

# Overview of the Economy

## GLOBAL ENVIRONMENT

The collapse of the US sub-prime market and worst ever global financial crisis has had serious repercussions not only for the developed world's economy but for the developing markets as well. The fallout has spread through an extensively interlinked global financial market and resulted in a tightening of credit and general drying up of liquidity. The impact of this crisis on developing and emerging economies is widespread. The crisis is not limited to the meltdown of financial markets, the real economy at the national and international levels, its institutions; its productive structures are also being affected. The financial meltdown inevitably backlashes on consumer markets, the housing market, and more broadly on the process of investment in the production of goods and services. The new growth power houses China and India are experiencing worst kind of slowdown in economic growth mainly because of the sub-prime meltdown in the US and the ensuing financial crisis and credit crunch around the world.

The world economy is likely to contract by 1.3 percent in 2009 with almost all developed countries are to post negative growth. Despite numerous stimulus packages and government action of unprecedented scale and nature, advanced economies are expected to contract by 3.8 percent in 2009. Notwithstanding, strenuous efforts by the US administration, including buying up of toxic assets and recapitalization of financial institutions and stimulus packages the world's largest economy US is projected to contract by 2.9 percent in 2009, further down from positive growth of 1.1 percent in the previous year.

Countries relying on trade as a primary means of boosting economic growth saw trade volumes disappear as contractions starts in trading partners. Growth in world trade volumes fell to 3.3 percent in 2008, as compared to 7.2 percent in 2007, and is expected to contract substantially by 11 percent in 2009. Exports from developing economies are projected to contract by 6.4 percent during the same period and developing economies started experiencing substantial slowdown in growth in 2008, with real GDP growing at 6.1 percent as compared to robust growth of 8.3 percent in 2007. Growth in these economies is projected to slow down further to 1.6 percent in 2009.

In emerging economies, the slowdown manifested itself through various channels like volatility in the financial markets led to a flight of capital. Emerging economies have already seen the spreads on sovereign and corporate debt widening, and a retreat in equity prices as a result of the global crunch. East Asian tigers Malaysia, Thailand, Korea, Philippines and Singapore all are prospective candidate for posting negative growth. Pakistan, India, Indonesia, Bangladesh and Sri Lanka are the rare positive growth depictees around the globe. The effects of adverse developments at global level have been felt unevenly and countries with weaker macroeconomic fundamentals taking a bigger hit. The impact from the global meltdown might be compensated to some extent through boosting local demand. However, vigilance by the policy-makers around the developing countries is needed to lessen the severity of downside risks posed by the current crisis. Pakistan economy also gained from compression of demand for external goods,

however, export slowdown is a serious cause of concern. Going forward the government has to pursue aggressive trade diplomacy to augment its access to external markets, beside ignite its efforts to diversify exports to optimal exploitation of export potential.

## DOMESTIC ENVIRONMENT

Pakistan's macroeconomic environment is affected by intensification of war on terror and deepening of the global financial crisis which penetrated into domestic economy through the route of substantial decline in Pakistan's exports and a visible slowdown in foreign direct inflows. Although contraction in export receipts is more than compensated by massive import compression emanating from global crash of crude oil and commodity prices, the external sector vulnerabilities remain a threat. Pakistan's economy continues to remain exposed to the vagaries of international developments as well as internal security environment. The intensity of the global financial crisis has further added to Pakistan's predicament. Despite support from the IMF and other bilateral and multilateral donors, Pakistan's external account remains exposed to a host of uncertainties. The dependence on external inflows needs some rationalization and to this end additional domestic resource mobilization is instrumental.

Pakistan's economy has lost significant momentum in the last few years. One of the prime contributors to this derailing is Pakistan's proactive role in war against terror. Pakistan being a front line state has to bear the fallout of events unfolded after 9/11. At the outset of the war, normal trading activities were disrupted with substantial increase in the cost of international trade because of higher rate of insurance cover; economic growth slowed down; import demand compressed with consequential decline in tax collection; and inflows of foreign investment and privatization were adversely affected. Pakistan not only lost precious lives and infrastructure but a very conservative estimate has placed economic cost of this war for Pakistan at around US\$ 35 billion since 2001-02. The current fiscal year has witnessed the height of this increased cost. The expenditure overrun has

created many uncertainties for public finances. The loss in economic opportunity was compounded by exogenous oil and commodity price shocks, which led to a significant deterioration of the macroeconomic indicators of Pakistan in 2007-08.

The problem was exacerbated in the July-October period of the current fiscal year. Major financial inflows dried up during the July-November 2008 period. The current account deficit widened with imports rising more than exports with a significant depletion in SBP's FE reserves which enhanced country's default risk. The FDI inflows fell by 21.4 percent from July-November 2008 against a 9.8 percent decline in the same period of year before. The external account, however, does depict certain positives. Even in the face of the world economic downturn, workers' remittances have remained strong and grew by 19.5 percent. In addition, declines in international commodity and food prices has helped reduce the country's import bill and thus impact favourably on the large current account deficit.

At the beginning of this fiscal year (2008-09), Pakistan economy was confronted with four major challenges which posed threat to Pakistan's recovery and socio-economic growth including *regaining macroeconomic stability, poverty reduction, fiscal retrenchment and weaknesses in the external account*. The overall vision is to regain macroeconomic stability and to attain GDP growth rate of 6 percent by 2012-13 from 2.0 percent in 2008-09. In order to ensure that macroeconomic difficulties do not further slow down the pace of job creation and adversely affect poverty reduction, the government has recently reached an agreement with IMF for a US \$7.6 billion package with interest rate varying from 3.51 to 4.51 percent spread out over a period of 23 months. For the first time, IMF has accepted Pakistan's homegrown proposals/programs which have two main objectives: (i) to restore the confidence of domestic and external investors by addressing macroeconomic imbalances through a tightening of fiscal and monetary policies until visible signs of demand curtailment; and (ii) to protect the poor and preserve social stability through well-targeted and adequately funded social safety nets. The government's new broad-based

program for economic stabilization was mainly focused on rationalization of expenditures, removal of unproductive subsidies to reduce the burden on the budget; significant cuts in expenditures to reduce budgetary deficit and a tight monetary policy to fight inflation.

The government adopted the following measures to address the above challenges:

- a. Strong adjustments in the petroleum prices were undertaken to reduce the budget deficit;
- b. Significant cuts were made in the expenditures to curtail aggregate demand;
- c. Tight monetary policy was followed by the State Bank of Pakistan to contain inflationary spiral;
- d. Electricity tariffs were periodically adjusted to rationalize energy prices;
- e. Government adopted a Nine-Point Program for economic and social recovery encompassing the following elements:
  - i. Macroeconomic Stability and Real Sector Growth
  - ii. Protecting the Poor and the Vulnerable
  - iii. Increasing Productivity and Value Addition in Agriculture
  - iv. Integrated Energy Development Program
  - v. Making Industry Internationally Competitive
  - vi. Human Capital Development
  - vii. Removing Infrastructure Bottlenecks through Public Private Partnerships (PPPs)
  - viii. Capital and Finance for Development
  - ix. Governance for a Just and Fair System
- f. Prioritized the scarce government expenditures available for development-related programs;
- g. Directed immediate support to the most vulnerable groups through the Benazir Income Support Programme (BISP). These are small (Rs.1000 per month per family) cash grants channeled through women to help satisfy the

most fundamental needs of vulnerable households. Currently reaching 3.5 million poor households, the scope of the programme is expected to expand to 7.0 million households in 2009-10;

- h. Implemented improved and transparent targeting of Benazir Income Support Programme (BISP) and other programmes aimed at the poor and the vulnerable groups.
- i. Intensified public-private partnerships with the objective of making private investments, including foreign investors, the most important funding source for economic development; and
- j. Reinforced the importance of sound governance, managerial and systemic mechanisms to ensure that investments in the social sector are cost-effective and aimed at output-oriented service delivery.

Pakistan's stabilization programme is supported by the Stand-By Arrangement (SBA) with the IMF approved on November 24, 2008. The SBA envisaged a significant tightening of fiscal and monetary policies to bring down inflation and strengthen the external position adopting several structural measures in the fiscal and financial sectors including strengthening of the social safety net. In addition, to stabilize the macroeconomic situation, the Programme aimed at addressing some of Pakistan's long standing economic problems. In particular, it called for a comprehensive tax reform to raise budgetary revenue and phase out the electricity subsidies to create greater fiscal space for public investment and social spending. Initial developments in the economy since the implementation of the Programme have been positive:

- ▶ The exchange rate has broadly stabilized enabling the State Bank of Pakistan (SBP) to buy foreign exchange on a net basis.
- ▶ SBP reserves have strengthened from US\$ 3.5 billion at end October 2008 to US\$ 7.1 billion on end March 2009.
- ▶ T-Bill auctions have been consistently oversubscribed with wide participation of

banks enabling the government to retire some of its debt to the SBP.

- ▶ Headline Consumer Price Index (CPI) inflation is estimated to have declined from 25.3 percent in August 2008 to 17.2 percent in April 2009.
- ▶ The overall fiscal deficit is estimated to have been restricted to 4.3 percent in 2008-09.

The government is conscious of the cost being imposed on poor families from the sharp escalation in food prices. Many of these needs are strongly linked and need to be addressed holistically — unless health services are improved, the incidence of ill health will continue to rise; unless educational retention is improved, children will never be able to exit from poverty because they will be concentrated in low-return employment or remain unemployable. It is, therefore, important to address primary needs via social protection, while simultaneously focusing on the mechanisms that ensure that the exit from absolute poverty is permanent for the majority of the vulnerable and a large proportion of the chronically poor. The national Poverty Reduction Strategy covers the three-year PRSP-II period of 2008-09 – 2010-11 while also providing a framework for thinking well beyond this timeframe and is, therefore, to be viewed as an approach to a long-term national economic strategy that has its main focus on reduction of poverty.

