

2.0 ECONOMIC OVERVIEW

Pakistan, an impoverished and underdeveloped country, suffers from internal political disputes, lack of foreign investment, and a costly confrontation with neighboring India. Pakistan's economic prospects, marred by poor human development indicators, low levels of foreign investment, and reliance on international creditors for hard currency inflows, were nonetheless on an upswing through most of 2001.

2.1 Key Economic Indicators

2.1:1 GNP: The Gross National Products for last three years are included in table **2.1.1**.

2.1:2 GNP growth rate:

Gross National Product (GNP) grew by **2.4** percent in FY 01 compared to **3.5** percent last year. Negative value added by net factor income from abroad has persisted over the past six years, keeping GNP growth below GDP.

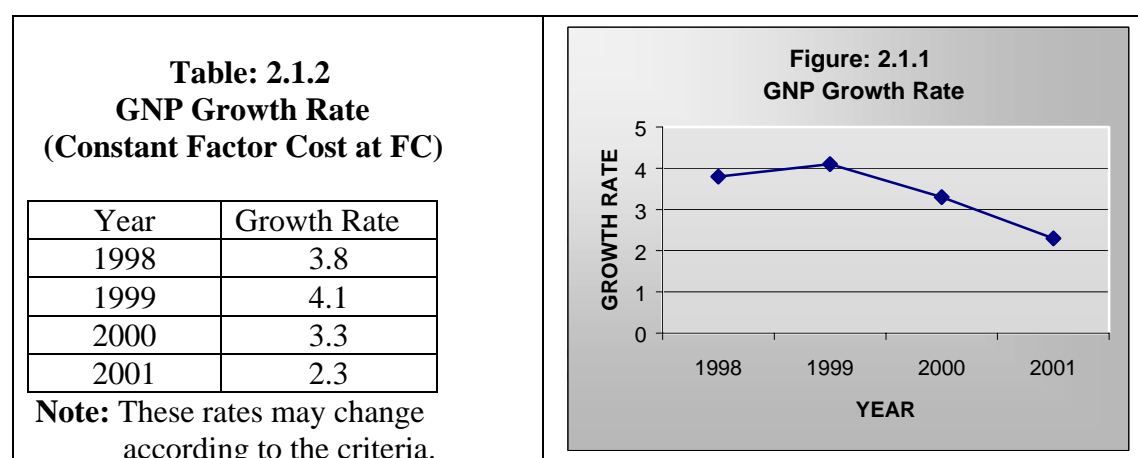


Table: 2.1.1-Gross National Product

SECTOR	AT CURRENT FACTOR COST		
	98/99	99/2000 (R)	2000/01(P)
1.Agriculture	739569	776219	797455
Major crops	279713	308	298124
Minor crops	123342	108931	119799
Livestock	316292	330945	347018
Fishing	16940	20300	22000
Forestry	3282	7215	10514
2.Industrial Sector	649475	672207	735494
Mining and Quarrying	14512	16613	19906
Manufacturing	423524	446877	500223
Large Scale	307647	319098	361325
Small Scale	115877	127779	138898
Construction	88395	97517	99231
Electricity & Gas Distribution	123044	111200	116134
Commodity Producing Sector (1+2)	1389044	1448426	1532949
3. Service Sector	1346899	1503254	1658864
Transport, Storage and Communication	277548	315834	353470
Wholesale and Retail Trade	410678	442478	493612
Finance & Insurance	88230	98532	107519
Ownership of Dwellings	123501	135518	146272
Public Administration & Defense	206997	246134	264353
Community, s & p services	239945	264758	293638
4. Gross Domestic Product (DC)	2735943	2951680	3191813
5. Indirect Taxes	220697	256903	304879
6. Subsidies	18261	25761	24543
7. Gross Domestic Product (MP)	2938379	3182822	3472149
8. Net Factor Income from Abroad	-25547	-44699	-60816
9. Gross National Product (FC)	2710396	2906981	3130997
10. Gross National Product (MP)	2912832	3138123	3411333
11. Population (in million)	133.01	136.01	139.08
12. Per Capita Income in Rupees (FC)	20377	21373	22512
13. Per Capita Income in Rupees (MP)	21899	23073	24528
Value in PK Rs. Million			
R: Revised			
P: Provisional			
FC: Factor Cost			
MP: Market Price			
<i>Source: State Bank of Pakistan.</i>			

2.1:3 GNP per capita:

The per capita income has bounced back after remaining subdued for the past three years. In real terms, the per capita income has increased by 1.6 percent in 99/2000 as against 9 percent increase of 1998.

With Pakistan's population growing at 2.3 percent, per capita income in year 2001 increased marginally by **0.9** percent compared to **1.6** percent in year 2000.

In terms of US dollar, the per capita rose by 2.1 percent. One positive development about recent rise in per capita income is that it was consistently declining in dollar terms for the four years but bounced back in 99/2000, mainly because of the stable exchange rate. The developments in per capita income are summarized in Table 2.1.3.

Year	FC 80/81 (Rs)	% Growth	Current MP (Rs)	% Growth	US \$	% Growth
96/97	4601	-1	19212	11.5	493	-3.9
97/98	4575	-0.6	20415	6.3	473	-4.1
98/99	4615	0.9	21712	6.4	434	-8.3
99/2000	4688	1.6	22939	5.7	443	2.1
2000/01		0.9				

Source: Economic Survey 99/2000.

2.1:4 GDP – Refer Table 2.1.1

2.1:5 Sectoral Shares as Percentages of GDP

The shares of the various components of the Gross Domestic Product have changed little over last one decade. The shares of agriculture, manufacturing and services have remained, more or less, unchanged. However, when viewed from the longer-run perspective major structural transformation in the components of GDP can be observed. As shown in Table 2.1.4 the share of commodity producing sectors declined from 61.1 percent in 69/70 to 49.7 percent in 2001 and at the same time the share of services sector increased from 38.4 percent to 50.3 percent during the same period. Within the commodity-producing sector, the share of agriculture has declined from almost 39 percent to 25 percent – a decline of 13 percentage points in three decades.

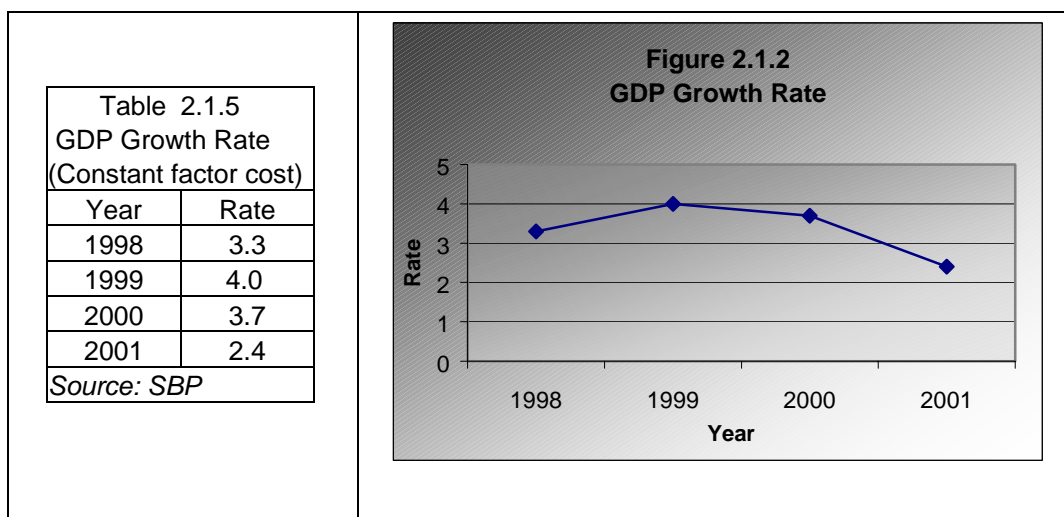
However, what is interesting to note is that the share of manufacturing has remained stagnant over the last three decades. The decline in the share of agriculture sector has been compensated by the almost equal increase in the share of services sector.

The structural transformation has various stages. In the first stage of transformation, the decline in the share of agriculture is compensated by an almost equal increase in the share of manufacturing sector, with the share of services remaining more or less stagnant. In the second stage of development, substitution of share takes place between manufacturing and services with agriculture remaining stagnant. In the case of Pakistan the data reveals only one stage of transformation, i.e. from agriculture to services with manufacturing remaining the same. The details of sectoral share are given in Table 2.1.4.

	69/70	97/98	98/99	99/2000	2000/01
Commodity Producing Sector	61.6	51.4	51	51	49.7
1.Agriculture	38.9	26	25.7	25.9	24.7
- Major Crops	23.4	10.7	10.4	10.9	10.0
- Minor Crops	4.2	4.8	4.9	4.8	4.2
- Livestock	10.6	9.3	9.3	9.2	9.3
- Fishing	0.5	0.9	0.9	0.9	0.9
- Forestry	0.1	0.1	0.1	0.1	0.3
2.Mining & Quarrying	0.5	0.5	0.5	0.5	0.4
3.Manufacturing	16	17.1	17.8	16.8	17.4
- Large Scale	12.5	12.2	12.3	11.7	12.2
- Small Scale	3.5	4.9	5	5.1	5.2
4.Costruction	4.2	3.7	3.4	3.5	3.4
5.Electricity & Gas Distribution	2	4.2	4.2	4.3	3.9
Services Sector	38.4	48.6	49	49	50.3
6.Transport, Storage and Communication	6.3	10.2	10.2	10.1	10.4
7.Wholesale and Retail Trade	13.8	15.4	15.2	14.9	15.2
8.Finance and Insurance	1.8	2.2	2.4	2.5	2.6
9.Ownership of Dwellings	3.4	5.8	5.9	6	6.1
10.Public Administration and Defense	6.4	6.2	6.2	6.3	6.4
11.Other Services	6.7	8.9	9.1	9.3	9.6
GDP (Constant Factor Cost)	100	100	100	100	100
<i>Source: Economic Survey</i>					

2.1:6 GDP Growth Rate

Overall economic activities slackened considerably in FY01.Growth in real Gross Domestic Product (GDP) decelerated from 3.9 percent in FY00 to **2.6** percent in FY01 against the target of 5.0 percent.



