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PAKISTAN

April 2015

SIXTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND MODIFICATION OF PERFORMANCE CRITERIA—STAFF REPORT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR PAKISTAN

In the context of the Sixth Review Under the Extended Arrangement and Modification of Performance Criteria, the following documents have been released and are included in this package:

- The **Staff Report for** the Sixth Review Under the Extended Arrangement and Modification of Performance Criteria prepared by a staff team of the IMF for the Executive Board's consideration on March 27, 2015, following discussions that ended on February 5, 2015, with the officials of Pakistan on economic developments and policies underpinning the IMF arrangement under the Extended Fund Facility. Based on information available at the time of these discussions, the staff report was completed on March 12, 2015
- A **Staff Supplement** of March 26, 2015 updating information on recent developments.
- A **Press Release** including a statement by the Chair of the Executive Board.
- A **Statement by the Executive Director** for Pakistan.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Pakistan*
Memorandum of Economic and Financial Policies by the authorities of Pakistan*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

PAKISTAN

March 12, 2015

SIXTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND MODIFICATION OF PERFORMANCE CRITERIA

EXECUTIVE SUMMARY

Extended Arrangement under the Extended Fund Facility (EFF): A 36 month, SDR 4,393 million (425 percent of quota) Extended Arrangement under the EFF was approved by the Executive Board on September 4, 2013 and the fourth and fifth reviews were completed on December 17, 2014, for a total disbursement of SDR 2,160 million. The sixth tranche amounting to SDR 360 million will be available upon the completion of this review.

Status of the program: All end-December 2014 quantitative performance criteria (PCs) were observed, as well as the indicative target on cash transfers under the Benazir Income Support program (BISP). Although the indicative target on federal tax revenues was missed, the authorities have taken actions to address the shortfall and are on track to meet the end-March 2015 indicative target. The end-December 2014 structural benchmark (SB) on amendments to the relevant tax laws and submission of the Anti-Money Laundering Act (AMLA) was met, as were the end-February SBs on enhancing internal operations and risk management of the State Bank of Pakistan (SBP) and improving monetary policy operations. Adjustments to the end-March PCs on NIR and NDA are proposed to reflect higher reserves accumulation by the SBP and new end-June PCs and four new SBs are proposed.

Key issues: Discussions focused on: (i) saving the windfall from falling oil prices to strengthen buffers—including foreign exchange reserves and the fiscal stance—against adverse shocks; (ii) preventing a further loss of export competitiveness; (iii) reducing electricity subsidies; (iv) introducing compensatory measures to cover the revenue shortfall; (v) steps to broaden the tax base and improve tax administration; (vi) progress on safeguarding financial stability and expanding credit growth; (vii) enhancing structural reforms in the energy sector, central bank independence, anti-money laundering framework, public debt management, trade, and the business climate to unlock Pakistan’s long-term growth potential. The mission retained its growth projection at 4.3 percent, but lowered inflation forecast to 5.5 percent for FY2014/15. Risks are balanced with downside risks due to political uncertainties and security challenges, and upside risks from further falls in oil prices. Outreach activities included a press release, press conference (held in Dubai) and bilateral interviews with journalists.

Approved By
Mark Flanagan and Daniela Gressani

Discussions took place in Dubai during January 26–February 5, 2015. Staff representatives comprised J. Franks (head), H. Finger, A. Shahmoradi, C. Geginat, (all MCD), K. Al-Saeed (MCM), S. Cevik (FAD), T. Mirzoev (Resident Representative), and H. Zaidi (Resident Representative Office, Islamabad). J. Mojarrad (ED) joined the mission. Ferhan Salman, Botir Baltabaev, (MCD) and Camilo Tovar (SPR) contributed from Washington D.C. M. Orihuela-Quintanilla and Y. Liu assisted in the preparation of the report. The mission chief issued a press release in Dubai on February 5, 2015.

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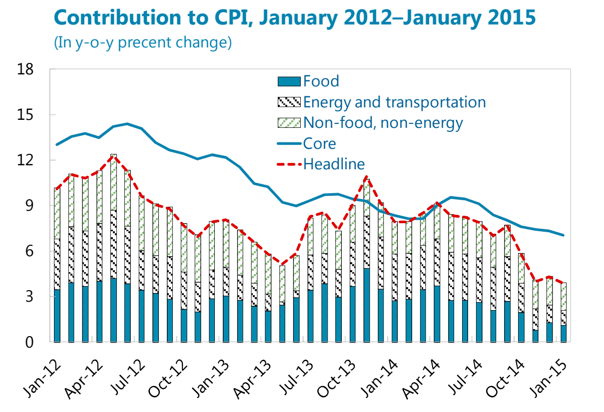
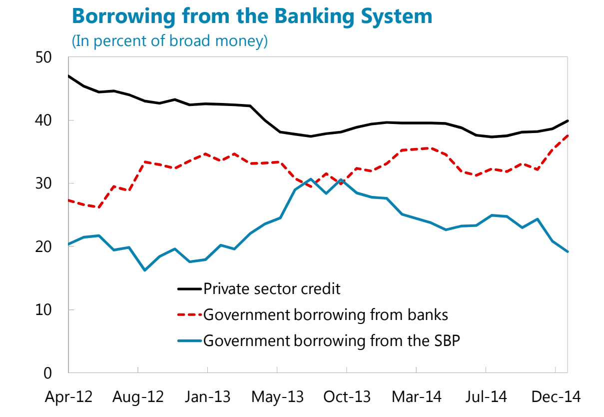
INTRODUCTION

1. **The macroeconomic picture is improving**. Real GDP is projected to grow by some 4.3 percent in FY2014/15, driven mainly by the agriculture and construction sectors.[1] The plunge in oil prices has reduced the import bill and improved the trade balance, but exports have also weakened due to lower cotton prices and the loss of competitiveness from real exchange rate appreciation. Remittances continue to increase at double-digit rates (16.6 percent y-o-y). The financial account has also improved, supported by a recent international Sukuk issue and multilateral disbursements. The Rupee has gained 1.2 percent over the last quarter against the dollar and the real effective exchange rate (REER) has appreciated 10.6 percent since the onset of the program. Headline inflation has dropped further, to 3.9 percent in January 2015, with core inflation also easing to 7.0 percent.



Sources: State Bank of Pakistan; and IMF staff calculations.

2. **Financial system indicators remain sound with robust earnings and high solvency ratios**. The pre-tax profit of the system increased, mainly due to increased net interest income, lower provision charges, and higher noninterest income. Asset quality has slightly improved with a decline in the nonperforming loan (NPL) ratio to 12.3 percent. The capital adequacy ratio (CAR) increased to 17.1 percent due to accumulation of profits and fresh equity injection by some banks. Private sector credit grew at a 7.4 percent annual pace, mainly in the manufacturing, construction, and transportation sectors.



Sources: Pakistani authorities; and IMF staff calculations.

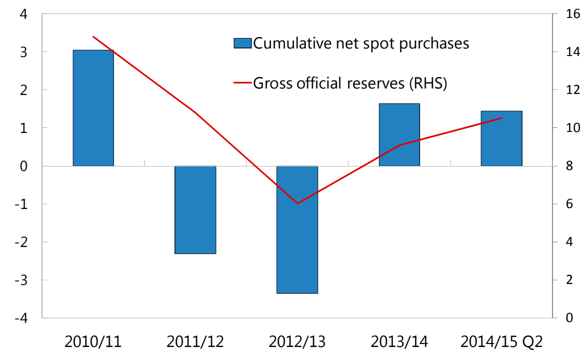
3. **Program performance has been strong since the last review**. All PCs for the review were met, as was the indicative target on social transfer payments. Specifically:

[1] Pakistan's financial year runs from July 1–June 30.

- **Budget deficit, tax revenues and social spending**. The budget deficit (excluding grants) was below the end-December PC by PRs 50 billion (0.2 percent of GDP), partly by restraining development expenditure. Tax revenues at the federal level, however, fell short of the second-quarter indicative target by PRs 22 billion (0.08 percent of GDP) due to legal challenges to a number of revenue measures and to lower tax collections related to the drop in international oil prices. The end-December indicative target on cash transfers under the Benazir Income Support Program (BISP) was met.

- **Government borrowing from the SBP** was below the end-December ceiling by PRs 86 billion due to: (i) issuing a US$1 billion international Sukuk issue in late-November; (ii) issuing ample T-bills and Pakistan Investment Bonds (totaling PRs 363 billion); and (iii) the outright selling of SBP holdings of government securities on the secondary market (PRs 90 billion), which compensated for the deferred sale of a stake in Oil and Gas Development Company Limited (OGDCL).

Gross Reserves and Net Spot Intervention
(In billions of U.S. dollars)

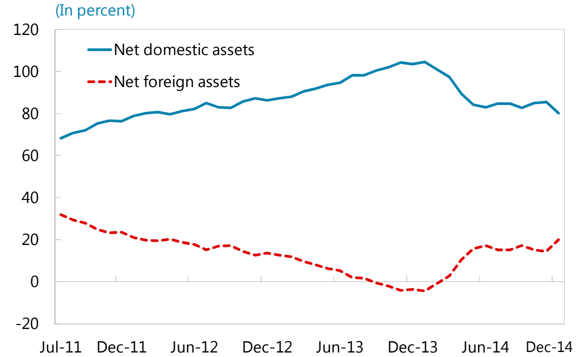


Sources: Pakistani authorities; and IMF staff calculations.

- **Net international reserves and net swaps/forward position**. The 2014 end-December NIR target was comfortably met (by over US$800 million). SBP spot purchases of nearly US$1 billion compensated for the shortfall in privatization revenues. The SBP's net short position of swap/forward contracts also narrowed to US$15 million below the program target.

- **Net Domestic Assets**. The authorities over-performed the end-December NDA target by PRs 281 billion, as borrowing from the SBP was contained, foreign exchange inflows were adequately sterilized, and excess liquidity of Islamic banks absorbed by selling Ijarah Sukuk papers.[2]

Contribution to Reserve Money Growth
(In percent)



Sources: Pakistani authorities; and IMF staff calculations.

[2] The SBP purchased Ijarah Sukuk issued by the government on a deferred payment basis from commercial banks and sold it to Islamic banks, absorbing their excess liquidity. This is a temporary measure to contract NDA.

- **Structural benchmarks**:

  - **Anti-Money Laundering (AML) framework** (MEFP ¶28). The SB on requiring the enactment of amendments to the relevant tax laws and submitting the AML Act to the National Assembly (NA) was met.

  - **Monetary policy operation** (MEFP ¶8). The end-February SB on announcing a time-bound plan to improve the effectiveness of monetary policy and improve the efficiency of the interest rate corridor was met.

  - **Internal control of the SBP** (MEFP ¶10). The SB on improving internal operations and risk management of the SBP by constituting the investment committee of the SBP Board and auditing the program monetary data was met.

  - **Energy sector reforms**. Supply-side and revenue management reforms continue. Electricity tariffs were further adjusted (by PRs 0.60/kWh) through a surcharge taking advantage of the recent decline in fuel prices, which should reduce electricity subsidies to 0.7 percent of GDP for the current fiscal year from 1.3 percent of GDP in 2013/14.

  - **Privatization**. The government completed sales of minority shares in Allied Bank Limited in December 2014 raising around US$150 million.

4. **The authorities remain commited to their economic reform program, but they continue to face significant challenges**. Security conditions remain difficult due to ongoing military operations against the Taliban and the fallout from the recent attack on a school in Peshawar. While political pressures have eased somewhat, as sit-ins organized by different opposition groups during the summer of 2014 have ended, sensitivities remain in implementing some structural reforms, particularly in energy tariff adjustments, central bank independence, and greater exchange rate flexibility. In indirect Senate elections held in late February for one half of the chamber, the government's PML-N party picked up additional seats but fell short of its objective of a majority. This will likely complicate approval of government's legislative reform agenda. Judicial challenges to privatization and tax measures are also constraining progress.

MACROECONOMIC OUTLOOK AND RISKS

5. **Growth and inflation prospects are favorable, with downside risks due to political uncertainties and security challenges roughly balanced against upside risks from the decline in oil prices**.

- **Growth** is expected to reach 4.7 percent next year (0.3 percent higher than previous projections), helped by the decline in oil prices and imports. It should rise further over the medium-term with improvements in the energy sector, public enterprises, the investment climate, and remove key bottlenecks for investment.

- **Inflation** is expected to hover around 5 percent in FY2014/15 (about 3 percent lower than previously forecast) as energy prices ease and inflation expectations are anchored by prudent monetary policy.

- **The current account deficit** is expected to remain around 1.2 percent of GDP in FY2014/15, due to declining oil prices and strong remittances (Box 1). However, export growth will underperform due to real exchange rate appreciation and declining cotton prices. This will partly offset the positive impact of lower oil prices.

- **Foreign exchange reserves** reached US$10.5 billion by end-December—72 percent of the adequate level according to the ARA metric[3]—and are expected to exceed US$15 billion by end-June 2015, supported by the oil windfall, SBP interventions, multilateral and bilateral disbursements, and privatization proceeds.

6. **Crisis risks have eased as program policies reduce macroeconomic imbalances**. Key risks include:

- ***Slippages in policy implementation*** could discourage investment, weaken growth prospects, and delay needed structural reforms.

- ***Challenging political and security conditions*** could disrupt economic activity, discourage investment, and undermine fiscal consolidation. Conversely, an improvement in the security situation could boost investment and growth.

- ***External vulnerabilities*** including a protracted period of slower growth in key advanced (e.g., Euro Area and Japan) and emerging market economies, could impair exports and hurt remittances, and surge in global financial volatility or a market reassessment in sovereign risk could make debt issuance more difficult and costly. Increased volatility in oil prices could destabilize investment or efforts to reform energy subsidies. A persistent dollar appreciation with limited exchange rate flexibility may also contribute to erode export competitiveness.

- ***On the positive side, persistently low oil price*** could help improve the current account balance, ease energy supply bottlenecks, improve macroeconomic performance, and boost growth.

[3] The ARA reserve adequacy metric encompasses a broad set of risks including a drop in external demand or terms of trade shock, capital flow drains due to external liabilities stocks (e.g., short-term debt or medium- or long-term equity of debt liabilities), and/or capital flight risk.

Box 1. Impact of Oil Price Shocks

Pakistan stands to benefit from the fall in oil prices mainly through lower inflation and imports. The price of crude oil plummeted by nearly 60 percent from US$105 per barrel in June 2014 to less than $50 as of end-January 2015 (Figure 4). Accordingly, the WEO baseline projection for average crude oil prices for FY2014/15 has been lowered from an average of US$88 per barrel to US$68. This positive terms-of-trade shock is expected to benefit Pakistan mainly by reducing the import bill, easing inflation pressures, providing a boost to consumer and investment spending. Consumer price inflation is now projected to decline by 2 percentage points as a result of the fall in oil prices, and to drop further in the medium term to 5 percent. The impact on economic growth, however, will materialize with some lag in FY2015/16, 0.3 percentage points higher than previous forecast. Growth will hover around 5 percent over the medium term.

Current account dynamics are highly sensitive to the changes in oil prices. Pakistan's net oil imports amounted to US$12.6 billion (or about 5 percent of GDP) in 2013/14. Assuming no change in other macroeconomic conditions, the recent fall in crude oil prices is expected to reduce the net import bill by US$2.8 billion in FY2014/15 and by US$12 billion on a cumulative basis over the next three years. This windfall will improve the current account by almost a percent of GDP in FY2014/15. However, the largest effects will be felt with a lag in FY2016/17 and FY2017/2018 (0.7 and 0.9 percent of GDP respectively) once oil prices reach their minimum levels. Although remittances are expected to continue to grow, there is a tangible risk that those from Gulf Cooperation Council (GCC) countries might decelerate further reducing the windfall from the oil price plunge.[1]

Gains from lower energy subsidies will partially offset lower energy-related tax collection. Without compensatory measures, the fall in oil prices would worsen Pakistan's fiscal position, since price changes do not automatically affect the amount of energy subsidies but lead to a marked decline in oil-related tax revenues. As part of the energy rationalization strategy, the authorities have made further adjustments in electricity tariffs for the remainder of 2014/15, lowering the fiscal cost of energy subsidies below 0.7 percent of GDP. At the same time, the government has increased the GST rate on petroleum products (excluding furnace oil) from 17 to 27 percent and imposed an additional 5 percent regulatory duty on furnace oil imports to cover for the shortfall caused by the fall in oil prices. Overall Pakistan stands to gain from this positive terms-of-trade shock through a reduction in the oil import bill, an increase in disposable income and consumer spending, business profitability and capital spending in nonenergy related sectors of the economy. Nonetheless spillovers from the energy-exporting GCC countries in particular in the form of reduced workers' remittances, and a global decline in commodity prices—including cotton—may create crosscurrents.

[1] GCC countries are the source of about ⅔ of Pakistan's total remittance's, half of which comes from Saudi Arabia. The plunge in oil prices has not always led to an immediate deceleration or decline in remittances from GCC countries. In fact, during the global financial crisis, remittances proved to be quite resilient. See Kock and Sun, 2011, Remittances from Pakistan—why have they gone up and why aren't they coming down? IMF Working Paper WP/11/200.

POLICY DEVELOPMENTS

A. Fiscal Policy

7. **Fiscal consolidation remains on track, despite challenges on the revenue side**. Overperformance on the deficit target in the first half of FY2014/15 due to prudent spending confirms progress toward the year-end program target of 4.9 percent. Federal tax collections increased by 14.8 percent in the first half of FY2014/15, but the second-quarter indicative target was missed due to: (i) legal challenges to tax measures; and (ii) the fiscal effects of the drop in crude oil prices. Due to legal challeneges, the GIDC has so far produced only about one-tenth of an expected annual yield of 0.6 percent of GDP (including GST on the GIDC) in FY2014/15. In addition, a court stay has blocked a 10 percent tax on the value of bonus shares, which was estimated to bring in 0.1 percent of GDP. The plunge in oil prices has produced a shortfall in GST revenue from petroleum products, which fell by 19 percent in the second quarter of FY2014/15. Without corrective measures, these would have have resulted in a fiscal gap of 0.45 percent of GDP relative to the program target for end-FY2014/15.

8. **The authorities and staff agreed on measures to address the revenue shortfall going forward (prior action)**. The additional revenue measures introduced include: (i) raising the GST rate on petroleum products (excluding furnace oil) from 17 to 27 percent in two stages; (ii) levying regulatory duties on steel products and scrap metal; (iii) introducing a regulatory duty on mobile phones; (iv) levying an additional 5 percent regulatory duty on furnace oil; (v) increasing the withholding tax on nonfiler contractors, service providers, and importers; and (vi) increasing import duty on luxury items; (vii) levying regulatory duty on metal scrap; and (viii) reducing electricity subsidies by 0.1 percent of GDP. In addition, the authorities will retrieve the GIDC already collected by large fertilizer companies.[4] Together, these steps are expected to raise 0.45 percent of GDP.

9. **The fall in oil prices presents an opportunity to further reduce distortions in the energy sector, while allowing for some fall in consumer tariffs**. The authorities have taken steps to reduce energy subsidies to 0.7 percent of GDP in FY2014/15. Most recently, the government implemented a surcharge of PRs 0.30 in October and an additional PRs 0.60/kWh in January to partly recoup costs in the electricity sector. In addition, the government has started applying a new FY2014/15 electricty tariff, with a more comprehensive view of production and distribution costs. These steps could reduce on-budget subsidies by another 0.1 percent of GDP and thus help address the revenue shortfall. In addition, it should begin to reverse the accumulation of circular debt by closing the gap between electricity tariffs and the cost-recovery level (¶24).

[4] The government will continue to work with the legal system to recover the remaining GIDC in private companies accounts.

10. **The authorities are tackling the backlog on GST refund claims**. The number of outstanding GST refund claims was lowered by 5 percent and monthly refund payments were increased by 15 percent in the first half of FY2014/15. Although the stock of refund claims increased between June and November 2014 due in part to old claims being logged into the system, the upward trend has been reversed and the amount of outstanding refund claims declined by PRs 4.4 billion in December 2014. To clear the refund backlog and process new GST refund claims on a timely manner, the FBR will prepare an action plan by June 2015, including the introduction of an automated system of pre-verification.

11. **Efforts to broaden the revenue base by eliminating tax concessions, exemptions and loopholes are bearing fruit**. The elimination of some Statutory Regulatory Orders (SROs) and additional tax base-broadening measures in the FY2014/15 budget have yielded better-than-expected results in the first half of the year. Looking forward, removing all designated SROs is expected to yield 1-1½ percent of GDP over the program period. To permanently prohibit the issuance of SROs to grant tax concessions or exemptions, the government will draft the necessary legislation by end-March 2015 (structural benchmark), with enactment expected by end-December 2015.

12. **The authorities are pressing ahead with plans to improve tax compliance and enforcement** (MEFP ¶18–19). The FBR issued more than its target of 150,000 first notices to nontaxpayers by end-December 2014, as part of their plan to bring more potential income taxpayers into the tax base. It has also initiated a GST collection scheme for over 25,000 large retailers and over 1.3 million small retailers as new potential GST payers. The authorities are also improving the IT infrastructure and expand access to taxpayer information from multiple sources including financial and real estate transactions, motor vehicle procurement, and international travel. Furthermore, the FBR will merge the National Tax Number (NTN) system covering 3.6 million individuals with the Computerized National Identity Card (CNIC) database that covers about 150 million people by end-September 2015 (new structural benchmark). To enhance the efficiency and progressivity of Pakistan's tax regime, the FBR will focus enforcement efforts on nonfilers who have the potential to contribute at least the average tax paid by currently registered taxpayers and especially on a list of high wealth individuals, including elected representatives and key public figures.

13. **The authorities will submit to parliament a draft FY2015/16 budget with a deficit target of under 4 percent of GDP excluding grants**. The government remains committed to reducing the budget deficit (excluding grants) to around 3½ percent by the end of the program and thereby putting the debt-to-GDP ratio on a firmly declining path (Box 2 and Annex I). This requires further fiscal consolidation of about 1 percent of GDP in FY2015/16, with the remainder in FY2016/17. The bulk of this adjustment will come from broadening the tax base and eliminating tax concessions, exemptions and loopholes, while making further progress in removing untargeted subsidies, along with steps to streamline public administration, including wage and salary costs and fringe benefits (MEFP ¶11–12).

Box 2. Debt Sustainability and Public Debt Management

Pakistan's public debt is on a downward path, but there is an urgent need to strengthen debt management (MEFP ¶23). The Debt Sustainability Analysis (DSA) indicates that the stock of public debt will come down from 64.3 percent of GDP in 2013 to 59.4 percent by 2019 (Annex I).[1] The heavy reliance on short-term borrowing makes debt dynamics sensitive to interest rate shocks, and emphasizes the need for extension of the yield curve. Efforts will continue to be needed to diversify financing and lengthen the maturity profile of domestic debt, and improve the balance between domestic and external debt.

Enhancing the quality and effectiveness of public debt management remains a priority. The Debt Policy Coordination Office (DPCO) is expected to publish the updated Medium Term Debt Strategy by September 2015, while continuing to provide Fund staff with a detailed quarterly financing plan for the coming 12 months and publish the rolling quarterly issuance program for domestic public securities every month. The authorities are expected to strengthen the DPCO by revamping its structure, increasing staffing capacity, taking steps to strengthen risk management and strategy functions, and identifying procedures to bring the debt management up to best international practices. Specifically, they will: (i) identify the infrastructure needs of the credit risk management unit of the DPCO by end-March 2015, market risk management functions by end-December 2015, and operational risk management functions by end-December 2016; (ii) strengthen the primary dealership system and arrange a formal linkage between the DPCO and the SBP as the agent in executing borrowing auctions; and (iii) draft the required rules under the Fiscal Responsibility and Debt Limitation Act 2005 by end-September 2015. These actions should lead to savings in, and more effective decision-making for, government borrowing.

[1] Public debt does not include circular debt, which accrues in public and private firms, but has been periodically cleared by budgetary transfers. Inclusion of this flow does not substantially alter the DSA analysis.

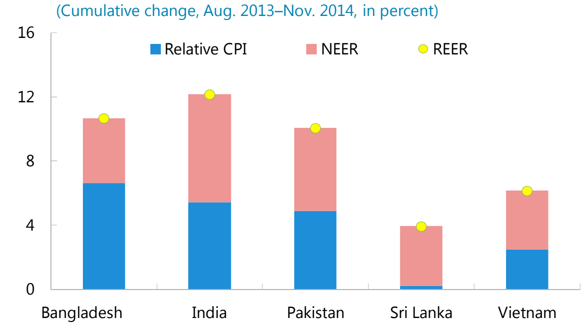
14. **Provincial governments remain crucial in the fiscal reform process, especially by improving revenue collection at the provincial level**. With a series of constitutional amendments and National Finance Comission (NFC) awards, Pakistan has adopted a more decentralized federal system of government. The most recent NFC award granted 57.5 percent of most revenues to the provinces, along with devolution of spending responsibilities and taxation authority in agriculture, property and services. Looking forward to the new round of NFC negotiations, the federal government will seek an agreement to balance devolution of revenue and expenditure responsibilities in a way that is consistent with the objective of macroeconomic stability and long-term sustainablity of intergovernmental fiscal relations. The new NFC negotiations are scheduled tobegin in the coming months, and IMF and World Bank technical advice will be provided to help inform the discussions. Among other recommendations, staff have encouraged the modernization of agricultural taxation, within the existing constitutional framework.

15. **Increasing targeted social assistance to the poor remains a key component of the program**. The authorities met the end-December indicative target on cash transfers through the BISP, reaching over 4.8 million households. The quarterly stipends paid to women account holders in the poorest families were increased from PRs 3,600 to PRs 4,500 per quarter in FY2014/15. Going forward, the BISP coverage is expected to reach around 5.0 million by end-June 2015 (0.3 million lower than previously anticipated). The phasing-in of more effective payment cards has been delayed due to administrative challenges within the BISP, which are now being addressed. New banking contracts will be signed by June 2015. To ensure timely payments to beneficiaries during the transition, the contracts with the commercial banks that are currently making e-payments have been extended until December 2015. In partnership with the provincial governments, the authorities have also made progress in the rollout of the education-conditional cash transfers (MEFP ¶21).

B. Monetary and Exchange Rate Policies

16. **The plunge in oil prices provides an opportunity to boost reserve accumulation and reduce external vulnerabilities**. To this end, the authorities have agreed to increase NIR targets for forthcoming reviews. The end-March PC will be raised by US$500 million and the end-June PC will be set some US$1 billion above the previous indicative target. The SBP has also stepped up its spot market purchases of foreign exchange, which have netted some US$1.8 billion so far in this fiscal year as of end-February 2015. These actions will increase the reserve coverage well above three-months of imports, bolstering resilience against future external shocks. In spite of the recent stability of the rupee against the dollar, the real effective exchange rate has continued to appreciate. Staff stressed that the recent appreciation of the dollar against other currencies, the lack of downward exchange rate flexibility, and a high inflation differential relative to trading partners has caused a further loss of Pakistan's export competitiveness in world markets.

Nomimnal and Real Effective Exchange Rate and Relative Inflation
(Cumulative change, Aug. 2013–Nov. 2014, in percent)



Sources: Pakistani authorities; IMF World Economic Outlook (WEO); and IMF staff calculations.

17. **A continued prudent monetary policy stance is essential to maintain price stability and anchor inflation expectations**. Helped by recent drop in oil and commodities prices, headline inflation fell to historically low levels and core inflation eased (¶1). The real interest rate has been raising and inflation is expected to stay low and inflation expectations remain subdued. In light of these developments, the SBP cut the policy interest rate by 100 bps to 8.5 percent in January 2015, which should be consistent with keeping inflation at about 5½ percent. To anchor inflation expectations and preserve program achievements, the SBP will adhere to NDA targets, improve the functioning of the interest rate corridor (¶18), and set the policy rate in a forward-looking fashion to maintain real interest rates positive and in line with further reserves accumulation and a stable inflation path.

18. **The SBP continues to improve monetary policy operations**. To enhance the effectiveness of monetary policy, better manage liquidity in the interbank market, and conduct open market operations, the SBP has announced its time-bound plan in February to improve its interest rate corridor by differentiating between the refinancing rate and the policy rate and setting the latter between the floor and ceiling rates of the corridor. The central bank will make the improved interest rate corridor operational by end-September 2015 (new structural benchmark). Staff stressed that to better manage foreign exchange demand and make it more predictable and transparent, the SBP should gradually move toward implementing best international practices in the foreign exchange market, including by exploring an auction framework for intervention transactions.

19. **Enhanced central bank independence is important for an improved monetary policy framework**. The authorities submitted amendments to the SBP Act to the Assembly, but the legislation is still pending in committee. Staff provided comments on proposed amendments, noting that while the draft addresses some weaknesses identified in the safeguards report others remain, including constraints to the SBP's autonomy in the pursuit of its price objective, and weaknesses in the SBP's governance and internal control framework. The authorities will submit a revised draft law—incorporating IMF staff comments—to the NA by mid-March 2015 (prior action) and to enact the legislation by end-June 2015 (structural benchmark). The law should strengthen the SBP's autonomy through (i) full operational independence with the pursuit of price stability as the primary objective, (ii) governance structure; and (iii) strengthened personal autonomy of Board members and the financial autonomy of the SBP. The amendments should also establish an independent decision-making committee to design and monitor implementation of monetary policy.

20. **The SBP is taking further steps to enhance its internal operations**. While awaiting approval of the new legislation, the SBP introduced additional measures to further improve internal operations. Specifically: (i) the Investment Committee of the SBP Board begun regular oversight and approval of the reserves management strategy and risk practices; and (ii) the authorities provided confirmation that in line with standard IMF safeguard procedures, the Internal Audit Department has conducted reviews of the program monetary data reported to the IMF for end-December, and will continue to do so within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff (MEFP ¶10).

C. Financial Sector Policies

21. **Progress with bank capitalization is satisfactory** (MEFP ¶24). The number of capital adequacy ratio (CAR) noncompliant banks has fallen from three to two due to capital injections, with one of the banks under moratorium. The combined shortfall for the two remaining noncompliant banks (all private) has decreased to PRs 7.96 billion (less than 0.03 percent of GDP) by end-

December 2014. Staff stressed that SBP should closely monitor these banks' activities to ensure compliance with CAR by end-March 2014.[5] [6]

22. **Staff supported the ongoing financial sector reforms to ensure financial stability**. However, due to a congested legislative agenda, the timing of some measures has been rephrased. The authorities are: (i) finalizing the draft Securities Bill, after incorporating comments from the IMF, with the expectation of enactment by January 2016 (modified structural benchmark); (ii) working to finalize the Corporate Restructuring Companies Act to deal with bankruptcy issues; (iii) developing detailed procedural guidelines for the effective implementation of an early warning system for effective supervision of financial conglomerates; (iv) working on consolidated supervision by SBP and SECP; and (v) preparing a draft Deposit Protection Fund (DPF) Act to be finalized and submitted to parliament by end-March 2015. The authorities now expect enactment of the law by end-September 2015 (modified SB). In the meantime, the SBP will undertake preparatory work to establish the corporate infrastructure of the Deposit Protection Fund (PDF) and will request IMF technical assistance to help in this process. The DPF is expected to become operational by January 2016 (MEFP ¶27).