The sharp rise in international oil and food prices last year and the global financial crisis not only adversely impacted the macroeconomic indicators in Pakistan but also increased the number of the poorest of the poor. Recognizing the urgent need to protect the poor and the vulnerable, the Government of Pakistan (GoP) launched the Benazir Income Support Programme (BISP) in 2008 as its main social safety net programme. This programme would serve as a platform to provide cash transfers to the vulnerable identified on the basis of a poverty scorecard and would be backed by an exit strategy. This strategy includes imparting training to one member of each vulnerable family to sustain itself. The Programme

also envisages a workfare initiative through social mobilization. BISP intends to cover 3.4 million families or 22.75 million people in the current year. In the next year, the government intends to at least double the allocation for BISP to cover 7 million families. The government would require additional resources of US\$ 3.05 billion over the next two years to sustain the above programme.

Notwithstanding all these stabilization measures, recent trends in most macroeconomic variables suggest that the disciplined implementation of the macroeconomic stabilization program is started paying some dividends. Improvement in fiscal discipline is complementing the still relatively tight monetary policy to aggregate demand compression to a meaningful level which has improved prospects of lower inflation in the last two months of the current fiscal year (May-June 2009). The demand compression is also manifested from improvement in the cumulative Jul-April 2008-09 trade deficit which is the first reduction in the last six years. The narrowing of trade deficit and robust remittances has caused a reduction of over \$2 billion in the current account deficit and even for the month of February 2009, we have witnessed first surplus in monthly current account surplus since June 2007. The current account deficit is likely to decelerate from as high as 8.5 percent of GDP to around 5.3 percent of GDP in 2008-09 — a reduction of 3.2 percentage points in just one year. The improvement allowed for a build-up of the country's foreign exchange reserves beyond \$11 billion.

Nevertheless, Pakistan's economy still faces pressures from uncertain security environment, higher inflation driven by spike in food prices, the acute power shortages, and bewildering stock market, perceptible contraction in the large-scale manufacturing and slowdown in services sector; lower than anticipated inflows and growing absolute financing requirements. Abatement of inflationary pressure remained oblivious and prices depicted stubbornness.

## REAL SECTORS

In the wake of above mentioned international and domestic environment the economy lost significant

growth momentum owing to massive contraction in the industrial sector. The economic growth of 2.0 percent achieved during 2008-09 seems reasonable albeit it implies definite slippage against 4.1 percent growth of the last year and this year's target of 4.5 percent. However, it should be looked in the backdrop of global recession where positive growth is an exception and international developments where real GDP in Pakistan's main trading partners is estimated to contract by almost 3 percent on average in 2009, depressing the external demand for Pakistan's exports. The domestic environment was also not supportive to the growth momentum.

The industrial sector in general and large-scale manufacturing in particular has contributed to this slowdown in economic growth by posting dismal performance. The poor show of the LSM is understandable in the context of acute energy shortages and constrained international demand for Pakistan's manufactured exports. The massive downward correction in services sector's growth is mainly because of poor show of the financial sector beside saturation level attained in the communication sub-sector.

Notwithstanding the challenges of the fertilizer operations and credit squeeze, agriculture sector is the saving grace of this year's economic growth and performed exceptionally well on the back of extraordinary performance of major crops (mainly wheat, gram and rice). Livestock, a major component of agriculture, exhibited slight adjustment from 4.2 percent growth of last year to 3.7 percent growth in 2008-09. Construction sector witnessed worst growth performance for almost a decade owing to constricted activity in the private housing market, shrinkage of spending on physical infrastructure due to huge adjustment to rationalize development expenditure, and slowdown in reconstruction activities in earthquake affected areas.

The services sector has compensated some of the lost growth of the industrial sector by growing at 3.6 percent and provided much needed sanity to economic growth. Barring social services and public admn & defence almost all sub-sectors of services sector felt the pinch of recessionary trend.

Consumer spending remained strong with real private consumption rising by 5.2 percent as against negative growth of 1.3 percent attained last year. However, gross fixed capital formation could not maintain its strong growth momentum and real fixed investment growth contracted by 6.9 percent as against the expansion of 3.8 percent in the last fiscal year.

The current slowdown is substantially different from the deceleration of the 1990s or early 2000s. The aggressive monetary tightening posture of the SBP has witnessed a reversal in the last monetary policy statement by notional downward adjustment of policy rate in April 2009 to ensure that stubbornness of monetary policy might not haemorrhage the economic activity. The recent monetary policy has tried to strike a balance between sustaining the growth momentum and containing the inflation in stabilization mode.

### Growth and Investment

**Real GDP** grew by 2.0 percent in 2008-09 as against 4.1 percent last year and growth target is met 4.5%. The modest growth of just 2.0 percent is shared between Commodity Producing Sector (CPS) (0.08) and services sector (1.92). Within the CPS, agriculture contributed 1.0 percentage points or 50.1 percent to overall GDP growth (a significant increase from its contribution of only 5.0 percent last year) while negative performance of industry dragged 0.92 percentage points or 46.1 percent to neutralize positive contribution of the agriculture. In the services sector major contributions to GDP growth came from transport, storage & communication (0.3 percentage points or 14.6 percent), wholesale & retail trade (0.7 percentage points or 27.1 percent) and social services (0.8 percentage points or 38.6 percent).

**Agriculture sector** has depicted a stellar growth of 4.7 percent as compared to 1.1 percent witnessed last year and target of 3.5 percent for the year. **Major crops** accounting for 33.4 percent of agricultural value added registered an impressive growth of 7.7 percent as against a negative growth of 6.4 percent last year and a target of 4.5 percent. The **livestock sector** grew by 3.7 percent in 2008-09 as against 4.2 percent last year. Output in **the**

**manufacturing sector** has contracted by 3.3 percent in 2008-09 as compared to expansion of 4.8 percent in last year and over-ambitious target of 6.1 percent. *Small and medium manufacturing sector* maintained its healthy growth of last year at 7.5 percent. **Large-scale manufacturing** depicted contraction of 7.7 percent as against expansion of 4.0 percent in the last year and 5.5 percent target for the year. The massive contraction is because of acute energy outrages, security environment and political disruption in March 2009.

The **services sector** grew by 3.6 percent as against the target of 6.1 percent and last year's actual growth of 6.6 percent. Value added in the **wholesale and retail trade sector** grew at 3.1 percent as compared to 5.3 percent in last year and target for the year of 5.4 percent. **Finance and insurance sector** witnessed slowed down to 12.9 percent in 2007-08 but registered negative growth of 1.2 percent in 2008-09. The performance of this sector shows that Pakistan's financial sector is integrated in the world economy and feeling the heat of the financial crisis plaguing international financial markets. The **Transport, Storage and Communication** sub-sector depicted a sharp deceleration in growth to 2.9 percent in 2008-09 as compared to 5.7 percent of last year.

Pakistan's **per capita real income** has risen by 2.5 percent in 2008-09 as against 3.4 percent last year. Per capita income in dollar term rose from \$ 1042 last year to \$ 1046 in 2008-09, thereby showing marginal increase of 0.3 percent. **Real private consumption** rising by 5.2 percent as against negative growth of 1.3 percent attained last year. However, gross fixed capital formation could not maintain its strong growth momentum and real fixed investment growth contracted by 6.9 percent as against the expansion of 3.8 percent in the last fiscal year.

The **total investment** has declined from 22.5 percent of GDP in 2006-07 to 19.7 percent of GDP in 2008-09. **Fixed investment** has decreased to 18.1 percent of GDP from 20.4 percent last year. **Private sector investment** was decelerating persistently since 2004-05 and its ratio to GDP has declined from 15.7 percent in 2004-05 to 13.2 percent in 2008-09. Public sector investment to

GDP ratio was rising persistently from 4.0 percent in 2002-03 to 5.6 percent in 2006-07, however, declined to 4.9 percent in 2008-09. The **national savings** rate has declined to 14.4 percent of GDP in 2008-09 as against 13.5 percent of GDP last year. Domestic savings has also declined substantially from 16.3 percent of GDP in 2005-06 to 11.2 percent of GDP in 2008-09.

## INFLATION

As inflationary pressures across the globe continue to dissipate, sparking deflationary concerns in even some countries like Thailand and India which shared pain of galloping inflation with Pakistan a few months ago, Pakistan still faces high double-digit inflation. Although all the price indices like the CPI including core inflation, WPI and SPI have shown a downward trend in recent months, the decline has been subject to stiff downward rigidity. The month on month increase in food and non-food inflation in the last three months (February-April) has been especially disappointing. Going forward the government has to rationalize electricity tariff which will be inflationary in nature. Th

Notwithstanding difficult domestic environment, the inflation rate as measured by the changes in **Consumer Price Index (CPI)** showed an easing trend beginning in November 2008, touching 17.2 percent in April 2009 after reaching a record level of 25.5 percent in August 2008. While the food group was the major source of inflation in Pakistan during the first ten months of 2008-09, the non-food component of the CPI has also been persistently high, resulting in overall stubbornness of the inflation. The CPI inflation averaged 22.3 percent during July-April 2008-09 as against 10.3 percent in the comparable period of last year. Given current trends and barring any adverse shocks, it is expected that the average inflation for the year (2008-09) as measured by CPI will be close to 21 percent. The **core inflation** which represents the rate of increase in cost of goods and services excluding food and energy prices also went up from 7.1 percent to 18.0 percent.