This slowdown, originating in the agriculture sector, was imminent due to the drought like situation caused by the acute shortage of water throughout the country. Lower than targeted production of cotton, rice, sugarcane and wheat, pushed the growth of agriculture down to negative 2.5 percent. Counterbalancing the impact of agriculture, industrial sector, with its impressive recovery of 4.2 percent during FY01 (against a decline of 0.1 percent year 2000), provided impetus to other allied sectors of the economy. Commodity producing sectors, primarily due to the fall in agriculture, witnessed marginal growth of 0.8 percent. On the other hand, services performed well at 4.4 percent, which is close to the past ten year annual average of 4.6 percent.

The depressed prospects for cotton and sugarcane, evident by the end of Q1-FY01, had already put into doubt the production target of major crops. By March 2000, unanticipated degree of water shortage, made it apparent that major crops would register negative growth for the year. To deal with the mounting crises, provincial authorities resorted to alternate sources of irrigation.

A great volume of water was released to areas where tube well irrigation was not feasible, while concessionary rates were maintained for electric consumption by tube wells. These steps helped to alleviate the problems brought about by the shortage of water.

A broad based recovery was registered in large-scale manufacturing (LMS), with positive growth posted in all the industrial groups for the first time in the past seven years. The momentum in the 8.4 percent growth started to build early in the year.

Growth in LSM was 10.9 percent by end Q1-FY01, considerably higher than the 3.6 percent achieved during Q1-FY00. This trend continued throughout the year except in Q2-FY01, when late crushing of sugarcane and the closure of sugar mills in first half of December, had created a temporary vacuum. The timely decision regarding imports and processing of raw sugar in Pakistan saved the sugar industry from another crisis; during FY00, the sugar industry declined by 31.6 percent against positive growth of 14.8 percent this year. Items related to petroleum products, fertilizers, home appliances, automobiles and paper products, performed well and surpassed the growth registered last year.

The services sector grew by 4.4 percent during FY01 compared to 4.8 percent last year. Transport, storage and communication and wholesale & retail trade contributed with growth of 4.1 percent and 3.8 percent respectively. As shown in Table 2.1.4, services helped the economy, along with the industrial sector, in arresting the decline momentum brought about by agriculture.

2.1:7 GDP per capita

The GDP per capita income has declined continuously during past three years. In terms of US dollar, the GDP per capita income decreased by 4.3 percent in 2001 compared to decrease of 4.8 percent last year. Refer Table 2.1.6.

	98/99	99/2000	2000/01
GDP (Current Factor cost, in billions of \$)	58.47	57.01	55.78
GDP Growth Rate %	4.2	3.9	2.6
GDP Per Capita	434	414	397

Source: US commercial service.

2.1:8 Investment

Investment activities slowdown considerably during FY01, total investment at current prices grew by only 2.5 percent compared with 8.6 percent in FY00. (See Table 2.1.7). The total Fixed Investment to GNP ratio declined to 14.9 percent in FY01 from 15.8 percent last year. This does not augur well for the economy as investment plays a key role in the potential of the country.

Gross fixed investment, which is the major part of gross total investment, grew by a major 1.8 percent during FY01. Sectoral break up indicates that the deceleration in investment was mainly on account of a marginal decline in private investment from PK Rs 262.2 billion in FY00 to PK Rs 261.9 billion year 2001. Although public investment grew by 4.6 percent in FY01 compared with 2.9 percent last year, it could not stimulate the pace of overall investment. Lack of infrastructure development projects in the recent past seemed to have diluted the “crowding-in” aspects of public investment.

Reasons for downturn – in private sector gross fixed investment

- ❖ The continuing effect of the town survey
- ❖ Lower GDP growth
- ❖ Depreciation of rupee
- ❖ Abnormal profits in textiles due to higher domestic cotton prices in FY01.

More specifically, the weakening Rupee had a direct bearing on the import unit value index of machinery, which went up by 12.6 percent in FY01. Also, leading rates, were higher this year, up from 12.9 percent in FY00 to 14 percent. Moreover, the excess capacity available in industries like cement, sugar and electricity, in the face of sluggish demand, has acted as impediment towards any new investment by private sector.

Table 2.1.7 Investment and Savings					
At Current Prices					
	Growth Rates				
	FY97	FY98	FY99	FY00 (R)	FY01 (P)
1. Gross total investment	8	9	-3.6	8.6	2.5
2. Gross fixed investment	7.7	1.5	1.6	8.7	1.8
Public sector	-5.3	-14.8	25.8	2.9	4.6
Private sector	19.5	13.3	-11.4	13.2	-0.1
3. Net external resource inflow	-2.9	-45	38.7	-47.9	15.5
4. National savings	14.8	37.1	-12.4	27.3	0.8
Public savings	-22.8	-85.8	679.3	-65.5	337.7
General government	-26.2	77.2	96.5	-2075.1	35.7
Others	-4.8	-6.3	-36.4	42.9	49.8
Private savings	19.8	48.5	-18.5	35.1	-6.5
House hold	19.8	48.5	-18.5	35.1	-6.5
Corporate	19.8	48.2	-18.3	35.1	-6.5
5. Net factor income from abroad	-314.2	-22.8	3.5	-53.1	-18.8
6. Domestic savings	23.1	35.8	-11.6	29.7	2.7
	As percentage of GNP				
1. Gross total investment	18.1	17.9	15.7	15.8	14.9
2. Gross fixed investment	16.5	15.2	14.1	14.2	13.3
Public sector	6.9	5.3	6.1	5.8	5.6
Private sector	9.6	9.9	7.9	8.4	7.7
3. Net external resource inflow	6.2	3.1	3.9	1.9	2
4. National savings	11.9	14.8	11.8	13.9	12.9
Public savings	1	0.1	0.9	0.3	1.2
General government	-1	-1.5	0	-1	-0.6
Others	2	1.7	1	1.3	1.8
Private savings	10.9	14.7	10.9	13.7	11.7
House hold	9.6	12.9	9.6	12	10.4
Corporate	1.3	1.7	1.3	1.6	1.4
5. Net factor income from abroad	-1.2	-1.4	-1.2	-1.7	-1.9
	As a % of GDP				
1. Domestic savings	13	16	12.9	15.4	14.5
2. National savings	65.7	82.7	75.1	88.1	86.6
R = Revised P = Provisional					
Source: Federal Bureau Statistics, Planning and Development Division, GOP					

Real fixed investment

Real fixed investment, which is computed after allowing for depreciation of existing capital and the effect of inflation, grew by 0.2 percent in FY 01 compared with 3.6 percent during FY00 (see Table 2.1.8). Its sectoral break up indicates that public sector investment has grown by 5.1 in FY01, compared with 1.6 percent FY00. On the other hand, private sector investment experienced negative growth of 3.5 percent in contrast to 5.1 percent in FY01. Investment in mining & quarrying, electricity & gas distribution and trade sectors, have shown an improvement compared with massive declines observed in the remaining sectors in FY00. The sectoral shifts in investment between manufacturing & services during the last few years, probably reflects a decline in returns, on capital in large-scale manufacturing and construction, relative to investment in transport, storage and communication and mining & quarrying.

Table 2.1.8: Growth of Real Fixed Investment At constant prices of 1980-81						
Sectors	Total fixed Investment		Public fixed Investment		Private fixed Investment	
	FY00 (R)	FY01 (P)	FY00 (R)	FY01 (P)	FY00 (R)	FY01 (P)
Agriculture	8.5	-6	-45	128	19.3	-18.6
Mining and quarrying	-20.8	8	-31.4	28.1	-14.7	-1.3
Manufacturing	-0.5	-12.5	-33.1	-57.8	14.4	-0.5
- Large scale	-0.1	-21.2	-33.1	-57.8	27	-5.4
- Small-scale	-1.2	7.3	-	-	-1.2	7.3
Construction	-4.8	-10.9	-38.3	55.4	6.7	-24
Electricity and gas distribution	-9	3.9	16.3	7.3	-55.8	-12.5
Transport, storage and communication	22.7	-0.6	24.6	-1.1	19.5	0.1
Wholesale and retail trade	11.8	12.5	-	-	11.8	12.5
Finance and insurance	3.2	-0.5	-9.4	4.9	3.7	-0.6
Services	3.2	-0.6	-15.9	7.3	5.7	-1.4
General government	0.8	13.5	0.8	135	-	-
Total	3.6	0.2	1.6	5.1	5.1	-3.5
R = Revised P = Provisional Source: Federal Bureau of Statistics						

2.1:9 Domestic Savings:

Public Savings (Government & Enterprise)

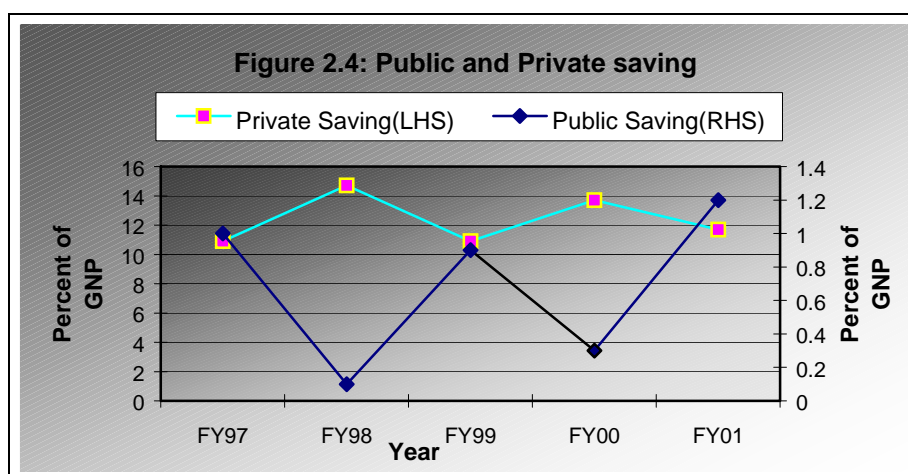
During FY01, public savings showed exceptionally high growth of 337.7 percent as against a decline of 65.5 in FY00 (see table 2.1.7). It's ratio to GNP increased from 0.3 percent in FY00 to 1.2 percent in FY01 (see figure 2.4). This boost in public savings can be attributed to main factors,

1) Higher revenues and lower budget deficit, and (2) improved governance of public sector enterprises.