23. **The Financial Action Task Force (FATF) determined that Pakistan had substantially addressed its strategic AML/CFT deficiencies**. The amendments to the Anti-Terrorism Ordinance of 2013 to bring it in line with the action plan agreed with the FATF were enacted by the NA. The end-December 2014 SB requiring the enactment of amendments to the relevant tax laws and submitting the AML Act (AMLA) to the NA for approval (MEFP ¶28) was also met. In the end, the inclusion of serious tax offenses as predicate crimes to money laundering did not necessitate the amendments to the tax laws, and only required introducing amendments to the AMLA. In November 2014, the Financial Monitoring Unit issued guidance on the risks of abuse of the investment incentive scheme. In recognition of these efforts, in February 2015 FATF removed Pakistan from the list of jurisdictions which have strategic AML/CFT deficiencies. Going forward, staff urged the authorities to continue bolstering the effectiveness of the framework to mitigate the ML/FT risks including the proceeds of corruption and tax evasion. In particular, the authorities intend to adopt the amendments to the AMLA by end September 2015 (new SB) and bring the regulatory framework in line with the international standards, including in relation to politically exposed persons.

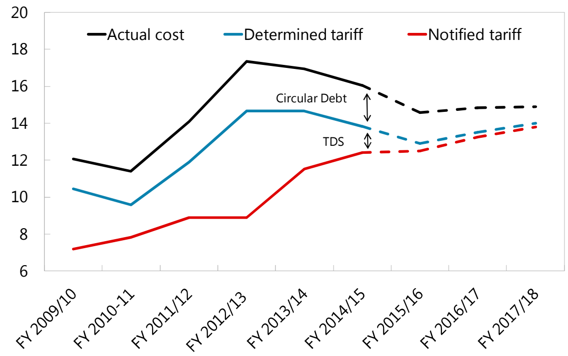
[5] These banks comprise 1.39 percent of banking assets.

[6] The authorities are receiving TA to improve their consolidated supervision for better crisis preparedness.

D. Structural Issues

Energy

Average Cost of Electricity
(In Pakistani rupees per kilowatt hour)



Sources: Pakistani authorities; and IMF staff calculations.

24. **The authorities are moving forward with their plans to deal with the accumulation of arrears in the electricity sector** (MEFP ¶30–31). As of January 2015, arrears in the power sector stood at nearly 2 percent of GDP.[7] To stem further accumulation of arrears in the system, the authorities issued policy guidelines requiring the electricity regulator NEPRA to reflect additional efficiency costs in the next tariff determination. With the latest increase in the electricity tariffs (¶3), distribution companies (DISCOs) began to recover part of the costs stemming from technical losses and under-collections. Over time, the flow of new circular debt is expected to be eliminated. The stock would likely be dealt with via some form of conditional transfers, although this remains under discussion.

25. **Performance of DISCOs is improving**. In the first half of FY2014/15, revenue-based load shedding produced moderate improvements in collections from private consumers (by 2.2 percent) and the agricultural sector (by 3.1 percent). However, during the same period, collections from the public sector declined by 7.5 percent due to payment delays from one government department. The federal government will take action to deal with this department. To strengthen the management of DISCOs, the authorities replaced some chief executives of poorly performing companies. Finally, several DISCOs have been included the authorities' privatization plans (MEFP ¶37).

26. **Power sector regulatory reform is progressing** (MEFP ¶32–35). The vacancies on the board of the regulator NEPRA were filled in November. Preparations for a multi-year tariff framework are on track, with a view towards implementation with the FY2015/16 determination. The amendments to the Penal Code of 1860 and the Code of Criminal Procedures 1898 were enacted in March 2015, which will allow DISCOs to tackle electricity theft through stipulating it as criminal offense.

[7] There were significant fuel shortages in Pakistan in January. These appear to have been caused by low inventories in Pakistan State Oil which were unable to cope with higher consumer demand due to lower prices and to the diversion of natural gas supplies away from vehicles toward household heating during the winter months. These difficulties have since been resolved.

27. **Progress in the gas sector has been uneven** (MEFP ¶38). The notification of new gas prices was postponed for a second time and is now planned for July 2015.[8] Staff expressed concerns about this delay and urged the authorities to reconsider unification of determination and notification with the regulator—Oil and Gas Regulatory Authority (OGRA). Construction of a Liquefied Natural Gas (LNG) terminal is nearly complete, and the first LNG imports are on track for April 2015. The authorities remain committed to full pass-through of the cost of imported LNG to the end-user purchase price (including Compressed Natural Gas) as it comes online. The conversion of existing domestic gas concessions to higher producer prices (under the 2012 Policy) will be expedited with the signing of Model Supplemental Agreement in February 2015. The authorities are also planning to award contracts for an additional 10–15 exploration fields by June 2015 to help tackle the gas shortages.

Public Sector Enterprises

28. **Staff welcomed progress in the privatization program, despite recent setbacks** (MEFP ¶42). The authorities are moving forward with the transactions for Habib Bank Limited (HBL) and Heavy Electrical Complex (HEC), which are due for end-March 2015. Their program continues to aim at offering and/or marketing at least one transaction in each quarter for the current year.

Timeline of the Privatization of PSEs

	PSEs	Transaction	Timeline
1	Habib Bank Limited (HBL)	Capital Market Transaction - GDRs for sale of 25 of HBL shares (60 percent GoP shares)	End-March 2015
2	Heavy Electrical Complex (HEC)	100 percent sell-out of strategic asset	End-March 2015
3	National Power Construction Corp. (NPCC)	88 percent sell-out of strategic asset	End-May 2015
4	Faisalabad Electric Supply Company (FESCO)	Strategic & Asset Sale	End-August 2015
5	Convention Center	100 percent sell-out of strategic asset	End-August 2015
6	Northern Power Generation Company Limited (NPGCL)	Strategic & Asset Sale	End-October 2015
7	Islamabad Electric Supply Company (IESCO)	Strategic & Asset Sale	End-December 2015
8	Lahore Electric Supply Company (LESCO)	Strategic & Asset Sale	End-December 2015

29. **The restructuring of Pakistan Steel Mills (PSM), Pakistan International Airlines (PIA), and Pakistan Railways (PR) is progressing** (MEFP ¶42). Financial advisors (FAs) have been re-advertised for PSM in February 2015 and the appointment is expected for end-March 2015. A newly appointed chief executive officer of PSM and the new board have approved a comprehensive restructuring plan to improve operational efficiency and capacity utilization. The FA for PIA was hired in July 2014 (SB) and will complete the due diligence process by end-March 2015. The potential offering to a strategic investor is scheduled for end-December 2015 (SB). Finally, the

[8] Gas price notifications are done on a bi-annual basis in January and July of every year. Due to political protests July 2014 notification was postponed to January 2015.

renewal of the PR Board was completed in end-February 2015. The government finalized a comprehensive restructuring plan for PR, which in the short-term will have a focus on improvements in freight transportation. In the meantime, PR revenues increased by 30 percent in the first half of FY2014/15 through rationalization of tariffs and expenditures and improved occupancy rates.

Business Climate and Trade Policy

30. **Staff welcomed efforts to implement investment climate and trade policy reforms** (MEFP ¶38). A virtual one-stop shop is now online to facilitate business registration and a review of the filing process for sales and income tax is underway to make tax filing easier for businesses. It is expected to be finalized by end-March 2015 (SB). Furthermore, the authorities are developing a National Financial Inclusion Strategy (NFIS) to improve access to finance for poor, women, and marginalized segments of the society. A critical component of the NFIS is to improve the credit information system. The Credit Bureau Act was submitted to Parliament in February 2014 and will be enacted by end-November 2015 (new SB). The elimination of some SROs at the outset of the current fiscal year has already begun to create a more level playing field for businesses, in addition to raising revenues (¶11).

PROGRAM MODALITIES AND OTHER ISSUES

31. **The attached Letter of Intent (LOI) and Memorandum of Economic and Financial Policies (MEFP) describe the authorities' progress in implementing their economic program, set out their commitments, and propose the modification of end-March 2014 and establishment of end-June 2015 PCs and indicative targets**. End-March PCs for NIR and NDA are proposed for modification to ensure higher reserves accumulation, and four new structural benchmarks are proposed. The authorities have completed three prior actions by mid-March 2015.

32. **Financing, program risks, and capacity to repay the Fund**. Pakistan's program financing needs are fully covered for the next 12 months. The country's capacity to repay the Fund has strengthened as a result of the improved macroeconomic performance and sustained improvement in its reserve coverage ratios. Moreover, disbursements from multilateral and bilateral partners are materializing, the privatization program continues to advance despite a recent setback, and the recent international Sukuk issue demonstrates international market access and reduced financing risks going forward. The Fund's exposure to Pakistan increased with the disbursements made upon approval of the fourth and fifth review, reaching SDR 2.16 billion (about US$3.6 billion, 34 percent of gross official reserves or 5.5 percent of total external debt) by end-December 2014 (Table 9). Fund exposure is expected to increase further over the next 12 months as new EFF program disbursements are made (Table 11). The materialization of risks to the economic outlook could erode Pakistan's capacity to repay to the Fund, particularly in a context of increased Fund exposure (¶5).

STAFF APPRAISAL

33. **Macroeconomic prospects remain solid and the threat of a crisis has receded**. GDP growth will be above 4 percent this year and next, reflecting strong manufacturing output and lower world oil prices. Headline inflation has declined sharply, and a prudent monetary stance should help reduce core inflation for the remainder of FY2014/15. The authorities have made significant progress addressing fiscal and balance of payments imbalances. Foreign exchange reserves are recovering, and should reach benchmark levels of adequacy in the coming months. Fiscal consolidation is on track, and the government has reduced borrowing from the SBP and continues to improve its debt financing by diversifying sources and lengthening maturities.

34. **Much has been accomplished in the first 1½ years of this three year program**. Foreign exchange reserves have recovered from only US$3 billion in November 2013 to over US$11 billion, and are on track to exceed US$15 billion in the next few months. Inflation has fallen and growth has begun to rise, albeit slowly. The fiscal deficit has been reduced from over 8 percent of GDP to under 5½ percent last fiscal year, and should fall below 5 percent of GDP this year. Electricity subsidies have been reduced from nearly 2 percent of GDP to 0.7 percent of GDP, while tax revenues have increased by ½ percent of GDP last fiscal year and are slated to rise by nearly 1 percentage point this year. Important structural reforms are underway in the energy sector, tax policy, central bank operations, the trade regime, and public enterprises. The authorities should be commended for attaining all performance criteria under the program for the sixth review, notwithstanding significant political and security challenges.

35. **However, much remains to be done to achieve a sustainable economic transformation**. Pakistan still lags behind other emerging market countries in key macroeconomic and business climate indicators. Economic growth is still below the 5–7 percent per year rate needed to achieve significant improvements in living standards. The fiscal deficit is still too high and the tax-to-GDP ratio remains among the lowest in the world. The country has barely begun the structural reforms needed to boost private investment, ease growth bottlenecks, and enhance the economy's productivity and competitiveness. The rupee has been appreciating in real effective terms—most recently due to the stability of the rupee vis-à-vis the strengthening U.S. dollar—and this constitutes a headwind to further development of the tradable sector.

36. **The recent sharp decline in oil prices has presented Pakistan with an historic opportunity to strengthen buffers against future economic shocks and to address long-standing structural barriers to sustainable higher growth**. The authorities' decision to accelerate the accumulation of foreign exchange reserves is a wise response. Despite some negative tax implications, the positive shock to energy prices can also be used to accelerate the reduction in electricity subsides and to tackle the persistent problem of payments arrears in the sector, without increasing consumer prices. While much progress has been made under the program in reducing budgeted subsidies, the problem of the off budget "circular debt" still generates some 1 percent

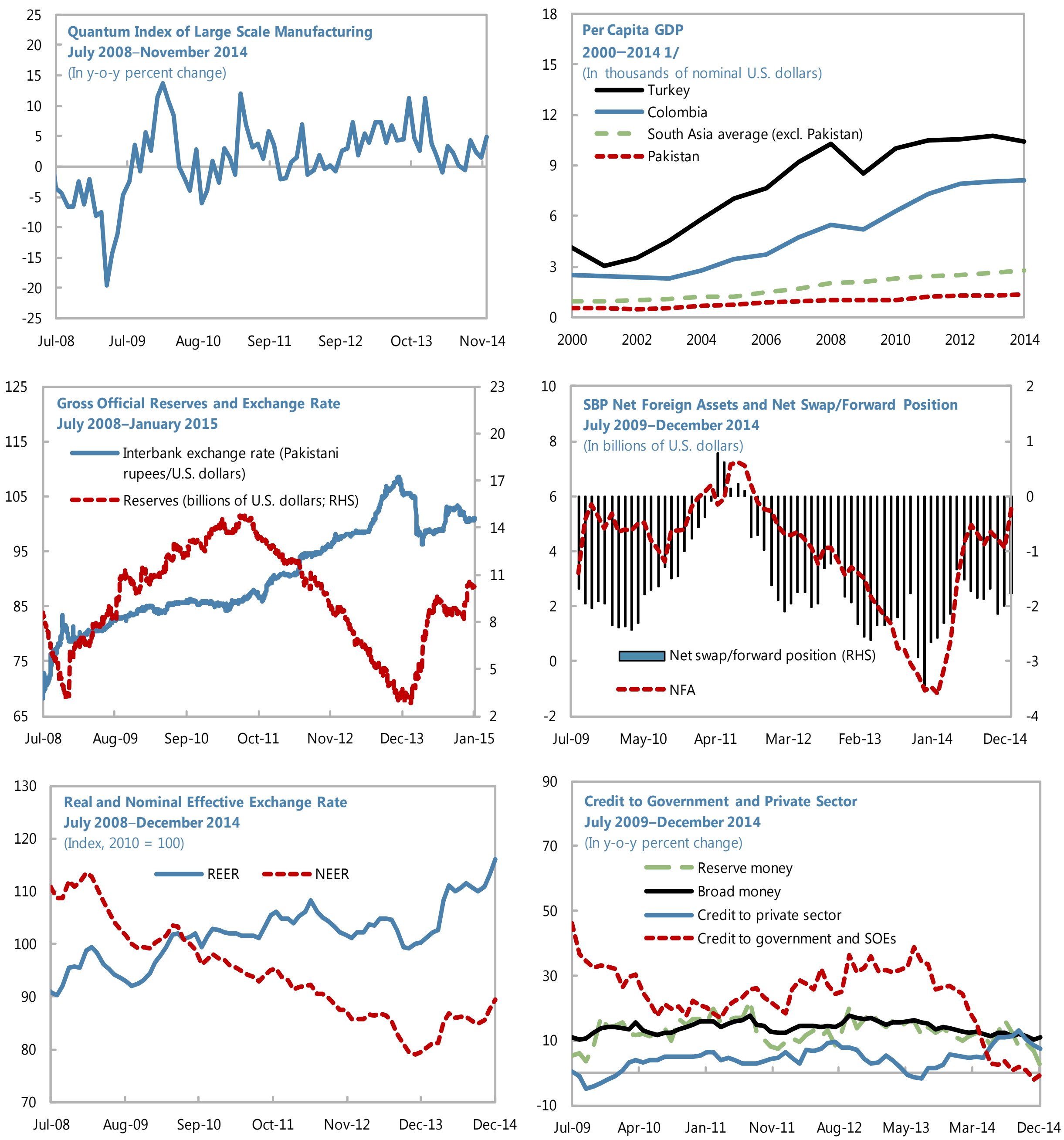
of GDP in losses per year and periodically threatens the functioning of the energy system.[9] An ambitious approach reducing these losses will improve energy supplies, fiscal sustainability, and will place the Pakistani economy in a position for sustained higher growth.

37. **Continued strong political commitment at the highest levels, together with steadfast implementation by the government and the SBP, are key to keeping the program on track**. As crisis risks ease and competing political priorities surface, there are renewed pressures to put off politically sensitive reforms. However, permanent improvement in the economy can only be achieved if the reform process continues. The authorities need to step up efforts to explain the benefits of the difficult fiscal, monetary, and structural measures contained in the program to political and business leaders, as well as to the general public. While many of these measures may entail short-term political costs, they will bring lasting benefits to the country with higher and more inclusive economic growth and reduced risk of future crises.

38. **On the basis of Pakistan's performance under the extended arrangement, staff supports the authorities' request for modifications of the end-March PCs on NIR and NDA, and completion of the sixth review under the arrangement**. Staff also recommends the establishment of the end-March 2015 and end-June 2015 PCs, setting of four new structural benchmarks, and the revised timelines of structural benchmarks as proposed in the attached MEFP.

[9] The stock of circular debt is estimated to be PRs 540 billion, around 2 percent of GDP.

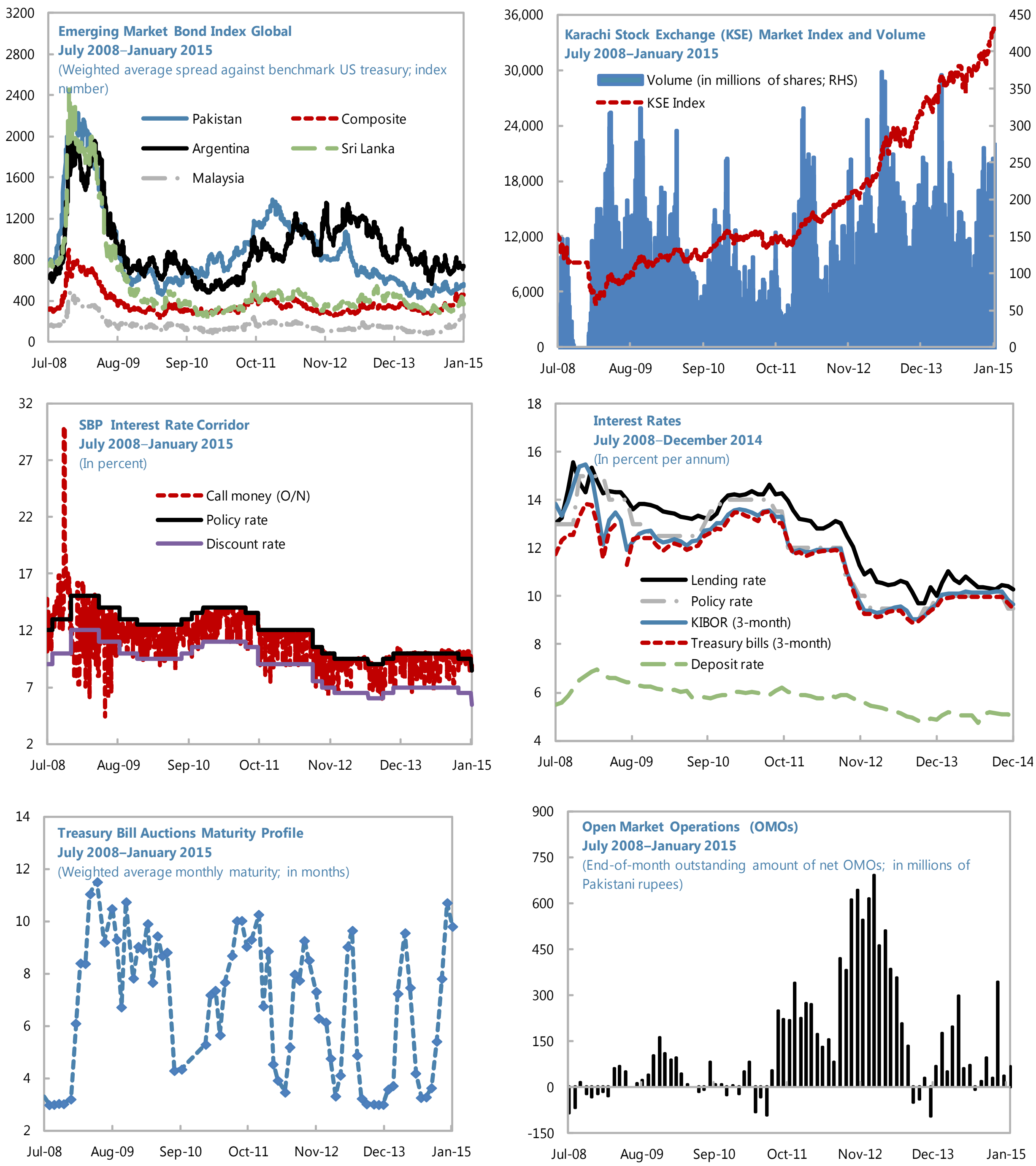
Figure 1. Pakistan: Selected Economic Indicators, 2008–14



Sources: Pakistani authorities; IMF World Economic Outlook; and IMF staff calculations.

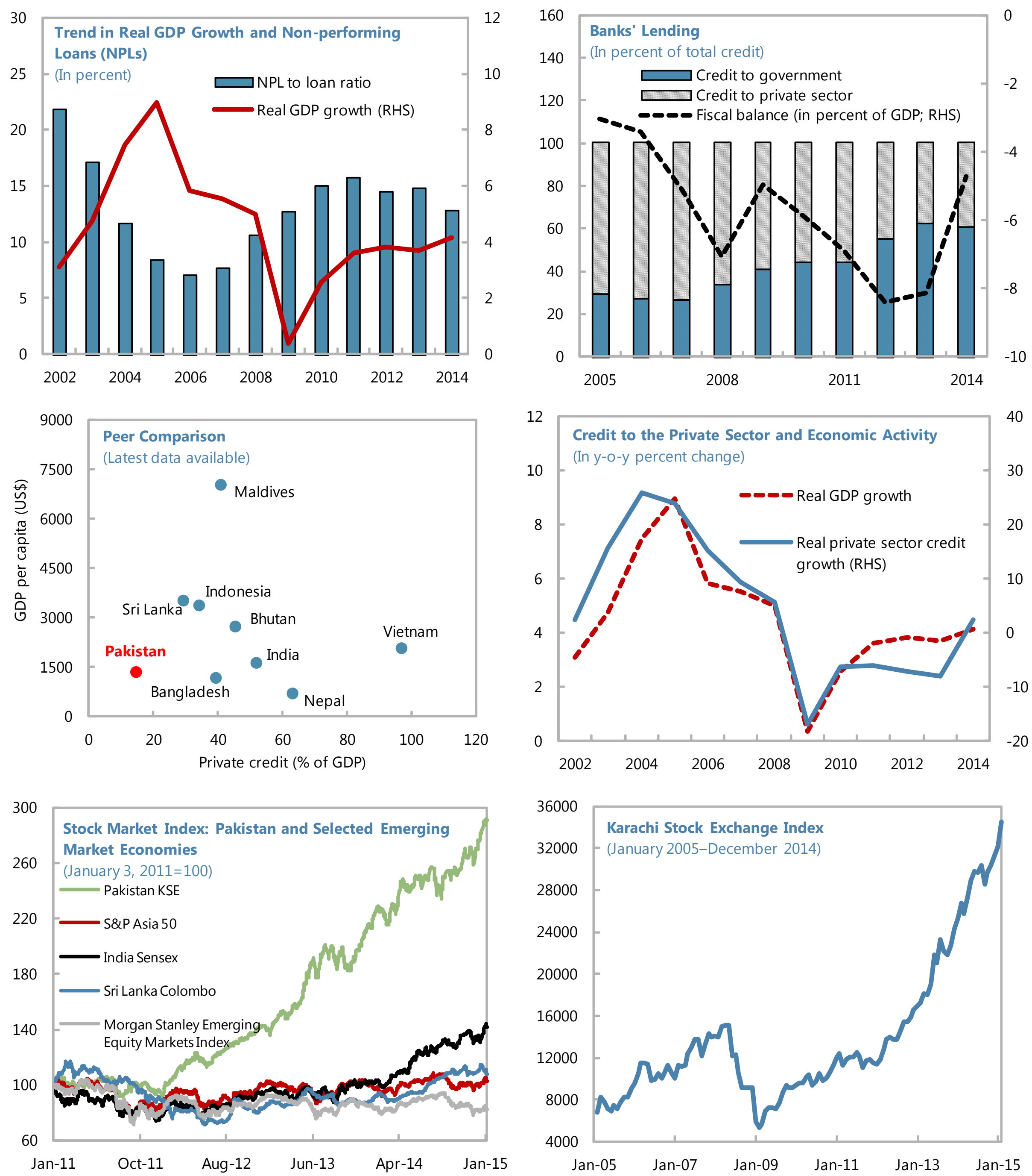
1/ 2014 per capita GDP figures for countires other than Pakistan are estimated.

Figure 2. Pakistan: Selected Financial Indicators, 2008–15



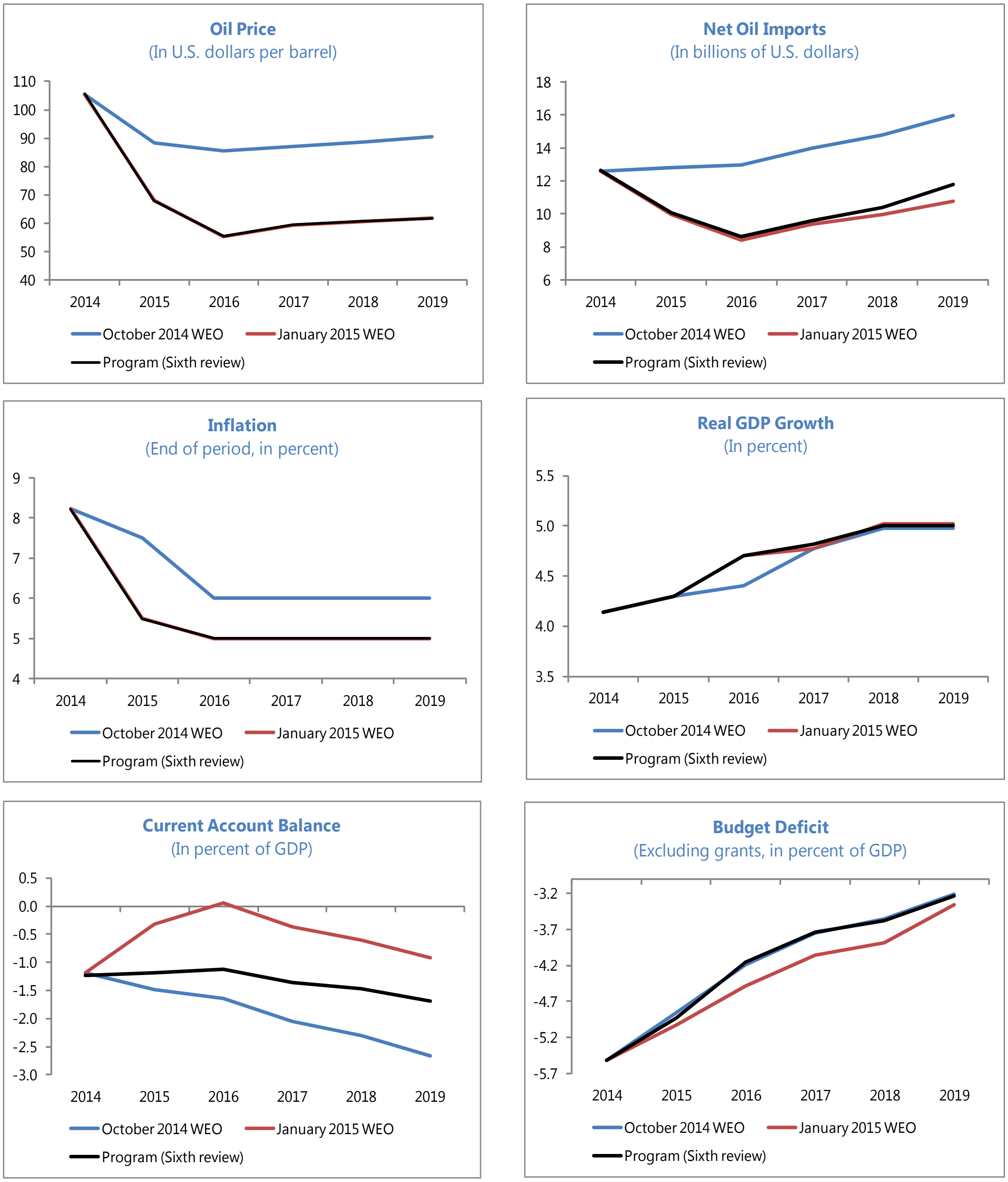
Sources: Pakistani authorities; Bloomberg; and IMF staff calculations.

Figure 3. Pakistan: Selected Banking and Financial Indicators



Sources: Pakistani authorities; Bloomberg; and IMF staff calculations.

Figure 4. Pakistan: Impact of Oil Price Scenarios



Sources: Pakistani authorities; IMF World Economic Outlook (WEO); and IMF staff estimates.

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets FY2013/14–FY2015/16 1/

(In billions of rupees, at program exchange rates, unless otherwise specified)

	FY2012/13	FY2013/14	FY2014/15							FY2015/16	
	end-June	end-June	end-September	end-December			end-March		end-June	end-September	end-December
							Current	Revised	proposed		
	Actual		Fourth and Fifth Review	Sixth Review			Program			Projection	
		Actual	Actual	Target	Adjusted target	Actual					
Performance Criteria											
Floor on net international reserves of the SBP (millions of U.S. dollars)	-2,437	2,678	2,630	3,500	2,683	3,500	4,500	5,000	6,750	8,000	8,500
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,402	2,355	2,316	2,436	2,505	2,224	2,365	2,340	2,270	2,210	2,150
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	2,012	1,402	337	722	730	672	1,087	1,087	1,387	354	665
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	2,255	1,725	1,675	1,775	1,775	1,760	1,775	1,775	1,700	1,550	1,550
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3/	2,168	2,328	2,289	2,000	2,000	1,914	1,905	1,905	1,865	1,800	1,750
Continuous Performance Criterion											
Accumulation of external public payment arrears by the general government (continuous)	0	0	0	0	0	0	0	0	0	0	0
Indicative Targets											
Cumulative floor on Targeted Cash Transfers Spending (BISP) (billions of Pakistani rupees)	54	66	21	36	36	44	69	69	95	22	45
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	1,936	2,266	539	1,195	1,195	1,174	1,883	1,846	2,691	625	1,416

Sources: Pakistani authorities; and Fund staff estimates.

1/ All items as defined in the TMU. Fiscal year runs from July 1 to June 30.

2/ Excluding grants, FY2012/13 overall budget deficit is a stock.

3/ FY 2012/13, total stock of government debt as of June 30, 2013.