## MONETARY POLICY

The SBP has kept its tight monetary policy stance in the period July 01, 2008-April 20, 2009. The policy rate was adjusted upward in November 2008 to shave-off some aggregate demand from the economy and kept constant in January 2009. However, noticing visible signs of demand compression enabled the SBP to reduce 100 basis points on April 20, 2009. During July 01, 2008-May 16, 2009, money supply (M2) expanded by 4.6 percent against the target of expansion of 9.3 percent for the year and last year expansion of 8.1 percent in the comparable period of last year. The reserve money witnessed growth of 2.4 percent in this period as against expansion of 13.2 percent in the comparable period of last year.

*Net domestic assets (NDA)* have increased by Rs.443.8 billion as compared to increase of Rs.702.5 billion in last year, thereby showing an increase of 11.0 percent in this period whereas, last year the growth in the comparable period was 22.8 percent. *Net foreign assets (NFA)* have recorded a contraction of Rs.227.3 billion against the contraction of Rs.322.8 billion in the comparable of last year. *Government borrowing for budgetary support* has recorded an increase of Rs.332.2 billion as compared to Rs.361.0 billion in the comparable period of the last year. The SBP financing has shown a net increase of Rs.198.2 billion and financing from scheduled banks witnessed a net increase of Rs.134.0 billion during July 01, 2008-May 16, 2009.

*Credit to private sector* witnessed a net disbursement of Rs.26.8 billion as compared to Rs.369.4 billion in the comparable period of last year. *Weighted average lending rate* have witnessed decline from 15.5 percent in October 2008 to 14.3 percent in March 2009. *Weighted average deposit rate* on the other hand has decreased from 9.5 percent in October 2008 to 8.0 percent in March 2009 which implies increase in the spread amidst intensive deposit mobilization efforts on the part of the banks. The *weighted average yields on 6 months T-bill* has declined by almost 250 basis points to 11.5 percent in March 2009 as against 14 percent in November 2008 but inched up to 12.4 percent in April 2009.

## FISCAL POLICY

The government has decided in the economic stabilization program to adhere to the fiscal deficit target reverently and during the first nine months (July-March) the fiscal deficit hovered around 3.1 percent of the projected GDP for 2008-09 which is consistent with annual fiscal deficit target of 4.3 percent. The fiscal improvement in the first nine months (July-March 2008-09) has largely based on reduction of oil subsidies and a cut in development spending. All meaningful efforts to expand revenues particularly by broadening the tax base will only work in the medium-term.

The financing patterns of fiscal deficit remained dominated by the banking system which financed 85 percent of the fiscal deficit and only 15 percent were financed by the non-bank sources. The government remained well ahead of the SBP financing limit allowed by the Economic Stabilization Program.

*The overall FBR tax collection* remained less than satisfactory and actually witnessed deceleration in real term. Resultantly, the FBR tax collection to GDP ratio is likely to deteriorate around 9 percent of GDP as against the target of bringing it in to the vicinity of 10 percent of GDP. *Tax Revenue* collected by the FBR amounted to Rs.898.6 billion during the first ten months (July-April) of the current fiscal year, which is 17.7 percent higher than the net collection of Rs.763.6 billion in the corresponding period of last year. The *net Direct tax* collection was estimated at Rs. 332.5 billion against the target of Rs 496 billion which implies a growth of 16.9 percent during Jul-April 2008-09.

*Indirect taxes* grew by 18.2 percent during Jul-April 2008-09 and accounted for 62 percent of stake in overall tax revenue. The *sales tax collections* grew by 22.2 percent and stood at Rs.358.9 billion as against Rs.293.6 billion in comparable period last year. The *net customs duty collection* has inched up from Rs.114.9 billion in 2007-08 to Rs.117.2 billion in 2008-09, thereby showing modest growth of 2.1 percent. The net collection of *federal excise* stood at Rs 90.0 billion during Jul-April 2008-09 as against Rs. 70.6

billion in the corresponding period of last year, thereby, showing an increase of 27.5 percent.

Despite a decline in fiscal deficit in the first nine months of 2008-09, the growth in *domestic debt* accelerated reflecting non-availability of financing through external sources. The stock of domestic debt grew by Rs.484.1 billion during July-March 2008-09. This strong growth in the domestic debt reflects non-realization of privatization proceeds and reduced availability of net external financing due to increase in external debt repayments on maturing stock of foreign currency bonds. The main contribution came from 17.5 percent rise in floating debt which increased by Rs.286 billion. The stock of permanent debt has increased by Rs.44 billion. Unfunded debt witnessed a growth of 15.1 percent or Rs.154.2 in Jul-March 2008-09 mainly because of uncertainty in the financial market and very attractive rates offered by NSS schemes.

## EXTERNAL SECTOR

The external sector has shown definite signs of improvement. The current and trade account balance has improved but there is some slippages on account of current transfers. The buoyancy in remittances is more than off-set by substantial declining trend in inflows through exchange companies. There is a substantial decline of around \$2 billion in services trade deficit during the first ten months of the current fiscal year because of tapering off in the demand pressures on the one hand and lower freight and insurance payments on the other. The financial account witnessed slackening of capital inflows by staggering \$ 2.7 billion mainly on account of lower FDI inflows, higher portfolio outflows, lower disbursements of loan and higher amortization payments. The worsening of external account in the period of July-October 2008-09 is compensated by substantial improvement in the external account in the period November-April 2008-09.

*Exports* were targeted at \$ 19.0 billion or 6.9 percent lower than last year. Exports started to face heat of global financial crisis since November 2008 and the contraction of world over demand has exacerbated export contraction. The exports

witnessed negative growth of 2.6 percent — declining from \$ 16.4 billion last year to \$ 16.0 billion in July-April 2008-09. *Imports* registered a negative growth of 9.8 percent in July-April 2009. The imports stood at \$26.77 billion as against \$28.715 billion in the comparable period of last year. The growth in imports reflects impact of substantial fall in oil and food imports in monetary terms and these two items were responsible for 80 percent of additional imports bill last year. Import compression measures coupled with massive fall in international oil prices have started paying dividends and imports witnessed marked slowdown during the last two months.

*Trade Balance* The merchandise trade deficit improved by 12.3 percent and declined from \$10.7 billion in July-April 2008-09 to \$ 12.3 billion in July-April 2008-09. The substantial decrease of 9.8 percent in imports outstripped otherwise significant decrease of 3.0 percent in export growth, which caused the trade deficit to improve by 12.3 percent. *Workers Remittances* totaled \$ 6.4 billion in July-April 2008-09 as against \$ 5.3 billion in the comparable period of last year, depicting an increase of 19.5 percent. Deep recession in the US economy, which constitute close to one-third of Pakistan's remittances started taking its toll and witnessed negative growth of 1.9 percent. The trend will be expected to continue in the months to come, however, overall outlook of remittances from other source countries is positive.

*Current Account Balance* Pakistan's current account deficit shrank by 23.5 percent during July-April 2008-09. Current account deficit shrank to \$ 8.5 billion as against \$ 11.2 billion last year. In the month of February 2009, the current account witnessed a surplus which is a rare development in Pakistan economy. This was first monthly surplus since June 2007. It turned to deficit in March and April 2009. *Exchange rate* after remaining stable for more than 4 years, lost significant value against the US dollar and depreciated by 21% during March-December 2008. Most of the depreciation of rupee against dollar was recorded in post November 2007 owing to combination of factors like political uncertainty, trade related outflows and speculative activities. With successful signing of Standby arrangements with the IMF, the rupee

got back some of its lost value. With substantial import compression and revival of external inflows from abroad in the coming months of the fiscal year, the exchange rate will remain stable at around Rs.80-82 per dollar.

**The overall foreign investment** during the first ten months (July-April) of the current fiscal year has declined by 42.7 percent and stood at \$ 2.2 billion as against \$3.9 billion in the comparable period of last year. **Foreign direct investment (private)** shown some resilience and stood at \$3205.4 million during the first ten months (July-April) of the current fiscal year as against \$3719.1 million in the same period last year thereby showing a decline of 13.8 percent. If viewed in the massive fall in capital flows to emerging economies, even this decline in FDI seems to be reasonably good. **Private portfolio investment** on the other hand showed an outflow of \$451.5 million as against an inflow of \$98.9 million during the comparable period of last year.

The hemorrhage to the **foreign exchange reserves** have been arrested in the post-November period and over \$ 3 billion are added to the SBP reserves inspite of \$500 million Eurobond payment in February 2009. Notwithstanding, improvement in the external sector outlook remain hostage to expected inflows in the last quarter. Foreign Exchange Reserves declined substantially in the initial months of 2008-09 dropping from \$11.4 billion at end-June 2008 to a low of \$6.4 billion by November 25, 2008. This depletion of reserves in the five months (July-November 2008) was much higher than fall in forex reserves for the entire fiscal year 2007-08. The subsequent partial recovery since November 25, 2008 onward owed essentially to the inflow of \$ 3.1 billion from the IMF following Pakistan's entry into a macroeconomic stabilization program. The import coverage ratio declined to an uncomfortable level of 9.1 weeks as of end-October 2008 from 16.8 weeks of imports as of end-June 2008 but it improved to 18 weeks of imports by end-April 2009.