The overall improved profitability of public sector enterprises is on account of two main factors (1) reducing losses through restructuring and better governance, and (2) improving production by streamlining procedures as well as better marketing.

Private savings

While public savings showed an improvement, private savings declined during FY01. Private savings, which consists of household and corporate savings, recorded a decline of 6.5 percent over FY00. Lower GDP growth and increased consumption of durables by the private sector, may have caused this decline. Production of durables like refrigerators, motorcycles and cars increased on the basis of this higher demand, which was financed by leasing companies. Moreover, import of consumer goods recorded an increase, reflecting high domestic absorption. Also, downward changes in National Saving Schemes (NSS) rates has also contributed to this decline; only PK Rs36.7 billion was invested in NSS during the FY 01, as compared to PK Rs 96.5 billion in FY00.



2.1:10 National Savings:

National savings at current market prices recorded a marginal increase of 0.8 percent to Rs 441.09 billion during the year compared with a rise of 27.3 percent in the preceding year. Consequently, the savings to GNP ratio fell to 12.9 percent to FY01 from 13.9 percent last year (see Table 2.1.7). According to the UN system of National Accounts, savings is a balancing item that arises as a residual of disposable income, which is not used in final consumption. However, the existing system of National Accounts of Pakistan, estimates national savings through the investment approach.

Under the investment approach, savings is derived by taking estimated actual investment and deducting the part financed by external resources, usually labeled as foreign savings. Hence under this approach, the trend in national savings is determined by investment activity and inflows of foreign savings. Given the nature of this approach, it would be difficult to identify the true underlying determinants of savings with much certainty. Furthermore the estimates of national savings are susceptible to errors that occur in the estimation of investment and foreign savings.

2.1:11 Balance of payment

Although FY00 was spent in relative calm, it was clear that Pakistan was unable to enhance repayment capacity as envisioned in the first debt rescheduling agreement. Since the consolidation period was to end in December 2000, this meant that either Pakistan would be in a position to meet normal debt payments in calendar 2001, or it would have to secure another round of debt rescheduling. A pre-requisite for the latter was an IMF program. Given this sense of urgency, Pakistan's economic managers realized that the focus of the IMF stabilization program would be on improving the country's external sector.

The Standby Arrangement (SBA) signed with the IMF in November 2000 enabled Pakistan to resume net inflows from IFI s, and to obtain further rescheduling of its external debt. These actions provided the much-needed comfort to the country's external payments positions.

Despite the global slowdown, Pakistan's balance of payments showed strong signs of improvement during FY01. The most impressive development was the current account surplus of US\$ 331 million, which was achieved for the first time in the history of Pakistan (see Table 2.1.9). A lower trade deficit, but more importantly, a sharp increase in current transfers, was able to exceed higher payments on account of services. Above all, this reversal in BOP was driven by two main factors: (1) a change in the accounting treatment of the Saudi Oil Facility (SOF) from non-food aid (loan) to a straight forward grant (official transfers), and (2) higher than projected purchases of hard currency from the kerb market. If one were to compare the current account deficits for FY99 and FY01, by excluding the role of outright purchases and SOF, the external gap only narrows from US\$ 2,776 million in FY99 to US\$ 2,509 million during FY01.

The capital account witnessed a sharp decline in notional outflows, primarily because of the modalities of Pakistan's debt rescheduling arrangement and the resumption of external assistance; the exceptional financing gap fell from US\$ 3,966 million in FY00 to only US\$692 million during FY01 (see Table 2.1.9). More specifically, the improvement can be traced to the following factors: (1) fresh inflows from IFIs that were not available during FY00, (2) larger inflows in short-term financing (particularly in June 2001), and (3) the absence of restructuring/rollover of Euro bonds, commercial credit (PTMA)(This refers to Pakistan Trade Maintenance Agreement, which is a credit from Commercial banks for the financing primarily of oil imports) and FE-45 deposits, as was the case last year. In fact, FY01 witnessed hard currency payments on account of PTMA and FE- 45.

With the change in the presentation, Pakistan's foreign exchange reserves rose to US\$ 3,219 million as on end-June 2001, from US\$ 1,968 million last year. However, the most visible change was the Rupee/Dollar parity; against almost negligible devaluation during FY00, the sharp depreciation of 18.6 percent seen during FY01, one again revived the domestic dollarization drive.

Table 2.1.9: Balance of Payment			
Million US \$			
	FY99	FY00	FY01
1.Trade balance	-2085	-1412	-1269
Exports	7528	8190	8926
Imports	9613	9602	10195
2.Services (Net)	-2618	-2794	-3137
Shipment	-803	-751	-820
Other transportation	110	71	61
Travel	-122	-142	-180
Investment Income	-1808	-2018	-2156
- Interest Payment	-1399	-1598	-1547
- Profit and dividend	-409	-420	-609
Other goods, services & income	5	46	-42
3. Current Transfers (Net)	2847	3989	4737
Private Transfers	2274	3063	3898
Official Transfers	573	926	839
4.Current account balance (1+2+3)	-1856	-217	331
5.Financing	1856	-1143	-331
Capital Account (net)	-2278	-4177	-648
Foreign Investment	570	-76	137
Direct investment abroad	-44	1	-37
Direct investment in Pakistan	472	472	323
Portfolio investment in Pakistan	147	-549	-149
of which :stock markets	28	73	-140
Foreign long term loans	0	-1087	-636
- Disbursements	2474	1471	1654
Project Aid	1499	988	785
Non - food aid	230	191	0
Non - food aid	550	125	678
Others	195	167	191
-Amortization	2474	2558	2290
Official	2038	1967	1795
Others	436	591	495
Official assistance	-863	-220	432
FCA (non-residents)	-2295	-1884	-96
Outstanding export bills	40	-432	-232
Others	270	-478	-253
Changes in reserves (-inc/+dec)	-824	-72	-1000
Assets	-1254	208	-1085
SDRs	2	0	1
Frex (SBP)	-809	379	-727
Frex (commercial banks)	-447	-171	-359
Liabilities	430	-280	85
Use of Fund credit	430	-280	85
Purchases/drawings	626	0	324
Re-purchases	-196	-280	-239
Errors & omissions	992	499	626
Exceptional financing	3966	3966	692

SBP reserves	1740	1358	2087
SBP reserves (excluding FE-25)	1740	997	1688
<i>Source: State Bank of Pakistan</i>			

2.1:12 Exchange Rates

In sharp contrast to FY00, the PK Rupee/Dollar parity weakened dramatically by 18.6 percent during FY01. It could seem that the Pakistan Rupee has continuously depreciated against US dollar. The depreciation in FY01 is cumulative of two fiscal years-FY00 and FY01. In FY00, the induced stability had kept nominal exchange rate almost unchanged. If this factor is taken into account, the Rupee/Dollar parity returns to its historical trend.

Although, low inflation and a narrowing of the current account deficit characterized FY00, more important was the absence of an IMF program that allowed a degree of freedom to manage the exchange rate as deemed necessary. This leeway allowed SBP to maintain a stable parity during the year, but at the cost of stagnant liquid reserves.

Table: 2.1.10

Exchange rate					
	96/97	97/98	98/99	99/00	2000/01
Australian Dollar	30.53	29.347	29.396	32.567	31.375
Indian Rupee	1.089	1.128	1.0935	1.1901	
Japanese Yen	0.338	0.341	0.3797	0.481	0.5109
Singapore Dollar	27.457	27.056	27.6043	30.530	33.160
Sri-Lankan Rupee	0.682	0.704	0.6869	0.7199	
UK-Sterling Pound	63.068	71.145	76.8085	82.494	84.739
US Dollar	38.994	43.195	46.7904	51.771	58.438
IMF	55.248	58.465	63.685	70.582	

Source: SBP & Economic Review 99/2000.

2.1:13 Interest Rates

The advance rates in Pakistan were very high, compared with other regional countries. In June 1999, weighted average lending rate in Pakistan was 14.8 percent while it was 5.4 percent in Australia, 5.9 percent in China, 12 percent in India and 14 percent in Bangladesh. The higher lending rates are detrimental to a vibrant and promising private sector. In Pakistan, higher lending rates was one of the factors behind the emergence of a mounting debt and default culture, in the 1990s.