Table 2. Pakistan: Program Modalities and Structural Benchmarks

Item	Measure	Time Frame (by End of Period) Current	Time Frame (by End of Period) Rescheduled	Status	Macroeconomic rationale
Prior Actions					
1	Revise the draft SBP law in the NA committee incorporating the recommendations of the IMF safeguards assessment mission and comments provided by Fund staff and submit the revised draft to the full assembly	mid-March 2015			
2	Raise the GST rate on petroleum products from 17 to 27 percent, introduce additional fiscal measures, including 0.1 percent of GDP reduction in electricity subsidies, with total yield of 0.35 percent of GDP to assure compliance with the year-end fiscal targets.	Five days before the board date			
3	Take measures to recover part of the GIDC proceeds focusing on areas where large collecting agents have already collected the GIDC in their price, with yield of 0.1 percent of GDP.	Five days before the board date			
Structural Benchmarks					
Fiscal sector					
1	Increase the issuance of first notices (u/s 114) to 75,000 and follow up with a second notice (u/s 122c) to 75 percent of those who did not respond satisfactorily to their first notice within 60 days by end-March, 2014. Issue a provisional tax assessment to 75 percent of those who did not respond satisfactorily within 60 days to the second notice by end-March, 2014.	end-March 2014		Met	Broaden the tax base and improve tax compliance.
2	Eliminate exemptions and concessions granted through SROs for an amount consistent with the fiscal deficit reduction objective in the FY2014/15 budget.	end-June-2014		Met	Reduce distortions and improve revenue collection.
3	Approve an administrative order to consolidate the responsibilities of public debt management in the debt management office.	end-September 2014		Not met, but the order fell short of unifying fragmented debt management functions.	Strengthen the organizational framework for effective public debt management.
4	Enact amendments to the relevant tax laws (as defined in the TMU) and submit amendments to the Anti-Money Laundering Act (AMLA) to Parliament.	end-December 2014		Met	Use antimoney laudering tools to combat tax evasion, and faclitate detection of potential cases of abuse of the investment incentive scheme to lauder criminal proceeds.
5	Draft legislation that will permanently prohibit the practice of issuing SROs that grants exemptions and loopholes.	end-March 2015			Reduce distortions and improve revenue collection.
6	Reorganize the Debt Policy Coordination Office as a middle office responsible for updating the MTDS and monitoring its implementation, coordinating the credit risk management functions.	end-March 2015			Strengthen the organizational framework and improve public debt management.
Monetary sector					
7	Improve the internal operations of the SBP by: (i) reestablishing an advisory monetary policy committee to advise the Board on its policy decisions; (ii) establishing a Board committee to centralize and oversee risk management activities across the bank; and (iii) begin publishing summaries of the monetary policy proceedings of the Board meetings and monetary policy committee deliberations.	end-August 2014		Met	Independent of the legislation, improve the operational autonomy of the SBP and enhance risk management.
8	Announce a time-bound plan to improve the SBP's interest rate corridor by setting the policy rate between the floor and ceiling rates of the corridor.	end-February 2015		Met	Improve SBPs liquidity management.
9	Improve the internal operations of the SBP by the following measures: (i) the Investment Committee of the SBP Board will begin regular (at least four times per year) oversight and approval of the reserves management strategy and risk practices; and (ii) the authorities will provide confirmation that in line with standard IMF procedures, the Internal Audit Department conducts reviews of the program monetary data reported to the IMF, within two months after each quarter, for accuracy and compliance with the TMU.	end-February 2015		Met	Improve monetary policy framework through enhanced central bank independence.
10	Enact the amendments to the SBP law to give SBP autonomy in its pursuit of price stability as its primary objective, while strengthening its governance and internal control framework, in line with Fund staff advice.	end-June 2015			Prerequisite for an independent monetary policy framework.
Financial sector					
11	Enact the Securities Bill, in line with Fund staff advice.	end-June 2015	end-January 2016		Enhance the resilience of the financial sector.
12	Enact the Deposit Protection Fund Act, in line with Fund staff advice.	end-June 2015	end-September 2015		Enhance the resilience of the financial sector.
Structural Policies					
13	Initiate revenue based load shedding in six remaining electricity distribution companies .	end-January 2014		Met	Boost sustainable and inclusive growth, by removing bottlenecks, encourage long-term, sustainable increases in electrictity supply; improve the efficiency of the economy through privatization and use its proceeds to hel ease fiscal and balance of payments pressures.
14	Hire three financial advisors for three PSEs in the capital market transactions list and three financial advisors for the three PSEs in the strategic private sector enterprises list for privatization in the TMU.	end-March 2014		Met at end-July, 2014	
15	Conduct a diagnostic study of the regulatory framework of the power sector and prepare an interim report.	end-April 2014		Met	
16	Offer the minority shares in United Bank Limited and Pakistan Petroleum Limited to domestic and international investors.	end-June 2014		Met	
17	Fill the vacancies in the NEPRA Board.	end-July 2014		Met at end-November, 2014	
18	Conduct a review to reduce the number of existing processes and forms for paying sales and income taxes.	end-March 2015			
19	Privatize 26 percent of PIA's shares to strategic investors.	end-December 2015			
New Structural Benchmarks					
1	Make the improved interest rate corridor of the SBP operational	end-September 2015			Improve SBPs liquidity management.
2	Merge the NTN system covering 3.6 million individuals with the CNIC database that covers about 150 million people	end-September 2015			Broaden the tax base and improve tax compliance.
3	Enact the Credit Bureau Act	end-November 2015			Extend credit to broader sections of society
4	Adopt the amendments to the AMLA that will include the serious tax crimes from the relevant tax laws (as defined in the TMU).	end-September 2015			Use antimoney laudering tools to combat tax evasion, and faclitate detection of potential cases of abuse of the investment incentive scheme to lauder criminal proceeds.

Table 3. Pakistan: Selected Economic Indicators, 2010/11–2015/16 1/

Population: 186.3 million (2013/14)
Per capita GDP: US$1,343 (2013/14)
Poverty rate: 12.4 percent (2010/11)
Main exports: Textiles ($13.6 billion, 2013/14)
Unemployment: 6.2 percent (2012/13)

	2010/11	2011/12	2012/13	2013/14	2014/15		2015/16
					Fifth Review	Projections	Projections
			(Annual percentage change)				
Output and prices							
Real GDP at factor cost	3.6	3.8	3.7	4.1	4.3	4.3	4.7
GDP deflator at factor cost	19.5	5.7	7.6	7.0	8.0	6.0	5.2
Consumer prices (period average) 2/	13.7	11.0	7.4	8.6	7.9	6.0	5.3
Consumer prices (end of period) 2/	13.3	11.3	5.9	8.2	7.5	5.5	5.0
Pakistani rupees per U.S. dollar (period average)	2.2	4.1	8.5	5.8			
			(In percent of GDP)				
Saving and investment							
Gross saving	14.2	13.0	13.5	12.8	14.1	13.8	14.9
Government	-4.2	-5.1	-5.0	-1.3	-1.2	-1.5	-0.4
Nongovernment (including public sector enterprises)	18.4	18.1	18.5	14.1	15.3	15.2	15.3
Gross capital formation 3/	14.1	15.1	14.6	14.0	15.6	15.0	16.0
Government	2.5	3.3	3.1	3.4	3.2	3.2	3.4
Nongovernment (including public sector enterprises)	11.6	11.7	11.5	10.6	12.4	11.8	12.5
Public finances							
Revenue and grants	12.6	13.2	13.3	15.1	15.0	14.8	15.3
Expenditure (including statistical discrepancy)	19.8	21.9	21.5	19.5	19.5	19.4	19.2
Budget balance (including grants)	-6.9	-8.4	-8.1	-4.7	-4.5	-4.6	-3.9
Budget balance (excluding grants)	-7.1	-8.8	-8.3	-5.5	-4.8	-4.9	-4.2
Primary balance	-3.1	-4.0	-3.7	-0.2	0.2	0.0	0.6
Total general government debt 4/	55.3	60.5	62.3	63.0	61.2	61.8	60.7
External general government debt	22.4	22.4	20.0	19.6	19.8	18.8	19.0
Domestic general government debt	32.9	38.1	42.3	43.4	41.4	42.9	41.7
			(Annual changes in percent of initial stock of broad money, unless otherwise indicated)				
Monetary sector							
Net foreign assets	2.8	-2.9	-3.4	3.7	3.7	4.9	2.7
Net domestic assets	6.6	23.8	19.3	8.8	8.7	7.3	9.4
Broad money (percent change)	9.4	20.9	15.9	12.5	12.4	12.2	12.1
Reserve money (percent change)	16.2	12.2	15.8	12.9	12.0	11.5	10.0
Private credit (percent change)	7.6	3.9	-0.6	11.0	14.0	12.0	13.0
Six-month treasury bill rate (period average, in percent)	13.3	12.3	10.1	11.9			
External sector							
Merchandise exports, U.S. dollars (percentage change)	28.9	-2.6	0.4	1.1	0.9	-0.4	-0.2
Merchandise imports, U.S. dollars (percentage change)	14.9	12.8	-0.6	3.7	6.0	3.2	-1.9
Current account balance (in percent of GDP)	0.1	-2.1	-1.1	-1.2	-1.5	-1.2	-1.1
			(In percent of exports of goods and services, unless otherwise indicated)				
External public and publicly guaranteed debt	153.4	160.3	144.6	166.6	167.1	163.6	176.0
Debt service	12.0	16.2	21.6	23.5	22.9	23.0	24.9
Gross reserves (in millions of U.S. dollars) 5/	14,784	10,799	6,008	9,096	14,103	15,439	20,190
In months of next year's imports of goods and services	3.6	2.7	1.5	2.1	3.0	3.6	4.5
Memorandum items:							
Real effective exchange rate (annual average, percentage change)	4.2	3.8	1.7	-1.4	1.2	2.8	-2.1
Terms of trade (percentage change)	7.2	-10.5	-0.6	-0.8	-1.6	3.7	4.8
Real per capita GDP (percentage change)	1.5	1.7	1.6	2.1	2.3	2.3	2.7
GDP at market prices (in billions of Pakistani rupees)	18,276	20,047	22,489	25,402	28,602	28,084	30,948
GDP at market prices (in billions of U.S. dollars)	213.6	225.1	232.8	250.1			

Sources: Pakistani authorities; and IMF staff estimates and projections.
1/ Fiscal year ends June 30.
2/ Inflation after 2009/10 based on new CPI weights, recalculated in September 2011.
3/ Including changes in inventories. Investment data recorded by the Pakistan Bureau of Statistics are said to underreport true activity.
4/ Excludes obligations to the IMF except budget financing, military debt, commercial loans, and short-term debt.
5/ Excluding gold and foreign currency deposits of commercial banks held with the State Bank of Pakistan.

Table 4. Pakistan: Medium-Term Macroeconomic Framework, 2010/11–2019/20

	2010/11	2011/12	2012/13	2013/14	2014/15		2015/16	2016/17	2017/18	2018/19	2019/20
					Fifth Review	Projections	Projections				
					(Annual percentage change)						
Output and prices											
Real GDP at factor cost	3.6	3.8	3.7	4.1	4.3	4.3	4.7	4.8	5.0	5.0	5.0
Consumer prices (period average)	13.7	11.0	7.4	8.6	7.9	6.0	5.3	5.0	5.0	5.0	5.0
					(In percent of GDP)						
Saving and investment balance	0.1	-2.1	-1.1	-1.2	-1.5	-1.2	-1.1	-1.4	-1.5	-1.7	-2.0
Government	-6.7	-8.4	-8.1	-4.7	-4.5	-4.6	-3.9	-3.5	-3.4	-3.1	-2.8
Non-government (including public sector enterprises)	6.8	6.3	7.1	3.5	3.0	3.5	2.7	2.2	1.9	1.4	0.8
Gross national saving	14.2	13.0	13.5	12.8	14.1	13.8	14.9	15.6	16.5	17.3	17.3
Government	-4.2	-5.1	-5.0	-1.3	-1.2	-1.5	-0.4	0.1	0.2	0.5	1.1
Non-government (including public sector enterprises)	18.4	18.1	18.5	14.1	15.3	15.2	15.3	15.5	16.3	16.7	16.2
Gross capital formation	14.1	15.1	14.6	14.0	15.6	15.0	16.0	17.0	18.0	19.0	19.3
Government	2.5	3.3	3.1	3.4	3.2	3.2	3.4	3.6	3.6	3.7	3.9
Non-government (including public sector enterprises)	11.6	11.7	11.5	10.6	12.4	11.8	12.5	13.4	14.4	15.3	15.4
					(In billions of U.S. dollars, unless otherwise indicated)						
Balance of payments											
Current account balance	0.2	-4.7	-2.5	-3.1	-4.0	-3.3	-3.3	-4.2	-4.9	-6.0	-7.5
Net capital flows 1/	2.3	1.4	0.5	7.0	7.4	8.1	6.0	5.8	6.5	7.8	9.5
Of which: foreign direct investment 2/	1.6	0.8	1.5	1.7	1.8	1.6	2.6	2.5	2.8	2.6	3.2
Gross official reserves	14.8	10.8	6.0	9.1	14.1	15.4	20.2	21.9	23.4	24.9	26.8
In months of imports 3/	3.6	2.7	1.5	2.1	3.0	3.6	4.5	4.5	4.5	4.4	4.4
External debt (in percent of GDP)	31.1	29.1	26.2	26.2	24.5	24.6	25.3	24.9	24.3	23.8	23.3
					(In percent of GDP)						
Public finances											
Revenue and grants	12.6	13.2	13.3	15.1	15.0	14.8	15.3	15.5	15.6	15.7	15.7
Of which: tax revenue	9.5	10.4	9.9	10.4	11.2	11.1	11.9	12.6	12.7	12.9	12.9
Expenditure (incl. stat. discr.), *of which:*	19.5	21.6	21.4	19.8	19.5	19.4	19.2	19.0	19.0	18.8	18.5
Current	16.5	17.9	16.6	16.2	16.2	16.2	15.7	15.4	15.4	15.2	14.6
Development (incl. net lending)	2.6	3.4	4.7	3.8	3.2	3.2	3.5	3.6	3.6	3.7	3.9
Primary balance 4/	-3.1	-4.0	-3.7	-0.2	0.2	0.0	0.6	0.5	0.6	0.7	0.5
Overall fiscal balance 4/	-6.9	-8.4	-8.1	-4.7	-4.5	-4.6	-3.9	-3.5	-3.4	-3.1	-2.8
Total public debt (including obligations to the IMF)	59.5	64.0	64.3	64.2	61.8	63.3	62.9	61.9	60.4	59.4	58.0

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ Difference between the overall balance and the current account balance.
2/ Including privatization.
3/ In months of next year's imports of goods and services.
4/ Including grants.

Table 5. Pakistan: Balance of Payments, 2011/12–2019/20

(In millions of U.S. dollars, unless otherwise indicated)

	2011/12	2012/13	2013/14	2014/15						2015/16			2016/17	2017/18	2018/19	2019/20
				End-Year	End-Year	Q1	Q2	Q3	Q4	Q1	Q2	End-Year				
				Fifth Review	Projections	Actual		Projections					Projections			
Current account	-4,658	-2,496	-3,096	-4,006	-3,289	-1,647	-715	-257	-670	-836	-1,116	-3,261	-4,202	-4,866	-5,968	-7,475
Balance on goods	-15,765	-15,431	-16,666	-18,906	-18,101	-6,038	-3,767	-4,324	-3,972	-4,437	-4,600	-17,323	-18,327	-19,773	-21,085	-22,960
Exports, f.o.b.	24,696	24,795	25,065	25,381	24,957	5,960	6,260	6,130	6,607	5,824	6,129	24,912	25,781	27,148	29,585	31,442
Imports, f.o.b.	40,461	40,226	41,731	44,287	43,058	11,998	10,027	10,454	10,579	10,261	10,730	42,235	44,108	46,922	50,671	54,402
Services (net)	-3,192	-1,472	-2,545	-2,806	-2,185	-489	-674	-327	-695	-837	-784	-3,379	-3,884	-3,889	-4,735	-5,652
Services: credit	5,035	6,733	5,322	5,864	6,273	1,709	1,114	1,854	1,596	1,441	1,542	5,991	6,194	7,053	7,212	7,588
Of which: Coalition Support Fund	0	1,806	1,050	1,455	1,812	735	0	717	360	240	225	915	225	0	0	0
Services: debit	8,227	8,205	7,867	8,670	8,458	2,198	1,788	2,181	2,291	2,278	2,325	9,369	10,078	10,942	11,947	13,240
Income (net)	-3,245	-3,685	-3,943	-4,236	-4,646	-812	-1,500	-936	-1,398	-1,019	-1,497	-5,126	-5,775	-6,439	-7,459	-7,992
Income: credit	826	488	541	594	562	100	167	131	164	89	102	399	516	678	615	953
Income: debit	4,071	4,173	4,484	4,830	5,208	912	1,667	1,067	1,562	1,109	1,599	5,526	6,291	7,117	8,074	8,944
Of which: interest payments	1,589	1,452	1,552	2,128	1,987	346	599	371	671	414	735	2,320	2,603	3,052	3,573	3,605
Of which: income on direct investment	2,177	2,714	2,932	2,702	3,221	566	1,067	697	891	695	864	3,206	3,689	4,065	4,501	5,339
Balance on goods, services, and income	-22,202	-20,588	-23,154	-25,947	-24,932	-7,339	-5,941	-5,587	-6,065	-6,293	-6,881	-25,828	-27,986	-30,101	-33,280	-36,603
Current transfers (net)	17,544	18,092	20,058	21,941	21,643	5,692	5,226	5,330	5,395	5,458	5,764	22,567	23,784	25,236	27,312	29,129
Current transfers: credit, *of which:*	17,686	18,183	20,215	22,111	21,845	5,745	5,295	5,370	5,435	5,497	5,804	22,726	23,943	25,395	27,471	29,288
Official	658	412	373	517	359	89	132	99	39	68	208	425	411	355	895	1,075
Workers' remittances	13,186	13,922	15,837	17,340	17,254	4,695	4,287	4,032	4,240	4,466	4,506	18,011	19,109	20,441	21,808	23,229
Other private transfers	3,842	3,849	4,005	4,253	4,231	961	876	1,239	1,155	963	1,091	4,290	4,423	4,598	4,768	4,983
Current transfers: debit	142	91	157	170	202	53	69	40	40	40	40	159	159	159	159	159
Capital account	183	264	1,860	678	615	60	192	228	135	119	166	534	341	341	155	145
Capital transfers: credit	186	266	1,860	678	615	60	192	228	135	119	166	534	341	341	155	155
Of which: official capital grants	180	250	355	678	608	58	187	228	135	119	166	534	534	341	155	155
Capital transfers: debit	3	2	0	0	0	0	0	0	0	0	0	0	0	0	0	10
Financial account	1,280	549	5,457	6,469	7,255	1,216	1,186	2,269	2,584	1,275	2,272	5,487	5,502	6,115	7,693	9,364
Direct investment abroad	-77	-198	-128	-97	-222	-18	-32	-60	-112	-56	-65	-310	-339	-347	-348	-202
Direct investment in Pakistan	821	1,456	1,669	1,809	1,620	153	376	281	810	602	635	2,553	2,477	2,806	2,632	3,188
Of which: privatization receipts	0	0	516	1,040	470	0	0	20	450	300	250	750	600	600	0	0
Portfolio investment (net), *of which:*	-144	26	2,760	2,710	1,213	182	1,001	70	-40	-140	900	760	846	3,417	4,859	4,543
Financial derivatives (net)	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Other investment assets	9	-314	211	772	-160	442	-242	-160	-200	7	0	-193	1,078	280	400	200
Monetary authorities	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
General government	3	-2	5	-3	-3	1	-4	0	0	0	0	0	0	0	0	0
Banks	-91	-126	8	185	-358	218	-156	-170	-250	-3	-50	-353	200	200	200	200
Other sectors	97	-186	198	590	201	223	-82	10	50	10	50	160	878	80	200	0
Other investment liabilities	671	-421	945	1,275	4,804	457	83	2,138	2,126	861	802	2,677	1,441	-42	150	1,636
Monetary authorities	-105	710	146	-1,065	-1	0	-1	0	0	0	0	0	0	0	0	0
General government, *of which:*	998	248	1,545	791	2,300	346	-94	719	1,330	315	601	2,237	1,206	-1,090	-1,081	-897
Disbursements	2,633	2,530	4,284	4,431	5,986	1,161	728	1,689	2,408	1,301	1,451	6,376	4,356	2,252	2,373	2,664
Amortization	1,577	2,282	2,734	3,641	3,685	815	822	970	1,078	986	850	4,139	3,151	3,343	3,454	3,561
Banks	220	-1,117	-293	381	479	173	196	100	10	50	45	152	267	265	175	360
Other sectors	-442	-262	-453	1,168	2,026	-62	-18	1,319	787	496	155	289	-32	783	1,056	2,173
Net errors and omissions	-80	-309	-363	240	193	36	157	0	0	0	0	0	300	0	0	0
Reserves and related items	3,275	1,992	-3,858	-3,380	-4,774	335	-820	-2,240	-2,048	-558	-1,322	-2,760	-1,641	-1,590	-1,879	-2,034
Reserve assets	4,430	4,530	-3,285	-5,100	-6,390	62	-1,527	-2,559	-2,367	-1,015	-1,833	-4,751	-1,714	-1,469	-1,539	-1,829
Use of Fund credit and loans	-1,155	-2,538	-573	1,720	1,616	273	707	319	318	457	511	1,991	73	-121	-340	-205
Memorandum items:																
Current account (in percent of GDP)	-2.1	-1.1	-1.2	-1.5	-1.2							-1.1	-1.4	-1.5	-1.7	-2.0
Current account (in percent of GDP; excluding fuel imports)	4.3	5.0	4.7	3.9	3.0							2.3	2.2	2.1	2.1	1.8
Exports f.o.b. (growth rate, in percent)	-2.6	0.4	1.1	0.9	-0.4							-0.2	3.5	5.3	9.0	6.3
Imports f.o.b. (growth rate, in percent)	12.8	-0.6	3.7	6.0	3.2							-1.9	4.4	6.4	8.0	7.4
Oil imports (in million US$, cif)	14,368	14,066	14,774	14,612	11,561							9,852	10,992	11,885	13,439	14,306
Terms of trade (growth rate, in percent)	-10.5	-0.6	-0.8	-1.6	3.7							4.8	-1.8	-0.5	-1	0
External debt (in millions of U.S. dollars)	65,478	60,899	65,636	66,373	67,939							73,558	76,947	80,160	83,686	87,752
Gross external financing needs (in millions of U.S. dollars) 1/	7,016	4,920	8,679	9,031	8,477							8,649	8,936	9,557	12,366	13,340
End-period gross official reserves (millions of U.S. dollars) 2/	10,799	6,008	9,096	14,103	15,439	8,943	10,514	13,073	15,439	16,454	18,287	20,190	21,904	23,374	24,913	26,752
(In months of next year's imports of goods and services)	2.7	1.5	2.1	3.0	3.6	2.2	2.5	3.1	3.6	3.8	4.1	4.5	4.5	4.5	4.4	4.4
GDP (in millions of U.S. dollars)	225,060	232,757	250,136													

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

2/ Excluding foreign currency deposits held with the State Bank of Pakistan (cash reserve requirements) and gold.

Table 6a. Pakistan: General Government Budget, 2008/09–2014/15
(In billions of Pakistani rupees)

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15 Fifth Review	2014/15 Projections
Revenue and grants	1,878	2,130	2,306	2,642	2,988	3,831	4,288	4,152
Revenue	1,851	2,079	2,261	2,567	2,949	3,625	4,191	4,073
Tax revenue	1,331	1,500	1,738	2,076	2,231	2,635	3,209	3,129
Federal	1,285	1,445	1,673	1,969	2,081	2,445	2,995	2,903
FBR revenue	1,157	1,329	1,558	1,881	1,936	2,266	2,756	2,691
Direct taxes	440	529	602	732	736	884	1,139	1,136
Federal excise duty	116	121	137	122	119	139	159	159
Sales tax/VAT	452	517	633	809	841	1,002	1,167	1,123
Customs duties	148	161	185	218	240	241	291	273
Petroleum surcharge	112	89	83	60	110	104	122	123
Gas surcharge and other	16	28	32	27	35	43	43	47
GIDC 1/	…	…	…	…	…	32	75	41
Provincial	46	55	65	107	151	190	214	226
Nontax revenue	520	579	523	491	717	990	982	944
Federal	436	512	461	443	646	941	902	884
Provincial	84	68	62	48	71	49	80	60
Grants	27	51	46	75	39	206	98	79
Expenditure	2,531	3,008	3,566	4,326	4,816	5,027	5,577	5,458
Current expenditure	2,093	2,482	3,012	3,579	3,742	4,123	4,637	4,552
Federal	1,547	1,855	2,227	2,611	2,647	2,950	3,292	3,231
Interest	638	642	698	889	991	1,148	1,344	1,298
Domestic	559	578	630	821	920	1,073	1,225	1,184
Foreign	79	64	68	68	71	75	119	114
Other	909	1,213	1,529	1,722	1,656	1,802	1,948	1,933
Defense	330	375	450	507	541	623	711	710
Other	579	838	1,078	1,215	1,116	1,179	1,237	1,223
Of which: subsidies 2/	244	227	493	556	305	336	254	234
Of which: grants	136	361	259	291	368	372	463	472
Provincial	546	627	786	968	1,095	1,173	1,345	1,321
Development expenditure and net lending	404	558	469	681	1,058	966	925	905
Public Sector Development Program	398	519	462	669	695	865	917	897
Federal	196	260	216	293	324	435	477	467
Provincial	202	258	246	375	372	431	440	430
Net lending	7	39	7	12	363	101	8	8
Statistical discrepancy ("+" = additional expenditure) 3/	34	-32	46	67	16	-62	0	0
Overall Balance (excluding grants)	-680	-929	-1,306	-1,760	-1,867	-1,402	-1,387	-1,384
Overall Balance (including grants)	-653	-878	-1,260	-1,685	-1,828	-1,196	-1,289	-1,305
Financing	653	878	1,260	1,685	1828	1,196	1,289	1,305
External	75	138	62	53	24	320	297	334
Of which: privatization receipts	1	0	0	0	0	1	2	2
Of which: IMF	0	0	0	0	0	0	0	0
Domestic	579	740	1,198	1,631	1804	876	992	971
Bank	351	304	727	1,102	1317	322	412	404
Nonbank	227	436	471	529	487	553	580	567
Memorandum items:								
Primary balance (excluding grants)	-43	-287	-608	-871	-876	-254	-43	-87
Primary balance (including grants)	-16	-236	-562	-796	-837	-48	55	-7
Total security spending	330	375	450	507	541	623	711	710
Total government debt	7,387	8,448	10,112	12,130	14,021	16,015	17,497	17,351
Domestic debt	3,860	4,654	6,014	7,638	9,521	11,024	11,837	12,061
External debt 4/	3,527	3,794	4,098	4,492	4,500	4,991	5,661	5,290
Total government debt including IMF obligations	7,805	9,138	10,879	12,822	14,454	16,313	17,686	17,786
Nominal GDP (market prices)	13,200	14,867	18,276	20,047	22,489	25,402	28,602	28,084

Sources: Pakistani authorities; and IMF staff estimates and projections.
1/ For historical series, GIDC is part of non-tax revenue
2/ Includes Rs 391 billion in FY2011/12 for the payment of energy and food subsidies delivered in previous years.
3/ The statistical discrepancy is believed to arise mainly from double-counting of spending at the provincial level.
4/ Excludes obligations to the IMF except budget financing, military debt, commercial loans, and short-term debt.

Table 6b. Pakistan: General Government Budget, 2009/10–2014/15

(In percent of GDP, unless otherwise indicated)

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	
						Fifth Review	Projections
Revenue and grants	14.3	12.6	13.2	13.3	15.1	15.0	14.8
Revenue	14.0	12.4	12.8	13.1	14.3	14.7	14.5
Tax revenue	10.1	9.5	10.4	9.9	10.4	11.2	11.1
Federal	9.7	9.2	9.8	9.3	9.6	10.5	10.3
FBR revenue	8.9	8.5	9.4	8.6	8.9	9.6	9.6
Direct taxes	3.6	3.3	3.7	3.3	3.5	4.0	4.0
Federal excise duty	0.8	0.8	0.6	0.5	0.5	0.6	0.6
Sales tax	3.5	3.5	4.0	3.7	3.9	4.1	4.0
Customs duties	1.1	1.0	1.1	1.1	0.9	1.0	1.0
Petroleum surcharge / Carbon tax	0.6	0.5	0.3	0.5	0.4	0.4	0.4
Gas surcharge and other	0.2	0.2	0.1	0.2	0.2	0.1	0.2
GIDC 1/	...	...	...	...	0.1	0.3	0.1
Provincial	0.4	0.4	0.5	0.7	0.7	0.7	0.8
Nontax revenue	3.9	2.9	2.4	3.2	3.9	3.4	3.4
Federal	3.4	2.5	2.2	2.9	3.7	3.2	3.1
Provincial	0.5	0.3	0.2	0.3	0.2	0.3	0.2
Grants	0.3	0.2	0.4	0.2	0.8	0.3	0.3
Expenditure	20.2	19.5	21.6	21.4	19.8	19.5	19.4
Current expenditure	16.7	16.5	17.9	16.6	16.2	16.2	16.2
Federal	12.5	12.2	13.0	11.8	11.6	11.5	11.5
Interest	4.3	3.8	4.4	4.4	4.5	4.7	4.6
Domestic	3.9	3.4	4.1	4.1	4.2	4.3	4.2
Foreign	0.4	0.4	0.3	0.3	0.3	0.4	0.4
Other	8.2	8.4	8.6	7.4	7.1	6.8	6.9
Defense	2.5	2.5	2.5	2.4	2.5	2.5	2.5
Other	5.6	5.9	6.1	5.0	4.6	4.3	4.4
Of which: subsidies 2/	1.5	2.7	2.8	1.4	1.3	0.9	0.8
Of which: grants	2.4	1.4	1.5	1.6	1.5	1.6	1.7
Provincial	4.2	4.3	4.8	4.9	4.6	4.7	4.7
Development expenditure and net lending	3.8	2.6	3.4	4.7	3.8	3.2	3.2
Public Sector Development Program	3.5	2.5	3.3	3.1	3.4	3.2	3.2
Federal	1.8	1.2	1.5	1.4	1.7	1.7	1.7
Provincial	1.7	1.3	1.9	1.7	1.7	1.5	1.5
Net lending	0.3	0.0	0.1	1.6	0.4	0.0	0.0
Statistical discrepancy ("+" = additional expenditure) 3/	-0.2	0.3	0.3	0.1	-0.2	0.0	0.0
Overall Balance (excluding grants)	-6.2	-7.1	-8.8	-8.3	-5.5	-4.8	-4.9
Overall Balance (including grants)	-5.9	-6.9	-8.4	-8.1	-4.7	-4.5	-4.6
Financing	5.9	6.9	8.4	8.1	4.7	4.5	4.6
External	0.9	0.3	0.3	0.1	1.3	1.0	1.2
Of which: privatization receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: IMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	5.0	6.6	8.1	8.0	3.4	3.5	3.5
Bank	2.0	4.0	5.5	5.9	1.3	1.4	1.4
Nonbank	2.9	2.6	2.6	2.2	2.2	2.0	2.0
Memorandum items:							
Primary balance (excluding grants)	-1.9	-3.3	-4.3	-3.9	-1.0	-0.1	-0.3
Primary balance (including grants)	-1.6	-3.1	-4.0	-3.7	-0.2	0.2	0.0
Total security spending	2.5	2.5	2.5	2.4	2.5	2.5	2.5
Total government debt 4/	56.2	55.3	60.5	62.3	63.0	61.2	61.8
Domestic debt	31.0	32.9	38.1	42.3	43.4	41.4	42.9
External debt 4/	25.2	22.4	22.4	20.0	19.6	19.8	18.8
Total government debt including IMF	60.8	59.5	64.0	64.3	64.2	61.8	63.3
Nominal GDP (market prices, billions of Pakistani rupees)	14,867	18,276	20,047	22,489	25,402	28,602	28,084

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ For historical series, GIDC is part of non-tax revenue

2/ Includes 1.8 percent of GDP in FY2011/12 for the payment of energy and food subsidies delivered in previous years.