The **external debt & liabilities** recovered in the third quarter and actually fell in absolute as well as relative terms between end-December 2008 and

end-March 2009, mainly because of lower than anticipated net disbursements and positive translation impact of appreciation of dollar versus yen, SDR and euro. External debt and liabilities (EDL) stood at US\$ 50.1 billion or 30.7 percent of the projected GDP for the 2008-09 at the end of March 2009 which is higher than end-June 2008 stock of \$46.3 billion or 27.6 percent of GDP. It implies that EDL grew both in absolute and relative terms during July-December period but witnessed some correction in the third quarter. Almost all categories of EDL barring Paris Club, Eurobond and military, have witnessed increase; however, highest increase in absolute term was recorded in debt stock owed to the IMF as a result of inflow of \$3.1 billion on account of Stand by Arrangements (SBA) signed with the IMF in end-November 2008. On the liabilities side \$500 million are added by Bank of China.

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## EXECUTIVE SUMMARY

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### 01. GROWTH AND INVESTMENT

The economy has lost significant growth momentum owing to massive contraction in the industrial sector. The lowest real GDP growth rate of 2 percent attained in the last eight years should be taken in the backdrop of major disruptions of extraordinary nature like political uncertainty hovering around for most part of the year, intensification of war on terror, acute energy shortage and extremely high inflation by Pakistan's standard, massive adjustment efforts to regain stability from a highly disruptive year (2007-08) of exceptionally high macroeconomic imbalances, and above all significant demand compression both on domestic and external front, the economic growth seemed to be satisfactory under the circumstances. **Real GDP** grew by 2.0 percent in 2008-09 as against 4.1 percent last year and growth target of 4.5%. The commodity producing sector witnessed marginal positive growth of 0.2 percent which is the lowest ever in the last eighteen years.

The modest growth of just 2.0 percent is shared between **Commodity Producing Sector (CPS)** (0.08) and **services sector** (1.92). Within the CPS, agriculture contributed 1.0 percentage points or 50.1 percent to overall GDP growth (a significant

increase from its contribution of only 5.0 percent last year) while industry dragged 0.92 percentage points or 46.1 percent to neutralize positive contribution of the agriculture. In the services sector major contributions to GDP growth came from transport, storage & communication (0.3 percentage points or 14.6 percent), wholesale & retail trade (0.7 percentage points or 27.1 percent) and social services (0.8 percentage points or 38.6 percent).

**Agriculture sector** has depicted a stellar growth of 4.7 percent as compared to 1.1 percent witnessed last year and target of 3.5 percent for the year. **Major crops** accounting for 33.4 percent of agricultural value added registered an impressive growth of 7.7 percent as against a negative growth of 6.4 percent last year and a target of 4.5 percent. The **livestock sector** grew by 3.7 percent in 2008-09 as against 4.2 percent last year. Output in **the manufacturing sector** has contracted by 3.3 percent in 2008-09 as compared to expansion of 4.8 percent in last year and over-ambitious target of 6.1 percent. **Small and medium manufacturing sector** maintained its healthy growth of last year at 7.5 percent. **Large-scale manufacturing** depicted contraction of 7.7 percent as against expansion of 4.0 percent in the last year and 5.5 percent target for the year. The massive contraction is because of acute energy out-ages, security environment and political disruption in March 2009. The **mining and quarrying sector** witnessed lowest ever growth in almost one decade and grew by 1.3 percent in 2008-09 as against 4.4 percent growth last year and target of 5.0 percent.

The **services sector** grew by 3.6 percent as against the target of 6.1 percent and last year's actual growth of 6.6 percent. Value added in the **wholesale and retail trade sector** grew at 3.1 percent as compared to 5.3 percent in last year and target for the year of 5.4 percent. **Finance and insurance sector** witnessed slow down of 1.2 percent compared with an expansion of 12.9% in 2007-08. The performance of this sector shows that Pakistan's financial sector is integrated in the world economy and feeling the heat of the financial crisis plaguing international financial markets. The **Transport, Storage and Communication** sub-sector depicted a sharp

deceleration in growth to 2.9 percent in 2008-09 as compared to 5.7 percent growth of last year.

Pakistan's **per capita real income** has risen by 2.5 percent in 2008-09 as against 3.4 percent last year. Per capita income in dollar term rose from \$ 1042 last year to \$ 1046 in 2008-09, thereby showing marginal increase of 0.3 percent. **Real private consumption** rising by 5.2 percent as against negative growth of 1.3 percent attained last year. However, gross fixed capital formation could not maintain its strong growth momentum and real fixed investment growth contracted by 6.9 percent as against the expansion of 3.8 percent in the last fiscal year.

The **total investment** has declined from 22.5 percent of GDP in 2006-07 to 19.7 percent of GDP in 2008-09. **Fixed investment** has decreased to 18.1 percent of GDP from 20.4 percent last year. **Private sector investment** was decelerating persistently since 2004-05 and its ratio to GDP has declined from 15.7 percent in 2004-05 to 13.2 percent in 2008-09. Public sector investment to GDP ratio was rising persistently from 4.0 percent in 2002-03 to 5.6 percent in 2006-07, however, declined to 4.9 percent in 2008-09. The **national savings** rate has increased to 14.4 percent of GDP in 2008-09 from 13.5 percent of GDP last year. Domestic savings has declined substantially from 16.3 percent of GDP in 2005-06 to 11.2 percent of GDP in 2008-09.

**The overall foreign investment** during the first ten months (July-April) of the current fiscal year has declined by 42.7 percent and stood at \$ 2.2 billion as against \$3.9 billion in the comparable period of last year. **Foreign direct investment (private)** showed some resilience and stood at \$3205.4 million during the first ten months (July-April) of the current fiscal year as against \$3719.1 million in the same period last year thereby showing a decline of 13.8 percent. **Private portfolio investment** on the other hand showed a net outflow of \$451.5 million as against a net inflow of \$98.9 million during the comparable period of last year.

US kept its distinction of being a largest investor in Pakistan with 23.2 percent stake in the FDI. Other big investors originated from Mauritius (10.0

percent), Singapore (7.7 percent), UK (6.9 percent), Switzerland (6.6 percent), UAE (5.3 percent) and Hong Kong (3.9 percent). The communication sector (including Telecom) spearheaded the FDI inflows by accounting for 27.3 percent stake during July-April 2008-09 followed by financial business (22.4 percent), energy including oil & gas and power (22.7 percent), and trade (4.9 percent). The current wave of uncertainty in the global demand and economic activity in the country has a major backlash on FDI inflows.

## 02. Agriculture

In spite of structural shift towards industrialization, agriculture sector is still the largest sector of the economy with deep impact on socio-economic set up. It is the source of the livelihood of almost 44.7 percent of the total employed labour force in the country. With the present contribution to GDP at 21.8 percent, agriculture sector is the mainstay of the rural economy around which socio-economic privileges and deprivations revolve. Thus given for its stretched distinct forward and backward linkages particularly with the industrial sector, a large impact on balance of payments and highest share in employment, agriculture sector has assumed an added significance in backdrop of global food crunch and food security. No strategy of economic reforms can be realized without sustained and broad based agricultural development which is critical for raising living standards, alleviating poverty assuring food security, generating buoyant market for expansion of industry and services, and making substantial contribution to the national economic growth.

Agriculture has grown at an average rate of 4.1 percent per annum since 2002-03 with variations, from 6.5 percent to 1.1 percent. The fluctuation in agriculture has largely stemmed from a fluctuation in major crops which in turn is the result of the behaviour of Mother Nature, pest attacks on crops.

The performance of agriculture sector has been stronger than expected during 2008-09 as against the target of 3.5 percent and last year's performance of 1.1 percent, overall agriculture this year is estimated to grow by 4.7 percent on account

of bumper wheat, rice and maize crops estimated as 23.42, 6.9 and 4.0 million tons respectively. Hence major crops accounting for 33.4 percent of agricultural value added registered stellar growth of 7.7 percent as against negative 6.4 percent last year. Minor crops contributing 12.0 percent to overall agriculture grew by 3.6 percent as against 10.9 percent last year. The performance of livestock – the single largest contributor to overall agriculture (51.8 percent) grew by 3.7 percent in 2008-09 as against 4.2 percent last year. The fisheries sub sector performed positively at 2.3 percent though the previous year's growth stood at 9.2 percent. Forestry has been experiencing negative growth since 2003-04 and this year too has posted negative growth of 15.7 percent in a row.

Pakistan's agricultural output is closely linked with the supply of irrigation water. As against the normal surface water availability at canal heads of 103.5 million-acre feet (MAF), the overall (both for Kharif and Rabi) water availability has been less in the range of 2.5 percent (2005-06) to 20.6 percent (2004-05) against the normal availability. Relatively speaking, Rabi season faced more shortage of water than Kharif during these years.

During the current fiscal year (2008-09), the availability of water for Kharif 2008 (for the crops such as rice, sugarcane and cotton) has been 0.3 percent less than the normal supplies and 5.5 percent less than last year's Kharif. The water availability during Rabi season (for major crop such as wheat), is, however, estimated at 24.9 MAF, which is 31.6 percent less than the normal availability, and 10.7 percent less than last year's Rabi.

The domestic production of fertilizers during the first nine months (July - March 2008-09) of the current fiscal year was up by 3.6 percent as compared with corresponding period last year. On the other hand, the import of fertilizer decreased by 51 percent, the total availability of fertilizer also decreased by 11.9 percent during the same period last year. Agricultural loans amounting to Rs. 151.9 billion were disbursed during (July-March, 2008-09) as against Rs.138.6 billion during the

corresponding period last year, thereby registering an increase of 9.6 percent.