Huge loan defaults have adversely affected profitability of the banks and availability of credit to the small but efficient investors and entrepreneurs. Due to mismanagement, mainly as a result of higher cost of lending, huge pre-tax losses were incurred by five major private banks, namely; National Bank Ltd., Habib Bank Ltd., United Bank Ltd., Muslim Commercial Bank Ltd., and Allied Bank Ltd, between 1996 and 1998.

A number of steps were taken in the recent past to bring down the lending rates and increasing the flow of credit to the private sector at lower cost. The State Bank of Pakistan lowered its repo rate twice during 89/99 and 99/2000. The repo rate was reduced from 14 percent in May 1999 to 11 percent in January 2000. As a follow up the five major banks also announced reduction in their lending rates by an average of 1.5 to 2.0 percent points first in April and again in January, 2000. Therefore, the monthly weighted average rate of return on advances (overall) declined to 13.0 percent in June 1999 to 9.4 percent in March 2000 and further to 7.6 percent in May 2000.

To judge the effectiveness of the prevailing lending and deposit rates, the table **2.1.11** shows the real rate of interest.

Table: 2.1.11
Interest Rates

Period	Weighted Average Lending Rate		Weight Average Deposit Rate	
	Nominal	Real	Nominal	Real
June 1997	14.6	2.8	8.5	-3.3
June 1998	15.6	7.8	8.4	0.6
June 1999	14.8	9.1	8.0	2.3
December 1999	14.4	11.0	-	-
Average 2000	14.6	5.8	8.3	-1.6

The real lending rate has registered a sharp increase over the periods, mainly due to declining inflation rate since 97/98.

2.1:14 Inflation:

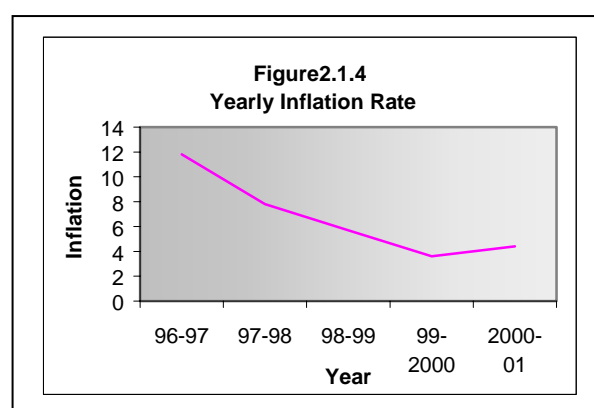
The inflationary pressure, which persisted in the early 90s due to excessive monetary overhang, combined with shortage of essential commodities continued until 1996-97. Inflation rate during the first seven years (1990-97) of the 1990s averaged at 11.8 percent but continued its declining trend thereafter.

Inflation measured on the basis of Consumer Price Index (CPI), declined to 7.8 percent in 97/98 & further to 5.7 percent in 98/99.

The sustained and significant reduction in inflation observed during the last three year constitutes one of the key achievements of Pakistan. (See Table 2.1.12) Relatively it tight monetary policy, improved supply situation of essential items, little upward movements in administered prices, reduction in tax and tariff rates, and depressed international prices of Pakistan's major imports are some of the factors contributed to bringing inflation down to the single-digit level.

Year	Rate of Inflation
	CPI %
96-97	11.8
97-98	7.8
98-99	5.7
99-2000	3.6
2000-01	4.7

Source: Federal Bureau of Statistics
(Economic Survey (2000-01))

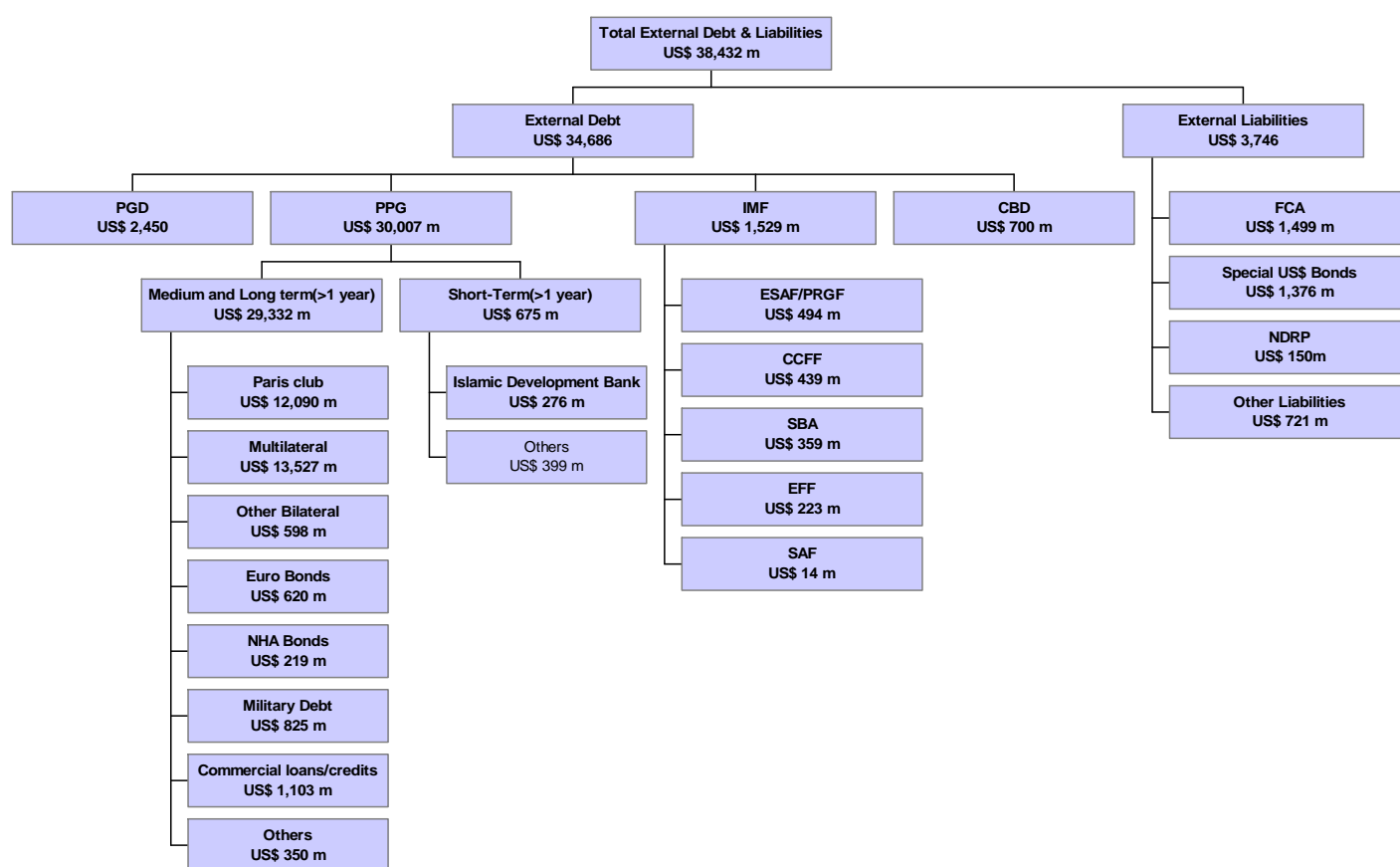


2.1:15 External Debt:

The government's growing indebtedness has become the gravest problem faced by the economy. The stock of total debt has exceeded Pakistan's Gross Domestic Product (a market price); income per capita is lower than per citizen indebtedness. This accumulated public debt is the result of structural weaknesses in the domestic economy and the external account.

Excessive government expenditures, stagnant tax Revenues, high returns on government securities and inappropriate sequencing of financial reforms, led to a bludgeoning domestic debt profile. On the external front, large current account deficits, stagnant export revenues and declining worker remittances, effectively forced Pakistan into an unsustainable situation. Until mid 1998, about half of the current account deficit was financed using inflows into resident and non-resident foreign currency accounts (FCAs); while the remaining part was covered (more or less) by expensive short-term commercial credit.

In rupee terms, FY01 saw the highest one-year increase in total debt mainly driven by large rupee depreciation during the course of the year. The share of external debt has risen to 55.5 percent (see Table **2.1.13**).

Chart 2.1: Pakistan's External Debt and Liabilities-2001

Abbreviations: PGD: Private non-guaranteed debt; PPG: Public & publicly guaranteed debt; CBD: Central bank deposits; CCFF: Compensatory contingent finance facility; ESAF: Enhanced structural adjustment facility; PRGF: Poverty reduction & growth facility; SAF: Structural adjustment facility; SBA: Standby arrangement; EFF: Extended finance facility; NDRP: National debt retirement program.