3/ The statistical discrepancy is believed to arise mainly from double-counting of spending at the provincial level.

4/ Excludes obligations to the IMF except budget financing, military debt, commercial loans, and short-term debt.

Table 6c. Pakistan: General Government, 2013/14–2015/16

(In billions of Pakistani rupees)

	2013/14	2014/15						2015/16	
		End-Year	End-Year	Q1	Q2	Q3	Q4	Q1	Q2
		Fifth Review	Projections	Actual		Projections		Projections	
Revenue and grants	3,831	4,288	4,152	842	919	1,068	1,323	957	1,133
Revenue	3,625	4,191	4,073	840	889	1,036	1,308	920	1,109
Tax revenue	2,635	3,209	3,129	628	735	781	985	719	902
Federal	2,445	2,995	2,903	583	685	728	907	668	836
FBR revenue	2,266	2,756	2,691	539	635	673	845	625	791
Direct taxes	884	1,139	1,136	190	269	307	370	235	341
Federal excise duty	139	159	159	25	40	38	55	39	46
Sales tax/VAT	1,002	1,167	1,123	259	255	262	348	287	328
Customs duties	241	291	273	65	71	66	72	65	76
Petroleum surcharge	104	122	123	28	32	31	33	32	32
Gas surcharge and other	39	37	40	8	6	9	17	9	11
GIDC 1/	32	75	41	7	8	13	13	0	0
Provincial	190	214	226	45	50	53	78	51	66
Nontax revenue	990	982	944	212	154	255	323	200	207
Federal	941	902	884	200	142	239	303	188	192
Provincial	49	80	60	12	12	16	20	13	15
Grants	206	98	79	2	30	32	16	37	23
Expenditure	5,027	5,577	5,458	1,178	1,224	1,382	1,673	1,273	1,421
Current expenditure	4,123	4,637	4,552	1,074	969	1,159	1,350	1,138	1,216
Federal	2,950	3,292	3,231	796	643	827	965	842	854
Interest	1,148	1,344	1,298	395	178	348	376	367	355
Domestic	1,073	1,225	1,184	376	149	326	334	333	312
Foreign	75	119	114	19	30	23	42	34	43
Other	1,802	1,948	1,933	401	465	479	588	475	500
Defense	623	711	710	165	165	178	203	168	194
Other	1,179	1,237	1,223	236	300	301	386	307	306
Of which: subsidies 2/	336	254	234	58	67	54	55	49	37
Of which: grants	372	463	472	75	124	118	155	119	130
Provincial	1,173	1,345	1,321	278	325	332	386	296	362
Development expenditure and net lending	966	925	905	98	181	223	403	136	204
Public Sector Development Program	865	917	897	93	176	221	407	133	202
Federal	435	477	467	40	86	109	232	56	92
Provincial	431	440	430	53	91	112	174	77	110
Net lending	101	8	8	5	5	2	-3	2	2
Statistical discrepancy ("+" = additional expenditure) 3/	-62	0	0	6	75	0	-81	0	0
Overall Balance (excluding grants)	-1,402	-1,387	-1,384	-338	-335	-347	-365	-354	-311
Overall Balance (including grants)	-1,196	-1,289	-1,305	-336	-305	-315	-350	-317	-288
Financing	1,196	1,289	1,305	336	305	315	350	317	288
External	320	297	334	-31	146	78	141	174	-80
Of which: IMF	0	0	0	0	0	0	0	0	0
Domestic	876	992	971	366	159	237	208	142	368
Bank	322	412	404	156	74	140	34	137	79
Nonbank	553	580	567	210	86	97	174	5	288
Memorandum items:									
Primary balance (excluding grants)	-254	-43	-87	57	-157	2	11	13	43
Primary balance (including grants)	-48	55	-7	59	-127	34	27	50	67
Total security spending	623	711	710	165	165	178	203	168	194
Total government debt	16,015	17,497	17,351						
Domestic debt	11,024	11,837	12,061						
External debt 4/	4,991	5,661	5,290						
Total government debt including IMF obligations	16,313	17,686	17,786						
Nominal GDP (market prices)	25,402	28,602	28,084						

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ For historical series, GIDC is part of non-tax revenue

2/ Includes Rs 391 billion in FY2011/12 for the payment of energy and food subsidies delivered in previous years.

3/ The statistical discrepancy is believed to arise mainly from double-counting of spending at the provincial level.

4/ Excludes obligations to the IMF except budget financing, military debt, commercial loans, and short-term debt.

Table 7. Pakistan: Monetary Survey, 2010/11–2015/16

	2010/11	2011/12	2012/13	2013/14	2014/15					2015/16	
					Q1	Q2	Q3	Q4	End-Year	Q1	Q2
					Actual		Projections		Fifth Review	Projections	
	(In billions of Pakistani rupees, unless otherwise indicated)										
Monetary survey											
Net foreign assets (NFA)	780	527	270	601	570	649	880	1,092	971	1,152	1,293
Net domestic assets (NDA)	5,915	7,115	8,588	9,367	9,392	9,762	9,659	10,095	10,236	10,036	10,414
Net claims on government, *of which: 1/*	2,983	4,197	5,629	5,710	5,713	5,677	6,126	6,327	6,351	6,440	6,440
Budget support, *of which:*	2,523	3,667	5,125	5,448	5,588	5,647	5,787	5,821	5,845	5,959	5,959
Banks	1,369	2,005	2,957	3,121	3,300	3,733	3,882	3,956	3,980	4,159	4,209
Commodity operations	397	436	468	492	469	467	339	505	505	482	482
Credit to nongovernment	3,547	3,653	3,664	4,102	4,149	4,377	4,533	4,636	4,645	4,713	4,929
Private sector	3,159	3,395	3,376	3,747	3,794	3,969	4,120	4,198	4,286	4,251	4,467
Public sector enterprises	388	257	288	355	355	407	412	437	359	462	462
Privatization account	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3
Other items, net	-612	-732	-702	-442	-467	-288	-997	-865	-757	-1,114	-952
Broad money	6,695	7,642	8,858	9,968	9,962	10,411	10,539	11,187	11,207	11,188	11,708
Currency outside scheduled banks	1,501	1,674	1,938	2,178	2,262	2,302	2,351	2,488	2,500	2,499	2,605
Rupee deposits	4,819	5,528	6,405	7,191	7,082	7,490	7,561	8,034	8,011	8,023	8,407
Foreign currency deposits	375	440	515	599	618	619	627	665	695	665	696
State Bank of Pakistan (SBP)											
NFA	614	389	134	490	482	555	786	998	883	1,058	1,200
NDA	1,352	1,800	2,401	2,372	2,310	2,226	2,266	2,193	2,322	2,057	1,909
Net claims on government	1,184	1,665	2,156	2,236	2,115	1,701	1,730	1,752	1,772	1,631	1,582
Of which: budget support	1,155	1,662	2,168	2,328	2,289	1,914	1,905	1,865	1,865	1,800	1,750
Claims on nongovernment	-6	-5	-6	-5	-6	-6	-6	-6	-6	-6	-6
Claims on scheduled banks	315	289	448	500	505	561	572	645	720	666	564
Privatization account	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3
Other items, net	-139	-146	-195	-356	-302	-27	-27	-195	-161	-231	-230
Reserve money, *of which:*	1,966	2,189	2,535	2,861	2,791	2,781	3,052	3,191	3,205	3,115	3,108
Banks' reserves	349	396	476	531	380	329	332	353	430	352	369
Currency	1,606	1,784	22,489	2,317	2,397	2,440	2,720	2,838	2,775	2,763	2,739
	(Annual percentage change, unless otherwise indicated)										
Broad money	15.9	20.9	15.9	12.5	12.2	10.9	12.3	12.2	12.4	12.3	12.5
NFA, banking system (in percent of broad money) 2/	4.1	-3.0	-3.4	3.7	5.3	6.3	7.6	4.9	3.7	5.8	6.2
NDA, banking system (in percent of broad money) 2/	11.8	66.0	19.3	8.8	6.9	4.6	4.7	7.3	8.7	6.5	6.3
Budgetary support (in percent of broad money) 2/	10.2	17.1	19.1	3.7	3.0	0.4	2.4	3.7	4.0	3.7	3.0
Budgetary support	30.4	45.3	39.7	6.3	5.0	0.7	4.1	6.8	7.3	6.6	5.5
Private credit	4.0	16.9	-0.6	11.0	13.0	7.4	11.0	12.0	14.0	12.0	12.5
Currency	15.9	70.4	15.8	12.4	14.0	10.3	11.0	14.2	14.8	10.5	13.2
Reserve money	17.1	47.9	15.8	12.9	8.2	2.1	11.5	11.5	12.0	11.6	11.8
Memorandum items:											
Velocity	2.7	2.6	2.5	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.6
Money multiplier	3.4	3.5	3.5	3.5	3.6	3.7	3.5	3.5	3.5	3.6	3.8
Currency to broad money ratio (percent)	22.4	21.9	21.9	21.8	22.7	22.1	22.3	22.2	22.3	22.3	22.2
Currency to deposit ratio (percent)	28.9	28.0	28.0	28.0	29.4	28.4	28.7	28.6	28.7	28.8	28.6
Foreign currency to deposit ratio (percent)	7.2	7.4	7.4	7.7	8.0	7.6	7.7	7.6	8.0	7.7	7.6
Reserves to deposit ratio (percent)	6.7	6.6	6.9	6.8	4.9	4.1	4.1	4.1	4.9	4.1	4.1
Budget bank financing (change from the beginning of the fiscal year; in Rs billions), *of which:*	589	1,144	1,458	324	140	199	339	373	397	137	137
By commercial banks	606	636	952	164	179	612	762	836	859	202	252
By SBP	-17	508	506	160	-39	-413	-423	-463	-463	-65	-115
NFA of SBP (change from beginning of the year; in billions of U.S. dollars) 3/	2.7	-3.0	-2.8	3.6	-0.3	0.4	2.7	4.7	3.2	0.2	1.6
NFA of commercial banks (millions of U.S. dollars)	1,937	1,464	1,377	1,130	861	913	908	905	815	872	874
NDA of commercial banks (billions of Pakistani rupees)	4,563	5,315	6,187	6,995	7,082	7,536	7,393	7,902	7,913	7,979	8,506

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ Difference between monetary and fiscal tables on banking sector claims on government and bank financing in 2011/12 reflects Rs391 billion in electricty payments.

2/ Denominator is the stock of broad (reserve) money at the end of the previous year.

3/ Includes valuation adjustments.

Table 8. Pakistan: Financial Soundness Indicators for the Banking System

(December 2010-December 2014)

	Dec. 2010	Dec. 2011	Dec. 2012	Mar. 2013	Jun. 2013	Sep. 2013	Dec. 2013	Mar. 2014	Jun. 2014	Sep. 2014	Dec. 2014
Capital adequacy 1/											
Regulatory capital to risk-weighted assets	13.9	15.1	15.4	15.1	15.5	15.5	15.1	14.8	15.1	15.5	17.1
Tier I capital to risk-weighted assets	11.6	13.0	12.8	12.7	13.0	13.2	12.8	12.5	12.5	13.6	14.3
Capital to total assets	9.8	9.6	9.0	8.9	8.9	9.3	8.9	8.9	8.8	9.0	10
Asset composition and quality											
Nonperforming loans (NPLs) to gross loans	14.9	15.7	14.5	14.7	14.8	14.3	13.0	13.4	12.8	13.0	12.3
Provisions to NPLs	66.7	69.3	71.8	71.9	73.2	76.5	78.4	77.8	79.5	77.6	79.8
NPLs net of provisions to capital	26.7	23.1	19.4	19.9	18.3	15.7	13.0	14.0	12.5	13.6	10.1
Earnings and profitability											
Return on assets (after tax)	1.0	1.5	1.4	1.2	1.1	1.1	1.1	1.3	1.4	1.4	1.5
Return on equity (after tax)	9.6	15.1	14.9	13.9	12.4	12.3	12.4	14.1	15.4	15.9	16.1
Net interest income to gross income	74.7	76.0	71.1	71.7	70.0	70.3	70.3	69.9	70.5	71.4	71.3
Noninterest expenses to gross income	52.7	51.1	53.9	57.5	56.4	56.8	57.4	56.8	54.6	54.8	53.3
Liquidity											
Liquid assets to total assets	36.1	45.5	47.4	47.4	49.0	46.7	47.3	48.3	47.8	54.8	49.2
Liquid assets to total deposits	47.1	59.5	63.3	63.8	63.7	59.2	60.0	63.7	60.6	61.4	64.5
Loans/Deposits	61.4	53.6	51.5	51.6	48.1	48.7	48.6	49.2	47.7	48.2	48.2

Source: State Bank of Pakistan.

1/ As of December 2013, CAR indicators are reported under Basel III.

Table 9. Pakistan: Indicators of Fund Credit, 2013–20
(In millions of SDR unless otherwise specified)

	2013	2014	2015	2016	2017	2018	2019	2020
			Projections					
	(Projected Level of Credit Outstanding based on Existing Drawings and Prospective Drawings)							
Total	2,296.8	2,463.0	3,600.0	4,393.0	4,393.0	4,243.0	3,823.0	3,163.0
Of which:								
ECF, SBA, and ENDA	1,576.8	303.0	0.0	0.0	0.0	0.0	0.0	0.0
Extended Fund Facility	720.0	2,160.0	3,600.0	4,393.0	4,393.0	4,243.0	3,823.0	3,163.0
In percent of end-period gross official reserves	101.8	33.7	29.0	32.6	30.1	27.6	25.9	20.2
As a share of external debt	5.8	5.4	7.6	8.6	8.3	7.7	6.6	5.2
	(Projected Debt Service to the Fund based on Existing and Prospective Drawings) 1/							
Total			237.3	63.5	72.2	223.0	494.5	715.0
Of which:								
Principal	-2,313.5	-1,273.8	207.2	0.0	0.0	150.0	420.0	660.0
Interest and charges	41.6	24.4	30.0	63.5	72.2	73.0	74.5	55.0
SBA and ENDA Principal	..	..	207.2	0.0	0.0	0.0	0.0	0.0
Extended Fund Facility Principal	..	..	207.2	0.0	0.0	150.0	420.0	660.0
In percent of end-period gross official reserves	..	..	1.9	0.5	0.5	1.4	3.4	4.6
As a share of total external debt service	..	..	0.5	0.1	0.1	0.4	0.9	1.2
Memorandum items								
Quota (millions of SDRs)	1,033.70	1,033.70	1,033.70	...	...	...	...	...
Gross official reserves (millions of U.S. dollars)	3,478	10,514	17,948	19,643	21,244	22,389	21,454	22,763
Total External Debt (millions of U.S. dollars)	60,899	65,636	68,133	73,929	77,328	80,530	84,045	88,098
Total External Debt Service (millions of U.S. dollars)	6,797	7,135	7,179	7,719	7,384	7,812	10,040	9,542

Source: IMF staff projections.

Table 10. Pakistan: Selected Vulnerability Indicators, 2010/11–2019/20

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
							Projections			
Key economic and market indicators										
Real GDP growth (factor cost, in percent)	3.6	3.8	3.7	4.1	4.3	4.7	4.8	5.0	5.0	5.0
CPI inflation (period average, in percent) 1/	13.7	11.0	7.4	8.6	6.0	5.3	5.0	5.0	5.0	5.0
Emerging market bond index (EMBI) secondary market spread (basis points, end of period)	857	1,136	703	501	...	...	...	...	...	...
Exchange rate PRs/US$ (end of period)	85.8	94.3	98.7	98.6	...	...	...	...	...	...
External sector										
Current account balance (percent of GDP)	0.1	-2.1	-1.1	-1.2	-1.2	-1.1	-1.4	-1.5	-1.7	-2.0
Net FDI inflows (percent of GDP)	0.7	0.3	0.5	0.6	0.5	0.8	0.7	0.7	0.6	0.8
Exports (percentage change of U.S. dollar value; GNFS)	25.0	-4.5	6.0	-3.6	2.8	-1.0	3.5	7.0	7.6	6.1
Gross international reserves (GIR) in billions of U.S. dollars	14.8	10.8	6.0	9.1	15.4	20.2	21.9	23.4	24.9	26.8
GIR in percent of ST debt at remaining maturity (RM) 2/	332.8	273.7	111.1	145.5	221.5	241.7	337.3	629.1	651.1	680.1
GIR in percent of ST debt at RM and banks' foreign exchange (FX) deposits 2/	169.3	125.4	56.5	73.8	115.3	132.3	158.7	203.0	205.9	209.7
Total gross external debt (ED) in percent of GDP, *of which:*	31.1	29.1	26.2	26.2	24.6	25.3	24.9	24.3	23.8	23.3
ST external debt (original maturity, in percent of total ED)	1.0	0.6	0.0	1.1	2.2	1.1	1.6	1.6	1.6	1.5
ED of domestic private sector (in percent of total ED)	10.8	10.8	10.4	13.3	16.5	17.7	19.5	24.2	29.1	33.6
ED to foreign official sector (in percent of total ED)	89.2	89.2	89.6	86.7	83.5	82.3	80.5	75.8	70.9	66.4
Total gross external debt in percent of exports	213.2	220.2	193.2	216.0	217.5	238.0	240.6	234.4	227.4	224.8
Gross external financing requirement (in billions of U.S. dollars) 3/	1.9	6.7	5.3	6.4	7.4	8.6	8.9	9.4	12.0	13.1
Public sector 4/										
Overall balance (including grants)	-6.9	-8.4	-8.1	-4.7	-4.6	-3.9	-3.5	-3.4	-3.1	-2.8
Primary balance (including grants)	-3.1	-4.0	-3.7	-0.2	0.0	0.6	0.5	0.6	0.7	0.5
Debt-stabilizing primary balance 5/	-7.8	1.4	-1.6	-3.1	-0.7	-0.8	-1.1	-1.2	-1.2	0.0
Gross PS financing requirement 6/	26.9	32.5	35.9	34.6	30.2	28.7	27.6	27.1	26.3	25.4
Public sector gross debt 7/	55.3	60.5	62.3	63.0	61.8	60.7	59.8	58.5	57.6	56.4
Public sector net debt 8/	52.0	57.2	59.2	59.8	58.6	57.5	56.6	55.3	54.4	53.2
Financial sector 9/										
Capital adequacy ratio (in percent)	15.1	15.4	15.5	15.1	...	...	...	...	...	...
Nonperforming loans (NPLs) in percent of total loans	15.7	14.5	14.8	12.8	...	...	...	...	...	...
Provisions in percent of NPLs	69.3	71.8	73.2	79.5	...	...	...	...	...	...
Return on assets (after tax, in percent)	1.5	1.4	1.1	1.4	...	...	...	...	...	...
Return on equity (after tax, in percent)	15.1	14.9	12.4	15.4	...	...	...	...	...	...
FX deposits held by residents (in percent of total deposits)	7.7	7.4	7.4	7.7	...	...	...	...	...	...
Government debt held by FS (percent of total FS assets)	41.2	54.9	63.6	57.3	...	...	...	...	...	...
Credit to private sector (percent change)	7.6	3.9	-0.6	11.0	...	...	...	...	...	...
Memorandum item:										
Nominal GDP (in billions of U.S. dollars)	213.6	225.1	232.8	250.1						

Sources: Pakistani authorities; and IMF staff estimates and projections.

1/ Inflation after 2009/10 based on new CPI weights, recalculated in September 2011.
2/ Debt at remaining maturity is defined as maturing short-, medium-, and long-term external official debt.
3/ Current account deficit plus amortization of external debt.
4/ Public sector covers general (consolidated) government.
5/ Based on the end of period debt stock in year t-1, and the baseline assumptions for the relevant variables (i.e., growth, interest rates, inflation, exchange rates) in year t.
6/ Overall balance plus debt amortization.
7/ Excludes obligations to the IMF except budget financing, military debt, commercial loans, and short-term debt.
8/ Net debt is defined as gross debt minus government deposits with the banking system.
9/ Financial sector includes all commercial and specialized banks; for government debt also includes nonbanks, but excludes State Bank of Pakistan.

Table 11. Pakistan: Schedule of Reviews and Purchases

Date	Amount of Purchase		Conditions
	Millions of SDRs	Percent of Quota	
September 4, 2013	360	35	Approval of arrangement
December 2, 2013	360	35	First review and end-September 2013 performance/continuous criteria
March 2, 2014	360	35	Second review and end-December 2013 performance /continuous criteria
June 2, 2014	360	35	Third review and end-March 2014 performance /continuous criteria
December 2, 2014	720	70	Fourth and Fifth reviews and end-June and end-September 2014 performance /continuous criteria
March 2, 2015	360	35	Sixth review and end-December 2014 performance /continuous criteria
June 2, 2015	360	35	Seventh review and end-March 2015 performance /continuous criteria
September 2, 2015	360	35	Eighth review and end-June 2015 performance /continuous criteria
December 2, 2015	360	35	Ninth review and end-September 2015 performance/continuous criteria
March 2, 2016	360	35	Tenth review and end-December 2015 performance /continuous criteria
June 2, 2016	360	35	Eleventh review and end-March 2016 performance /continuous criteria
August 1, 2016	73	7	Twelfth review and end-June 2016 performance /continuous criteria
Total	4393	425	

Source: IMF staff estimates.

Annex I. Public and External Debt Sustainability Analysis (DSA)

Pakistan's public debt is expected to decline from 64.3 percent of GDP in 2013 to 59.4 percent by 2019. The projected downward trajectory appears to be resilient to standard size shocks, as long as fiscal consolidation is sustained over the medium term. Nevertheless, risks from relatively high financing needs are somewhat ameliorated by a captive domestic investor base and the Fund-supported program. The heavy reliance on short-term borrowing makes debt dynamics sensitive to interest rate shocks, and emphasizes the need for extension of the yield curve.

1. **This is an update of the DSA conducted for the first review of the program in 2013**. The coverage used for public debt includes federal and provincial governments, but does not include public sector enterprises.[1] Prior to the current Fund-supported economic stabilization program, Pakistan's debt-to-GDP ratio was on an upward trend as a result of large fiscal deficits, even though debt dynamics benefited from low effective real interest rates. Significant fiscal adjustment—lowering the overall budget deficit from 8.1 percent of GDP in FY2012/13 to 4.7 percent in FY2013/14—has helped reverse the trend.

2. **Domestic debt is largely in local currency and short term**. The share of medium-term bonds remains below 20 percent, although it has been increasing recently as the authorities extend the yield curve. Therefore, funding remains reliant on short-term debt (over 50 percent) and on the national saving schemes, which provide a relatively captive investor base. Although the authorities have issued more external debt as part of their diversification strategy, public external debt remains largely with official creditors, as bonds and bank private creditors account for only about 3 percent of the total.

3. **The macroeconomic and fiscal assumptions underpinning the DSA are based on the medium-term baseline scenario**. The program assumptions on growth and inflation are realistic and remain in line with the incoming data. Real GDP growth is projected to improve over the medium-term above the levels observed in recent years, as the economy moves beyond the impact of the global crisis and the severe floods. However, while benefiting from the fall in international oil prices, Pakistan continues to face significant security concerns as a downside risk. The envisaged primary balance is larger and more persistent relative to Pakistan's previous track record.

4. **Public debt is projected to decline below 60 percent of GDP by 2019, but high gross financing needs are a source of vulnerability**. Fiscal consolidation under the program is the key driver of improvements in debt dynamics. Fiscal adjustment not only improves the debt ratio under the baseline scenario, but the declining trend is quite resilient to standard size shocks envisaged in the DSA. The fan charts show that debt would stabilize even under significant shocks, and it is only when one restricts the distribution of positive shocks to the primary balance that the debt-to-GDP

[1] Public debt does not include circular debt, as in its current rate it does not substantially change the public debt profile and DSA analysis.

ratio trends up under very strong shocks. However, gross financing needs are high and are sensitive to shocks. While the consolidation will ameliorate this risk, a more significant improvement in the debt profile will require longer term efforts. These gross financing needs indicators reflect the relatively large share of national savings schemes which, given their diversified base, might have a smaller rollover risk.

5. **The external DSA shows that the projected path for external debt is sustainable**. Gross external debt as a percentage of GDP has been in a declining trend—reaching 26.2 percent in 2014—and is expected to see a modest decline in the coming years. This is consistent with relatively stable gross financing needs, which are expected to remain in a range of 2.7 to 3.7 percent of GDP. Moreover, the short-term financing risk for nonbank private sector is expected to remain low. Bound and stress tests suggest that the external debt-to-GDP ratio is resilient to adverse shocks. While sensitive to growth and exchange rate shocks, the external debt ratio would not exceed 37 percent of GDP under any scenario.

Table 1. Pakistan: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

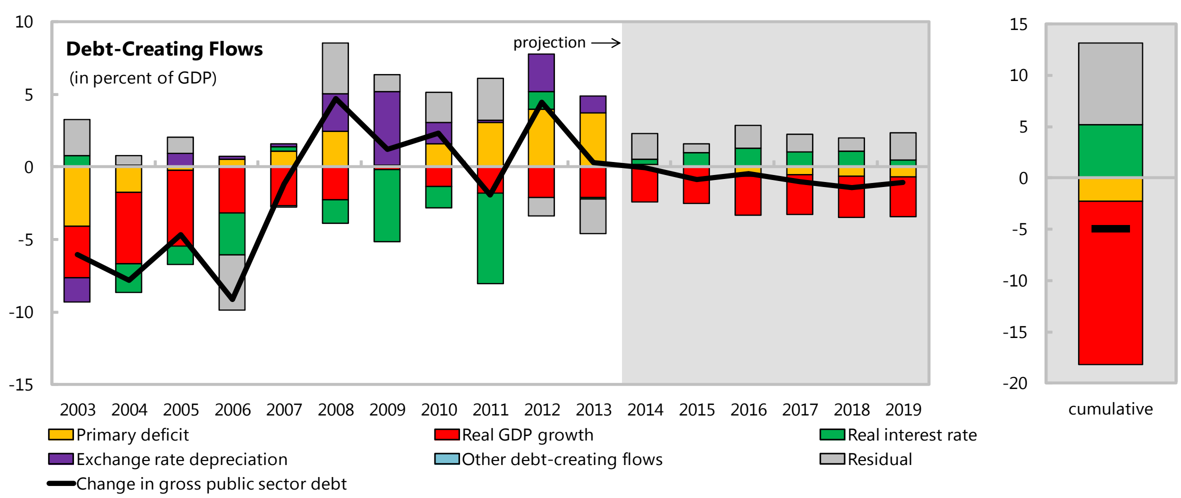
(In percent of GDP; unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of January 15, 2015		
	2003-2011 [2/]	2012	2013	2014	2015	2016	2017	2018	2019	Sovereign Spreads		
Nominal gross public debt	61.5	64.0	64.3	64.2	63.3	62.9	61.9	60.4	59.4	EMBIG (bp) 3/		425
Public gross financing needs	39.6	38.2	34.7	28.3	27.9	24.5	26.7	27.5	27.1	5Y CDS (bp)		604
Real GDP growth (in percent)	4.9	3.8	3.7	4.1	4.3	4.7	4.8	5.0	5.0	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	11.2	5.7	7.6	7.0	6.0	5.3	5.0	5.0	5.0	Moody's	Caa1	Caa1
Nominal GDP growth (in percent)	17.1	9.7	12.2	13.0	10.6	10.2	10.1	10.3	10.3	S&Ps	B	B
Effective interest rate (in percent) [4/]	7.4	8.2	7.7	7.9	8.0	7.7	7.1	7.2	6.1	Fitch	BBB+	BBB+

Contribution to Changes in Public Debt

	Actual			Projections							
	2003-2011	2012	2013	2014	2015	2016	2017	2018	2019	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-2.5	4.4	0.3	-0.1	-0.9	-0.5	-1.0	-1.4	-1.1	-4.9	
Identified debt-creating flows	-3.6	5.7	2.7	-1.8	-1.5	-2.0	-2.2	-2.4	-2.9	-12.9	
Primary deficit	0.3	4.0	3.7	0.2	0.0	-0.6	-0.5	-0.6	-0.7	-2.2	-2.3
Primary (noninterest) revenue and grant	14.4	13.2	13.3	15.1	14.8	15.3	15.5	15.6	15.7	92.0	
Primary (noninterest) expenditure	14.7	17.1	17.0	15.3	14.8	14.7	15.0	14.9	15.0	89.8	
Automatic debt dynamics [5/]	-3.9	1.7	-1.1	-2.0	-1.5	-1.4	-1.7	-1.7	-2.3	-10.6	
Interest rate/growth differential [6/]	-4.9	-0.8	-2.2	-2.0	-1.5	-1.4	-1.7	-1.7	-2.3	-10.6	
Of which: real interest rate	-2.2	1.2	-0.1	0.4	1.0	1.3	1.1	1.1	0.5	5.2	
Of which: real GDP growth	-2.8	-2.1	-2.1	-2.4	-2.5	-2.7	-2.8	-2.8	-2.7	-15.9	
Exchange rate depreciation [7/]	1.0	2.6	1.2	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
#TSREF! (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other debt flows (incl. ESM and Euroar	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	1.1	-1.3	-2.4	1.8	0.6	1.6	1.2	0.9	1.9	8.0	



Sources: Pakistani authorities; and IMF staff calculations.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