### 03. MANUFACTURING AND MINING

Manufacturing sector is the second largest sector of the economy having 18.4 percent contribution to GDP. This sector has recorded its weakest growth in a decade during current fiscal year. Overall manufacturing posted a negative growth rate of 3.3 percent during the current fiscal year against the target of 6.1 percent and 4.8 percent of last year. Large-scale manufacturing (LSM) accounting for almost 70 percent of overall manufacturing, witnessed a broad-based decline of 7.7 percent against the revised growth target of negative 5.0 percent during July-Mar 2008-09. Main contributors towards this broad based decline were the impact of severe energy shortages, deterioration in domestic law and order situation, sharp depreciation in rupee vis-à-vis US dollar and most importantly, weak external demand on the back of global recession coupled with slowdown in domestic demand. The increasing trend in inflation also affected consumers to curtail expenditure on durable goods.

Textile sector being an export oriented industry of Pakistan and more prone to international demand shocks has been under severe stress amid a global recession, however, textile production has declined slightly, by 0.7 percent over the same period last year.

The sustained growth in recent years in cement industry is an outcome of increase in its production capacity and exploitation of export markets. The cement sector posted a growth rate of 4.71 percent during the current fiscal year. Cement exports increased by 48.8 percent. Fertilizer industry also posted a positive growth due to increase in production. The performance of steel mill was unsatisfactory during the current fiscal year. The production value slid down from Rs.11133 million in 2007-08 to Rs. 9971 million in the current financial year, witnessing a decrease of 10.44 percent.

Mineral potential of Pakistan though recognized to be excellent is inadequately developed as its contribution to GDP at present stands at 2.4

percent. During the current fiscal year (*July-Mar 2008-09*), the mining and quarrying sector has registered almost flat growth rate i.e. 1.31 percent as against a target of 4.5 percent and 3.0 percent of last year. The growth rate of this sector declined sharply due to substantial diminishing trend in the production of Magnesite (51.3%), Sluphere (10.3%) and Dolomite (4.6%).

During the current fiscal year, the privatization commission completed the transaction of Hazara phosphate fertilizer limited (HPFL) fetching an amount of Rs.1340.02 million. SMEDA plays a vital role in creating market oriented economic growth, employment opportunities and reducing poverty. As many as 16 projects amounting to Rs.1680 million have been approved for implementation by SMEDA.

### 04. FISCAL DEVELOPMENT

The severity of the macroeconomic imbalances in the last fiscal year once again reinforces the importance of fiscal prudence for sustainable economic growth. The overhang from 2007-08 continued to haunt adjustment efforts. The fiscal consolidation efforts faced headwinds like deteriorating security environment, domestic political uncertainties along with the deepening of the global financial crisis and overall depressed macroeconomic environment. The unanticipated persistence of inflationary pressures on the economy kept fiscal policy options limited. The shrinking revenues constrict government's ability to pursue counter cyclical policy.

There has been significant improvement in fiscal performance during 2008-09 due to the policy shift, with the overall fiscal deficit estimated to have dropped to 4.3 percent of annual GDP. The fiscal improvement in 2008-09 has largely based on reduction of oil subsidies and a slash on development spending. Going forward Pakistan needs a substantial increase in resource base to augment its development efforts and fiscal consolidation efforts has to come from enhanced revenue base because we have already exhausted options for expenditure cuts. Pakistan's future economic development crucially hinges upon additional resource mobilization and for this end

extending the tax base to unexplored sectors is very crucial.

The expenditure of the government in relation to GDP exhibited replica of the past performance and showing an overall decline since the beginning of the 1990s. However, in 2008-09 total revenue as percentage of GDP slightly recovered, due to a marginal improvement in non-tax revenues as percent of GDP. Total revenue is expected to reach at Rs. 1910 billion, as compared to Rs. 1499.5 billion during the 2007-08.

The FBR revenue collection for the fiscal year 2008-09 was targeted at Rs.1250 billion at the time of presentation of the Federal Budget 2008-09. Tax collection during the first ten months (July-April) of the current fiscal year amounted to Rs.898.6 billion, which is 17.7 percent higher than the net collection of Rs.763.6 billion in the corresponding period of last year. The tax collection performance reflects the heat of slowing economy and falling imports. The customs duty collection deviated from its recent past track record of high growth mainly because of the fact that dutiable imports have undergone negative growth. The overall FBR tax collection remained less than satisfactory and actually witnessed deceleration in real term. Resultantly, the FBR tax collection to GDP ratio is likely to deteriorate around 9 percent of GDP as against the target of bringing it in to the vicinity of 10 percent of GDP. Tax revenue from all sources exhibited a decline in tax-GDP ratio from 10.3 percent in 2007-08 to around 10 percent in 2008-09.

The budgeted total expenditure for the fiscal year 2008-09 was Rs.2391 billion, which is 4.9 percent higher than the last year's revised estimate. On the other hand current expenditures were envisaged to remain more or less stagnant at Rs.1876 billions. The share of federal government in the current expenditure was to the extent of Rs.1359 billions and the remaining Rs. 517 billions were earmarked for provincial governments. Development expenditure (*after adjusting for net lending*) was targeted at Rs.396 billion in 2008-09 which is up by 7 percent than last year. On the basis of revenue and expenditure projections, the overall fiscal

deficit is estimated at Rs.562 billion or 4.3 percent of GDP as against 7.4 percent last year.

The current expenditure over run has become a norm because of intensification of war on terror and spike in security related expenditure in the last two years. This is feeding into a significant gap between budgeted and estimates in current expenditure. The current year has witnessed some deceleration in non-interest, non-defence expenditure, however, to follow fiscal deficit religiously, the government has to go an extra mile by development expenditure cutbacks. Notwithstanding this downturn, the growth in current expenditure remained strong. Pakistan's fiscal adjustment experience over the years suggests downward rigidity in current expenditure and much of the effort has to come from either additional revenue mobilization or development expenditure cutbacks. In case of any eventuality of revenue shortfall the development expenditure is the prospective candidate to bore the brunt of adjustment.

## 05. MONEY & CREDIT

In the light of continued inflationary buildup and increasing pressures in the foreign exchange market, the SBP announced a package of monetary measures on May 21, 2008 that included;(i) an increase of 150 bps in discount rate to 12 percent; (ii) an increase of 100 bps in CRR and SLR to 9 percent and 19 percent, respectively for banking institutions (iii) introduction of a margin requirement for the opening of letter of credit for imports (*excluding food and oil*) of 35 percent, and (iv) establishment of a floor of 5 percent on the rate of return on profit and loss sharing and saving accounts. Following a slight reversal in the mounting inflation, the SBP announced a decline of 100 bps on April 20, 2009. SBP's tight monetary policy and rationalization of fiscal subsidies and expenditure controls are the key factors that contributed a reasonable progress towards macroeconomic stability. Although the fiscal and external current account deficit reduced during the last year, still it remains high along with the risk of slippages.

The YoY growth in broad money (M2) declined sharply to 4.59 percent as on 9<sup>th</sup> May FY09 against 8.96 percent in the corresponding period last year. The money supply was limited to Rs 215.0 billion as the Net Foreign Assets (NFA) of the banking system recorded a decline of over Rs 227.1 billion during the first ten months of the current fiscal year to May 9<sup>th</sup>.

However, NFA has improved by Rs 130 billions as on 9<sup>th</sup> May, 2009 after contracting by Rs 357 billion on 6 December, 2008. This improvement mainly came towards end March 2009 as the government received \$ 500 million each from the World Bank and the Bank of China. The improvements in external account and hence in NFA are mainly owed to a rise in worker's remittances; increase in external financial inflows from multilateral and bilateral sources and substantial retirement of foreign currency loans to commercial banks.

On the other hand Net Domestic Assets (NDA) of the banking system decelerated sharply during Jul-May FY09 to 10.99 percent as compared to 21.3 percent during the same period last year. The sharp deceleration in NDA growth of banking system was mainly contributed by decrease in government borrowings and credit to non-government sector during Jul-May FY09. The credit of Rs 138.4 billion to the public sector enterprise (PSEs), and government borrowings worth Rs 119.8 billion for commodity operations has significantly contributed Rs 258.2 billion in NDA during Jul-May FY09 compared to an expansion of Rs 105.2 billion in the same period last year. Credit to PSEs increased by Rs 138.4 billion during July-May FY09 against an increase of Rs 44.3 billion in same period last year. The demand for credit from private sector decelerated. As it declined to Rs. 21.8 billion during July – May FY09 compared to Rs 369.8 billion in the corresponding period of the last year. This sharp decline in private sector credit during July-May FY09 was mainly due to the exceptionally low demand for working capital that has witnessed the lowest growth in the recent past.

According to the distribution of credit to the private sector, the manufacturing sector although declined to Rs 89.4 billion, still continued to be the

largest recipient of bank credit during Jul-March 2008-09. The overall manufacturing sector accounted for almost 85 percent of the credit to private sector business. The structure of loan portfolio of the banks has changed significantly as by end December 2008, 78 percent of the total bank advances were lent at the rate of 12 percent and above as compared to the 70 percent of bank advances were extended at rates between 9 to 12 percent during the same month last year. The bank have followed more strict credit criteria due to rising NPLs. Banks are focusing to finance those projects which are able to generate cash flows.

The impact of tight monetary stance and liquidity management began to translate into a rise in other interest rates, with varied magnitude, at different stages of the economy. For instance, 6-months T-bills cutoff witnessed an increase of 169 basis points to 13.2 percent during Jul-May FY09. However, 6-months and 12-months KIBOR decreased by 26 bps and 39 bps to 13.68 percent and 13.83 percent respectively at end May 2008 in view a cut of 100 bps in the policy rate in April 2009.