(Source: State Bank of Pakistan)

Table 2.1.13: Profile of Domestic and External Debt				
Billion Rupees (PK)				
	FY98	FY99	FY00	FY01
Total debt	2,671.90	3,135.40	3,416.20	4,003.30
1. Domestic debt	1,176.20	1,375.90	1,559.90	1,708.50
	-44	-43.9	-45.7	-42.7
2. External debt*	1,483.10	1,695.90	1,788.40	2,223.80
	-55.5	-54.1	-52.4	-55.5
3. Explicit liabilities*	12.6	63.6	67.8	71
	-0.5	-2	-2	-1.8
Total debt as % of GDP	99.8	106.7	107.3	115.3
Domestic debt as % of GDP	43.9	46.8	49	49.2
External debt as % of GDP*	55.4	57.7	56.2	64
Explicit liabilities as % of GDP	0.5	2.2	2.1	2
Total debt servicing	278.3	343.1	353.9	325
Total interest payment	191.6	220.1	256.8	237.1
Domestic	160.1	178.9	206.3	178.8
Foreign	28.7	38	44.9	50.5
Explicit liabilities	2.8	3.2	5.6	7.8
Repayment of principal* (Foreign debt)	86.7	123	97.1	87.9
Ratio of external debt servicing to				
Export earnings	55.4	35.3	36.5	37.4
Foreign exchange earnings	34.9	23.6	23.4	23.3
Ratio of external debt servicing to				
Tax revenue	78.4	87.2	87.2	68.9
Total revenue	64.8	73.2	65.9	57
Total expenditure	43.9	53	47.6	49.5
Current expenditure	52.5	62.7	55	49.3

*External debt is based on new format

*Explicit liabilities include special US \$ bonds, FEBC's and DBC's of which special

US \$ bonds is a foreign liability, while FEBC's and DBC's are also foreign liabilities payable in Rupees. Outstanding stock, so revolution effect is not included

*External debt to GDP ratio calculated by converting the external debt into PK Rupee using end-June exchange rates.

Figures in parentheses are shares in total debt or total interest payment.

Source: 1) SBP 2) MoF

2.1:16 Debt servicing

After the international sanctions imposed in mid 1998, Pakistan's inability to service external debt has led to two consecutive rescheduling by Paris club members and one from the quasi London club. After the end of first consolidation period in December 2000, it was clear that Pakistan was unable to build its repayment capacity. Consequently, another round of rescheduling was sought from sovereign and commercial creditors. Following the finalization of the SBA in November 2000, in January 2001, the Paris club other bilateral and commercial creditors agreed to restructure debts worth about US\$1.8 billion.

Despite this rescheduling, Pakistan has made debt payments from its own resources amounting to US\$ 3.2 billion and US\$ 3.7 billion in FY00 and FY01 respectively. If servicing of external liabilities is included, the total payments made out of its own resources were US\$ 3.8 billion in FY00 and US\$5.1 billion in FY01. It may be seen that the relief from debt rescheduling and rollover was only US\$2.8 billion in FY01. Compared to US\$ 4.0 billion in FY00. Such large payments and accumulation of net services to the level of US\$ 1.7 billion by end of June 2001 should dispel the popular view that Pakistan has to rely mainly on rescheduling from sovereign and commercial creditors to manage debt servicing. As a matter of fact, rescheduling only accounted for 35 percent of total debt service obligations.

Over the last decade, unsustainable commercial borrowing imposed a heavy burden on external payments. Pakistan's external debt/liabilities have risen from just over US\$ 22.0 billion in the late 1980s to over US\$ 38.0 billion at the end of the 1990s. More damaging is the shift towards short-term commercial loans, which had not only increased the volume of indebtedness per se, but also put tremendous pressure on yearly debt payments. However, the freeze on FCAs, low disbursements from IFIs and smaller inflows of commercial credit, have slowed the growth in the last few years.

Provisional estimates for year 2001 show that the total stock of external debt and liabilities has remained almost unchanged compared to year 2000 (revised estimates – see Table 2.1.14 and Chart 2.1).

Table 2.1.14: Pakistan's External Debt and Liabilities			
Million US\$			
	FY99	FY00 (R)	FY01 (P)
1.Public and publicly guaranteed debt	26,904	29,189	30,007
A. Medium and long term (>1 year)	26,486	28,628	29,332
Paris club	11,873	12,428	12,090
Multilateral	10,599	12,292	13,527
Other bilateral	629	639	598
Eurobond	608	620	620
Foreign currency bonds	263	241	219
Military debt	1,004	958	825
Commercial loans	1,160	1,100	1,103
Other	350	350	350
B. Short term (<1 year)	418	561	675
IDB	152	130	276
Others	266	431	399
2. Private non guaranteed Debts	3,435	2,842	2,450
3.Central bank deposits	700	700	700
4.IMS	1,825	1,550	1,529
Total external debt	32,864	34,281	34,686
5.Foreign external liabilities	3,736	3,942	3,746
Total external liabilities (1 to 5)	36,600	38,223	38,432
External liabilities payable in Rupees	3,391	1,720	1,243
<i>Source: SBP</i>			

2.1:17 Employment

The employed labor force is defined as all persons of ten year of age and above who worked at least one hour during the reference period, either as “paid employees” or “self employed”

The distribution of employed labor force by Rural / Urban areas is given in Table 2.15.

Table 2.1.15						
Employed labor Force by Area (million)						
Year	Employed Labor force	Annual Growth (%)	Rural		Urban	
			No.	% Share	No.	% Share
1996	32.6	2.5	22.9	70.3	9.7	29.7
1997	34.6	6.2	24.1	69.7	10.5	30.3
1998	35.4	2.4	24.6	69.5	10.8	30.5
1999	36.2	2.3	25.0	69.1	11.2	30.9
2000	37.0	2.3	25.4	68.6	11.6	31.4
2001	40.0	7.5				

Employed labour force by sectors

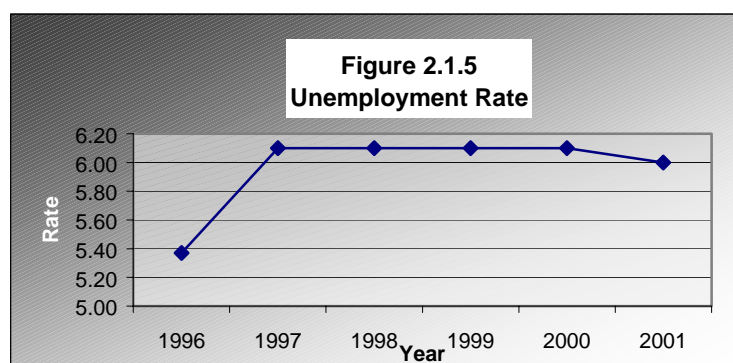
Changes in the growth patterns of the economy over the years have brought corresponding changes in the employment structure. Agriculture, the single largest contributor to the GDP, remained the single largest employer of Pakistan Work force. As economy develops over the time, the share of agriculture in GDP and employment has gradually declined while that of manufacturing increases.

Sector	1994		2000	
	No	Share %	No.	% Share
Agriculture	15.9	50.0	16.3	44.1
Manufacturing & Mining	3.2	10.1	4.2	11.2
Construction	2.1	6.5	2.5	6.8
Wholesale & retail trade	4.1	12.8	5.4	14.6
Transport	1.6	5.0	2.1	5.7
Finance, community & Social services	4.7	14.7	5.8	15.6
Others	0.3	0.9	0.7	2.0
Total	31.9	100	37.0	100

Unemployment

The rate of unemployment is higher in urban areas than in rural areas.

Year	Population (million)	Unemployed Labor Force			Unemployment Rate (%)		
		Total	Urban	Rural	Total	Urban	Rural
1996	125.4	1.9	0.7	1.2	5.37	6.90	4.80
1997	128.4	2.3	0.8	1.3	6.10	7.10	5.70
1998	131.5	2.3	0.8	1.5	6.10	7.10	5.70
1999	134.5	2.3	0.9	1.5	6.10	7.10	5.70
2000	137.5	2.4	0.9	1.5	6.10	7.10	5.70
2001	140.5				6.00		



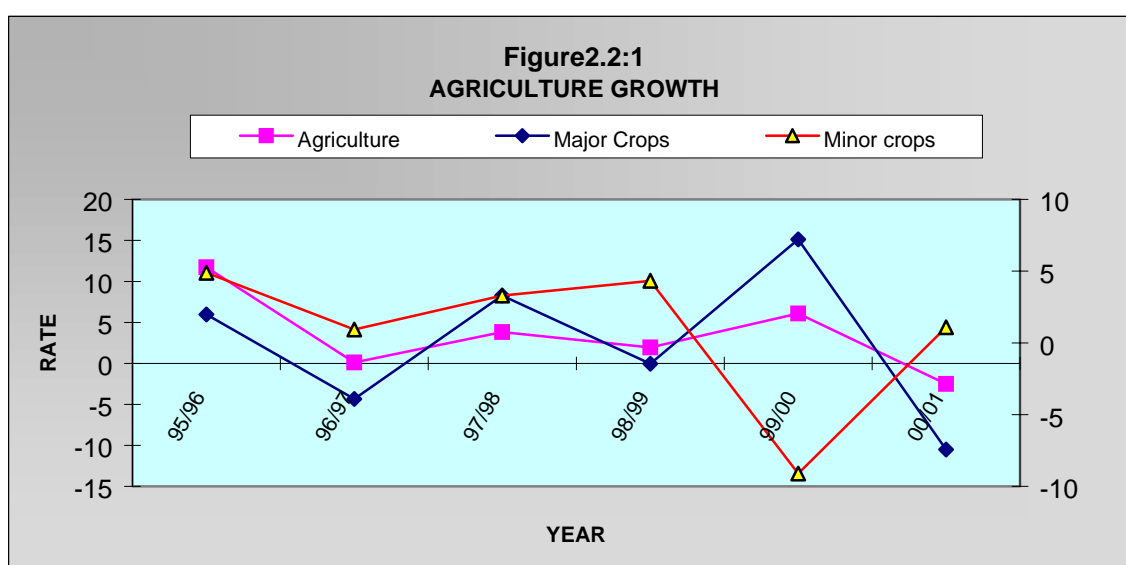
Source: Economic Review, US Trade

2.2 Economic Affairs

2.2:1 Major Agriculture Sectors

Although the economic importance of agriculture in terms of its contribution to GDP has been declining over the last 25 years, this sector still accounts for a large share of GDP and employment in many developing countries. In Pakistan, agriculture still contributes slightly above 25 percent to GDP, employs around 44 percent of work force, is the main source of foreign exchange earnings, and provides linkages through which it can stimulate growth sectors.