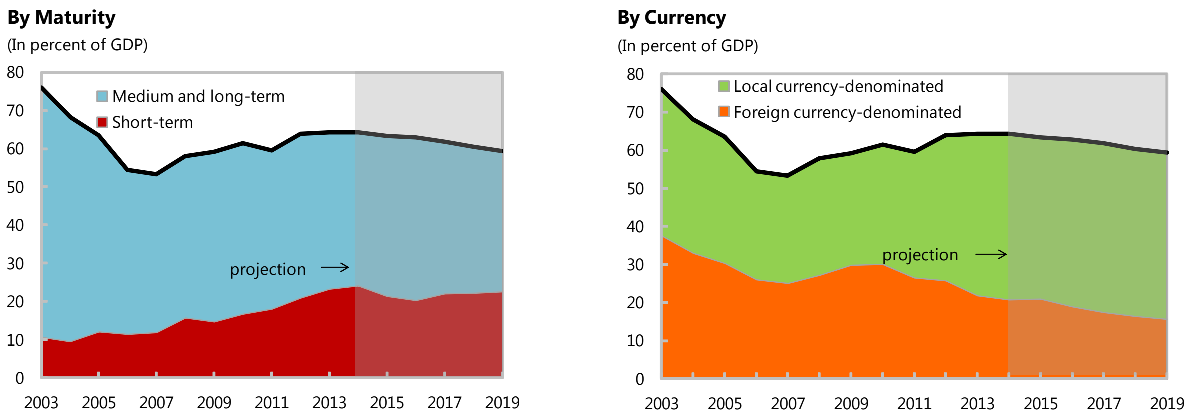
7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

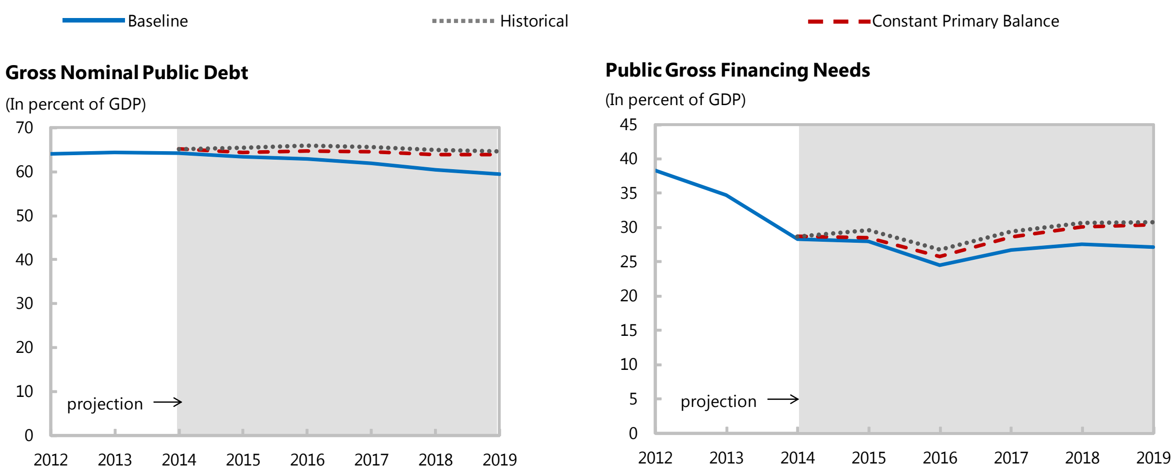
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 1. Pakistan: Public Debt Sustainability—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt



Alternative Scenarios



Underlying Assumptions

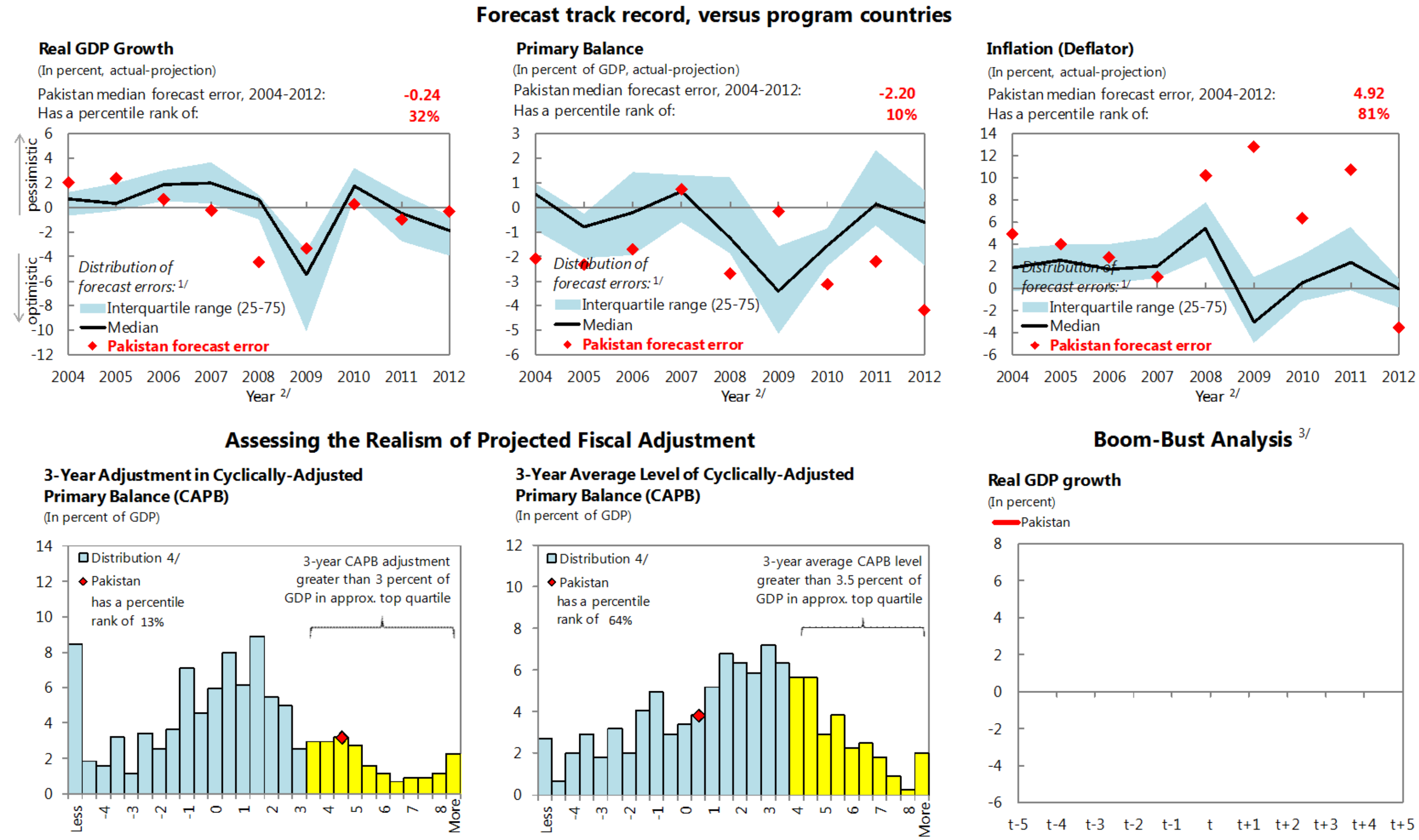
(In percent)

Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	4.1	4.3	4.7	4.8	5.0	5.0
Inflation	7.0	6.0	5.3	5.0	5.0	5.0
Primary Balance	-0.2	0.0	0.6	0.5	0.6	0.7
Effective interest rate	7.9	8.0	7.7	7.1	7.2	6.1
Constant Primary Balance Scenario						
Real GDP growth	4.1	4.3	4.7	4.8	5.0	5.0
Inflation	7.0	6.0	5.3	5.0	5.0	5.0
Primary Balance	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Effective interest rate	7.9	8.0	7.8	7.1	7.3	6.3

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	4.1	4.7	4.7	4.7	4.7	4.7
Inflation	7.0	6.0	5.3	5.0	5.0	5.0
Primary Balance	-0.2	-1.5	-1.5	-1.5	-1.5	-1.5
Effective interest rate	7.9	8.0	5.8	4.9	4.6	3.4

Sources: Pakistani authorities; and IMF staff calculations.

Figure 2. Pakistan: Public Debt Sustainability Analysis—Realism of Baseline Assumptions



Sources: Pakistani authorities; and IMF Staff calculations.

1/ Plotted distribution includes program countries, percentile rank refers to all countries.

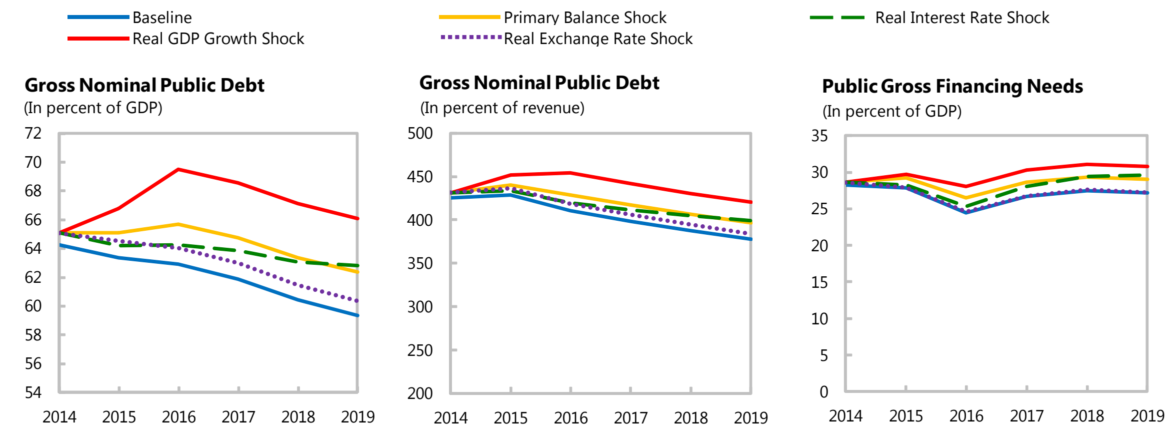
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Pakistan.

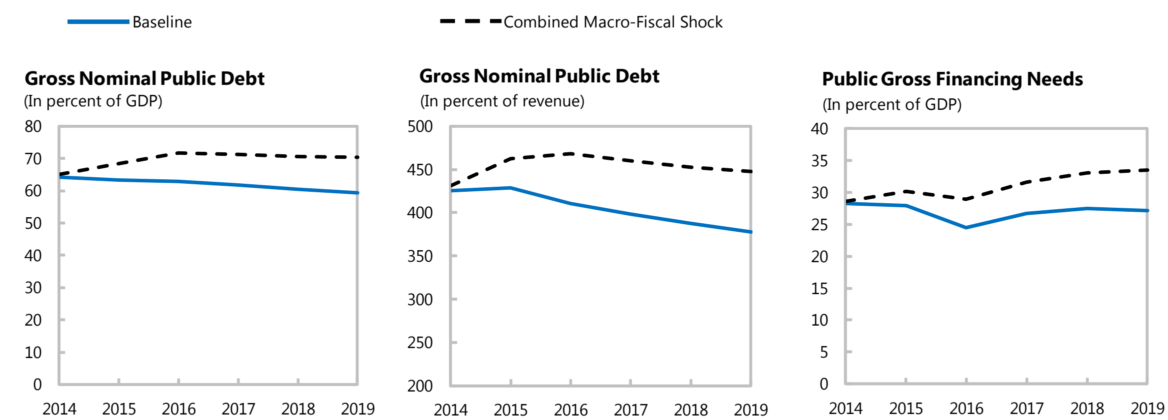
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 3. Pakistan: Public Debt Sustainability Analysis—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(In percent)

	2014	2015	2016	2017	2018	2019
Primary Balance Shock						
Real GDP growth	4.1	4.3	4.7	4.8	5.0	5.0
Inflation	7.0	6.0	5.3	5.0	5.0	5.0
Primary balance	-0.2	-1.0	-0.3	0.5	0.6	0.7
Effective interest rate	7.9	8.0	7.9	7.3	7.3	6.3
Real Interest Rate Shock						
Real GDP growth	4.1	4.3	4.7	4.8	5.0	5.0
Inflation	7.0	6.0	5.3	5.0	5.0	5.0
Primary balance	-0.2	0.0	0.6	0.5	0.6	0.7
Effective interest rate	7.9	8.0	8.6	8.1	8.4	7.5
Combined Shock						
Real GDP growth	4.1	1.8	2.3	4.8	5.0	5.0
Inflation	7.0	5.4	4.6	5.0	5.0	5.0
Primary balance	-0.2	-1.0	-0.5	0.5	0.6	0.7
Effective interest rate	7.9	8.0	8.5	8.1	8.4	7.5

	2014	2015	2016	2017	2018	2019
Real GDP Growth Shock						
Real GDP growth	4.1	1.8	2.3	4.8	5.0	5.0
Inflation	7.0	5.4	4.6	5.0	5.0	5.0
Primary balance	-0.2	-0.7	-0.5	0.5	0.6	0.7
Effective interest rate	7.9	8.0	7.8	7.3	7.3	6.3
Real Exchange Rate Shock						
Real GDP growth	4.1	4.3	4.7	4.8	5.0	5.0
Inflation	7.0	7.7	5.3	5.0	5.0	5.0
Primary balance	-0.2	0.0	0.6	0.5	0.6	0.7
Effective interest rate	7.9	8.0	7.6	7.0	7.1	6.0

Sources: Pakistani authorities; and IMF staff calculations.

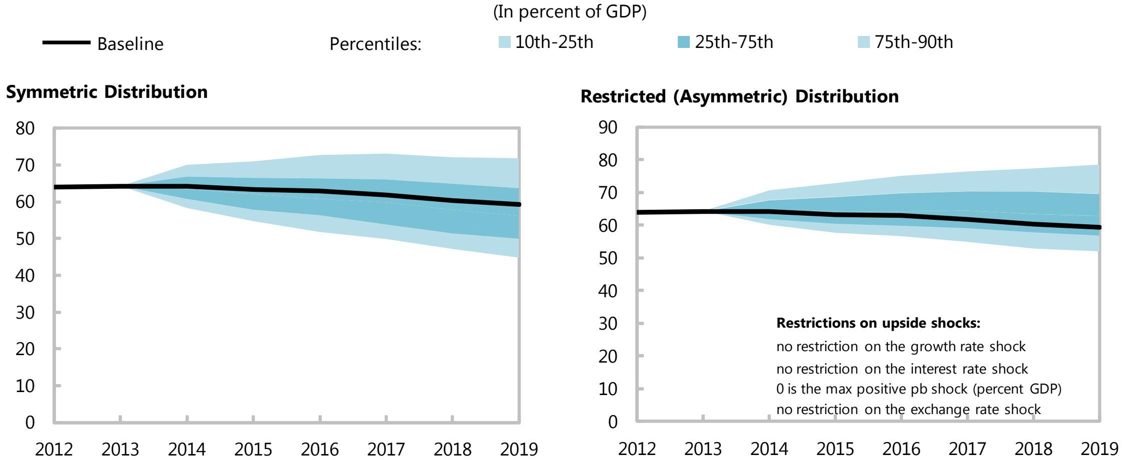
Figure 4. Pakistan: Public Debt Sustainability Analysis—Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

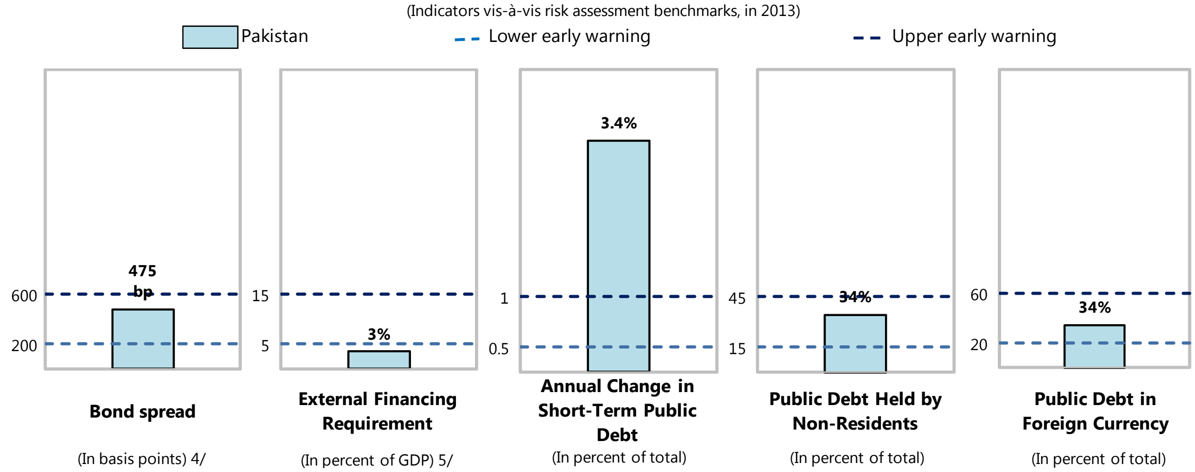
Evolution of Predictive Densities of Gross Nominal Public Debt

(In percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2013)



Sources: Pakistani authorities; and IMF staff calculations.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

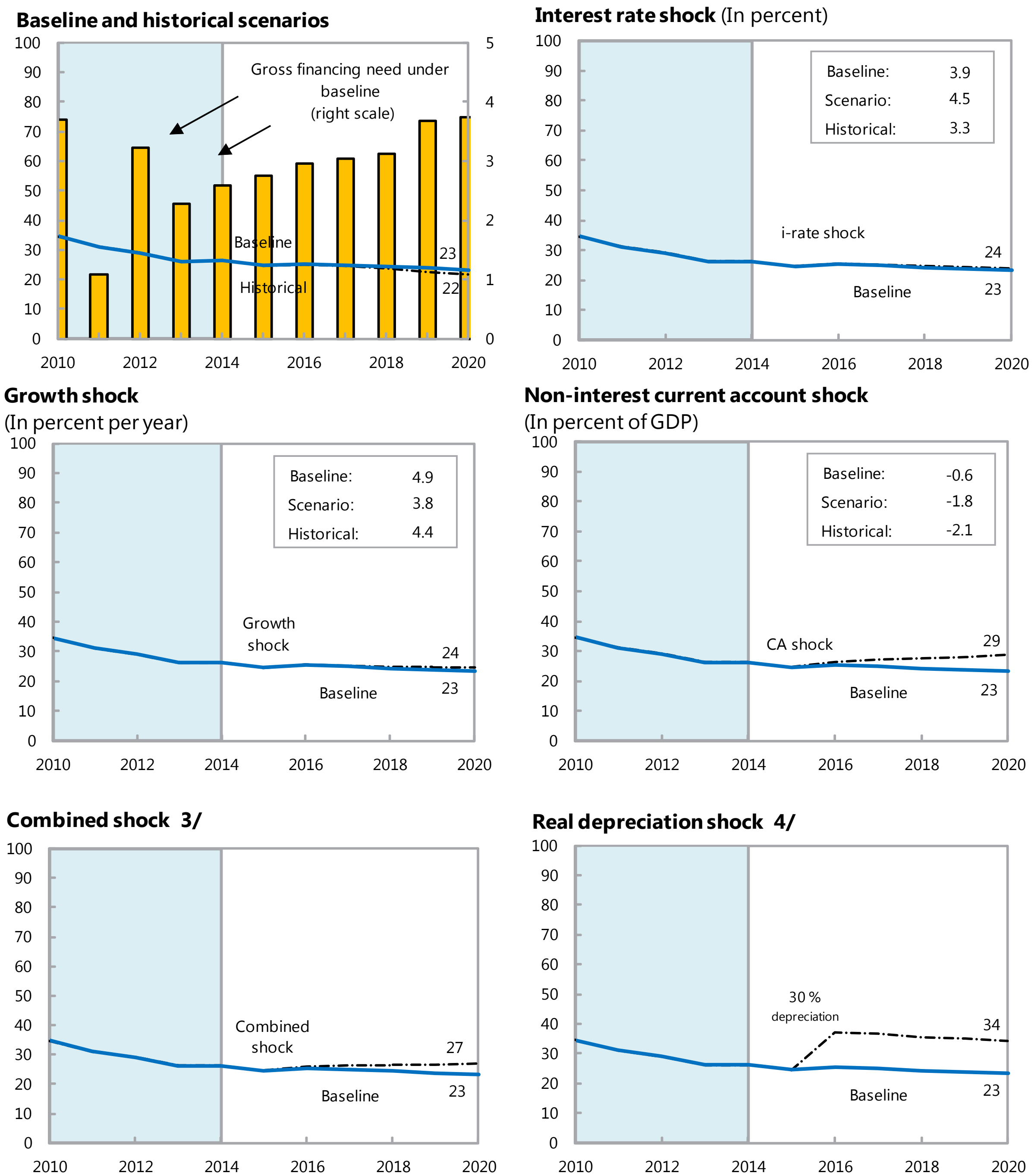
3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if 200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 17-Oct-14 through 15-Jan-15.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 5. Pakistan: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: Pakistani authorities; and IMF staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2015.

Table 2. Pakistan: External Debt Sustainability Framework, 2010-2020

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2010	2011	2012	2013	2014			2015	2016	2017	2018	2019	2020	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	34.7	31.1	29.1	26.2	26.2			**24.6**	**25.3**	**24.9**	**24.3**	**23.8**	**23.3**	**-1.5**
Change in external debt	3.8	-3.6	-2.0	-2.9	0.1			-1.6	0.6	-0.4	-0.6	-0.5	-0.4	
Identified external debt-creating flows (4+8+9)	-0.9	-7.1	0.2	-0.3	-1.2			-0.4	-0.9	-0.6	-0.5	-0.2	0.0	
Current account deficit, excluding interest payments	1.3	-0.8	1.4	0.4	0.6			0.5	0.3	0.5	0.5	0.7	1.0	
Deficit in balance of goods and services	7.4	5.8	8.4	7.3	7.7			7.4	7.1	7.2	7.2	7.3	7.6	
Exports	14.0	14.6	13.2	13.5	12.1			11.3	10.6	10.4	10.4	10.4	10.4	
Imports	21.5	20.4	21.6	20.8	19.8			18.7	17.7	17.5	17.5	17.8	18.0	
Net non-debt creating capital inflows (negative)	-1.5	-0.9	-0.3	-0.6	-0.9			-0.6	-0.9	-0.8	-0.8	-0.7	-0.9	
Automatic debt dynamics 1/	-0.7	-5.4	-0.9	-0.2	-0.9			-0.3	-0.3	-0.3	-0.2	-0.1	-0.2	
Contribution from nominal interest rate	0.9	0.7	0.7	0.6	0.6			0.7	0.8	0.8	0.9	1.0	1.0	
Contribution from real GDP growth	-0.8	-1.0	-1.1	-1.0	-1.0			-1.0	-1.1	-1.1	-1.2	-1.1	-1.1	
Contribution from price and exchange rate changes 2/	-0.9	-5.0	-0.5	0.2	-0.5			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	4.7	3.5	-2.2	-2.6	1.2			-1.2	1.5	0.2	-0.1	-0.4	-0.4	
External debt-to-exports ratio (in percent)	247.2	213.2	220.2	193.2	216.0			217.5	238.0	240.6	234.4	227.4	224.8	
Gross external financing need (in billions of US dollars) 4/	6.6	2.3	7.3	5.3	6.5			7.6	8.6	9.4	10.3	12.9	14.1	
in percent of GDP	3.7	1.1	3.2	2.3	2.6	10-Year	10-Year	2.7	3.0	3.0	3.1	3.7	3.7	
Scenario with key variables at their historical averages 5/								**24.6**	**25.1**	**24.5**	**23.7**	**22.6**	**21.6**	**-3.0**
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation							
Real GDP growth (in percent)	2.6	3.6	3.8	3.7	4.1	4.4	2.2	4.3	4.7	4.8	5.0	5.0	5.0	
GDP deflator in US dollars (change in percent)	2.9	16.9	1.5	-0.8	1.8	4.8	6.0	5.7	0.8	1.2	1.8	1.7	1.8	
Nominal external interest rate (in percent)	3.2	2.3	2.4	2.2	2.5	3.3	1.0	3.0	3.4	3.5	4.0	4.5	4.3	
Growth of exports (US dollar terms, in percent)	7.2	25.0	-4.5	6.0	-3.6	7.6	9.8	2.8	-1.0	3.5	7.0	7.6	6.1	
Growth of imports (US dollar terms, in percent)	-2.8	14.3	11.7	-0.5	2.4	12.1	17.7	3.9	0.2	5.0	6.8	8.2	8.0	
Current account balance, excluding interest payments	-1.3	0.8	-1.4	-0.4	-0.6	-2.1	2.3	-0.5	-0.3	-0.5	-0.5	-0.7	-1.0	
Net non-debt creating capital inflows	1.5	0.9	0.3	0.6	0.9	1.8	1.4	0.6	0.9	0.8	0.8	0.7	0.9	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

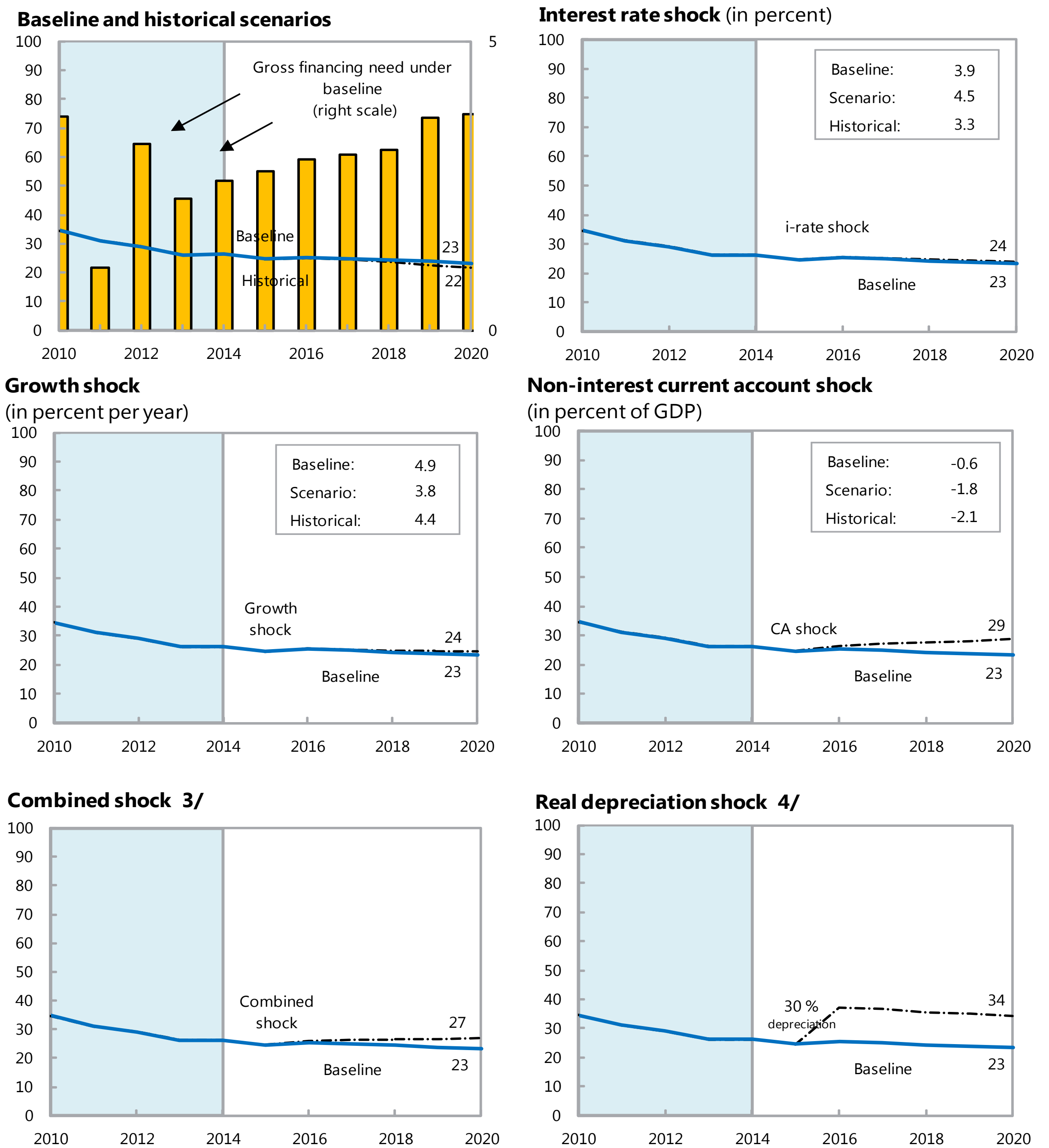
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 6. Country: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2010.

Appendix I. Letter of Intent

March 12, 2015
Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC, 20431

Dear Ms. Lagarde.

The Pakistani authorities reaffirm our commitment to our economic program supported by the International Monetary Fund (IMF). Performance for the sixth review was satisfactory. We have met all the performance criteria and continue to move forward with our ambitious structural reform agenda. While further effort is needed in some areas, we are committed to the actions described in the attached Memorandum of Understanding of Economic and Financial Policies (MEFP). There are signs of improvement in economic conditions and balance of payments pressures have been contained, reflecting improved macroeconomic policies as well as sharply lower oil prices. Although challenges remain, we believe that as structural reforms take hold, bottlenecks will ease, growth will accelerate, and vulnerabilities will recede. We are committed to firm policy implementation and to strengthening fiscal, monetary, and financial sector buffers to safeguard against risks.

Our performance on the quantitative targets and the structural reform agenda for the sixth review has been as follows (MEFP Tables 1 and 2):

Quantitative performance criteria and indicative targets. All end-December 2014 quantitative performance criteria (PCs) were observed, as well as the indicative target on transfers under the Benazir Income Support program (BISP). Although the indicative target on tax revenue was missed, we have taken action to address this shortcoming and are on track to meet the end-March 2015 indicative target.

Structural Benchmarks (SBs). The end-December 2014 SB on amendments to the relevant tax laws and submission of the Anti-Money Laundering Act was met, as were the end-February SBs on enhancing internal operations and risk management of the State Bank of Pakistan (SBP) and improving monetary policy operations. The program will continue to be monitored through quarterly reviews, prior actions, quantitative performance criteria and indicative targets, and structural benchmarks. As detailed in the MEFP, we propose four new structural benchmarks against which to measure progress under the program (MEFP, Table 2). The TMU explains how the program targets are measured.

In the attached MEFP, we set out our plans to further advance on the objectives of our macroeconomic program. In view of our performance under the program supported by the IMF, the Government of Pakistan and the SBP request modification to the end-March PCs on NIR and NDA, reflecting higher reserves accumulation by the SBP, and completion of the sixth review under the Extended Arrangement and modification of performance criteria as specified in the attached MEFP.

We believe that the policies set forth in this letter and in the letters of August 19, 2013, December 11, 2013, March 6, 2014, June 19, 2014, and December 2, 2014 are adequate to achieve the objectives of our economic program, but we stand ready to take additional measures as appropriate to ensure achievement of its objectives. As is standard under all IMF arrangements, we will consult with the IMF before modifying measures contained in this Letter or adopting new measures that would deviate from the goals of the program, and will provide the IMF with the necessary information for program monitoring. We authorize the IMF to publish this Letter of Intent and its attachments, and the related staff report.

