BUSINESS RECORDER
Founded by M.A. Zuberi

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Off to a slow start

Even though the FY2018-19 is now history, its full details are continuing to trickle down, and some of these have major implications for the new fiscal year. In this article we would review these new details and find out how they would affect the outcomes for the current fiscal year.

The data for large scale manufacturing (LSM) is now out for the 11-month period, Jul-May. It shows the production has declined by 3.8%. The declining trend has been steady with the exception of few months. Furthermore, with the exception of fertilizer and electronics, which have a share of 4.4% and 2.79%, and which have shown growth of 6.31% and 18.2%, all other sectors have suffered decline, some quite hefty. Automobiles (11.20%), Iron and steel (10.78%), petroleum products (7.13%), food and beverages (7.07%), pharmaceuticals (6.97%), cement (3.89%), chemicals (3.85%), paper & board (3.43%) and textiles (0.32%) are the main industries whose production has declined to the extent indicated in the parenthesis. Some of these declines are particularly concerning. Iron and steel (10.78%) coupled with cement (3.89) represents a challenge for construction and real estate sectors. Automobiles production is down significantly which has implication for employment. The decline in petroleum products of 7% is also significant and points toward a general slow-down.

The above picture of LSM when combined with agriculture where the last main crop of wheat is also short reflects that the revised GDP growth of 3.3% would finally turn out to be less.

The more interesting questions arise when we review the fiscal outcomes and their likely impact for the current year. The revised estimates of FBR revenues were shown to be Rs 4150 billion whereas the final figure has come out to be Rs 3820 billion, showing a shortfall of Rs 330 billion. On the other hand, the non-tax revenue was budgeted at Rs 772 billion but was revised to Rs 638 billion. As against this the first nine-month collection is only Rs 369 billion, leaving Rs 329 to be collected in the last quarter. In all likelihood such a high collection in the last quarter is impossible. But even if we allow the exceptional growth of about Rs 240 billion seen during 2017-18 in the last quarter, there would still be a shortfall of Rs 89 billion in non-tax revenues. Adding this to tax revenue shortfall of Rs 330 billion, gives an overall shortfall in total revenues of Rs 419 billion.

On the expenditure side, the biggest over-run would be on the interest payments. The revised budget has estimated it at Rs 1987 billion. Analysts estimate that a minimum Rs 200 billion would be added to the interest costs or roughly Rs 2200 billion. Adding this to the revenue shortfall of Rs 419 billion gives the total as Rs 619 billion or 1.6% of GDP. This would mean that the fiscal deficit for 2018-19 which was reported at 7.2% at the time of budget, is likely to be 8.8%.

What does this mean for the current year? First, the revenue collection target for FY20 would require an increase of Rs 1735 billion from the base rather than Rs 1400 billion which was estimated earlier. Second, the increased deficit of 8.8% as against 7.2%, would mean the primary deficit would be 3.1% (since interest payments are 5.7%) as opposed to 1.8% estimated by IMF in the program documents. This is a much larger adjustment that would be entailed if our numbers are finally borne out. There is also a discrepancy in the tax effort pointed out in the staff report and what was stated by the MOS-Revenues in the budget speech. As opposed to his claim that the tax effort was Rs 510 billion, the report shows it to be Rs 750 billion. This is a glaring difference and some explanation should be issued by the government so that a correct assessment is made and revenue measures are properly understood.

With massive fiscal imbalances it is not surprising that the public debt accumulation has been unprecedented. The central government debt, reported by SBP, as on 31-5-2019 was Rs 29.8 trillion. As against this, the debt was Rs 24.2 trillion as on 30-6-2018. This means that in the eleven months there has been an accumulation of Rs 5.6 trillion. The external debt for the same periods was Rs 10.0 trillion and Rs 7.8 trillion, implying an addition of Rs 2.2 trillion. This additionality includes the capital loss in the value of foreign debt denominated in rupee due to major devaluation of by more than 40% during the year. Even in eleven months, the increase in debt is highest ever in a single year.

The revenue collection performance of the first 20 days of July has been published in a news report. Reportedly, Rs 181 billion has been collected. What is the required performance during the month of July? There are different targets that can be set. Reportedly, FBR has set the target of Rs 310 billion. This means in the remaining 11 days of July Rs 129 billion has to be collected, which FBR reportedly is confident to achieve.

Under the IMF program, Q1 tax collections are required to be Rs 1067 billion. Based on this, the monthly target comes to Rs 356 billion. Relative to this target, in the next eleven days Rs 175 billions has to be collected. Which is a formidable task. Even when we take a more simple target of matching the same growth as implicit in the Q1 vs Q1 of the previous year, the required growth is 32%. Last year in July, Rs 251 billion was collection. At a growth rate of 32%, this gives a target of Rs 331. With respect to this target, Rs 150 billion would have to be collected in the next eleven days.

What the above analysis shows is the difficulties that are already visible in the tax collection efforts. Under the circumstances, it is imperative that the Government resolves tax issues that continue to remain contentious with the taxpayers, such as the requirement of CNIC for small purchases or with the unregistered customers.

The stock market has shown poor reception to the new fiscal year. Since July 3, when the IMF program was approved by the Executive Board, the stock market has mostly lost significant amount of its value. During this period, the market has lost close to 3000 points or 9% of the index. This has been aggravated by the policy rate increase by the SBP. With fabulous returns on fixed income securities, it is meaningless to expect investors would look toward stock market and investments to revive in the economy. Without being despondent, let it be said that the promised and expected upside of the Fund program is difficult to discern anywhere in the economy.

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