Being in such a dominant position, the growth of agriculture is itself a major component of overall economic growth. Over the last one decade, agriculture grew at an annual average rate of 4.4 percent with large fluctuation mainly on account of weather conditions and pest attacks on crops. Agriculture has also been suffering from various problems, such as traditional methods of farming, low yields, shortage of key inputs (credit, fertilizer, improved seeds), adulterated pesticides, unstable price market, and little attention to the sub sectors other than crop farming. The trends in agriculture growth is depicted in Figure 2.2:1



After achieving impressive growth of 6 percent last year (2000) the agriculture sector could not meet the 2.6 percent growth target and ended FY 01 with negative growth of 2.5 percent. (See table 2.2:1) This reversal was mostly due to shortage of irrigation water that persisted both in Kharif (May-Sept.) & Rabi (Oct-April) seasons, with supply 15.8 percent & 28.8 percent lower this year compared to already depressed levels during the corresponding seasons last year.

	Growth Rates		Share in Agriculture	
	FY00 (R)	FY01 (P)	FY00 (R)	FY01 (P)
Agriculture	6.1	-2.5	100	100
Major Crops	15.1	-10.5	44	40.4
Wheat	26.5	-20	14.1	11.6
Cotton	31.9	-6.3	12.2	12.2
Rice	12.7	-10.7	7.2	6.6
Sugarcane	-13.4	-7.7	5.8	5.5
Other crops	-4.8	5.9	4.1	4.4
Minor crops	-9.1	1.1	16.3	17
Livestock	2.4	4.8	35.1	37.7
Fishing	9.7	-3.6	3.6	3.5
Forestry	113	40.4	1	1.4

Source: SBP

The performance of major agriculture sector is described bellow.

Major crops:

This is the swing factor in the sharp reversal posted by agriculture this year (2001). Although the country's major crops accounted for 40.4 percent of agriculture and around 10.0 percent of GDP in FY01, it could not repeat the 15.1 percent growth recorded last year. Pakistan's major crops posted negative growth of 10.5 percent this year. Among major crops, production of food grains (wheat, rice, bajra, jowar, maize, barley) decreased by 8.5 percent to 26.0 million tones during FY01, while sugarcane, cotton and mustard decreased by 5.9 percent, 4.3 percent and 8.1 percent, respectively. Value added by Pakistan's four major crops –wheat, rice, sugarcane and cotton, dropped by 12.2 percent in contrast to a sharp rise of 17.6 percent last year. Not only did the scarcity of water limit the farmers' ability to maintain area under cultivation at last year's level, it also adversely impacted the per hectare yield of these crops.

<p style="text-align: center;"><u>Rice</u></p> <p>A simpler, labor and resource saving technique of raising mat type rice nursery was simplified and demonstrated successfully at farmers field. Rice transplanting with Chinese Modified Rice Transplanted was demonstrated in major rice growing areas of Punjab.</p>	Table: 2.2: 2 Growths in Important Major Crops (Percent)				
			Change in FY01 OVER FY00		
		Share In major crops	Area	Production	Yield
	Sugarcane	15.2	-4.9	-5.9	-1.1
	Cotton	28.0	-1.9	-4.3	-2.7
	Rice	16.3	-5.5	-6.8	-1.4
	Wheat	30.0	-3.3	-9.8	-6.7
Total	89.4	-3.5	-7.0	-1.4	
<i>Source: State Bank of Pakistan</i>					

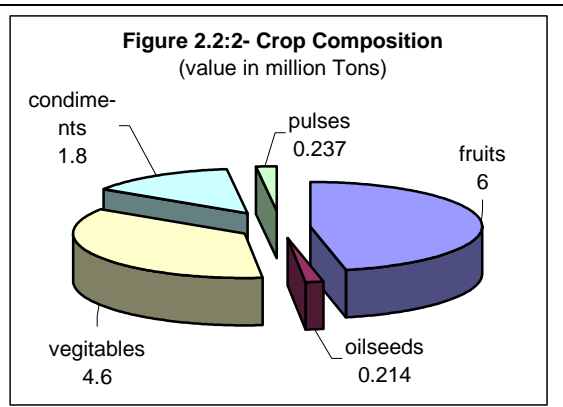
Minor Crops

Minor crops with 17.0 percent share in agriculture and 4.2 percent share in GDP, posted positive growth of 1.1 percent during FY01 against a decline of 9.1 percent last year. Given the variety of items included (e.g., vegetables, fruits, condiments, oil seeds and pulses-excluding gram), growth in individual crops showed a mixed trend. Production of oil seed declined by 3.4 percent while that of pulses increased by 6.2 percent. The other important minor crops: potatoes and onion registered declines of 9.2 percent and 9.7 percent, respectively.

A comparison of absolute numbers during the year reveals that total value addition by minor crops was PK Rs 27.9 billion, which was marginally higher than PK Rs 27.5 million realized last year. Nevertheless this is well below the PK Rs 30.3 billion and PK Rs 29.1 billion contributed during FY99 and FY98, respectively. However, there was a useful degree of reshuffling amongst the components, with fresh fruits emerging as the leading item. (See Figure 2.2:2)

Fruits/vegetables

Law chilling varieties of peach, plum and apple have been identified and are being multiplied for distribution to farmers. Better quality varieties of olive, guava and oranges have been identified. True Potato seed (TPS) technology is developed. At Tissue Culture Labs, virus free seed potatoes, produced and supplied to private sector for multiplication and distribution.



Livestock

Livestock is an important sector of agriculture in Pakistan, which accounts for nearly 37.7 percent of agriculture and 9.3 percent of GDP this year, on the basis of a doubling of its growth rate (to 4.8 percent) compared to last year. As the second largest contributor to agriculture after crops, this year's performances compensated to some extent the fall in agricultural production. With strong growth in poultry products (white meat and eggs), all other components of livestock, both in terms of population and products, showed positive growth.

Its net foreign exchange earnings were to the tune of PKRs 35.0 billion in 98/99, which is about 9 percent of the overall export earnings of the country. The role of livestock in rural economy may be realized from the fact that 30-35 million rural populations are engaged in livestock rising. The livestock include: cattle, buffalo, sheep, goat, camels, horses, asses and mules.

Production from livestock sector includes: milk, beef mutton, poultry meat, wool, hair, bones, fats, blood, eggs, hides and skins.

Fishing

Value added by fishing declined by 3.6 percent in FY01 against positive growth of 9.7 percent last year. This includes all commercial and substance fishing in coastal & offshore waters, rivers, canals, lakes, ponds and inundated tracks. As detailed information on fishing this year is still not available, we will use export data on fish and fish preparation as a proxy to analyze growth in the sector. Compared to positive growth of 13.7 percent (in exports of fish and fish preparation) during FY00, a decline of 8.8 percent was registered year1999. Despite this sharp fall in the quantity of export, receipts only fell by .8 percent.

This was on account of a 8.7 percent increase in the unit value of such exports, which was made possible by maintaining better hygiene conditions at harbors, and improving processing procedures as recommended by the European Union during FY01.

Forestry

Forestry registered an impressive growth of 40.4 percent this year compared to an even higher growth of 113.0 percent during FY00; its share in agriculture value added is, however, miniscule (0.3%). Forestry covers logging and the gathering of uncultivated forest products and can be classified in to two groups: (1) major products that include industrial wood like timber and firewood, and (2) minor products like grazing fodder, resin, medical herbs, etc. Although disaggregated data is sketchy, there is some evidence to say that these growth rates have been achieved on the basis of unsustainable deforestation.

Total forest area of Pakistan including rangelands is 10.5 million hectares. Out of the total forest area, 1.4 million hectares are the productive forests and the remaining are protected forests.

Pakistan is deficit in timber production and a demand gap of 734.7 thousand cubic meter of timber was met from imports. A large quantity of wood based products is imported annually to meet local demand. To earn foreign exchange, Pakistan also exports forest products. The export of wood based sport goods, which accounted for 66.9 percent of the total exported forest products.

