Daily Turnover (mn)

Current 134.79
Previous 183.67
Chg. -26.6%

Value Traded (PkRmn/US\$m)

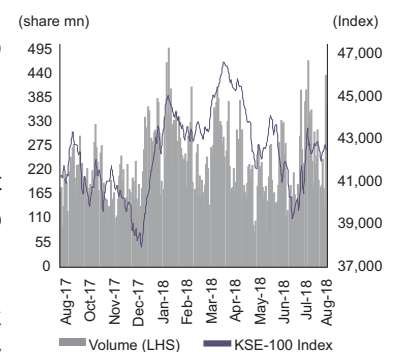
Current 5,768 / 46.45
Previous 7,709 / 62.08
Chg. -25.2%

AKD Daily

Thursday, Aug 30, 2018

News and Views

- The first meeting of the newly-reconstituted Economic Coordination Committee (ECC) of the Cabinet did not take any conclusive decision but appeared to be setting the stage for some serious business — to make fertilizer companies return PkR10bn windfalls to the economy and to address the root cause of power sector circular debt.
- The US Secretary of State Mike Pompeo and Chairman of the Joint Chiefs of Staff Committee General Joseph F. Dunford are expected to visit Islamabad next week to meet the new government.
- Prime Minister Imran Khan has directed the Commerce Division to work out a comprehensive strategy to check corrupt practices of illegal money transfers and smuggling which are negatively affecting the country's economy.



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Economy: Fiscal tweaks pose challenges

Amongst the key challenges facing the newly formed government is an escalating fiscal deficit (6.6% of GDP for FY18 vs. 5.8% in FY17 – marking the highest ever quantum PkR2.26trn). Riding on the populist wave of an election year, spillovers in provincial deficits (PkR22.4bn deficit vs. budgeted surplus of PkR274bn) along with slippages in non-tax revenue (down 21%YoY) paved the way for a massive breach of the GoP's revised target of 5.6% of GDP. For the PTI's economic policy set-up, enacting fiscal consolidation measures with the priorities of enhancing the tax base (currently less than 1%), while enacting austerity measures, limiting subsidies and reviving sick units serve as key tenets to cut back on expenditures. Even so, burdened by inevitable debt servicing (PkR1.7trn in FY19) as well as defense spending (PkR1.1trn), we maintain our fiscal deficit outlook (estimated at 5.4% of GDP vs. GoP target of 4.9%). We highlight possible constraints on development spending as a clear detriment to foreseeable growth prospects, posing headwinds (for construction and allied industries).

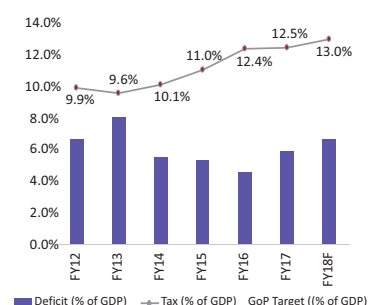
Consolidated Fiscal Balance

(PkRbn)	FY16	YoY	FY17	YoY	FY18	YoY
Revenue						
Tax Revenue	3,660	21%	3,969	8%	4,467	13%
Federal	3,377	20%	3,647	8%	4,066	11%
Provincial	283	38%	322	14%	401	25%
Non-Tax	787	-14%	967	23%	761	-21%
Federal	693	-17%	888	28%	614	-31%
Provincial	93	23%	79	-15%	147	85%
Total	4,447	13%	4,937	11%	5,228	6%
Total Expenditure						
Current Expenditure	4,694	6%	5,198	11%	5,854	13%
Of which : Mark-up Payments	1,263	-3%	1,348	7%	1,500	11%
Defence	758	9%	888	17%	1,030	16%
Development Expenditure & net lending	1,314	15%	1,681	28%	1,622	-4%
Total Expenditure	5,796	8%	6,801	17%	7,488	10%
Fiscal Deficit	-1,349	-7%	-1,864	38%	-2,260	21%
Financing	1,349	-7%	1,864	38%	2,260	21%
External	370	105%	541	46%	785	45%
Domestic	979	-23%	1,322	35%	1,475	12%
Non-Bank	192	-	277	44%	353	28%
Bank	787	-	1,046	33%	1,120	7%