## 6. CAPITAL MARKETS

The beginning of the fiscal year 2008 appeared promising for Pakistan's capital markets regardless of the sub-prime crisis intensifying its grip on financial systems all over the globe. The stock markets in Pakistan posted good gains and the KSE-100 index gained 11.6 percent by mid of April 2008 and touched the highest level of 15,676 points on April 18, 2008 with a gain of 1,747 points over the level of index as at start of the year 2008. Subsequent to this high time, however, the equity market has seen an episode of precipitous decline: the KSE-100 index has fallen by over 62 percent (as on December 31, 2008) since touching its peak in April 2008. While issues related to the macroeconomic scenario and a shaky political environment fuelled anxiety among the investor community and contributed to the fall in value, a dearth of adequate corporate governance measures aggravated the situation. Supplementing the extensive weakness was the diminishing foreign interest in the equity markets of Pakistan.

Notwithstanding, equity investors have embarked on a fractional recovery of their fortunes with an upsurge in the KSE-100 index of a fine 22.5 percent since the commencement of the calendar year 2009, driven up chiefly by signs of returning economic stability. A timely loan from the International Monetary Fund (IMF) approved in November 2008 and a materialization of pledges by Friends of Democratic Pakistan are collectively expected to help out the economy sail through what could be a tumultuous era. It goes without saying that the government's success in managing the economy has, without a doubt, served to build a soothing outcome.

The stock market observed gigantic foreign outflows owing to the removal of price floor mechanism in the middle of December 2008. The prospects of healthy foreign interest become doubly depressing by looking at the figure of foreign equity investment during the first nine months of the current fiscal year 2008-09. It stands at a negative \$418.4 million till March 2009. With no fresh merger and acquisition activity in the year 2008-09, the international investors remained keen to increase their ownership share.

Pakistan's debt market has witnessed an issuance of long term government securities amounting to about Rs. 49 billion and revision in deposit rates of National Savings Schemes on a quarterly basis in 2008-09. Three new TFCs have been issued. Interestingly, the non-bank market remained the principal issuers this time with no floatation related to the financial sector. Recent regulations by SECP that emphasize on increasing the minimum capital base and strict requirements for the classification of non-performing loans are anticipated to augment the strength of the NBFC sector.

Capital market reforms are an integral component of the structural reforms being supported by the government to restore macroeconomic stability and to build up the banking system, while developing a more contributing incentive regime for financial industry. Significant progress has been made on capital market reforms, including adoption of international standards and market practices and the streamlining of regulatory infrastructure to enhance surveillance and enforcement.

The government is keen to maintain the momentum to strengthen, deepen and broaden the base of capital markets. As a further step to fulfill this objective, the SECP has revived the Consultative Group on Capital Markets to act as an independent think tank for important policy decisions in relation to the development of capital markets in Pakistan.

## 07. INFLATION

Inflation rate as measured by the change in Consumer Price Index (CPI), averaged at 22.3 percent during the first ten months (July-April) 2008-09 as against 10.3 percent in the same period last year. Food and non-food inflation have been estimated at 26.6 percent and 19.0 percent against 15.0 percent and 6.8 percent in the same period of last year. This year inflation accelerated at rapid pace mainly because of food prices which increased as result of high prices of widely consumable items such wheat, wheat flour, sugar and meat etc, owing to their supply shortage. Other major factors that effected domestic prices include phasing out of subsidies on petroleum products, upward revision of support prices of wheat by above 50 percent thus pushing up the retail prices of wheat and wheat flour across the country.

Core Inflation, which represents the rate of increase in cost of good and services excluding food and energy prices, core also went up from 14.7 percent in July 2008 to 17.8 percent in April 2009. After hovering around the 18 percent since October 2008, core inflation came down slightly to 18.5 percent in March 2009 and further to 17.8 percent in April 2009. The demand supply gap in case of meat, the extreme shortage of onion in the market and decline in sugar production has been the most significant contributors to the pick-up in food inflation during 2008-09. Based on the trend of prices of these items, the contribution of food inflation to the overall inflation has increased to 48% and that of non-food at 50.7 percent.

To contain inflation within desirable limits, the government took various measures such as curtailing government expenditure through stringent fiscal discipline, supply augment arrangements through imports and smooth

distribution network of essential commodities. Throughout the year, the Economic Coordination Committee (ECC) keep a constant watch over prices and supply of essential commodities in their fortnightly meetings. And come up with recommendations to improve supply.

## 08. TRADE AND PAYMENTS

The external sector developments in 2008-09 followed a rollercoaster ride patterns: started with highest ever oil prices and unbearable commodity prices, punctuating the highs in October 2008 when current account crossed \$2 billion mark on the back of soaring energy prices and uncertainties, gradually caught into the financial crisis and accentuating the lows in February 2009 with a current account surplus. The year started with first quarter current account deficit of \$3.8 billion and reached to third quarter deficit of just \$0.3 billion. Notwithstanding this positive development, the external sector is still prone to some downside risk.

Overall exports recorded a negative growth of 3.0 percent during the first ten months (*July-April*) of the current fiscal year against positive growth of 10.2 percent in the same period of last year. In absolute terms, exports have decreased from \$ 15,222.9 million to \$ 14762.2 million in the period.

Imports during the first ten months (July-April) of the current fiscal year (2008-09) decline by 9.8 percent compared with the same period of last year, reaching to \$ 28.92 billion. Import compression measures lowering domestic demand coupled with massive fall in international oil prices have started paying dividends and imports witnessed slowdown. Beside that depreciation of rupee had also played a significant role for lower imports during current fiscal year.

Imports of the petroleum group registered declining growth of 7.6 percent and reached to \$8012.7 million. The petroleum group accounts for 27.7 percent of total imports but contributed 21.0 percent in the overall growth of imports for the year. The decline in imports of the petroleum group has been due to massive fall in oil prices in the international market. The imports of telecom decline by 54.8 percent during July-April 2008-09. This is followed by imports of consumer durables

group which exhibits negative growth of 16.4 percent. Petroleum group, Raw Materials and food groups witnessed a negative growth of 7.6 percent, 5.2 percent and 3.1 percent respectively. Import of machinery remained the only group which showed a nominal growth of 0.5 percent during July-April 2008-09.

Pakistan's current account deficit (CAD) moved back o US\$ 8.5 billion during Jul-April 2008-09 against US\$ 11.2 billion in the comparable period of last year, showing an improvement of 23.5 percent. The improvement in current account arises during November-April 2008-09 when it declined by 74 percent over the corresponding period last year on the back of reduction in trade deficit and improvement in invisible account. While on the other hand, current account balance worsened by 100.8 percent during the first four months of the current fiscal year 2008-09 compared with the same period last year owing to increased import payments on account of higher import prices and food imports. Trade deficit decelerated by 12.3 percent during July-April 2008-09.

Services account deficit shrank by 41.3 percent during Jul-April Fiscal Year 2008-09 to reach \$ 3.2 billion. This deterioration was contributed by factors like receipt from logistic support, deceleration in freight related charges and sharp fall in outflows from foreign exchange companies the result of action against undocumented fund transfer.

Financial account contracts from \$ 6,224 million to \$ 3,476 million during July-April 2008-09 against corresponding period last year. This decline was a result of variety of reasons which discourage the investment flows to Pakistan during July-April 2008-09, mainly weakening economic fundamentals, deteriorating law and order situation, slack functioning of stock market, lack of privatization proceeds and in the presence of global financial crises the foreign investors declined to invest as expectations of the lower degree of profitability.

Workers' remittances amounted to \$ 6355.6 million in July-April 2008-09 as against \$ 5319.1 in corresponding period last year, thereby showing

an increase of 19.5 percent. More than 75.0 percent of remittance during July-October 2008-09 routed through exchange companies whereas majority of the increase in remittances growth was contributed by higher inflows in banks during November-March 2008-09. This compositional change in remittance can be attributed to the FIA actions against the undocumented fund transfer during October 2008.

Pakistan's total liquid foreign exchange reserves amounted to \$ 11.6 billion by the end of May, 2009. Of which reserves held by State Bank of Pakistan stood at \$ 8.28 billion and by banks stood at \$ 3.32 billion. The trend of reserves is consisting of two parts during current fiscal year. As foreign exchange reserves declined to a low during the first five months of 2008-09 at \$ 6.4 billion by 25<sup>th</sup> November, 2008 from \$ 11.4 billion at the end of June 2008. Pressure on reserves eased due to reduction in current account deficit along with modest recovery in capital flows thereby bringing stability in exchange rate which further improved the position of foreign exchange reserves.

## 09. EXTERNAL AND DOMESTIC DEBT

**External debt and liabilities (EDL)** Pakistan's total external debt increased from US\$ 46.3 billion at end-June 2008 to US\$ 50.1 billion by end-March 2009 — an increase of US \$ 3.8 billion or 8.2 percent. In relative terms, EDL as percentage of GDP increased from 28.1 percent at end-June 2008 to 30.2 percent by end-March 2009— an increase of 2.1 percentage points. The country's debt burden is also defined as external debt and liabilities as percentage of foreign exchange earnings which increased from 124.3 percent by end-June 2008 to 144.3 percent by end-March 2009.

International capital markets have seen one of the most turbulent years in recent history. With the financial crisis instilling a sense of distrust amidst the market, access to financing has been restricted, with spreads widening for both developed and emerging economies alike. As negative sentiments prevail, the situation for Pakistan is compounded by weaker economic performance in 2008-09 and a highly volatile domestic security situation. The

spread on Pakistani sovereign bonds as given by the EMBI have gone up by 1550 bps and have a rating of B3/CCC+. Given the severity of the crisis in international markets, and hesitance with respect to investor confidence, Pakistan has not issued any new instruments in 2008-09.