2.2:2 Major Industry Sectors

Contrary to the decline of 0.1 percent last year, the industrial sector recovered with 4.2 percent growth in FY01. This recovery was led by the manufacturing sector, which dominates industrial activities with around 69.4 percent share. The sectoral growth of industrial sectors is as Table 2.2.3

	Growth rates		sectoral shares	
	FY 00	FY01	FY00	FY01
Manufacturing	1.4	7	67.5	69.4
- Large scale	-0.2	7.8	47.1	48.8
- Small scale	5.3	5.3	20.4	20.6
Mining & quarrying	6.1	-0.4	1.9	1.8
Construction	5.2	-0.4	14	13.4
Electricity & gas	-9.8	-3.1	16.6	15.4
Industry	-0.1	4.2	100	100
Source: SBP				

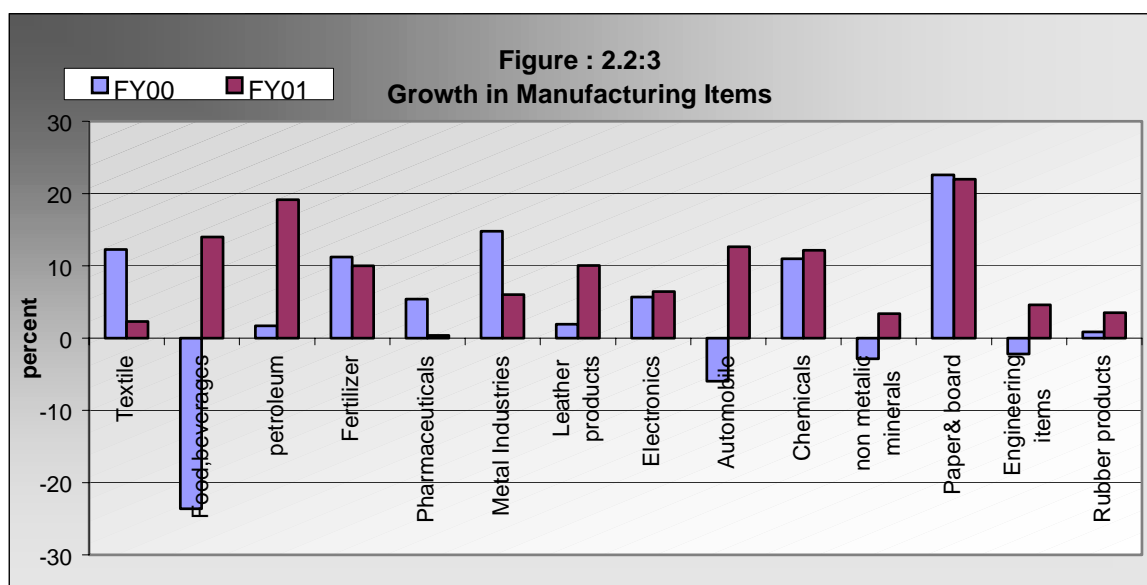
Manufacturing

It is staged a strong recovery with 8.4 percent growth during 2001 against a 0.1 % decline last year. The growth in large scale manufacturing in 2001 is broad based; for the first time in seven years, all industrial groups recorded positive growth.

More specifically, the production of sugar, cigarettes, vegetable ghee and cooking oil increased significantly during the year, against sharp declines last year. This is also evident from the fact that excluding these four items, LSM grew by only 6.7 percent during FY01 as compared to 8.4 percent FY00.

Table 2.2:4 Production of Selected Large - scale Manufacturing items

Items	Percentage change		
	Weight	FY00	FY01
Textile	19.069	12.27	2.32
Food, beverages	17.336	-23.6	14
Petroleum	7.824	1.71	19.17
Fertilizer	5.871	11.23	9.98
Pharmaceuticals	5.798	5.4	0.37
Metal Industries	3.317	14.81	6.02
Leather products	2.333	1.92	10.05
Electronics	2.976	5.68	6.41
Automobile	2.413	-5.94	12.65
Chemicals	2.335	10.99	12.18
Non metallic minerals	1.915	-2.86	3.36
Paper& board	1.359	22.59	21.99
Engineering items	0.691	-2.22	4.6
Rubber products	0.452	0.83	3.54



Mining & Quarrying and Electricity Generation

Share in Overall Industry	1.8%
Growth-FY01	-0.4%
-FY00	6.1%

Value addition by mining and Quarrying declined during FY01, compared to sound growth in the previous year. The major industries use these minerals include ceramics, glass and the chemical industry. The largest producer of ceramics in the country (Federal Chemicals and Ceramics Corporation) closed down its operation during the year 2001.

	Growth Rates	
Coal	-6.3	3.3
Crude oil	-49.0	3.4
Natural gas	10.8	7.0
Lime stone	1.3	13.3
Rock salt	14.1	2.7
China clay	-6.0	-26.6
Gypsum	46.7	2.5
Silica sand	5.7	-7.2
Chromites	39.5	-36.8

Growth in electricity generation declined primarily due to lower hydropower generation on account of the prolonged dry spell in the country.

Construction

Share in overall industry		13.4%
Growth	FY01	-0.4%
	FY00	5.2%

Constrained development spending, slack construction activities and rising building material prices, are the major factors for the fall in value addition by construction during FY01. At a micro level, two major developments took place this year that hindered house building and commercial construction.

First, the House Building Finance Corporation (HBFC) suspended disbursement of loans to housing of different modes of financing.

Secondly, the Karachi Building Control Authority (KBCA) formulated by-laws regarding the evaluation and approval of building projects, which has increased the cost of construction projects.

Electricity and Gas Distribution

Share in overall Industry		15.4%
Growth-FY01		-3.1%
	FY00	-9.8%

Although value addition by electricity and gas distribution fell by 3.1 percent during FY01, this still shows an improvement over the 9.8 percent decline last year. While the retail distribution of natural gas increased on account of more CNG stations during the year, transmission and distribution of electricity suffered due to the fall in electricity generation and poor financial conditions of Pakistan's public utilities.

Public sector Enterprises

Contrary to last year, production and net sales of public sector industries improved last year other than Pakistan steel mills corporation. Increase in fertilizer prices and higher production pushed up value growth in NFC; while strong growth in automobile demand, provided a boost to the production and net sales of PATO.

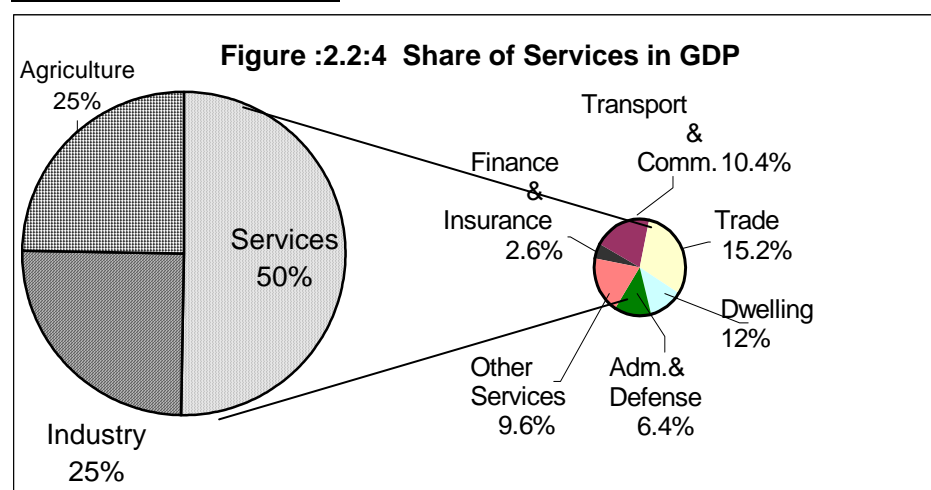
Table 2.2:6

Performance of selected public sector industries
Billion Rupees (PK)

	Production Value		Percentage Change	
	FY00	FY01	FY00	FY01
National Fertilizer Corp;	3.5	3.9	12.3	88.3
Pak Automobile Corp;	0.2	0.3	15.4	6.5
State Cement Corp;	0.6	0.4	-26	-5.5
State Engineering Corp;	1.3	1.3	-1.5	20.5
Pakistan Steel	5.6	5.9	3.8	5.4
Gross total	13	13	4.3	2.9

Source: SPB

Share of Services in GDP



2.2:3 Trade

Trade margins were estimated on the basis of Survey of Distributive Trade & Services 1984-85. Growth in this sector during fiscal year 2001 increased by 3.8 percent compared to 2.9 percent of last year. The developments in this sub sector are closely attached to the level of domestic production, consumption & import of consumer and capital goods. Within commodities, wholesale traders earn the highest trade margin, i.e. about 40 percent on manufactured products that enters in to the market for onward transactions. The higher contribution shown by manufacturing and imported goods also mitigated the impact of the agricultural slow down, in wholesale & retail markets.

2.2:4 Tourism

The Sports & Tourism Wing of the Ministry is the main body responsible for making policies and plans for the development and promotion of sports and tourism in the country. The wing is also responsible for implementation of the plans and projects in these areas.

Tourism Growth

In 1999, Pakistan attracted around 4,32,200 tourists from overseas and earned US\$ 76.4 million as foreign exchange receipts. The number of foreign tourist arrivals in the South Asia region was 5.

Tourist information centers in Pakistan for information, local assistance and booking of PTDC hotels, motels, transport and tours, can be obtained from PTDC Tourist Information...Centers <http://www.tourism.gov.pk/tourist_info_centers.html>

(Source: www.tourism.gov.pk)

2.2:5 Investment

Foreign investment

Although the government is making efforts to persuade foreign investors to invest in Pakistan, efforts have remained unsuccessful. During FY01 total foreign investment declined by US\$361.4 million from US\$ 543.4 million in the proceeding year. In terms of portfolio investment, there was an outflow of US\$140.4 million compared with in flow of US\$ 73.5 million. The heavy outflow of portfolio investment is mainly on account of a foreign fund that closed its operation in Pakistan. Although direct foreign investment also showed an absolute decline of US\$ 147.5 million over last year, its sectoral break up indicates that some sectors still remain attractive to foreign investors (see Table 2.2:3)

Million US \$	(Net)					
	FY98	FY99	FY00	FY01	Absolute change	
					FY00	FY01
Food, beverages and tobacco	19.1	7.4	49.9	45.1	42.5	-4.8
Textiles	27.3	1.7	4.4	4.6	2.7	0.2
Chemicals, Pharmaceuticals & fertilizers	72.1	54.1	119.9	26.3	65.8	-93.6
Petro chemicals and petroleum refinery	1.6	38.8	12	8.7	-26.8	-3.3
Cement	3	2	0.1	15.2	-1.9	15.1
Machinery	11.4	14.6	4.6	2.5	-10	-2.1
Electronics	2.7	1.2	2.3	2.8	1.1	0.5
Power	239.5	131.4	67.4	40.3	-64	-27.1
Construction	21.5	13.9	21.1	12.5	7.2	-8.6
Trade, transport, storage and communication	20.1	38.8	38.6	96.5	-0.2	57.9
Financial business	20.4	24.4	29.6	-34.9	5.2	-64.5
Mining & quarrying-and oil & gas	99.1	112.8	79.7	84.7	-33.1	5
Others	63.5	31.2	40.3	18.1	9.1	-22.2
Total	601.3	472.3	469.9	322.4	-2.4	-147.5

Source: State Bank of Pakistan

Foreign Direct Investment (FDI) registered a 31 percent decline, which is very disappointing compared to inflows of US\$ 472 million in 2000. Although, FY01 provided a better investment climate than the year before, in terms of the SBA and an amicable settlement of the longstanding dispute with Hubco, this could not translate into higher FDI.

