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- MISCELLANEOUS

A case of twin deficit

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The fiscal numbers are getting out of the bound. The consolidated deficit stood at 4.3 percent of GDP in three quarters of the current fiscal year, eluding any chance of meeting revised full year target of 5.5 percent of GDP – the budgeted deficit was mere 4.1 percent.

The average deficit of fourth quarter stood at 1.7 percent of GDP in the past four years of PMLN and it was 3.5 percent of GDP in last year of the previous regime. Given this, it's safe to assume that the deficit would be at least 2.0 percent in the last quarter; implying a full year toll at 6.1 percent of GDP – highest fiscal deficit in any year of PMLN government.

The current account deficit is standing at annualized 5.3 percent of GDP in 10FY18, which is highest in the regime too. Thus, the slippages in twin deficits sum the good governance of PMLN, which promised to correct the macroeconomic imbalances; rather the economy is passing on to new government not any different from what the incumbents inherited.

Seeing such high deficits, the new government would have no choice to run stabilisation policies by bringing austerity measures with or without IMF. This is the brief summary of deficits next government to inherit; let's delve into the details of fiscal operations in 9MFY18.

There is not much wrong on the revenue side as tax revenues increased by 16 percent in 9MFY18. Growth dominated within the indirect taxation – sales tax collection increases by 17 percent while the custom duties jumped by 25 percent.

On quarterly basis, third quarter tax collection slowed down relative to the numbers in the second quarter, barring excise duty; every head experienced a decline in Jan-Mar; depicting signs of economic slowdown.

In days of high expenditure, the efforts should have been on enhancing non-tax revenues. PMLN concentration lately is more on salvaging its political image; in this quest, economy is put at the back burner. The non-tax revenues tanked significantly both from previous quarter numbers and year on year. In 9MFY18, the non-tax revenues are down by 3 percent. One drawback this year is that there are no CSF flows; barring that, the non-tax revenues increased by 16 percent in 9MFY18.

The real problem is in expenditures where no austerity is visible. It is the election year, hence both current and development expenditure are on the rise. The party loyalists are getting portfolios and spending spree is visible everywhere. The concentration is on picking up development speed to cut all the ribbons by May end.

The total expenditure increased by 13 percent in 9MFY18. The spending speed really picked up in 3QFY18 as the toll increased by 14 percent over previous quarter, and year on year increase is at mammoth 22 percent. The debt servicing is growing and that is creating a vicious cycle.

The story of development expenditure is no different as the cost increases when the projects are expedited. The spending is up by 27 percent in 9M and the growth is doubled to 56 percent in 3Q.

This is the fiscal story where the expenditures are taking priority and higher deficit is an eventuality. The external deficit financing is more than double in 9MFY18, which is not a good sign. And lately, the external funding is hard to come by; financing reliance is coming back on domestic banking sources.

The domestic bank financing stood at Rs481 billion in 3QFY18, which is highest quarterly increase in this government tenure. It's likely to pick further in the 4QFY18. Yes, it's inflationary, and it crowds out private investment.

The core inflation reached 7 percent in April 2018. Seeing the deficit woes; the hawks should be awakening on Friday's monetary policy announcement. More on this tomorrow.