/s/
Ishaq Dar
Minister of Finance
Pakistan

/s/
Ashraf Wathra
Governor of the State Bank of Pakistan
Pakistan

Attachment I. Memorandum of Economic and Financial Policies

Recent Economic Developments and Outlook

1. **Economic activity is steadily improving**. For program purposes, we expect that GDP growth will reach about 4.3 percent in FY 2014/15, compared to 4.1 percent in FY2013/14, though the government retains its goal of achieving growth of 5.1 percent. Risks to growth are broadly balanced, with downside risks from possible negative international and domestic shocks roughly offset by upside prospects from further oil price declines. Headline inflation eased further in January 2015 to a 3.9 percent annual rate. We now expect it to reach around 5½ percent by the end of this fiscal year (6 percent annual average), helped by a favorable global commodity price outlook and continued prudent monetary and fiscal policies.

2. **The external current account deficit was lower than projected over the past quarter**. This improvement largely reflects lower imports—in particular, oil imports—and robust workers' remittances. The capital and financial account has also displayed a strong performance in FY2014/15, largely helped by the US$1 billion Sukuk placement, but also by significant bilateral and multilateral inflows. Gross reserves reached US$10.5 billion in December 2014, up from US$8.9 billion at end-September 2014. The rupee has appreciated slightly against the dollar over the same period, but remains some 2.6 percent down so far this fiscal year. For the remainder of FY2014/15, we expect the current account to show a substantial improvement, driven by a lower import bill, despite weak export performance. External financing will continue to be supported by significant program disbursements and the government privatization program. This financing, together with the oil windfall will allow us to accelerate the improvement in reserve coverage, which is now expected to reach 3½ months of imports by end FY2014/15.

3. **The fiscal deficit in the first half of FY2014/15 was in line with the program target**. Fiscal consolidation—a critical objective of the government's economic program—remains on track, bringing the budget deficit (excluding grants) from 8.3 percent of GDP in FY2012/13 to 5.5 percent in FY2013/14 and toward the program target of 4.8 percent of GDP in FY2014/15. Revenue collection at the federal level, however, was below the indicative target, partly due to continued legal challenges against the Gas Infrastructure Development Cess (GIDC) as well as lower tax receipts from the fall in oil prices. To achieve the deficit target, we have restrained expenditures.

Economic Policies

A. Monetary and Exchange Rate Policies

Monetary and exchange rate policy remains focused on building external buffers, maintaining price stability, and improving the effectiveness of monetary policy tools.

4. **Monetary aggregates grew in line with program objectives**. The State Bank of Pakistan (SBP) continued to accumulate foreign reserves, which helped the stock of Net Foreign Assets (NFA) to recover to well above pre-program levels and has led to a welcome change in the composition of reserve money toward foreign reserves. The growth rate of broad money declined to 10.9 percent y-o-y in December 2014. Helped by a contraction in Net Domestic Assets (NDA), reserve money grew by only 5.1 percent in the previous two quarters, the lowest rate in the past decade. Private sector credit continued its healthy expansion (10.2 percent so far in FY2014/15) driven mainly by businesses, and in particular manufacturing.

5. **All end-December monetary program targets were met and the SBP is on track to meet the end-March targets**. We met the end-December NIR target by over US$800 million, due in part to more aggressive spot market purchases, which more than compensated for a shortfall in privatization revenues. The ceiling on SBP's net short position of swap/forward contracts was also met. We over-performed on the end-December NDA target by PRs 281 billion, as we took actions to bring government borrowing from the SBP down to program targets (¶23), mopped-up excess liquidity, and sterilized foreign exchange inflows.

6. **The sharp decline in oil prices has created an opportunity to accelerate our accumulation of foreign exchange reserves to build buffers and reduce external vulnerabilities**. We recognize that these developments can be effectively used to strengthen our external accounts position on a sustainable basis by accelerating reserves build-up under a market-based exchange rate. At the same time, we recognize that our trade competitiveness needs to be strengthened, due in part to movements in international financial markets. Consequently, we have agreed to increase the NIR target for end-March and set subsequent PCs accordingly.

7. **Headline and core inflation remain on a declining path helped by the recent drop in oil prices and a prudent monetary policy stance, and we have revised our forecast sharply down for the remainder of FY2014/15**. In light of these developments, we cut the policy interest rate by 100 bps in January 2015, which we believe is consistent with keeping inflation sustainably below 5½ percent. Going forward, we believe that a cautious approach to monetary policy to anchor inflation expectations is the key element to preserve our achievements. In particular, we will adhere to program NDA targets, improve the functioning of the interest rate corridor (¶8), and maintain the policy rate in a forward-looking fashion to maintain real interest rates in line with a prudent and stable inflation path. The SBP will pursue inflation goals for monetary policy and improve communications with the public about its framework.

8. **We will continue to improve monetary and exchange rate operations**. To enhance the effectiveness of monetary policy, better manage liquidity in the interbank market, and conduct open market operations, the SBP is preparing to improve its interest rate corridor by setting the policy rate between the floor and ceiling rates of the corridor. To this end, the SBP has announced its time-bound plan in February 2015 and will make the improved interest rate corridor operational by end-September 2015 (new structural benchmark). To better internalize foreign exchange demand and make it more predictable and transparent to market participants, over time we will move gradually toward implementing best international practices with the help of IMF technical assistance.

9. **Enhanced central bank independence is key for an improved monetary policy framework**. We have submitted amendments to the SBP Act to the National Assembly (NA), but the legislation is still in the relevant parliamentary committee. The amendments will strengthen the autonomy of the SBP, including full operational independence in the pursuit of price stability as the SBP's primary objective. Among other things, the amendments will establish an independent decision-making monetary policy committee to design and implement monetary policy and prohibit any form of new direct lending from the SBP to the government. We are committed to working with the IMF to ensure that the final version of the law incorporates the recommendations of the IMF safeguards assessment mission and comments provided by Fund staff. To achieve this, we intend to submit a revised draft law—incorporating IMF staff comments—to the NA by mid-March 2015(prior action). Enactment of the legislation is now expected for end-June 2015.

10. **We are taking steps to enhance SBP operations**. While awaiting enactment of the amendments to the SBP law, we have introduced additional nonlegislative measures to improve internal operations of the SBP (structural benchmark). Specifically: (i) the Investment Committee of the SBP Board has begun regular (at least four times per year) oversight and approval of the reserves management strategy and risk practices; and (ii) we have provided confirmation that in line with standard IMF safeguard procedures, the Internal Audit Department has begun to conduct reviews of the program monetary data reported to the IMF for end-December 2014, and will continue to do so within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff.

B. Fiscal Policy

11. **We are determined to keep fiscal consolidation on track and lay the foundations for sustainable and inclusive growth**. We remain committed to reducing the budget deficit (excluding grants) to 4.8 percent of GDP in FY2014/15 and to around 3½ percent of GDP by the end of the three-year program, putting the debt-to-GDP ratio on a firmly declining path. This will require further fiscal consolidation of about 1 percent of GDP in FY2015/16, with the remainder in FY2016/17. The bulk of this adjustment will come from increasing revenues by broadening the tax base and closing loopholes, while creating fiscal space to finance increases in public infrastructure investment, security and defense, education, healthcare, and targeted social assistance to improve living standards across the country and to protect the most vulnerable segments of society.

12. **We will prepare and submit to the parliament a draft FY2015/16 budget with a deficit target of no more than 4 percent of GDP (excluding grants)**. The adjustment will come from revenue enhancements and further rationalization of untargeted subsidies. Revenue mobilization will come mainly through further elimination of tax concessions and exemptions and broadening the tax base, with some contribution from improved tax administration. These measures should help us avoid the need for further increases in general GST and incomes tax rates. On the expenditure side, we will continue implementing our strategy to remove subsidies, along with steps to address the circular debt problem in the energy sector (¶29-31) and to streamline public administration, including wage and salary costs.

13. **The plunge in oil prices has created an opportunity to further reduce distortions in the energy market while allowing for some fall in consumer tariffs**. We reduced energy subsidies from 2.3 percent of GDP in FY2011/12 to 1.3 percent in FY2013/14, and have already taken steps to bring them to 0.7 percent of GDP this fiscal year. Most recently, we implemented a PRs 0.60/kWh surcharge in January 2015 to cover costs in the electricity sector. In February, we took additional steps by applying a new FY2014/15 tariff which takes into consideration a more comprehensive view of production and distribution costs and begins to reverse the accumulation of circular debt by closing the gap between electricity tariffs and the cost-recovery level (¶30).

14. **Efforts to broaden the revenue base by eliminating tax concessions, exemptions and loopholes are bearing fruit**. The tax-to-GDP ratio increased from 9.7 percent of GDP in FY2012/13 to 10½ percent in FY2013/14, and tax collection at the federal level registered a nominal increase of 14.8 percent in the first half of FY2014/15, despite the legal challenges to the GIDC and the bonus shares taxes. The elimination of Statutory Regulatory Orders (SROs) and additional tax base-broadening measures in the FY2014/15 budget have yielded better-than-expected results in most areas in the first half of the year. As part of our strategy for comprehensive tax reform, the Federal Board of Revenue (FBR) has granted no new tax concessions or exemptions through SROs, which narrow the tax base, complicate tax administration, and weaken tax compliance. To permanently prohibit the issuance of SROs to grant tax concessions or exemptions, we are preparing the necessary draft legislation by end-March 2015 at the latest (structural benchmark) and we expect parliamentary approval of the legislation on or before end-December 2015. Looking forward, our plan for eliminating all designated SROs granting tax concessions and exemptions remains on track, with an expected yield of 1-1½ percent of GDP over the period of three years. We will update and improve the content of the Tax Expenditure Annex to be submitted with the FY2015/16 budget documents, so as to reflect and make transparent the impact of this plan. These steps will help turn the GST into a full-fledged integrated modern indirect system of taxation with few exemptions, along with an integrated income tax, by FY2016/17.

15. **However, despite gains from tax base broadening, revenue performance has been less than expected**. This mainly reflects two factors. First, court challenges to tax measures continue to hamper our revenue efforts. Legal challenges to the GIDC have not yet been resolved, limiting collections. Of an expected annual yield of 0.5 percent of GDP (plus another 0.1 percent of GDP in GST on gas), the GIDC has produced only about one-tenth of that so far this fiscal year. In addition,

a court challenge has blocked a 10 percent tax on the value of bonus shares, which was estimated to bring in 0.1 percent of GDP. Second, the drop in crude oil prices has produced a shortfall in GST revenue from petroleum products, which fell by 19 percent in the second quarter of FY2014/15. As a result, we missed the second-quarter indicative target on revenue collection at the federal level by PRs 22 billion (or about 0.08 percent of GDP), and in the absence of corrective measures this would grow in the coming months.

16. **We have taken steps to address the revenue shortfall**. To achieve the deficit target, we have restrained expenditures and introduced additional revenue measures at the federal level, including by: (i) raising the General Sales Tax (GST) rate on petroleum products (excluding furnace oil) from 17 to 27 percent in two stages; (ii) levying regulatory duties on steel products; (iii) introducing a regulatory duty on mobile phones; (iv) levying a regulatory duty on furnace oil; (v) increasing the withholding tax on nonfiler contracts, services, and commercial importers; (vi) levying a regulatory duty on luxury items; (vii) levying regulatory duty on metal scrap; and (viii) reduce electricity subsidies by 0.1 percent of GDP. Together, these steps are expected to raise 0.35 percent of GDP (prior action).

17. **We are committed to tackling the backlog on GST refund claims**. We have managed to lower the number of outstanding refund claims by some 5 percent and have increased monthly refund payments by 15 percent in the first half of FY2014/15. Although the stock of GST refund claims increased in July-November largely due to old claims being logged into the system, in December we reversed the upward trend and will continue to lower the stock in the coming months. Our new IT system for processing GST refund claims (computerized risk-based evaluation of sales tax or CREST) is helping to identify invoice discrepancies at different stages and to put an effective check on many fake invoices and inadmissible refund claims. The CREST verification system has allowed us to reject false claims worth about PRs 10 billion in the first half of FY2014/15. To deal with the refund backlog, the FBR is carrying out an exercise to process deferred claims by end-March 2015. The FBR will prepare a plan to address the issue of unpaid GST refund claims by end-June 2015. Looking forward, to process new GST refund claims in a timely manner, the FBR will adopt an automated system of pre-verification instead of the current system of post-verification by end-June 2015.

18. **We are continuing our efforts to improve tax compliance and enforcement**. We have built a monitoring system to track progress and set quarterly objectives on tax policy and administration initiatives (as described in the TMU). We issued 154,922 first notices by end-2014, over the target of 150,000, to bring more potential taxpayers into the revenue base. We have also initiated a GST collection scheme for over 25,000 large retailers and over 1.3 million small retailers as new potential GST payers. To enhance our tax compliance efforts, we will continue to improve the FBR's IT infrastructure and expand its access to taxpayer information from multiple sources including financial and real estate transactions, motor vehicle procurement, and international travel. We have announced the merger of the NTN system covering 3.6 million individuals with the CNIC database that covers about 150 million people by end-September 2015 (new structural benchmark). We will focus our enforcement efforts on nonfilers who have the potential to contribute at least the average

tax paid by currently registered taxpayers and especially high wealth individuals, including elected representatives, key public figures, sports persons, and performing artists. The FBR's Directorate General of Intelligence and Investigation (DGII) is working on the high net worth individuals identified through field surveys and information gathered from financial and property records. For those who are already in the tax net, this information is passed on to the relevant tax office for corroboration with the wealth statement filed by the cessee. For those who are outside the tax net, the DGII pursues their cases. We will also streamline the online filing scheme (which will facilitate registration and filing of personal income tax returns by simplifying the tax return form) and expand the coverage of tax audits to 7.5 percent of filed tax returns.

19. **We have made significant progress in implementing tax administration reforms, which will gradually deliver further improvements in revenue collection**. The FBR is moving forward with a strategy to address structural flaws in the taxation system, improve tax administration, and induce behavioral change among taxpayers. In particular:

a. We are in the process of awarding the contract for electronic volume tracking of production to improve GST collection. Working with the PPRA (the public procurement authority), we aim to award this contract to by end-March 2015.

b. After launching the risk-based e-registration system for the GST in October 2014, we are in the process of integrating our IT systems to better manage new registrations and subsequent processes.

c. We have revised valuation rulings in customs duties to mitigate wrong declarations and underinvoicing. Using data on international prices, we are now able to identify most of the risk-prone transactions. At the same time, we are developing a national valuation database, which will allow us to further improve the accuracy of customs duty assessment. Moreover, we have started the electronic data interchange (EDI) connectivity to streamline trade with Afghanistan and we are in discussions with China to develop a similar EDI connectivity.

d. We have already appointed an IT member to the FBR and constituted a project team to lead the development of an integrated end-to-end automated system for the GST and income tax.

20. **Provincial governments remain crucial in the fiscal reform process, especially by improving revenue collection at the provincial level**. With a series of constitutional amendments, Pakistan has adopted a more decentralized federal system of government. The most recent National Finance Commission (NFC) award granted 57.5 percent of most revenues to the provinces, along with devolution of spending responsibilities and sales taxation authority in services in addition to the existing taxation authority in agriculture and property. Looking forward to the new round of NFC negotiations, the federal government will seek an agreement to balance devolution of revenue and expenditure responsibilities in a way that is consistent with the objective of macroeconomic stability. In preparation for these negotiations, we are receiving technical assistance from our international

partners to reflect best practices by undertaking studies with the goal of achieving sustainable federal-provincial fiscal relations.

21. **We continue our support to the poor and most vulnerable segments of the population through the Benazir Income Support Program (BISP)**. To protect the vulnerable segments of society from inflation, and the impact of fiscal adjustment, we have increased the stipends paid to women account holders in the poorest families from PRs 3,600 to PRs 4,500 per quarter since July 2014. We now expect to expand the coverage of the program to 5.0 million by end-June 2015 (0.3 million lower than previously anticipated). As of end-December 2014, we have reached 4.8 million beneficiaries and have achieved the indicative targets for transfer payments for both end-September and end-December 2014. We will sign new banking contracts by June 2015 to phase in more effective payment cards. To ensure timely payments to beneficiaries during the transition, we have extended the contracts with the commercial banks that are currently making e-payments on behalf of the BISP until December 2015. In partnership with the provincial governments, we have also made significant progress in the rollout of the education-conditional cash transfers. As of end-January 2015, we have expanded the program from five pilot districts to 32 districts in all provinces. We are also in the process of resolving administrative and decision-making issues so as to ensure its smooth functioning.

C. Fiscal Financing

22. **We are committed to taking measures to contain budget financing from the SBP within the program ceiling**. We over-performed on the end-December ceiling on government borrowing from the SBP by PRs 86 billion. We achieved this by: (i) successfully attracting US$1 billion through an international Sukuk issue in late-November; (ii) issuing ample T bills and Pakistan Investment Bonds (about PRs 363 billion); and (iii) the outright selling of SBP holdings of government securities on the secondary market (PRs 90 billion), which compensated for deferment of the sale of a stake in Oil and Gas Development Company Limited (OGDCL).

23. **Enhancing the quality and effectiveness of public debt management continues to be a priority**. In September 2015, we expect to publish the updated Medium Term Debt Strategy (MTDS) covering the period FY2014/15–FY2018/19. Efforts continue to diversify financing from both domestic and external sources. We have already lengthened the maturity profile of domestic debt and improved the balance between domestic and external debt by placing sovereign bonds for US$2 billion and issuing Sukuk securities for US$1 billion in international debt markets. We will continue to strengthen the Debt Policy Coordination Office (DPCO), by revamping its structure, increasing staffing capacity, and identifying procedures to bring our debt management up to best international practices. Specifically: (i) we will continue to provide Fund staff with a detailed quarterly financing plan for the coming 12 months and publish our rolling quarterly issuance program for domestic public securities every month (including local Sukuk issue); (ii) we are taking steps to strengthen risk management and strategy functions by reorganizing the DPCO as a middle office responsible for updating the MTDS and monitoring its implementation. We will identify the infrastructure needs of the credit risk management unit of the DPCO by end-March 2015, market

risk management functions by end-December 2015, and operational risk management functions by end-December 2016; (iii) based on the September 2014 skills-gap analysis, we will be hiring additional staff and/or training staff with the help of international partners; and (iv) we will take steps to strengthen front office management of debt issuance both in domestic and external markets by arranging a formal linkage with the DPCO, executing the borrowing auctions with the SBP as the agent, and strengthening the primary dealership system. We will also draft the required rules under the Fiscal Responsibility and Debt Limitation Act 2005 by end-September 2015. Finally, we have also requested technical assistance from the Fund to strengthen our local sukuk operations. These actions should lead to savings in, and more effective decision-making for, government borrowing.

D. Financial Sector

24. **The banking sector of Pakistan remains sound, with robust earnings and high solvency ratios**. The pre-tax profit of the system surged by 49 percent (y-o-y) through December, mainly attributed to increased net interest income, lower provision charges, and higher noninterest income. As of end-December 2014, asset quality has slightly improved with a decline in the nonperforming loan (NPL) ratio to 12.3 percent, and the net NPLs to net loans ratio falling to 2.7 percent. The capital adequacy ratio (CAR) increased noticeably to 17.1 percent due to accumulation of profits and fresh equity injection by some banks (including previously CAR noncompliant banks). To further improve the market discipline and enhance the assessment of the soundness of the financial sector, the SBP has evaluated and identified the "encouraged" set of FSIs. The SBP is expected to engage with the IMF for dissemination of some additional FSIs for transparency purposes by mid-2015.

25. **The SBP is making progress in bolstering banks below the minimum capital requirement.** The number of CAR noncompliant banks has fallen from three to two due to capital injections. The combined CAR shortfall for the two noncompliant private banks has decreased by PRs 3.3 billion over the quarter to PRs 7.96 billion (less than 0.03 percent of GDP) as of end-December 2014. The risk to the banking system seems to be negligible, as they encompass only 1.39 percent of banking system assets. Of the two remaining banks, one increased its CAR to 9.41 percent via an injection of advance share deposit money in December 2014. The bank is expected to complete a rights issue by March 2015, which will enable it to become CAR-compliant. The Federal Government, at the request of the SBP, has placed the second bank under a moratorium for a period of six months, effective November 14, 2014. A scheme for reconstruction or amalgamation is under consideration. Four banks have expressed interest in acquiring the bank and are currently conducting due diligence.

26. **We remain dedicated to protecting financial stability by reinforcing the regulatory and supervisory framework**. Most importantly:

a. The draft Securities Bill is being finalized after incorporating proposed amendments from the IMF. It is now expected that the Parliament will enact the Bill by January 2016 (modified structural benchmark).

b. The revised Securities and Exchange Commission of Pakistan (SECP) Act to enhance the regulatory power of the SECP will be discussed with the IMF and will be considered by the Council of Common Interest (CCI) before being submitted to Parliament for enactment by April 2016.

c. The Futures Trading Bill is being finalized and will be placed before Parliament by end-June 2015.

d. A working group of the SBP-SECP joint task force is finalizing the guidelines on an early warning system for the effective monitoring of financial conglomerates. These guidelines once finalized and integrated into the existing framework, will facilitate supervision of financial conglomerates. The Technical Assistance on consolidated supervision from the IMF has started. The two sides are coordinating for early completion of the TA that will assist the SBP in establishing a framework for consolidated supervision of banking groups.

27. **Consultation with major stakeholders on a deposit insurance scheme and a bankruptcy law is underway**. The draft Deposit Protection Fund (DPF) Act will be finalized and submitted to parliament by end-March 2015, after completion of the ongoing review with the IMF. We now expect enactment of the law by end-September 2015 (modified structural benchmark). In the meantime, the SBP will undertake preparatory work to establish the corporate infrastructure of the DPF and will request IMF technical assistance to help in this process. The DPF will become operational by January 2016. The draft Corporate Restructuring Companies (CRC) Act will be finalized by end-February 2015. It will be of pivotal importance in cleaning up banks' balance sheets and allowing them to focus on their core areas of operation. After reviewing the company rehabilitation law of different jurisdictions, the SECP has also prepared a concept note for developing the Corporate Rehabilitation Act, which will be shared with stakeholders by end-June 2015.

28. **We are on track to include tax crimes in the Schedule of Offenses of the 2010 Anti-Money Laundering Act (AMLA)** that will enable the use of anti-money laundering (AML) tools to combat tax evasion. The FBR has identified a list of serious tax offenses to be included as predicate offences to Money Laundering that do not necessitate amending the tax laws, and we have submitted the draft amendments to AMLA before the parliament to include serious tax crimes in the Schedule of Offenses, meeting the end-December structural benchmark. Going forward, we are committed to adopting the amendments to the AMLA that will include the serious tax crimes from the relevant tax laws (as defined in the TMU) in line with international standards by end-September 2015 (new structural benchmark).

Energy Sector Reforms

29. **The National Energy Policy identified priority steps to anchor the reform agenda for the next three–five years**. We are implementing our time-bound strategy to tackle price distortions, insufficient collections, costly and poorly targeted subsidies, governance and regulatory deficiencies, and low efficiency in energy supply and distribution with the support of our international partners.

30. **Price Adjustments**.

a. **Previous adjustments**. The National Electric Power Regulatory Authority (NEPRA) finalized the determination of tariffs for FY2013/14 in June, but last-minute difficulties derailed the implementation of the new tariffs by July 1, 2014 as had been agreed at the time of the Third review. To remedy this problem, we levied a surcharge of PRs 0.30/kWh effective from October 1, 2014 and PRs 0.60/kWh effective from January 1, 2015, taking advantage of lower world oil prices to do so while allowing consumer prices to fall.

b. **New adjustments**. Going forward, we are taking advantage of lower world oil prices to bring additional costs into the tariff base set by NEPRA to strengthen cost recovery in the sector while allowing consumer prices to continue to fall. To that end, NEPRA will determine the FY2014/15 tariffs by February 2015. We will also ensure that technical loss diagnostic studies for all DISCOs will be finalized by June 2015 so that more realistic loss rates can be considered by NEPRA in its FY2015/16 tariff determination

c. **Subsidies**. We are committed to gradually reducing the effect that untargeted subsidies have on our budget while continuing to protect the most vulnerable consumers. To that end, we will notify the FY2014/15 tariffs by end-March 2015 consistent with our objective of reducing electricity subsidies further to 0.3 percent of GDP for FY2015/16 and of addressing the circular debt.

31. **Arrears (Circular Debt)**. The technical and financial audit of the system which was finalized in early-May 2014 identified the stock and flow of payables at all levels of the energy sector (including Power Sector Holding Company Limited, PHCL). We have developed a monitoring mechanism to track the stock and flow of payables (as defined in the TMU). There are two main components of this circular debt:

a. The payables in the power sector, which climbed to PRs 298 billion at end-December 2014, of which around PRs 80 billion constitute current payables. The remainder comprises: (i) a residual leftover from payables clearance of June and July 2013; (ii) A disputed amount with the Independent Power Producers (IPPs); (iii) Distribution Companies (DISCOs) nonrecovery and penalties levied on past nonpayment (as defined in the TMU); and (iv) transmission and distribution losses that are not recognized by the regulator.

b. The stock of past arrears included at the PHCL in the syndicated term credit finance (STCF) facility increased to PRs 335 billion by end-January 2015. We have levied a surcharge (as defined in the TMU) to service the interest on the facility.

32. **Building on this audit, we are moving forward with the roadmap to limit the accumulation of payables arrears and to gradually reduce the stock**. This plan includes steps to improve collections, reduce operating costs and losses, and to reduce price distortions in tariff structure.

a. We will continue to reduce losses and improve collections through capital expenditures and revenue-based load management. Overall losses fell by 0.3 percentage points in the first quarter of FY2014/15; however, they rebounded in the second quarter (to 18.9 percent). On the collections side, revenue from private consumers and agriculture improved, but collections from public sector went down due to payments delays particularly from one of the provincial government. To address increased losses in some DISCOs, the chief executives of the poorly performing ones have been replaced and we are working with the provincial government to address its payment problem. We will work on improving the average performance of the sector further in FY2014/15.

b. Taking advantage of the room created due to falling oil prices. We issued policy guidelines for incorporating the out of system costs and actual system technical losses into the FY2014/15 tariff. This has resulted in arresting a major portion of the build-up of the circular debt and improved cash-flow of the system.

33. **Monitoring and enforcement**. To tackle losses, raise payment compliance, and improve energy efficiency and service delivery, we have already signed performance contracts with the boards of all nine DISCOs. We have begun monitoring the performance indicators specified in the contracts and in cases of failure to comply we will invoke remedial measures for management and Boards as specified in the Companies' Ordinance. The amendments to Penal Code 1860 and the Code of Criminal Procedures 1898 have been promulgated through Presidential ordinance. Currently, the Bill stands at the Senate Committee after the clearance of the National Assembly. We expect it to be enacted by end-March, 2015. In parallel, we drafted the new Electricity Act to modernize governance of the sector and have circulated it to provinces for comments. The draft Act will be finalized and submitted to the CCI by end-February 2015. We will work with the Ministry of Law on creating an effective system for handling cases related to electricity theft that can be effective by June 2015.

34. **Demand Side Management**. To improve resource allocation and energy efficiency, we will use pricing (¶30) and other market-based instruments. In this regard, we have completed the consultative process with stakeholders on the draft Pakistan Energy Efficiency and Conservation Act. In August 2014, the CCI approved the bill and it is now in the National Assembly. We expect it to be enacted in early 2016. The act will include equipment performance standards, and would cover key electrical and gas equipment and appliances which are not yet covered. In parallel, we are also preparing the necessary implementing regulations.

35. **Supply Side Management**. We continue to prioritize the use of gas and coal rather than fuel oil in electricity generation and remain committed to a transition to market-based allocation of natural gas in the medium-term. To further improve supply, we will continue to rehabilitate generation plants, while upgrading electricity transmission and distribution facilities to reduce technical losses. In addition, we have signed performance contracts with two state-owned generation companies which are run on furnace oil to reduce their losses. We continue with the development of hydropower projects, with the recent approval of a World Bank loan to begin construction of the Dasu project, and held a USAID-funded information conference on the Daimer-Bhasha project in October 2014. We will promote policies for private investment for power generation through both the entry of new players as well as expanding existing capacity of those IPPs systematically adhering to energy mix targets and least-cost generation plans. The expansions are expected to add an additional 2,000 MW in generation capacity in 2015 and 2016.

36. **Governance, Regulatory, and Transparency Improvements**. Improving energy sector governance and transparency, and strengthening the regulatory framework are critical for delivering improved service and for attracting needed private sector investment. To begin addressing administrative and technical constraints, we have appointed a new Chairman and Board member with financial skills to NEPRA. NEPRA has begun preparations for a multi-year tariff framework. To facilitate the transition, we established three-year investment plans for all DISCOs and submitted the plans to NEPRA. The first phase of the determination and notification of multi-year tariffs will begin for the first three DISCOs by end-September 2015, with the remaining ones done annually on a rolling basis. We have set-up the Central Power Purchasing Agency Guarantee (CPPAG) by separating it from the National Transmission and Despatch Company (NTDC) and have amended the Articles of Association. To make CPPAG operational, we issued the standard operating procedures for payments and settlements and key CPPAG staff will be in place by end-February 2015. We will finalize all agency agreements by April 2015, and are committed to ensuring that CPPAG can settle the first round of payments by June 2015.

37. **Energy public sector enterprise (PSE) reform**. We have already transferred governance of DISCOs, three GENCOs, and the NTDC to new boards of directors and management. We are committed to building the institutional capacity of the Water and Power Development Authority (WAPDA), and we have begun to strengthen WAPDA's financial capacity by allowing the tariff to incorporate capital investment plans. We are also committed to ensuring timely payments by CPPAG for all power purchased from WAPDA Hydel. We have included several DISCOs in our privatization plans with the goal of privatizing them in two–three years (¶41). We are also committed to introducing competitive pricing and direct contracting between power producers and wholesale customers in the power sector.

Oil and Gas Sector

- **Supply**. To help tackle gas shortages, we are on track to receive the first Liquefied Natural Gas (LNG) imports by April 2015. We are committed to a full pass-through of the cost of imported LNG to the end-user purchase price (including Compressed Natural Gas) as it comes online and we are currently working out the contractual agreements with all relevant parties. We have issued new exploration and production concessions for domestic gas resources and continue to limit further expansion of the gas distribution networks for domestic consumption.

- **Pricing**. In December 2013 we drew up a gas price rationalization plan to encourage new investment, promote efficiency in gas use, assure that there will continue to be no fiscal cost from the gas sector, and eliminate distortions from the existing gas price structure. We remain committed to the plan and will step up action on it in the future:

  - Under the Petroleum Exploration and Production Policy 2012 (2012 Policy), we are incentivizing producers to enhance production from existing fields as well as to initiate new exploratory efforts, with price increases ranging from 2.8–3 U.S. dollars per MMBTU to 6–10 U.S. dollars per MMBTU. To this end, we are ensuring that existing concessions can be submitted for conversion to the 2012 Policy starting at the end of February 2015 with support from international partners. We have also awarded 45 concession agreements for the exploration of new blocks in FY2013/14 and are expecting to award an additional 10–15 exploration concessions by the end-June 2015.