In terms of FDI by economic groups, *chemicals & fertilizer, power (IPPs), food, beverages & tobacco*, and *construction* received lower inflows in FY01.

Mining and quarrying and oil and gas continued to be the preferred area for foreign investment in Pakistan. Union Taxes Pakistan, Lasmo Oil, Premier Exploration Pak, GECO Prakla Int.Ltd., Ocean Pakistan Ltd., Shell Developers & Offshore Pak and Orient Petroleum, were the leading companies in this sub sector. The increasing flow of foreign investment in this sector is driven by the policy measures taken by the government. This provided by impetus to exploration of oil & gas, which was largely ignored in the past. With the revival of Saindak copper project and further exploration of Lakhra coal reserves; the chances of attracting more foreign investment are brighter.

Trade, Transport, Storage and communication also fetched US \$ 96.5 million FDI, compared with US\$ 38.6 million in FY00. The improvement is to be seen in the context of fiscal relief given in the Federal Budget and follow-up steps for the promotion of information technology and software development in the country. Policy measures initiated during FY01 **mainly included duty-free imports of computer hardware and accessories in Internet tariff for ISP s etc. Textiles, electronics and construction have also shown an improvement in attracting FDI during the year2001.**

However, foreign investment in some sectors declined. In power it stood at \$ 40.3 million in FY01 compared to US\$67.4 million during last year. The break up in power reveals a large a share by Liberty power, Uch Power Ltd., Ghazi Brotha Hydro Power and Rousch (Pakistan) Power Ltd.

The slow down of foreign investment in power was mainly on two accounts: (1) saturation of foreign investment following the power policy of 1994 and (2) given the problems in the past, IPPs are engaged in consolidating their operations rather than expanding.

The inflow of foreign investment in chemicals, pharmaceuticals and fertilizer, also declined to US\$ 26.3 million during FY01 compared with US\$ 119.9 million last year. During the previous year, the considerable inflow to this sector was primarily on account of the commissioning of ICI's PTA plant that attracted about 38 percent of total FDI.

Notwithstanding significant deregulation followed by various incentives and efforts of the government, Pakistan is still trying to pave the way for further inflow of foreign investment. Historically, the USA, UK and Japan are the largest source of FDI in Pakistan. However, this had declined over the year on account of various reasons. Certain exogenous factors may also be responsible; merger and acquisition amongst multi national corporations, recession in US economy, lack of progress on privatization and the lackluster performance of stock exchanges in the country during FY01.

Inflow of Foreign Private Direct Investment in Pakistan
(In millions of US \$)

Country	98/99	99/00	00/01
USA	214.6	166.9	68.3
UK	89.3	169.0	82.7
UAE	6.9	5.7	4.2
GERMANY	19.8	10.5	12.0
FRANCE	9.8	1.6	0.7
JAPAN	59.0	17.7	8.3
SAUDI ARABIA	22.8	28.6	45.6
NETHERLANDA	5.9	10.7	3.2
KOREA	4.6	9.3	3.7

Source: State Bank of Pakistan-2000/01 data for ten-month period July-April

The United Kingdom has been the second largest foreign investor in Pakistan after the U.S. during the last three years with \$341million in foreign direct investment, followed by Saudi Arabia (\$97 million), Japan (\$85 million), and Germany (\$42.3million) Figures for Pakistani direct foreign investment abroad are unavailable.

Source: U.S. Department of Commerce.

2.2:6 Investment policies

Pakistan's **Investment Policy** has been formulated to create an investor-friendly environment, with a focus on further opening up the economy and marketing the potential for direct foreign investment. The essence of the policy is to strengthen Pakistan's competitiveness by improving the policy regime, offering fiscal and tariff relief and providing comprehensive facilitation services.

Pakistan's investment policy, generally recognized as one of the most favourable in the region, has long been characterized by steady moves to liberalization, deregulation, and privatisation.

Main Features of the Investment Policy

- All industries are open to investment without government permission (except four specified industries)
 1. Arms & Ammunitions
 2. High Explosives
 3. Radio-Active Substances
 4. Security Printing, Currency or Mint

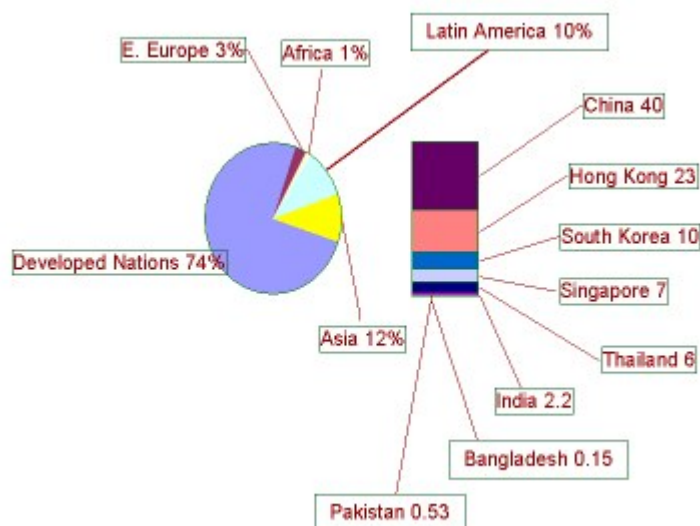
- Liberalization of service, infrastructure, social, and agriculture sectors for foreign investment (please track recent developments through the BOI's Web Site) <http://www.pakboi.gov.pk>
 - Industrial, infrastructure, and social sectors open to 100 percent foreign ownership
- Services has an upper limit of 60 percent foreign ownership (100 percent foreign equity allowed in services for the first five years)
 - Complete freedom of choice on location of activities
 - Full repatriation of capital, profits and dividends from all activities
 - Royalty, technical, and franchise fee payments allowed for all sectors
- No requirement of minimum investment amount in the industrial and agricultural sector. Requirement of minimum investment of US\$ 300,000 in infrastructure, social and services.
- Duty-free import of machinery for high technology, value-added, export industries, and corporate agriculture

Tariff incentives

- Duty exemption on machinery and equipment for IT and Agriculture sector. Customs duty at 5% only will be charged on import of Plants, Machinery and Equipment (PME) for value added. Export and hi-tech industries
- Concessional import duty at 10% on PME for other priority industries, services, infrastructure, and social sector projects

Tax incentives

- Tax relief (first-year allowance) for PME costs
 1. 90 % for value-added, export, and hi-tech industries
 2. 75% for other priority industries, infrastructure, and corporate agriculture
 3. 50% for services and social sector



World investment

Source: www.pakboi.gov.pk

2.2:7 Bi-lateral multi-lateral and Regional Agreements and Arrangements

Pakistan Administrative Arrangement Regarding Textiles

The following provisions are drawn from the United States - Pakistan bilateral textile and apparel agreement of November 10 and December 15, 1994 and have been agreed to be necessary for the proper implementation of restrictions notified to the Textiles Monitoring Body under Article 2.1 of the Agreement on Textiles and Clothing.

CLASSIFICATION

Tops, yarns, piece goods, made-up articles, garments, and other textile manufactured products (being products which derive their chief characteristics from their textile components) of cotton, wool, man-made fibers, silk blends, non-cotton vegetable fibers, or blends thereof, in which any or all of these fibers in combination represent the chief weight of the product, are subject to this Agreement. Components of an article which are not considered relevant to the classification under the General Rules of Interpretation or the Legal Notes to Section XI of the Harmonized System are likewise to be disregarded here.

Membership in Free Trade Arrangements

Pakistan is a member of the World Trade Organization (WTO). Pakistan is not a member of any free trade arrangement, but is party to two arrangements, which are seeking progress toward regional trade liberalization. The Economic Cooperation Organization (ECO), whose founding members are Pakistan, Turkey, and Iran, grants a 10 percent tariff preference on statutory rates for some goods.

(ECO membership was expanded to 10 in 1993, when Afghanistan, Azerbaijan, and the five formerly Soviet Muslim republics of central Asia were admitted.)

The South Asian Association for Regional Cooperation (SAARC) is comprised of India, Pakistan, Bangladesh, Sri Lanka, Nepal, Bhutan, and the Maldives. SAARC has proposed a South Asian Preferential Trading Agreement (SAPTA), which became operational after ratification by member countries in November 1994. Because the SAPTA provides for product-by-product negotiation, and because several members have similar production structures, therefore, SAPTA is not likely to have a large immediate impact on regional trade flows.

Pakistan's leading regional trading partners are, Bangladesh (its former eastern wing), India and Sri Lanka.

Pakistan is also a member (along with India and Nepal) of the Asian Clearing Union, which was founded in 1976 and aims at facilitating multilateral payments through the use of currencies of participating countries in regional transactions in order to expand intra-regional trade and save convertible foreign exchange.

Source: U. S. Department of Commerce - National Trade Data Bank, September 3, 1999.