Source: MoF, & AKD research

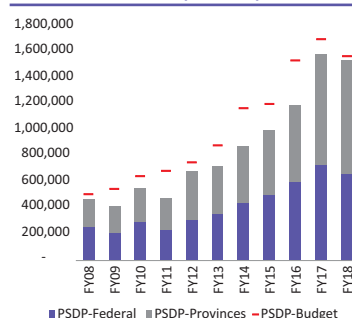
FY18 Fiscal Balance: Breaching the GoP's revised target of 5.6% of GDP, consolidated fiscal deficit clocked in at 6.6% of GDP (marking highest ever in absolute terms at PkR2.26trn – up 21%YoY) being a function of growth in expenditure outpacing revenues. These were further exacerbated by swings in the provincial deficit as populist measures took precedence for the outgoing Government. Despite tax revenue collection of PkR4.47trn (up 13%YoY – inclusive of PkR121bn collected under tax

Fiscal Indicator



Source: MoF & AKD Research

PSDP allocation (PkRbn)



Source: MoF & AKD Research



amnesty), non-tax revenue slipped to PkR761bn (down PkR206bnYoY) due to the absence of receipts from foreign agencies (including inflows under Coalition Support Fund). On the expenditure side, GoP curtailed its PSDP budget by 26.7%YoY from the initial allocation, while actual disbursement stood at PkR1.54trn (vs. revised budgeted of PkR1.55trn). Conversely, an ensuing uptick in debt servicing of PkR1.5trn (up 11%YoY) along with slippages in provincial expenditures (up 20%YoY to PkR2.06trn in FY18) advanced outlays to extend an already hefty deficit. In this regard, provinces posted combined deficit of PkR22.4bn against revised budgeted of PkR274bn surplus. These deficits were primarily financed through domestic borrowing (constituting 65% of total) where borrowing from the SBP and treasury bills (combined amount of PkR2.34trn) remained the foremost means of elevating government domestic debt to PkR17trn (49% of GDP vs. PkR9.8trn or 43% of GDP at FY13-end).

Federal Fiscal Position (PkRbn)

(PkRbn)	FY17A	FY18A	YoY%	FY19B	FY1PF (AKD)
Tax Revenue	3,647	4,066	11%	4,889	4,451
FBR collection	3,361	3,842	14%	4,435	4,200
Non-Tax revenue	902	630	-30%	772	724
Provincial share	1,966	2,217	13%	2,590	2,329
Total Revenue	4,549	4,696	3%	5,661	5,175
Current Expenditure	3,494	3,814	9%	4,179	4,099
Mark up Payments	1,348	1,500	11%	1,620	1,720
Defence	888	1,030	16%	1,100	1,100
Development Expenditure	733	661	-10%	800	720
Total Expenditure	4,362	4,704	8%	5,246	5,032
Provincial Budget	(163)	(22)	-86%	286	119
Consolidated Balance	(1,942)	(2,260)	16%	(1,890)	(2,067)
Deficit as % of GDP	5.8%	6.6%		4.9%	-5.4%

Source: MoF, Budget & AKD research

Outlook: Fiscal expansion during the tenure of last government along with substantial investments in development projects have led to massive external imbalances and a debt ridden economy (GoP's total debt standing at 70% of GDP vs. 61% by FY13-end). However, the newly formed PTI-led Government has prioritized fiscal discipline including both mobilization of domestic resources as well as restraining excess outlays. However fiscal consolidation would require unpopular measures, including: i) increasing the tax base (currently less than 1% file tax returns), ii) rationalizing tax exemptions, iii) removing subsidies (stripping the gas price differential) and iv) reviving sick units. That said, considering the stickiness of expenditures along with rising debt servicing (PkR1.7trn in FY19F) as well as defense budget of PkR1.1trn, we maintain our estimate of fiscal deficit at 5.4% of GDP (vs. GoP target of 4.9%).



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