  - The recent difficulties and oil-indexed decline in gas prices delayed the first gas price notification of FY2014/15 (due in July). The loss in cost recovery incurred by gas companies due to the delay will be fully recuperated in the new tariff which we will notify and implement by July 2015. We will also make any necessary adjustments to notified prices as needed when imported gas comes online, so that the cost of this gas will be fully reflected in the base tariff on a semiannual basis.

  - To better allocate gas consumption, we have adjusted the weighted average consumer prices at end-December 2013 through the application of the GIDC on industry and captive power plants. The GIDC was further adjusted with the FY 2014/15 budget to generate 0.55 percent of GDP in revenues. However, due to pending court cases, the recovery of the GIDC has been suspended despite the Presidential Ordinance which was issued following the previous Supreme Court decision. We are actively pursuing the ongoing litigation for an early decision to ensure full recovery of the GIDC. However, we have taken measures to recover part of the GIDC proceeds focusing on areas where large collecting agents have already collected the GIDC in their price (prior action).

- We are also evaluating the downstream gas business with the objective of reducing inefficiencies in the transmission and distribution segments. In this respect, we will hire consultants by end-June 2015 to conduct the study on the restructuring, unbundling, and eventual privatization of the two gas utility companies. This study will formulate recommendations based on international best practices to segregate the gas network into one transmission and multiple distribution companies, with independent profit and cost centers to ensure maximum efficiency. A mechanism will also be developed for determining separate transmission and distribution tariffs.

➢ **Governance**. We are committed to supporting the governance of the oil and gas market and to keeping the public informed about our strategy for the sector. To that end:

- We have established performance monitoring units in the Ministry of Water and Power and Ministry of Petroleum and Natural Resources which report progress quarterly to the Economic Coordination Council (ECC). We are committed to updating the public on reform progress and are therefore posting quarterly monitoring reports on the websites of the concerned ministries. To support the efforts of the regulator, we are committed to filling the vacancies on the Board of the Oil and Gas Regulatory Authority (OGRA) by end-March 2015 to ensure a decision making quorum on the Board.

- We have been enhancing the capacity of the Ministry of Petroleum and Natural Resources to fully implement the 2012 Policy, streamline approval processes, and complete the conversion to the 2012 Policy for those Petroleum Concession holders who wish to do so. We will further encourage bilateral contracting between producers and consumers and have improved rules for third party access to the gas transmission system.

- We are also pursuing companies to reduce losses by benchmarking international standards, through investment measures, managerial and administrative improvements, and through building the capacity of the gas distribution companies. The current level of unaccounted for gas losses (UFG) is on average 11.4 percent due to commercial and technical losses. The gas companies will submit loss reduction plans to the Ministry of Petroleum and Natural Resources by end-April 2015 and are working with the World Bank on the Natural Gas Efficiency Project (NGEP) for which activities are expected to start in mid-2015.

- Finally, in January 2014, the President promulgated the Gas (Theft Control and Recovery) Ordinance 2014, which was sent to Parliament. The Senate has approved the Ordinance and it is now under consideration by the National Assembly. We expect enactment by end-March 2015.

Improving the Business Climate, Liberalizing Trade, and Reforming Public Enterprises

We are working to improve the business climate, the trade regime, and Public Sector Enterprises (PSEs) to increase foreign and domestic private investment and boost economic growth.

38. **Business Climate**. Private investment and growth are hampered by impediments in the legal framework for creditors' rights and contract enforcement, barriers to new business start-ups, complex legal, taxation and border trade requirements, and impaired access to finance. In consultation with international partners, we finalized a time-bound detailed implementation plan in October 2014 that identified legislative and administrative actions, institutional roles and responsibilities, and resource requirements of the reform program. Our focus is on six indicators—construction permits, paying taxes, enforcing contracts, starting businesses, trading across borders, and getting credit. In parallel, we are building consensus and ownership for business climate reforms by provincial authorities with a special focus on property registration and contract enforcement.

- ***New Firms***. The SECP, FBR, and Employees' Old Age Benefits Institution (EOBI) have joined to launch a virtual One-Stop-Shop (OSS) for business registration in December 2014 and are expected to set up a physical OSS in Lahore in March 2015. By streamlining overlapping procedures and establishing database sharing and a common portal for registering businesses, the OSS will facilitate new firm creation.

- ***Contract enforcement***. We completed in March 2014 a study to identify necessary changes to the bankruptcy regime that would support the rehabilitation of weak but viable companies. Based on the findings of the study, we are reforming the bankruptcy framework through introducing two far reaching legislative measures: (i) the Corporate Rehabilitation Act, which will provide mechanism for reorganizing and rehabilitation of distressed companies; and (ii) the Corporate Restructuring Companies Act, which envisages setting up private Corporate Restructuring Companies to take over assets of bankrupt companies (¶27). In addition, we have established Alternative Dispute Resolution (ADR) Mechanisms in Karachi and Lahore. This ADR mechanism will be extended to Islamabad and Rawalpindi by end-June 2015 and we are beginning work to expand to other provincial capitals, (i.e., Peshawar and Quetta).

- ***Paying Taxes***. With the help of our international partners, we are conducting a review to reduce the number of existing processes and forms for sales and income tax by end-March 2015 (structural benchmark). Subsequently, we will work on an integrated end-to-end IT solution (IRIS) to serve all streamlined business taxpayer-related processes (registration, declaration, audit, recovery, refunds, and appeals).

39. ***Access to credit***. Access to finance for poor, women, and marginalized segments of society including micro, small and rural enterprises remains very limited owing to both demand and supply-side constraints. The SBP, with the help of World Bank experts, has developed a comprehensive National Financial Inclusion Strategy (NFIS) to implement financial sector reforms to meet their

financing needs. We are preparing the draft strategy document, which will identify policy reforms and interventions to enhance market information, infrastructure, and financial capability of consumers. It has been shared with all stakeholders for their input and buy-in. The multi-stakeholder National Financial Inclusion Council chaired by the Minister of Finance will launch the NFIS by end-April 2015. As a critical component of the NFIS to improve the credit information system to help banks extend credit to broader sections of society, the Credit Bureau Act was submitted to parliament in February 2014 and we expect it to be enacted by November 2015 to ensure that credit information sharing will protect the privacy rights of individuals (new structural benchmark).

40. ***Trade Policy***. *Tr*ade policy reforms will increase consumer welfare and stimulate growth as a result of increased competition. Simplifying tariff rates, phasing out SROs (¶11) that establish special rates and/or nontariff trade barriers in some 4,000 product areas, and improving trade relations should deliver the much needed competitive environment.

- ***Tariff simplification***. We are finalizing the design of the new system to simplify the tariff structure to move over three years to a simple, transparent framework, with four slabs between 1 and 25 percent rates with fewer exceptions.[1] For FY2014/15, we consolidated from seven tariff slabs to six. All items at 30 percent have been moved to a new maximum rate of 25 percent rate. The phase-in of the revised tariff rates and phase-out of trade SROs began in July 2014 (¶11). We are on track to further reduce tariff slabs to five and the next round of trade-related SRO elimination with the FY2015/16 budget cycle. Implementation of the new tariff structure would be completed by July 2017.

- ***Improved trade relations***. We are implementing a strategy to take full advantage of trade preferences available from the European Union who have extended the Generalized System of Preferences plus benefits from January 1, 2014 on a broad range of Pakistan's exports. We remain committed to promoting trade with regional countries, especially under various regional trade arrangements.

41. **Public Sector Enterprises (PSEs)**. We are working to reform or privatize PSEs, focusing on limiting poor performance and improving public sector resource allocation. The Cabinet Committee on Privatization initially approved a list of 31 PSEs for action and subsequently added another 7 PSEs to the list. We have developed a plan to sequence the capital market and pre-privatization restructuring for these firms. The privatization program is aimed at offering and/or marketing one or two transactions in each quarter during the upcoming year.

[1] In addition, we maintain our current Free and Preferential Trade Agreements with some countries.

- ***Capital Market Transactions Roadmap***. We have identified eleven companies, (listed in the TMU), in the oil and gas, banking and insurance, and power sectors for block sales and primary or secondary public offerings. We successfully sold minority stakes in United Bank Limited (UBL) and Pakistan Petroleum Limited (PPL) in June 2014. While the share offer for OGDCL planned for November was postponed due to unfavorable market conditions, we sold a minority stake in Allied Bank Limited (ABL) in December 2014. We hired financial advisors for Habib Bank Limited (HBL), in December 2014 to sell market minority stakes by end-March 2015.

- ***Strategic Private Sector Participation***. We have identified 24 companies (listed in the TMU) for strategic partnerships, which will act as a catalyst in unlocking their potential through their managerial and investment participation, and can also increase the value of Government's residual shareholding. We will make efforts to balance the objectives of sale proceeds while adequately addressing labor market issues and social implications.

  - **DISCOs**. We appointed financial advisors for share sales of Faisalabad Electric Supply Company (FESCO) in July 2014 and plan to complete the transaction by end-July 2015. For Islamabad Electric Supply Company (IESCO) and Lahore Electric Supply Company (LESCO), we have hired financial advisors in January 2015 for expected completion of transactions by end-December 2015. We have advertised for financial advisors for Hyderabad, Peshawar, and Quetta Electric Supply Companies (HESCO, PESCO, and QESCO) and will hire them by end-March 2015, with a view towards private participation in early 2016.

  - **Other companies**. We will finalize the sale of Heavy Electric Complex (HEC) by March 2015. We plan to finalize the offer for National Power Construction Co. (NPCC) by end-May 2015. We appointed financial advisors for Northern Power Generation Company Limited (NPGCL) and expect to complete the transaction by end-October 2015. We have hired a financial advisor for Convention Center in January 2015 for a transaction by August 2015. Plans are being developed for the remaining companies on the list.

- ***Restructuring***. We have developed restructuring plans for Pakistan Steel Mills (PSM) and Pakistan Railways (PR), and our financial advisors are finalizing a plan for Pakistan International Airlines (PIA). Specifically,

  - **Pakistan International Airlines**. We have appointed financial advisors in July 2014 (structural benchmark) to seek potential options for restructuring and strategic private sector participation in the core airline business by end-December 2015 (structural benchmark). The diligence process will be completed by end-March 2015. Plans for private participation will be developed thereafter.

- **Pakistan Steel Mills**. We have appointed a professional board and a new chief executive officer and approved a comprehensive restructuring plan to prepare for potential strategic private sector participation in the company. Operational efficiency has begun to improve and capacity utilization has already climbed from 18 to 40 percent. In January 2015, we advertised for appointment of financial advisors, however, it was disqualified during the evaluation process. We have re-advertised on February 15, 2015 and expect to complete the appointment of financial advisors by end March 2015 so that the due diligence process can be initiated.

- **Pakistan Railways**. Aging and shortage of equipment, overstaffing, and large debts continue to weigh on railway operations. Nevertheless, we have improved revenue in FY 2013/14 by 32 percent through rationalization of tariffs and expenditures and improved occupancy rates. We further increased revenues by over 30 percent in the first half of FY 2014/15. In April 2014, we finalized a needs analysis and developed a comprehensive restructuring plan, which includes improvements in business processes and the institutional framework, financial stability, and service delivery. In the short-term we are focusing on improvements in freight transportation through creation of a freight company, and adding more locomotives and wagons, which is projected to double revenues from freight operations before the end of the current fiscal year. Appointment of the Railway Board will be completed by end-February 2015.

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets FY2013/14–FY2015/16 1/

(In billions of rupees, at program exchange rates, unless otherwise specified)

	FY2012/13	FY2013/14	FY2014/15							FY2015/16	
	end-June	end-June	end-September	end-December			end-March		end-June	end-September	end-December
							Current	Revised	proposed		
	Actual		Fourth and Fifth Review	Sixth Review			Program			Projection	
		Actual	Actual	Target	Adjusted target	Actual					
Performance Criteria											
Floor on net international reserves of the SBP (millions of U.S. dollars)	-2,437	2,678	2,630	3,500	2,683	3,500	4,500	5,000	6,750	8,000	8,500
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,402	2,355	2,316	2,436	2,505	2,224	2,365	2,340	2,270	2,210	2,150
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	2,012	1,402	337	722	730	672	1,087	1,087	1,387	354	665
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	2,255	1,725	1,675	1,775	1,775	1,760	1,775	1,775	1,700	1,550	1,550
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3/	2,168	2,328	2,289	2,000	2,000	1,914	1,905	1,905	1,865	1,800	1,750
Continuous Performance Criterion											
Accumulation of external public payment arrears by the general government (continuous)	0	0	0	0	0	0	0	0	0	0	0
Indicative Targets											
Cumulative floor on Targeted Cash Transfers Spending (BISP) (billions of Pakistani rupees)	54	66	21	36	36	44	69	69	95	22	45
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	1,936	2,266	539	1,195	1,195	1,174	1,883	1,846	2,691	625	1,416

Sources: Pakistani authorities; and Fund staff estimates.

1/ All items as defined in the TMU. Fiscal year runs from July 1 to June 30.

2/ Excluding grants, FY2012/13 overall budget deficit is a stock.

3/ FY 2012/13, total stock of government debt as of June 30, 2013.

Table 2. Pakistan: Program Modalities and Structural Benchmarks

Item	Measure	Time Frame (by End of Period)		Status	Macroeconomic rationale
		Current	Rescheduled		
Prior Actions					
1	Revise the draft SBP law in the NA committee incorporating the recommendations of the IMF safeguards assessment mission and comments provided by Fund staff and submit the revised draft to the full assembly	mid-March 2015			
2	Raise the GST rate on petroleum products from 17 to 27 percent, introduce additional fiscal measures, including 0.1 percent of GDP reduction in electricity subsidies, with total yield of 0.35 percent of GDP to assure compliance with the year-end fiscal targets.	Five days before the board date			
3	Take measures to recover part of the GIDC proceeds focusing on areas where large collecting agents have already collected the GIDC in their price, with yield of 0.1 percent of GDP.	Five days before the board date			
Structural Benchmarks					
Fiscal sector					
1	Increase the issuance of first notices (u/s 114) to 75,000 and follow up with a second notice (u/s 122c) to 75 percent of those who did not respond satisfactorily to their first notice within 60 days by end-March, 2014. Issue a provisional tax assessment to 75 percent of those who did not respond satisfactorily within 60 days to the second notice by end-March, 2014.	end-March 2014		Met	Broaden the tax base and improve tax compliance.
2	Eliminate exemptions and concessions granted through SROs for an amount consistent with the fiscal deficit reduction objective in the FY2014/15 budget.	end-June-2014		Met	Reduce distortions and improve revenue collection.
3	Approve an administrative order to consolidate the responsibilities of public debt management in the debt management office.	end-September 2014		Not met, but the order fell short of unifying fragmented debt management functions.	Strengthen the organizational framework for effective public debt management.
4	Enact amendments to the relevant tax laws (as defined in the TMU) and submit amendments to the Anti-Money Laundering Act (AMLA) to Parliament.	end-December 2014		Met	Use antimoney laudering tools to combat tax evasion, and faclitate detection of potential cases of abuse of the investment incentive scheme to lauder criminal proceeds.
5	Draft legislation that will permanently prohibit the practice of issuing SROs that grants exemptions and loopholes.	end-March 2015			Reduce distortions and improve revenue collection.
6	Reorganize the Debt Policy Coordination Office as a middle office responsible for updating the MTDS and monitoring its implementation, coordinating the credit risk management functions.	end-March 2015			Strengthen the organizational framework and improve public debt management.
Monetary sector					
7	Improve the internal operations of the SBP by: (i) reestablishing an advisory monetary policy committee to advise the Board on its policy decisions; (ii) establishing a Board committee to centralize and oversee risk management activities across the bank; and (iii) begin publishing summaries of the monetary policy proceedings of the Board meetings and monetary policy committee deliberations.	end-August 2014		Met	Independent of the legislation, improve the operational autonomy of the SBP and enhance risk management.
8	Announce a time-bound plan to improve the SBP's interest rate corridor by setting the policy rate between the floor and ceiling rates of the corridor.	end-February 2015		Met	Improve SBPs liquidity management.
9	Improve the internal operations of the SBP by the following measures: (i) the Investment Committee of the SBP Board will begin regular (at least four times per year) oversight and approval of the reserves management strategy and risk practices; and (ii) the authorities will provide confirmation that in line with standard IMF procedures, the Internal Audit Department conducts reviews of the program monetary data reported to the IMF, within two months after each quarter, for accuracy and compliance with the TMU.	end-February 2015		Met	Improve monetary policy framework through enhanced central bank independence.
10	Enact the amendments to the SBP law to give SBP autonomy in its pursuit of price stability as its primary objective, while strengthening its governance and internal control framework, in line with Fund staff advice.	end-June 2015			Prerequisite for an independent monetary policy framework.
Financial sector					
11	Enact the Securities Bill, in line with Fund staff advice.	end-June 2015	end-January 2016		Enhance the resilience of the financial sector.
12	Enact the Deposit Protection Fund Act, in line with Fund staff advice.	end-June 2015	end-September 2015		Enhance the resilience of the financial sector.
Structural Policies					
13	Initiate revenue based load shedding in six remaining electricity distribution companies .	end-January 2014		Met	Boost sustainable and inclusive growth, by removing bottlenecks, encourage long-term, sustainable increases in electrictity supply; improve the efficiency of the economy through privatization and use its proceeds to hel ease fiscal and balance of payments pressures.
14	Hire three financial advisors for three PSEs in the capital market transactions list and three financial advisors for the three PSEs in the strategic private sector enterprises list for privatization in the TMU.	end-March 2014		Met at end-July, 2014	
15	Conduct a diagnostic study of the regulatory framework of the power sector and prepare an interim report.	end-April 2014		Met	
16	Offer the minority shares in United Bank Limited and Pakistan Petroleum Limited to domestic and international investors.	end-June 2014		Met	
17	Fill the vacancies in the NEPRA Board.	end-July 2014		Met at end-November, 2014	
18	Conduct a review to reduce the number of existing processes and forms for paying sales and income taxes.	end-March 2015			
19	Privatize 26 percent of PIA's shares to strategic investors.	end-December 2015			
New Structural Benchmarks					
1	Make the improved interest rate corridor of the SBP operational	end-September 2015			Improve SBPs liquidity management.
2	Merge the NTN system covering 3.6 million individuals with the CNIC database that covers about 150 million people	end-September 2015			Broaden the tax base and improve tax compliance.
3	Enact the Credit Bureau Act	end-November 2015			Extend credit to broader sections of society
4	Adopt the amendments to the AMLA that will include the serious tax crimes from the relevant tax laws (as defined in the TMU).	end-September 2015			Use antimoney laudering tools to combat tax evasion, and faclitate detection of potential cases of abuse of the investment incentive scheme to lauder criminal proceeds.

Attachment II. Technical Memorandum of Understanding (TMU)

March 12, 2015

This memorandum sets out the understanding between the Pakistani authorities and the IMF staff regarding the definitions of quantitative performance criteria and indicative targets, as well as respective reporting requirements used to monitor developments, for the program under the Extended Arrangement. To this effect, the authorities will provide the necessary data to the IMF as soon as it becomes available. The definitions used in this TMU will be adjusted to reflect any changes in accounting classifications introduced during the program period. For the purposes of monitoring under the program, all assets and liabilities as well as debt contracted, denominated in SDRs or in currencies other than the U.S. dollar, will be converted into U.S. dollars at the program exchange rates. Net external budget financing and external cash grants will be converted into Pakistani rupees at the program exchange rate. The program exchange rate of the Pakistani rupee to the U.S. dollar is set at 99.66 rupee per one U.S. dollar. The corresponding cross exchange rates for other foreign currencies are provided in Table 1.

A. Quantitative Targets

The program sets performance criteria and indicative targets for defined test dates (Table 1 in the LOI). The program sets the following performance criteria:

Performance criteria

- Floor on the net international reserves (NIR) of the State Bank of Pakistan (SBP) (millions of U.S. dollars);
- Ceiling on the net domestic assets (NDA) of the SBP (stock, billions of Pakistani rupees);
- Ceiling on the general government budget deficit excluding grants (cumulative flows, billions of rupees);
- Ceiling on net government budgetary borrowing from the SBP (including provincial governments) (stock, billions of rupees);
- Ceiling on SBP's stock of net foreign currency swap/forward contracts (millions of U.S. dollars);

Continuous performance criteria

- Ceiling on the accumulation of external payment arrears by the general government;

Indicative targets

- Floor on targeted cash transfers spending (BISP) (cumulative, billions of Pakistani rupees)
- Floor on net tax revenues collected by the Federal Bureau of Revenue (FBR) (cumulative, billions of Pakistani rupees)

B. Definitions of Monitoring Variables

1. **The general government** is defined as the central (federal) government and local (provincial) governments, excluding state-owned enterprises. The definition of the general government includes any new funds, or other special budgetary or extra-budgetary entities that may be created during the program period to carry out operations of a fiscal nature as defined in the IMF's Manual on Government Finance Statistics 2001. The authorities will inform IMF staff on the creation of any such entities without delay.

2. **Net revenue of the FBR** is defined as the sum of revenues collected from (i) general sales tax (GST) on goods; (ii) customs duties, customs registration fees and levies; (iii) excise duties on imported products; (iv) excise duties on domestic products; (v) levies (toll) on oil derivatives; (vi) other proceeds and fees; (vii) sales tax; and (viii) unclassified revenues minus the tax refunds. Net revenue collection will be defined, for each test date, as the cumulative sum of net revenues collected since the beginning of the current year. The floor on the collection of gross revenues by the FBR will be measured quarterly on the basis of cumulative end-of-quarter data.

3. **Net international reserves** (stock) of the SBP are defined as the dollar value of the difference between usable gross international reserve assets and reserve-related liabilities, evaluated at the program exchange rates. On June 30, 2014, the NIR of Pakistan amounted to US$2,678 million.

4. **Usable gross international reserves** of the SBP are those readily available claims on nonresidents denominated in foreign convertible currencies and controlled by the monetary authorities for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency exchange rate, and for other related purposes. Gross official reserves include (i) holding of foreign currencies, (ii) holdings of SDRs, (iii) the reserve position in the IMF, and (iv) holdings of fixed and variable income instruments. Excluded from usable reserves, inter alia, unless there is also a reserve-related liability associated with it, are: (i) claims on residents; (ii) assets in nonconvertible currencies; (iii) precious metals (iv) illiquid assets; (v) assets that are pledged or collateralized.

5. **Reserve-related liabilities** of the SBP include all foreign exchange liabilities to residents or nonresidents, including (i) foreign currency liabilities with remaining maturity of one year or less, (ii) any foreign exchange liabilities arising from derivatives (such as futures, forwards, swaps, and options) on a net outstanding basis—defined as the long position minus the short position, (iii) outstanding IMF credits to Pakistan, (iv) foreign exchange deposits with the SBP of foreign governments, foreign central banks, foreign deposit money banks, international organizations, and

foreign nonbank financial institutions, as well as domestic financial institutions. General government foreign exchange liabilities at the SBP will not be included in reserve-related liabilities.

6. **Aggregate net position in the foreign exchange derivatives** is defined as the aggregate net positions in forward and futures in foreign currencies of the SBP vis-à-vis the domestic currency (including the forward leg of currency swaps). The SBP's aggregate position was –US$2.3 billion at end-June 2013.

7. **Reserve money** (RM) is defined as the sum of: currency outside schedule banks (deposit) money banks); schedule banks' domestic cash in vaults; schedule banks' required and excess rupee and foreign exchange deposits with the SBP; and deposits of the rest of the economy with the SBP, excluding those held by the federal and provincial governments and the SBP staff retirement accounts.

8. **Net domestic assets** of the SBP are defined as RM minus NIR, minus other assets not included in gross official international reserves, minus commercial bank required and excess reserves at the SBP in foreign currency, plus medium and long-term liabilities (i.e., liabilities with a maturity of one year or more) of the SBP, plus other foreign liabilities not included in official reserve liabilities, minus the balance of outstanding Fund purchases credited to the government account at the SBP. NDA is composed of net SBP credit to the general government plus outstanding credit to domestic banks by the SBP (including overdrafts) minus liabilities not included in RM and other items net.

9. **Net government budgetary borrowing from the SBP (including provincial governments)** is defined as SBP claims on the government minus government deposits with the SBP. SBP claims on the government include government securities, treasury bills, treasury currency, and debtor balances. SBP claims on the government exclude accrued profits on government securities. Government deposits with the SBP exclude the Zakat Fund (Table 4).

10. **Net purchase of foreign exchange** is defined as outright purchase of foreign exchange minus outright sale of foreign exchange in the foreign exchange spot market as net addition to the stock of NIR of the SBP by using foreign exchange market intervention.

11. **External public debt arrears** are defined as all unpaid debt-service obligations (i.e., payments of principal and interest) of the general government (government, SBP, and state-owned enterprises) to nonresidents arising in respect of public sector loans, debt contracted or guaranteed, including unpaid penalties or interest charges associated with these obligations that are beyond 30 days after the due date. The definition of debt, for the purposes of the EFF, is set out in Point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Executive Board Decision No. 6230–(79/140), last amended by Executive Board Decision No. 14416–(09/91), adopted August 31, 2009).The ceiling on external payment arrears is set at zero.

12. **The overall budget deficit (excluding grants)** will be monitored quarterly under the cash balance of the general government balance, excluding grants, including the operations of local (provincial) governments financed from local funds. It will be measured below the line and will include:

- **Net external financing**, excluding valuation gains and losses.
- **Change in net domestic credit from the banking system**, excluding valuation gains and losses from deposits denominated in foreign currency.
- **Change in the net domestic nonbank financing**, excluding valuation gains and losses. These include (i) domestic privatization receipts transferred from the privatization accounts to the budget, (ii) the stock of issued government securities held outside the general government and the banking system, net of valuation changes, (iii) net deposits and reserves received by the government (public accounts deposits), (iv) any other government borrowing from domestic nonbank sources net of repayments, minus (v) government deposits with nonbank financial institutions.
- **Total external grants to the federal and provincial governments**. These are defined as the sum of project grants, cash external grants for budgetary support, capital grants reflecting the principal amounts of external debt cancellation or swaps, and other grants.

13. **Net external program financing** is defined to include external privatization receipts; budget support grants; budget support loans from multilateral (other than the IMF, but including World Bank and Asian Development Bank (ADB) budget support and program loans), official bilateral budget support loans, and private sector sources (e.g., bonds); rescheduled government debt service and change in stock of external debt service arrears net of government debt amortization due on foreign loans, the latter including any accelerated amortization including related to debt swaps or debt cancellation recorded as capital grants. It also includes foreign loans on lent to financial institutions and companies (public or private) and emergency relief lending. Program financing excludes all external financing counted as reserve liabilities of the SBP (defined above). Amounts projected for net external program financing and external grants are provided in Table 3.

14. **Net external budget financing** is defined as net external program financing minus privatization receipts, minus budget support grants, plus all other external loans for the financing of public projects or other federal or provincial budget expenditures, plus transfers of external privatization receipts from the privatization account to the budget.

15. **Structural benchmark on hiring of six transaction advisors for end-March 2014 is defined as follows**: Three transaction advisors to undertake the sale of minority shares for three PSEs from the list of capital market transactions with at least one offering in the domestic and one offering in international markets. From the list of strategic private sector participation one transaction advisor for electricity distribution company and one generation company, and finally one transaction advisor to undertake the restructuring of Pakistan International Airlines Corp (PIAC) and will seek for a strategic investor.

16. **The "relevant tax laws" in the structural benchmark on "submission of amendments to the relevant tax laws and submission of amendments to the Anti-Money Laundering (AML) Act for end-December 2014" is defined as follows**: Income Tax Ordinance, 2001; the Federal Excise Act, 2005; the Sales Tax Act, 1990; the Customs Act, 1969; and any other relevant law.

17. **Electricity Tariff Pricing Formulas and Definitions** (MEFP ¶30)

(i) The increase in the weighted average tariffs by 4 percent on electricity consumers' electricity consumption is defined as follows

Weighted Average Notified Tariff for electricity consumers =

(Changes in the Industrial Users Tariff Rate for each category x DISCOs' estimated sales to Industrial Users for each category

+ Change in the Residential Users Tariff Rate for each category above 200kWh x DISCOs' estimated sales to Residential Users for each category

+ Change in the Commercial Users Tariff Rate for each category x DISCOs' estimated sales to Commercial Users for each category

+ Change in the Single Point Supply for further distribution Tariff Rate for each category x DISCOs' estimated sales to Point Supply for further distribution Users for each category)

+ Change in the AJ&K users' Tariff Rate for each category x DISCO's estimated sales to AJ&K Users for each category)

+ Change in the Other users' Tariff Rate for each category x DISCOs' estimated sales to Other Users for each category)/ DISCO's total sales to Industrial, Residential Users consuming more than 200kWh, Commercial, Single Point Supply, Other Users and AJ&K Users

= 4 percent

(ii) Current notified electricity tariffs for users at 0-50 kWh will be retained.

(iii) On January 1, 2015 an additional surcharge of PRs 0.6/kWh has been levied to increase weighted average tariffs by 4 percent as defined in (i). The current average NEPRA determined tariff is PRs 13.81/kWh. The current effective notified tariff is PRs 12.42/kWh. The difference between the determined and effective notified tariff represents the average Tariff Differential Subsidy (TDS). Going forward, the effective notified tariff will be further adjusted taking advantage of the negative Fuel Price Adjustments (FPA) expected in the coming months as defined in the following Table as required.

(PRs/kWh)	November 2014	December 2014	January 2015	February 2015	March 2015
Estimated change in FPA[1]	-0.61	-0.63	-0.69	-0.36	
Actual change in FPA	-2.97	-3.20			
Notified tariff	11.82	11.82	12.42		

1/ Energy mix is calibrated from 2013/14. Subject to variation due to different fuel mix during FY14/15.

(iv) Syndicated Term Credit Finance (STCF) Surcharge "Debt Servicing Surcharge" (¶31) of PRs 0.43/kWh is currently included in the current effective notified electricity tariff (excluding lifeline consumers, 0–50kWh) to service the interest payments on debt incurred by Power Sector Holding Company Limited (PHCL). The PRs 0.43/kWh surcharge is composed of PRs 0.30/KWh applied since October 1, 2014 and additional PRs 0.13/kWh (out of the total surcharge of PRs 0.60 applied since January 1, 2015). The STCF Surcharge is defined as follows:

STFC Surcharge = Total Annual Interest Paid on STCF balance/Estimated volume of electricity sales in FY 2014/15.

	Q1	Q2	Q3	Q4	FY 2014/15
STFC Debt Service (PRs millions)	8,960	6,945	10,195	6,420	32,520

STFC Surcharge = PRs 32,520(millions)/68000(GW) = PRs 0.48/kWh

- The balance = PRs 0.48/kWh – PRs 0.43/kWh = PRs 0.06/kWh.
- Calculations based on projected collections with FY2013-14 base case losses (18.6 percent) and collection rate (89.1 percent)
- The STCF Surcharge will be adjusted upward or downward depending on the timing of tariff notification, and due to new loans taken under PHCL to ensure that the annual STCF Debt Service (see Table above) will be fully financed within the fiscal year. Any deficit amount will be borne by the government. Any excess amount will be held by PHCL and utilized for payment of principal part of the debt service.