**Public debt** increased by Rs.1367 billion in the first nine months of 2008-09, reaching a total outstanding amount of Rs.7268 billion; an increase of 23.2 percent in nominal terms. Total public debt has been growing at an average of 12 percent per year since the fiscal year 1999-2000. The increase in total public debt is shared between rupee and foreign currency debt in the ratio of 40:60. The rise in foreign currency debt is mainly because of massive depreciation of the Pak rupee in the first quarter of the fiscal year. In absolute terms \$3.1 billion are added to the public external debt in the period July-March 2009. Public debt as a percentage of GDP (*a critical indicator of the country's debt burden*) has declined by 1.9 percentage points in the nine months down from 57.4 percent by end-June 2008 to 55.5 percent of GDP by end-March 2009.

**Total domestic debt** is positioned at Rs 3758.6 billion at end-March 2009 which implies net addition of Rs.484.1 billion in the nine months of the current fiscal year. In relation to GDP the domestic debt stood at 28.7 percent of GDP which is lower than end-June 2008 level at 31.3 percent. The domestic debt grew by 14.8 percent which is lower than last years' growth of 23.3 percent. The increase in domestic debt is lower than nominal GDP growth which helped reduction of 2.7 percentage points of GDP.

**Interest payments on domestic debt** stood at Rs 551 billion which sums to 41.8 percent of tax revenues and 30.5 percent of total revenues estimates of 2008-09. As a percentage of total expenditure budgeted for 2008-09, interest payments are currently 23.0 percent. The interest payments on domestic debt stood at 4.3 percent of GDP for 2008-09.

## 10. EDUCATION

Education is extensively regarded as a route to economic prosperity being the key to scientific and

technological advancement. Hence, it plays a pivotal role in human capital formation and a necessary tool for sustainable socio-economic growth. Education also combats unemployment, confirms sound foundation of social equity, awareness, tolerance, self esteem and spread of political socialization and cultural vitality.

Public expenditure on education as a percentage to GDP is lowest in Pakistan due to fiscal resources constraint. The trend of investment on Education in terms of GDP has been 2.50 % and 2.47 % in the years 2006-07 and 2007-8 respectively whereas it is estimated to be 2.10 % during the 2008-09. It is on the lower side compared with requirements given the importance of the sector. The budget allocation has increased by 8.6 % in 2008-09 as against an increase of 17 % in 2007-08.

According to Pakistan Social and Living Measurement (PSLM) Survey data (2007-08), the overall literacy rate (age 10 years and above) is 56% (69% for male and 44% for female) in 2007-08 compared to 55% (67% for male and 42% for female) in 2006-07. Literacy remains higher in urban areas (71%) than in rural areas (49%) and more in men (69%) compared to women (44%). When analyzed provincially, literacy rate in Punjab stood at 59 % followed by Sindh (56%), NWFP (49%) and Balochistan at 46%. The literacy rate of Punjab and Balochistan has improved considerably during 2006-07 to 2007-08. The overall school attendance (age 10 years and above) is 58% (71% for male and 46% for female) in 2007-08 compared to 56% (68 % for male and 44% for female) in 2005-06.

According to the Ministry of Education, there are currently 227,243 educational institutions in the country. The over all enrolment is recorded at 34.49 million with teaching staff of 1.27 million.

## 11. HEALTH & NUTRITION

The government attaches a very high priority to the improvement of health facilities so as to translate the economic success into social benefits. In Pakistan, the coverage of health facilities has improved over the years. The existing network of medical services consists of 948 hospitals, 4794 dispensaries, 5310 basic health units (BHUs), 561

rural health centres (RHCs) and the availability of 103037 hospital beds. Besides, there are 133956 doctors, 9012 dentists and 65387 nurses in the country. During the calendar year 2008, the population medical facilities ratio in terms of doctor works out 1212 person per doctor, 18010 person per dentist, 2478 person per nurse and availability of one hospital bed for 1575 persons.

The total outlay on health during 2008-09 is estimated at Rs.74 billion which shows an increase of 23 percent over last year and works out to be 0.5 percent of GNP. The new health facilities added to the overall health services system during 2008-09, include the construction of 48 new facilities (35 BHUs and 13 RHCs), up-gradation of 890 existing facilities (850 BHUs and 40 RHCs), addition of 4300 hospital beds and training of 4500 doctors, 400 dentists, 3200 nurses and 5000 paramedics beside training of 96000 LHVs. To control the common diseases and to alleviate their pain and suffering, various health programmes like TB, Malaria and AIDS Control Programmes were carried out. The caloric intake per person has been estimated as 2363 per day in 2008-09 and per capita protein availability has increased from 69.5 gram last year to 70.0 gram in the 2008-09.

## 12. POPULATION, LABOUR AND EMPLOYMENT

The population of Pakistan stood at 163.67 in mid 2008-09. If the existing trend remains unchanged, it will reach 167 million by the year 2010 and 194 million by 2020 (NIPS). The density of population per person is 185 (2003). According to 2007 province wise demographic estimates of the planning and development division, Punjab has 55.46 percent of the total population of Pakistan. Sindh has 22.92 percent of entire population NWFP has 13.73 percent population. Baluchistan is the least populous with 5.15 percent of population while Islamabad has 0.7 percent population and Federally administered Tribal Areas have 2.37 percent of entire population.

Crude birth rate (CBR) measures the growth and crude death rate (CDR) measures the decline of a population. These also give the birth and death rates among a population of 1000. CBR in Pakistan

is estimated at 25 while 10 years ago it was 31.7 which is a good trend, similarly CDR is 7.7 and about a decade ago it was 9. Both of these indicate that improvement on the population front is evident. This also shows that health statistics are gradually improving. Infant mortality rate was 81.1 in 1998 while it is 70.2 per thousand live births now. The decline explains that certain diseases have been controlled and there has been greater access to health care for the people.

Pakistan has a labour force of 51.78 million people. Women labour force has increased; which stood at 10.96 million that is 0.1 million more than the previous year. The total number of people employed was 49.09 that is 1.44 million more than the previous year. The supply of labour force in the economy and the composition of the country's human resource is determined by the labor force participation rate (LFPR). Crude activity rate is the currently active population expressed as a percentage of the total population in Pakistan. Crude activity has increased negligibly in 2007-08; it is 32.2 percent. Agriculture dominates the distribution of employed persons among all the major sectors leading at (44.65%) during 2007-08, manufacturing has the share of (12.99%). The "Others" category has the combined distribution of employed persons in several industries of (0.1%). During the period 1999-2000 to 2005-06, 11.33 million work opportunities were created, due mainly to the strong economic growth. However, in the subsequent year i.e. 2007-08, an increase of 1.44 million employed persons was seen.

### 13. POVERTY

The main objectives of government policies are to raise the standard of living and improve the socio-economic conditions of the people and thus reduce the incidence of poverty in the country.

Food prices have a significant bearing on poverty incidence. A review of price trends of essential items during 2007-08 indicates that the major portion of food inflation during this period stemmed from hike in the prices consumed by the poor household such as wheat, flour, rice, edible oil, vegetables and pulses. Since April 2007, the economy has witnessed over 200 percent increase

in the price of palm oil; and an increase of 150 percent in wheat prices, while over 100 percent increase in the price of oil in the international market.

Moreover, economic growth has slowed down considerably during the last three years. The industry and construction sectors have contracted due to the domestic slowdown and energy shortage and also due to global recession. Thus job absorbing capacity of the economy shrank.

Based on the Federal Bureau of Statistics' PSLM data, the Centre for Poverty Reduction and Social Policy Development (CPRSPD), Planning and Development Division estimated a sharp decline in the headcount poverty ratio for 2007-08. However, these findings appear to contradict other assessments conducted subsequently, and which better reflect global and domestic price developments after June 2008. These subsequent assessments point towards a strong likelihood of a sharp increase in the poverty incidence in Pakistan as a result of unprecedented food inflation and transmission of international energy prices to domestic consumers.

The Report of a UN Inter Agency Assessment Mission fielded during June-July 2008 found that food security in Pakistan in 2007-08 had significantly worsened as a result of food price hike. The total number of households falling into this category was estimated to be seven million households or about 45 million people in 2008. The survey further indicates that more than 40 percent of households reported no change in income in 2008 since last year. Forty five percent of the population working as employees witnessed decrease in their real wages. The Report shows an increase in the share of severely food insecure population, from 23 percent in 2005-06 to 28 percent in 2008. The main findings indicate that the high food prices are undermining poverty reduction gains, as food expenditures comprise a large share of the poor's total expenditures and food price hike has severely eroded poor household purchasing power.

The Planning Commission's constituted Panel of Economists in its Interim Report based on 2004-05

poverty head count number of 23.9 percent suggested an increase of around 6 percentage points in poverty incidence for the year 2008-09. Similarly, the Task Force on Food Security based on the World Bank estimates of head count ratio of 29.2 percent in 2004-05 poverty estimated that poverty head count increased to 33.8 percent in 2007-08 and 36.1 percent in 2008-09 or about 62 million people in 2008-09 were below the poverty line.

Subsequent to the poverty estimates of 2007-08 produced by CPRSPD, a validation exercise was conducted by the World Bank. In its analysis, the World Bank disaggregated the full year estimate into quarterly estimated HCR and found an almost 4 to 5 percentage point increase in the last quarter of 2007-08, to around 21 percent.

