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- EDITORIALS

Budget-II for 2018-19

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One of the first priorities of the elected government must be to formulate and obtain parliamentary approval for a revised budget 2018-19 given that the budgeted revenue sources and expenditure allocations contained in the Abbasi-led administration's budget announced on 27 April 2018 are grossly unrealistic leading to a widening of the deficit with each passing day. This is borne out by the statement of the caretaker Finance Minister that the deficit was 6.1 percent on 12 June 2018; however, she refrained from speculating as to what it would be by the end of the month. Informed Finance Ministry sources have told *Business Recorder* that if the deficit is 7.5 percent by end June 2018 - or in effect 1.4 percentage points higher after merely 18 days - a level regarded as unsustainable by economists, then there would be a measure of comfort in the Ministry indicating that the actual deficit is projected as even higher.

Unfortunately, the newly-installed government neither has the luxury of time, the budget formulation is usually a four- to five-month exercise, nor knowledge of the true state of the economy given the extent of data manipulation. To add to the extremely challenging task is a current account deficit in excess of 18 billion dollars, eroding foreign exchange reserves (at present not enough to cover two months of imports) and the need to generate at least 10 billion dollars from external sources (multilaterals/bilaterals/commercial bank borrowing/debt equity though issuance of Eurobonds or sukuk) in the very short-term to keep from defaulting. The options are getting increasingly limited and the critical question facing the new government is how much expenditure can it slash - current and development - and how to begin the process of making the tax structure more equitable, fair and less anomalous?

Apart from gross data manipulation, the Abbasi-led government made three major errors in the assumptions it made in the 2018-19 budget. First, that reducing income taxes across the board, given the extremely narrow income tax base, would fuel growth which in turn would raise revenue collections. In Pakistan, there is no evidence of a linkage between growth and higher tax collections. During the past five years, total collections rose due to: (i) heavier reliance on withholding taxes in the sales tax mode but crediting it as income tax accounting for up to 80 percent of all direct tax collections. Income taxpayers whose tax was already deducted at source were being taxed as and when they procured goods and services; (ii) diverting revenue from non-tax sources to other taxes, including petroleum levy, natural gas development surcharge, gas infrastructure development cess amounting to in excess of 400 billion rupees in the current fiscal year; and (iii) taxes are levied on the basis of ease of collection which accounts for heavy taxes on petroleum and products as well as electricity which explains the cost differential in terms of cost of basic inputs, energy and transport, between manufacturing in Pakistan and regional countries.

Thus the budgeted rise in revenue collections of 17.9 percent over the revised estimates of 2017-18 are grossly unrealistic, burden the existing taxpayer and make our products uncompetitive in foreign markets as well as domestically given our huge porous borders where smuggling remains largely unchecked. It is imperative that an effort be made to make the tax structure fair which requires mandatory filing, without allowing a legal way out not to file, and all tax exemptions must end as they provide a non-level playing field.

Secondly, expenditure priorities by the Abbasi-led government are baffling to say the least, for example, 230 billion rupees were budgeted to be generated through self-financing by corporations/authorities for a 1 trillion rupee Public Sector Development Programme. Miftah Ismail who hails from a parched Karachi did not allocate a single rupee for clean drinking water for all and made no attempt to curtail the current expenditure but, instead, increased it by a whopping 27 percent over the budgeted estimates for 2017-18 and 11.2 percent over the revised estimates of last year.

And finally, the PML-N administration massively increased reliance on expensive foreign loans (from the foreign commercial banking sector). Granted that the country cannot default on foreign loans yet no attempt was made to reduce current expenditure on other sectors. It is critical for the next government to engage and negotiate with all sectors of the economy, including defence and civil administration, and form a consensus on reducing their annual budgeted allocations for the current year. Failure to do so would place a burden on the common man that would be simply untenable and may lead to widespread protests.

The measures that are required to be put in place as far as the FBR is concerned are medium to long-term as initially the new government would have to remain engaged in fire fighting focusing on accessing funds from cheap sources; or in other words, it appears to be a foregone conclusion that negotiations for yet another IMF package would begin soon and the conditions would be particularly harsh on the common man till of course the appropriate reforms can be implemented. However, one would hope that the new government does not agree to what the IMF supported in its last programme (September 2013-16) notably focusing on raising revenue rather than on reforming the tax structure.

To conclude, to attain macroeconomic stability would be no easy task and the rest of the 11 months of the current year would have to focus on fire fighting measures which if effective would then allow the government to bring in some of its election promises to fruition in fiscal year 2019-20.

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