18. **Monitoring mechanism to track stock and flow of payables** (¶31)

Overdue payables (over 45 days) stand at **PRs 218 billion** as of end-December 2014. The projected evolution of overdue payables, excluding measures for FY2014-15 and its components are given in the following Table:

FY2014–15 (PRs Billions)	**2014/15Q2** (Actual)	**2014/15Q3**	**2014/15Q4**	**2015/16Q1**	**2015/16Q2**
Stock of Overdue Payables (end of period)	218	250	297	387	413
Build-up of payables during the quarter					
Excess T&D Losses	-	5	20	36	(2)
Under collection	16	18	18	44	13
Penalties	7	8	9	11	14

C. Adjustors

19. **The floor on NIR will be adjusted upward** (downward) by the cumulative excess (shortfall) of cash inflows from multilateral and bilateral creditors, Coalition Support Fund (CSF), and bond issuance relative to projected inflows (Table 2). Cumulative cash inflows are defined as external disbursements (including grants) from official multilateral creditors (including, but not limited to Asian Development Bank, Islamic Development Bank, and World Bank), official bilateral creditors (including, but not limited to DFID, UK, USAID), and external bond placements that are usable for the financing of the central government budget. The adjustor is modified for the end-June 2014 calculation of the fourth review to exclude the proceeds of the US$2 billion Eurobond transaction. This modification does not apply to subsequent reviews.

20. **The ceiling on NDA will be adjusted downward** (upward) by the cumulative amount of any excess (shortfall) of budget support loans or budget support grants compared to the program amounts (Table 3) and Euro bond issuance or project grants compared to projected inflows (Table 2). Budget support grants to the public sector are defined as grants received by the government (including provincial governments) for direct budget support from external donors and not related to the projected financing. Budget support loans to the public sector are defined as disbursements of loans from bilateral and multilateral donors for budget support (including provincial governments).

21. **The ceiling on the consolidated overall budget deficit** (excluding grants) for FY2013/14 and FY2014/15 will be adjusted upward for the cumulative excess in net external program financing in rupee terms for up to PRs 15.0 billion at end-September, PRs 25.0 billion at end-December, PRs 42.0 billion at end-March, and PRs 50 billion at end-June. The ceiling for FY2013/14 and FY2014/15 will be adjusted downward for any shortfall in federal PSDP spending below PRs 25 billion at-end September, PRs 80 billion at end-December, PRs 243 billion at end-March and PRs 410 at end-June. The ceiling will be adjusted downward for any shortfall in the targeted cash transfers (BISP). The ceiling will be adjusted upward for over performance in the BISP up to PRs 12 billion from their indicative targets.

D. Public Sector Enterprises

List of Companies for **Capital Market Transactions**

- Oil and Gas Development Co. Ltd (OGDCL)
- Pakistan Petroleum Ltd (PPL)
- Mari Petroleum Ltd.
- Government Holding Private Ltd (GHPL)
- Pak Arab Refinery Ltd (PARCO)
- Habib Bank Limited (HBL)
- United Bank Limited(UBL)
- Allied Bank Limited (ABL)
- National Bank Limited (NBP
- State Life Insurance Corp. (SLIC)
- Kot Addu Power Company Ltd. (KAPCO)

List of Companies for **Strategic Private Sector Participation**

- National Insurance Co. Ltd. (NICL)
- National Investment Trust Ltd. (NITL)
- Small & Medium Enterprise (SME) Bank
- Pakistan Reinsurance Co Ltd. (PRCL)
- Heavy Electrical Complex (HEC)
- Islamabad Electric Supply Co. Ltd (IESCO)
- Faisalabad Electric Supply Co. Ltd (FESCO)
- Lahore Electric Supply Co. Ltd (LESCO)
- Gujranwala Electric Power Co. Ltd (GEPCO)
- Mutan Electric Power Co. Ltd (MEPCO)
- Hyderabad Electric Supply Co. Ltd (HESCO)
- Sukkur Electric Power Co. Ltd (SEPCO)
- Peshawar Electric Supply Co. Ltd (PESCO)
- Quetta Electric Supply Co. Ltd (QESCO)
- Lakhra Power Generation Company
- Jamshoro Power Generation Co. Ltd (JPCL)
- Northern Power Generation Co. Ltd (NPGCL)—Thermal Power Station—Muzaffargarh)
- National Power Construction Co. (NPCC)

- Pakistan Steel Mills Corp (PSMC)
- Pakistan Engineering Co Ltd (PECO)
- Pakistan International Airlines Corp (PIAC)
- Pakistan National Shipping Corp (PNSC)
- Convention Centre, Islamabad.
- PIA InvestmentLtd—Roosevelt Hotel NY & Scribe Hotel, Paris

List of Companies for **Restructuring followed by Privatization**

- Pakistan State Oil Co Ltd (PSO)
- Sui Southern Gas Co Ltd (SSGC)
- Sui Northern Gas Pipelines Ltd (SNGPL)

E. Program Reporting Requirements

22. **Performance under the program** will be monitored from data supplied to the IMF by the SBP, Ministry of Finance and Ministry of Water Power as outlined in the table below. The authorities will transmit promptly to IMF staff any data revisions as well as other information necessary to monitor the arrangement with the IMF.

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
State Bank of Pakistan (SBP)	SBP balance sheet	Summary	Weekly	First Thursday of the following week
	SBP balance sheet	Summary at program exchange rates; and by official exchange rates	Monthly	Within 15 days of the end of each month
	Monetary survey	Summary banking system balance sheet for the central bank at both program exchange rates and by chart of accounts at actual official exchange rates; the consolidated balance sheet of commercial banks at actual official exchange rates	Monthly	Within the first 30 days of each month.
	International reserves	By (i) program exchange rates; and (ii) at actual official exchange rates.	Daily	The following working day
	Foreign exchange market	Market exchange rates (buying and selling); weighted average customer exchange rate; monthly trade volume, and high and low exchange rate of the interbank, the KERB market.	Daily/ Monthly	Within one day/ monthly within 5 working day
	Foreign exchange market	SBP foreign exchange operations, and intervention,(volume)	Daily	Within one day
	Foreign exchange market	SBP operation against the domestic currency in swap/forwards by (volumes)	Daily	Within one day
	Foreign exchange market	Breakdown of short, long, counterparts, of the swap/forward contracts	Monthly	Third working day of the following month
	Foreign exchange market	Outstanding swap/forward positions by maturity buckets, and counterparties.	Monthly	Third working day of the following month

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	Net International Reserves	Net International reserves at program exchange rates as defined in TMU, including a breakdown by currency and specification of *nostro* balances with foreign branches of National Bank of Pakistan.	Quarterly	Seventh working day after quarter end
	External financing	Foreign assistance received and projections for the coming four quarters. Please categorize all grants and loans by program/project, and the amounts received/expected in cash.	Quarterly	Within 15 days of the end of each quarter
	Interbank money market	Daily interbank repo volume and interest rate of trades	Daily	Within one day
	SBP operations	Repo (reverse repo) operations, open market operations,	Weekly	First Monday of the following week
	Bank liquidity	Excess reserves, in local currency	Bi-weekly	With a lag of 15 days
	T-bill and coupon bond financing, SBP securities	Auction data: date, original and remaining maturities, issuance volume, allocation, average yield and coupon yield (if available)	Fortnightly	Last working day of the fortnight
	Banking data	Sectoral distribution of loans and deposits; loans and deposits by local and foreign currency; deposit and lending rates,;	Monthly	Within 25 days of the end of each month.
	Banking data	Loan maturities	Quarterly	Within 45 days of the following quarter
	Banking indicators	Capital adequacy; asset composition and quality; profitability; liquidity; open FX positions;	Quarterly	Within 45 days of the following quarter
	Banking sector stress tests	Results of stress tests on exchange rate, liquidity, and credit risk	Quarterly	Within 60 days
	Transfers	Workers' remittances.	Monthly	Within 25 days of the following month
	Other monetary data	The SBP survey, ODCs and DCs published in IFS.	Monthly	Within 45 days of the end of each month
	Balance of payments	Detailed export and import data Detailed balance of payments data	Monthly	Within 28 days of the end of each month
	Privatization receipts	Balance on the PC Fund account; gross inflows into and outflows from the PC Fund account during the month, specifying the nature of each transaction	Quarterly	Within seven days of the end of each quarter
Ministry of Finance (MOF)	External debt	Disbursements and stock of outstanding short-term and contracting or guaranteeing and outstanding stock of medium-and long-term external debt of the government, the SBP, and state-owned companies; any stock of arrears on external debt service and outstanding stock of government guarantees and external arrears.	Monthly	Within 25 days of the following month
	External financing	Foreign assistance received and projections for the coming four quarters. Please	Quarterly	Within 15 days of the end of each quarter

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
		categorize all grants and loans by program/project, and the amounts received/expected in cash and in kind.		
	Federal government	State budget	Monthly	Within 30 days of the end of each month
	Consolidated general government	Federal and provincial governments	Quarterly	Within 45 days of the end of each quarter
	Consolidated general government	Federal and provincial governments	Annual	Within 180 days of the end of each year
	Federal government	Fiscal financing sources: Detailed quarterly financing plan for the coming 12 months including projections for domestic public securities (issuance and maturities), external financing, SBP profits, short-term borrowing, other financing schemes, and borrowing from the SBP.	Monthly	One month in advance
	Federal government	Stock of government borrowing from the SBP	Quarterly	Within the first 5 days of each quarter.
Pakistan Bureau of Statistics (PBS)	SPI, CPI, WPI	Detailed monthly price indices	Monthly	Within five days of the following month
	CPI	Index of core inflation	Monthly	Within 21 days of the end of each month
Federal Board of Revenue (FBR)	Revenue collection Tax credits	Total revenue collected separately by the tax administration and customs administration, including revenue by individual tax, and social contributions.	Monthly	Within 7 days of the end of each month
	Tax arrears	By category	Monthly	Within seven days of each month
		By type of tax	Monthly	Within 7 days of the end of each month
	GST refund claims in arrears	For the 30 largest debtors	Monthly	Within 7 days of the end of each month
	Automated GST refunds	Detailed data, by type of tax, of outstanding tax credits for all types of tax revenues	Quarterly	Within 7 days of the end of each month
		Number of refunds that were processed automatically (share of total refunds); total value of automated and automatic refunds and offsets; average waiting time (days) to receive refund	Quarterly	Within 7 days of the end of each month
	Large taxpayers	Data on the number of taxpayers and amount of taxes managed by the large tax payer units (LTUs)	Quarterly	Within 7 days of the end of each month

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	Import data	Total value of recorded imports Total value of duty-paid recorded imports; Number of total transactions involving recorded imports; Number of total transactions involving non-duty free recorded imports	Quarterly	Within 30 days of the end of each quarter
	Audits	Percentage of selected companies and identified revenue from audits	Quarterly	Within 45 days of the end of each month (monthly data provided on a quarterly basis)
Ministry of Water and Power		Key Power Sector Statistics (Please see the attached template) Cumulative Monthly Subsidy Position (Rs. Billion) PEPCO Month End Payables and Receivables Positions And Aging Schedule, Rs. Billion Receivables Positions - Total and DISCO-wise Break-up CPPA/PEPCO Month-wise Consolidated Cash Flow AT&C Statistics Monthly TDS Claims by DISCOs and Total Inter Corporate Circular Debt Sheet Prepared by Ministry of Finance DISCOs Consolidated Income Statement Net Electrical Output & Power Purchase Price by Source, GWh Generation, Demand and Shortfall for FY10 to date Net Electrical Output (MkWh) Plant and Fuel-wise Detail Working Capital Loans For each loan type	Quarterly	Within 30 days
	Domestic expenditure arrears	Energy arrears	Quarterly	Within 45 days of the end of each month for government arrears
		Determined and Notified Tariff's for each User and User Group (Please see template)	Annual	Within 30 days of determination and notification
Ministry of Petroleum and Natural Resources		Gas supply Gas prices	Quarterly on monthly frequency	Within 30 days from the end of the quarter
OGRA		UFG losses	Quarterly	Within 30 days from the end of the quarter
BISP	Targeted cash transfers	Coverage (number of beneficiaries paid) and payment by conditional and unconditional transfers.	Quarterly	Within 30 days from the end of the quarter

Table 1. Exchange Rates of the SBP

(as of June 28, 2013 in U.S. dollars per currency)

Currency	Rupee per Currency	Dollars per Currency
EUR	130.18	1.31
JPY	1.01	0.01
CNY	16.24	0.16
GBP	151.80	1.52
AUD	92.11	0.92
CAD	95.04	0.95
THB	3.21	0.03
MYR	31.54	0.32
SGD	78.77	0.79
INR	1.68	0.02

Table 2. Projected Disbursements to Pakistan

(In millions of U.S. dollars)

	Jun-14	Sep-14	Dec-14		Mar-15	Jun-15	Sep-15	Dec-15
			Projection	Actual	Projection			
Multilateral and bilateral disbursement	2,885	1,270	1,358	964	2,006	2,562	1,468	1,805
of which: in cash 2/	2,608	407	879	543	1,400	1,850	1,060	1,304
International debt issuance	2,000	0	1,500	1,000	0	0	0	1,000
Coalition Support Fund	375	735	240	0	717	360	240	225
Other 1/	831	0	20	0	20	450	300	250
Gross Inflows	6,091	2,005	3,118	1,964	2,743	3,372	2,008	3,280
of which: in cash	5,814	1,142	2,639	1,543	2,137	2,660	1,600	2,779
Debt service	943	989	963	1,128	1,157	1,515	1,210	1,316
Memorandum items								
Gross International Reserves	9,096	8,943	10,953	10,514	13,004	15,275	16,214	17,948
Program Net International Reserves	1,800	3,000	3,500	3,500	5,000	6,750	8,000	8,500

1/ Includes privatization and 3G licenses.

2/ Numbers need to be confirmed with the MoF.

Table 3. External Inflows to the General Government
(In millions of U. S. dollars)

	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15
Non Tax revenue	322	353	1206	735	0	717	360	540	225
Of which: Coalition Support Fund	322	353	375	735	0	717	360	240	225
3G Licences	0	0	831	0	0	0	0	300	0
Grants	99	1537	152	89	132	99	39	68	208
External interest payments	202	155	215	174	306	187	437	224	466
Net external debt financing	50	-115	3501	846	2257	2475	1500	315	1601
Disbursements	645	760	4713	846	2257	3445	2578	1301	2451
of which budgetary support	309	285	2042	24	26	622	1269	59	702
Amortization	594	875	1212	0	0	970	1078	986	850
Privatizations	0	0	5	0	0	20	450	0	250
Memorandum item									
Program financing	408	1822	2199	113	158	741	1758	127	1160

Table 4. Government Sector (Budgetary Support)
(End-of-period stocks/PRs. Millions)

Item	June 30, 2013	June 30, 2014	Prov. December 31, 2014
Central Government	**5,561,994**	**6,059,496**	**6,385,462**
Scheduled Banks	**3,320,870**	**3,491,821**	**4,128,722**
Government Securities	1,117,115	2,413,134	2,912,752
Treasury Bills	2,611,512	1,550,476	1,730,271
Government Deposits	-407,757	-471,789	-514,301
State Bank	**2,241,124**	**2,567,674**	**2,256,740**
Government Securities	3,127	2,786	2,786
Accrued Profit on MRTBs	44,959	82,070	74,194
Treasury Bills	2,275,183	2,852,274	2,521,206
of which: MTBs created for replenishment of cash balances	2,274,675	2,851,765	2,520,697
Treasury Currency	8,653	8,654	7,988
Debtor Balances (Excl. Zakat Fund)			
Government Deposits	-96,260	-383,571	-354,896
(Excl. Zakat and Privatization Fund)			
Payment to HBL on a/c of HC&EB	-287	-287	-287
Adjustment for use of Privatization Proceeds			
for Debt Retirement	5,749	5,749	5,749
Provincial Governments	**-315,607**	**-510,138**	**-619,805**
Scheduled Banks	**-287,393**	**-352,258**	**-351,609**
Advances to Punjab Gc Advances to Punjab Government for Cooperatives	1,024	1,024	1,024
Government Deposits	-288,417	-353,282	-352,633
State Bank	**-28,214**	**-157,880**	**-268,196**
Debtor Balances (Excl. Zakat Fund)	13,715	802	1,976
Government Deposits (Excl.Zakat Fund)	-41,930	-158,682	-270,172
Net Govt. Budgetary Borrowings			
from the Banking system	**5,246,387**	**5,549,357**	**5,765,657**
Through SBP	2,212,910	2,409,794	1,988,544
Through Scheduled Banks	3,033,477	3,139,563	3,777,113
Memorandum Items			
Accrued Profit on SBP holding of MRTBs	**44,959**	**82,070**	**74,194**
Scheduled banks ' deposits of Privitization Commission	**-5,433**	**-6,438**	**-6,999**
Outstanding amount of MTBs (Primary market; discounted value)	**2,529,412**	**1,525,175**	**1,679,252**
Net Govt. Borrowings (Cash basis)			
From Banking System	**5,124,762**	**5,448,424**	**5,647,443**
From SBP	2,167,951	2,327,724	1,914,350
From Scheduled Banks	2,956,811	3,120,700	3,733,094

INTERNATIONAL MONETARY FUND

PAKISTAN

March 26, 2015

SIXTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND MODIFICATION OF PERFORMANCE CRITERIA—SUPPLEMENTARY INFORMATION

Approved By
Daniela Gressani and Mark Flanagan

Prepared By
Middle East and Central Asia Department

1. **This supplement provides an update on economic and policy developments since the issuance of the staff report on March 13, 2015**. The additional information does not change the thrust of the staff appraisal.

2. **The authorities have taken steps to meet the prior actions for this review**:

- **Fiscal prior actions**. The authorities implemented a fiscal adjustment package with a total yield of 0.45 percent of GDP. The first component of this package, the prior action on measures to recover part of GIDC (0.1 percent of GDP) collected but not remitted to the government, was achieved. The composition of the remainder of the package was somewhat different than originally envisaged in the second prior action. The authorities originally envisaged 0.25 percent of GDP in revenue measures and a further reduction of 0.1 percent of GDP in electricity subsidies. Administrative difficulties delayed the subsidy reduction component and the authorities substituted revenues from the bonus shares tax, whose court challenge has been resolved. This, together with the higher GST on oil and fuels, and other small tax measures, completed the package, which yields more than originally envisaged. Although one component of this prior action was not met and a different measure was taken, in staff's view, the authorities' actions accomplish the objective of the prior action, and are sufficient to support staff's recommendation for the completion of the review.

- **Prior action on revised central bank independence legislation**. The government has submitted revised amendments to the State Bank of Pakistan (SBP) law to the National Assembly, meeting the prior action. The new version would substantially strengthen the Monetary Policy Committee—the monetary policy governing body—which was a key staff concern with the previous draft.

In particular, revised amendments would improve the operational independence of the SBP and enhance its governance structure. Staff takes the view that the prior action was met by the revised amendments. Staff will continue to work with the authorities, including through nonlegislative measures, to address some concerns that were not fully addressed in the new version, including strengthening the personal autonomy of Board members.

3. **Gross official reserves stand at US$11 billion as of March 23, 2015**. The SBP has continued to purchase foreign exchange in the spot market, with purchases so far in the quarter totaling over US$625 million, placing the SBP on track to meet the end-March Net International Reserves target. The nominal exchange rate has depreciated by 3 percent against the U.S. dollar in the current fiscal year (since June 2014). The net short position in foreign exchange swap/forward contracts remains below the end-March program ceiling.

4. **Headline inflation eased further in February 2015 to 3.2 percent (y-o-y)**. Deflation in food and energy prices helped headline inflation to recede to historically low levels, with core inflation also easing to below 7 percent. In light of this continued strong inflation performance, the SBP cut its policy rate by 50 bps to 8 percent.

Press Release No. 15/146
FOR IMMEDIATE RELEASE
March 27, 2015

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Sixth Review Under the EFF for Pakistan

The Executive Board of the International Monetary Fund (IMF) today completed the sixth review of Pakistan's economic performance under a 36-month program supported by an Extended Fund Facility (EFF) arrangement. The Board's decision enables the immediate disbursement of an amount equivalent to SDR 360 million (about $501.4 million), bringing total disbursements under the arrangement to SDR 2.52 billion (about $3.5 billion).

On September 4, 2013, the Executive Board approved the three-year extended arrangement under the EFF in the amount of SDR 4.393 billion (about US$6.12 billion, or 425 percent of Pakistan's quota at the IMF). (See Press Release No. 13/322).

At the conclusion of the Executive Board's discussion, Mr. Mitsuhiro Furusawa, Acting Chair and Deputy Managing Director, issued the following statement:

"The authorities' strong performance under Pakistan's Fund-supported program is to be commended. Progress has been made in restoring economic stability, improving growth prospects, and reducing crisis risks. It will be important to build on these gains and continue determined efforts to implement the reform agenda to achieve economic transformation and higher sustainable growth.

"Fiscal consolidation is underway through efforts to broaden the tax base and reduce costly and inefficient electricity subsidies. Scope remains to increase tax compliance and enforcement and further reduce energy subsidies, while continuing to protect the most vulnerable. Enhanced public debt management remains a priority, together with further efforts to diversify fiscal financing and reduce reliance on central bank borrowing.

"Monetary policy remains prudent and foreign exchange reserves are increasing. However, legislation to enhance central bank independence remains crucial and should conform to international best practices. Efforts to improve central bank functioning should also continue, including through improved functioning of the interest rate corridor, effective open market operations, and strengthened risk management and internal operations.

"The financial sector remains stable and profitable and progress in bank capitalization is satisfactory. Further reforms are needed to safeguard financial stability, and a number of legislative actions are underway in this regard. Commendable efforts to combat terrorism financing, money laundering, and tax offenses have been made and would need to be sustained.

"Structural reforms are progressing, albeit with some difficulties. While the power sector regulatory reform continues, progress in the gas sector has been uneven. Implementation of gas price rationalization should help better allocate current supply and encourage new production. The current environment of lower oil prices provides an opportunity to speed-up electricity tariff rationalization while continuing to improve the operations and collections of energy companies. The authorities remain committed to privatization of public sector enterprises, as well as to trade policy and business climate reforms."

Statement by Jafar Mojarrad, Executive Director for Pakistan and Shahid Mahmood, Senior Advisor to Executive Director
March 27, 2015

Our Pakistani authorities thank staff for their hard work and quality discussions during the Sixth Review under the Extended Arrangement, and management and the Executive Board for their continued support.

Despite the challenging circumstances, program implementation has been strong. All end-December performance criteria and structural benchmarks, and the indicative target on transfers under the Benazir Income Support Program (BISP) have been met. The sole exception was the indicative target on tax revenue, which has not been met but, as highlighted below, significant steps have been taken to address the shortfalls, and the Federal Board of Revenue (FBR) is well-positioned to meet the end-March 2015 indicative target. The authorities have also shown strong resolve and commitment in carrying forward the reforms in energy sector, taxation, public debt management, and business climate. Monetary and exchange rate policies remain focused on containing inflation and strengthening foreign exchange reserve buffers. The authorities intend to stay the course in implementing their reform agenda notwithstanding potential headwinds from political and legal challenges.

Recent Economic Developments and Outlook

The macroeconomic landscape is improving with most of the indicators showing positive performance. Despite the difficulties faced during the early part of the current fiscal year as a result of floods, security-related operations, and legal challenges to privatization, taxation, and energy sector reform, the economy has shown resilience and is expected to strengthen further in FY 2014/15. While the authorities aim at achieving real GDP growth of 5.1 percent, they have retained the staff's conservative growth projection of 4.3 percent for program purposes. The oil price factor has had a particularly salutary effect on the economy by lessening pressure on the external sector. Headline inflation has fallen significantly, and is expected to reach 6 percent on average this fiscal year, reflecting prudent macroeconomic policies helped by the fall in commodity prices. Remittances continue to post strong growth, helping maintain the current account deficit at 1.2 percent of GDP even with a relatively weak export performance due to lower cotton prices. The recent international Sukuk issue has been well received by investors, reflecting improved confidence and contributing to further strengthening of reserves.

Fiscal Policy

The authorities have continued with fiscal consolidation. They reduced the budget deficit (excluding grants) from 8.3 percent of GDP in FY 2012/13 to 5.5 percent last fiscal year and aim to achieve the program target of 4.8 percent in FY 2014/15. They remain committed to bringing the deficit to around 3½ percent by the completion of the three-year program to put public debt-to-GDP ratio on a firm declining trend. To this effect, the draft budget for FY 2015/16, to be submitted to the Parliament, will seek to achieve a fiscal deficit of no more than 4 percent of GDP (excluding grants). While expenditures were restrained in 2014 to maintain the budget deficit below the end-December PC, much of the consolidation effort is focused on broadening the tax base, improving tax collection, and strengthening tax administration. Tax collection for end-December has been lower than targeted, owing to legal challenges to imposition of Gas Infrastructure Development Cess (GIDC) and lower tax receipts from the fall in oil prices, but the authorities took a number of compensatory measures. First, as oil prices started falling, affecting energy taxes, the authorities increased GST rate on petroleum products from 17 percent to 22 percent and then to 27 percent. Second, additional revenue measures were introduced at the federal level to meet the shortfall, including levying regulatory duties on a number of products, and increasing the withholding tax on non-filer service providers and importers (MEFP ¶16).

Building on earlier efforts, progress has been made toward eliminating tax concessions, exemptions, and loopholes. The FBR has granted no new tax concessions or exemptions through Statutory Regulatory Orders (SROs), and the authorities are preparing draft legislation by end-March 2015 (structural benchmark) to permanently prohibit the issuance of SROs. This alone is expected to boost revenue by 1-1 ½ percent of GDP over the program period. Stepped-up efforts have been made to improve tax collection and enforcement, including issuing first-time tax notices in excess of the end-2014 target (MEFP ¶18), initiating collection schemes for large and small retailers, and improving FBR's IT infrastructure. In this regard, a landmark measure to bring a larger number of taxpayers into the tax net is the announced merger of the existing database of 3.6 million individuals holding the National Tax Number (NTN) with the Computerized National Identity Card (CNIC) database, comprising 150 million.

The authorities are seizing the opportunity of the drop in oil prices to further reduce energy subsidies and rationalize the energy market. An additional surcharge of PRs 0.60/kWh was introduced effective January 1, 2015 and new electricity tariffs are being applied from February 2015, which will help bring down the energy subsidy cost to below 0.7 percent of GDP at the end of this fiscal year.

Support to the most vulnerable segments of the population through the BISP as continued, and the indicative targets for transfer payments for end-September and end-December 2014 have been achieved. The BISP coverage is expected to expand to 5.0 million by end-June 2015, and new banking contracts will be signed to phase in more effective payment cards. The authorities have also made significant progress in the rollout of the education-conditional cash transfers, as the program was expanded from five pilot districts to 32 districts in all provinces.

Public Debt Management

The authorities have made efforts to improve the quality and effectiveness of public debt management by lengthening the debt profile and reducing the cost of borrowing, together with the planned fiscal consolidation, to ensure that the downward trend will be sustained. To deepen this reform, work on an updated Medium-Term Debt Strategy (MTDS) for the period FY 2014/15–FY 2018/19 has begun and the results will be published in September 2015. As indicated during the Fifth Review, the Debt Policy Coordination Office is being strengthened by enhancing its human resource capacities and revamping its structure (MEFP ¶23).

Monetary and Exchange Rate Policies

All monetary program targets for end-December have been comfortably met, reflecting prudent fiscal and monetary policies. Accumulation of foreign reserves remained robust with a billion dollar Sukuk issuance and spot purchases by the State Bank of Pakistan (SBP) for the quarter ending December 2014. The SBP reserves now exceed US$11 billion, recovering from a precariously low level a year ago, and reserve coverage is expected to be above three months of imports by the end of this fiscal year. To further enhance resilience to external shocks, the authorities have agreed to increase reserve targets for end-March and end-June 2015, as indicated in the report. Headline and core inflation have remained on a declining path, paving the way for a policy rate cut of 100 bps in January 2015. Our authorities are committed to adhering to the NDA and NIR targets, improving the interest rate corridor, and maintaining interest rates in line with a stable inflation path.

Enhancing central bank independence remains a key priority. Following the earlier submission of amendments of the SBP Act to the Assembly, the authorities will submit a revised draft law incorporating IMF staff comments. The legislation, which is expected to be enacted in June 2015, will strengthen the SBP’s operational independence, its governance structure and financial autonomy, as well as the personal autonomy of Board members. In the meantime, the SBP is taking steps to enhance its internal operations, as highlighted in MEFP ¶10.

Financial Sector

Pakistan's banking sector remains sound with high profitability and solvency ratios. Asset quality improved with a decline in NPL ratio to 12.3 percent and the ratio of net NPLs to net loans falling to 2.7 percent as of end-December 2014. The Capital Adequacy Ratio increased to 17.1 percent on average, and the number of CAR non-compliant banks was reduced from three to two. Of the two banks, one is close to meeting the CAR requirement of 10 percent (presently at 9.41 percent) and the remaining one has been placed under moratorium for six months and is being considered for restructuring or amalgamation with another bank.

Concerted work is also being done to carry out financial sector reforms through administrative and legislative means. The current focus is on: draft Securities Bill; Corporate Restructuring Companies Act; draft Deposit Protection Fund Act; draft Credit Bureaus Act; and detailed guidelines for effective supervision of financial conglomerates.

The authorities have brought necessary amendments to remove deficiencies in the AML/CFT regime. In recognition of this, in February 2015, the Financial Action Task Force (FATF) removed Pakistan from the list of jurisdictions which have strategic AML/CFT deficiencies. The authorities are committed to adopting amendments to the Anti-Money Laundering Act (AMLA), to include serious tax crimes from the relevant tax laws, in line with international standards, by end-September 2015 (structural benchmark).

Structural Reforms

Restructuring and privatization of PSEs remain important elements of the authorities' plan to strengthen efficiency. Energy sector reforms aim at improving the performance of distribution and generation companies, reducing subsidies, eliminating arrears, and improving energy supply. The process of privatization of these entities has also been initiated. Similarly, restructuring of Pakistan Steel and Pakistan Railways, and processes for privatization of Pakistan International Airlines through a strategic investor sale of 26 percent of shares, have been initiated. Stepped-up efforts have been made to improve the business climate, including the opening of an online one-stop shop to facilitate business registration and tax filing. Work is underway to improve access to finance for the poor and women.

Conclusion

Pakistan's strong performance since the last review attests to our authorities' commitment to bring a wholesome change to improve the overall macroeconomic situation. It is in this context that the authorities have agreed on four new structural benchmarks during the sixth review. This leaves no doubt about the authorities' firm commitment to the program, and their determination to continue the fruitful cooperation with the Fund and development partners.