The World Bank has estimated, using methodology consistent with that used by CPRSPD in its poverty estimation, and taking current projections of real GDP growth, that the poverty Head Count Ratio could rise to over 25 percent by 2009-10.

Given the flux produced by large changes in food and energy prices since late 2007, the government intends to commission a rapid household income and expenditure survey to better assess the current position regarding poverty incidence and vulnerability in the country. This survey is expected to be conducted shortly.

Second generation poverty reduction strategy paper (PRSP-II) built up on nine pillars has been finalized with an aim to reduce poverty by regaining macroeconomic stability. Social sector and poverty related expenditures are projected to be Rs 760 billion during 2008-09, constituting 5.86 percent of GDP which is in line with the fiscal responsibility and Debt Limitation Act 2005, stipulating that expenditures on social sectors should not be less than 4.5 percent of GDP in any given year.

During year 2008-09, government took various initiatives to combat poverty which included PPAF, micro finance SME operations, Benazir Income Support programme, Peoples Works programme, Pakistan Bait-ul-Mal and Punjab

Government initiatives including tractor subsidy, sasti roti and Punjab food support scheme; which will help enhance absolute per capita income, and widen the scope to earn livelihood.

#### **14. TRANSPORT AND COMMUNICATION**

Transportation network of any country is of vital importance to its development and affects all sectors through economic linkages. It ensures safe and timely traveling, encourages business activities and cuts down transportation costs while granting access to producers for marketing their goods. Pakistan's economic development partly depends on improvement/modernization of its transport sector accounting for 11 percent of GDP & 16 percent of fixed investment.

Pakistan has a vast road network covering 258,350 kilometers including 176,589 KM of high type roads and 81,761 KM of low type roads. Total roads network which were 229,595 Km in 1996-97, increased to 258,350 Km by 2008-09 indicating an increase of 12.5 percent. During the out-going fiscal year, the length of the high outgoing type road network increased by 1.3 percent but the length of the low type road network declined by 2.7 percent because most of the low typed roads have been converted to high type roads.

An effective railway system facilitates commerce and trade, reduces transportation cost and promotes rural development and national integration while reducing the burden on commuters. Pakistan Railway carried 63.0 million passengers and 5.4 million tons of freight during current fiscal year and its earning stood at Rs. 17442 million.

The outgoing year (2009) was also exceptionally difficult for PIA, as the airline was equally affected by the unprecedented increase in fuel cost coupled with weaker Pakistani-Rupee which severely hurt PIA and eventually it had to bear huge loss on its US \$ loans. PIA international passenger traffic, excluding Hajj traffic registered an increase of 3.5 percent (passengers despite the seat (capacity) reduction of 2.3 percent. On domestic routes passenger traffic also registered an increase of 3.6 percent passengers, despite the seat (capacity) reduction of 7.4 percent. Hence in terms of

capacity utilization, overall Passenger Seat Factor (excluding Hajj) increased to 74.5 percent during the year 2008 as compared to 70.3 in 2007 although Airline was constrained to mount less ASKs (Available Seat Kilometers) by 5.7 percent. Similarly, though Cargo capacity was also lowered by 13.8 percent during the year 2009. load factor compared to the year 2008 improved by 2.7 percent.

Karachi Port Trust (KPT) is contributing to the economic growth of the country, by its record cargo handled at KPT. During the first seven months of the current fiscal year, it posted a remarkable increase of 44.3 percent in exports handled at Karachi Port Trust during first nine months of current financial year 2008-09, Port Qasim Authority handled 18.01 million tones cargo depicting a shortfall of 9 percent over Jul 07-Mar 08 owing to global economic crisis. Pakistan National Shipping Corporation (PNSC) lifted 5762.2 million tones of liquid cargo and 865.0 million tons of dry cargo during the current fiscal year. The consolidated revenues of the Group for the quarter ending March 31, 2009 were Rs.9503 million during the period under review as against Rs.7,471 million for the corresponding period last year showing an increase of 27 percent.

Telecom sector of Pakistan exhibited positive but slow growth in terms of revenue, subscribers and teledensity. During the current fiscal year total teledensity reached to 60.6 percent. However, cellular segment leads the share in total teledensity by 93.7 percent followed by Fixed Local Loop (FLL) 3.8 percent and Wireless Local Loop (WLL) 2.5 percent. During the first 9 months of 2008-09, cellular Market added 3,422,599 subscribers with average of 0.3 million per month and total subscribers reached 91.4 million. Total fixed line subscribers in Pakistan stand at a total of 3.7 million as of March, 2009, yielding total teledensity of 2.3 percent. Total WLL subscribers stood at 2.5 million and density in the country touched 1.5 percent in March, 09. There are currently more than 12,000 cities/ towns/villages covered by WLL services.

## 15. ENERGY

The outgoing year has witnessed number of internal and external challenges in Pakistan's economy and shortfall in energy sector is among the major problems. During the current year, supply and consumption of energy remained lower than previous years. The consumption of energy remained low due to overall slow down of economy. While the major cause behind the lesser energy supplies remained circular debt issue in the energy sector. Energy shortages dragged the performance of economy especially large scale manufacturing.

The consumption of petroleum products, gas and coal during the first nine months (July-March 2008-09) of the current fiscal year decreased by 3.4 percent, 2.5 percent and 26.5 percent, respectively over the corresponding period of last year. On the other hand, supply of crude oil, petroleum products, coal, and electricity during the first nine months of the outgoing fiscal year 2008-09 decreased by 5.5 percent, 2.8 percent, 26.5 percent and 17.9 percent, respectively over the corresponding period of last year

Production of crude oil per day has decreased to 66,531 barrels per day during July-March 2008-08 from 70,165 barrels per day during the same period last year, showing a decrease of 5.2 percent. On average, the transport sector consumes 51.6 percent of the petroleum products, followed by power sector (33.1 percent), industry (10.3 percent), household (1.7 percent), other government (2.1 percent), and agriculture (1.1 percent) during last 10 years i.e. 1998-99 to 2007-08.

The average production of natural gas per day stood at 3,986.5 million cubic feet during July-March, 2008-09, as compared to 3,965.9 million cubic feet over the same period last year, showing an increase of 0.52 percent. On average, the power sector consumes 37.2 percent of gas, followed by industrial sector (20.4 percent), household (16.8 percent), fertilizer (19.8 percent), Transport (2.0 percent), commercial sector (2.7 percent) and cement (1.0 percent) during last 10 years i.e. 1998-99 to 2007-08.

The total installed generation capacity has increased to 19,754 MW during July-March 2008-09 from 19,566 MW during the same period last year, showing a marginal increase (1.0 percent). Total installed capacity of WAPDA stood at 11,454 MW during July-March 2008-09 of which, hydel accounts for 57.2 percent or 6,555 MW, thermal accounts for 42.8 percent or 4,899 MW. The number of villages electrified increased to 133,463 by March 2009 as compared to 126,296 by March 2008, showing an increase of 5.7 percent. Presently, some 2.700 CNG stations are operating in the country. By March 2009 about 2.0 million vehicles were converted to CNG as compared to 1.70 million vehicles during the same period last year, showing an increase of 17.6 percent. With these developments Pakistan has now become the largest CNG using country.

## 16. ENVIRONMENT

The Government of Pakistan has declared 2009 as the National Year of Environment. In this regard the current year was kicked off with a Regional level workshop on Climate Change, which was inaugurated by the Prime Minister of Pakistan. A Medium Term Development Framework 2005-2010 (MTDF) adopted by the GoP in mid-2005 coincided with the approval of a new and far-reaching National Environmental Policy (NEP), with the goal to *“protect, conserve and restore Pakistan’s environment in order to improve the quality of life of the citizens through sustainable development”, and establishing directions for water supply and management, air quality, waste management, forestry, biodiversity, energy efficiency, and agriculture.* The Government has also made a considerable increase in its fund allocation for Environmental projects in the Public Sector Development Programme (PSDP).

Realizing the importance and role of sanitation in the improvement of environment as well as the commitment to achieve the MD sanitation goals, the MoEnv presented the National Sanitation

Policy of Pakistan before the Federal Cabinet soon after the Second South Asian Conference. The Ministry in collaboration with UNICEF, Water & Sanitation Programme (World Bank), Water Aid, Rural Support Programme Network (RSPN) etc, launched awareness and training programmes in the year 2008, the International Year of Sanitation (IYS 2008). Installation of water filtration plants in different areas is underway, the implementation of which is targeted to be completed within this fiscal year.

The latest figures released by the MoEnv estimated that about 38 percent of Pakistan's irrigated land is waterlogged; the productivity of soil is being lost due to salinity and sodicity. To achieve the MDGs target of vegetation cover of 6 percent by 2015, the Planning Commission proactively interacted with the MoEnv and the Provincial Forest Departments to come up with project for afforestation/ reforestation to meet the MTDF and MDGs targets. The President of Pakistan launched a Mass Afforestation Programme on December 22, 2008. This programme will be spread over a period of five years and shall largely be sponsored by private entrepreneurs for planting trees on state and other suitable lands.

Climate Change is also a matter of concern for Pakistan because of the impact it will have on glaciers releasing water for crops. Planning Commission has recently established a task force to investigate the impact of climate change on the country's agriculture, economy and natural resources. The Government also initiated the Technical Advisory Panel (TAP) Feb 2008 on Climate Change. So far, the Government has taken significant initiatives in collaboration with international agencies to address complex issues responsible for environmental degradation. A pragmatic approach towards multifarious challenges requires in depth and focused research, without which desired results will remain unachievable.