INTERNATIONAL MONETARY FUND

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PAKISTAN

December 2014

FOURTH AND FIFTH REVIEWS UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRIETERIA—STAFF REPORT; STAFF SUPPLEMENT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR PAKISTAN

In the context of the Fourth and Fifth Reviews Under the Extended Arrangement and Request for Waivers of Nonobservance of Performance Criteria, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 17, 2014, following discussions that ended on November 8, 2014, 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 December 2, 2014
- A **Staff Supplement** of December 11, 2014 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

December 2, 2014

FOURTH AND FIFTH REVIEWS UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR WAIVERS OF NONOBSERVANCE 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 third review was completed on June 27, 2014, with a total of SDR 1,440 million disbursed. Fifth and sixth tranches totaling of SDR 720 million will be available upon the completion of this review.

Status of the program: The program is broadly on track. Two quantitative performance criteria (PCs) for end-June were missed (on Net Domestic Assets—NDA—and government borrowing from the State Bank of Pakistan—SBP). For end-September, three PCs were missed (on Net International Reserves (NIR), NDA, and government borrowing from the SBP); however, corrective measures have been taken through prior actions on government borrowing and NDA, and other policy steps to put the authorities on track to meet end-December targets. Of the seven actions covered by structural benchmarks (SBs) pending since completion of the third review, four have been completed and another partially met, while the others are being rephased. In addition, five new structural benchmarks and one new indicative target on net revenues by the Federal Board of Revenue (FBR) are proposed.

Key issues: Particular attention was given to: (i) reviewing fiscal performance and measures in the FY2014/15 budget; (ii) measures to bring NDA within program targets, while accommodating an acceleration of private sector credit growth; (iii) steps to bring government borrowing from the SBP back within program parameters; (iv) challenges on the balance of payments and efforts to address external vulnerabilities and boost reserves; (v) progress with broadening the tax base and improving tax administration; (vi) ongoing efforts to safeguard financial stability; and (vii) structural reforms in the energy sector, central bank independence, public debt management, anti-money laundering framework enhancement, trade, and the business climate. The mission retained its FY2014/15 growth forecast. Downside risks to the outlook remain due to recent floods and security and political concerns. Any slippages in implementing key policy reforms could also damage growth prospects and undermine progress in macroeconomic stabilization. Outreach activities (organized with assistance from COM) 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 October 29–November 8, 2014. Staff representatives comprised J. Franks (head), F. Salman, A. Shahmoradi, B. Baltabaev (all MCD), K. Al-Saeed (MCM), C. Tovar (SPR), S. Cevik (FAD), and H. Zaidi (Resident Representative Office, Islamabad). C. El Khoury (LEG) and W. Amr (COM) also participated in some discussions. A. Jbili (Senior Advisor, OED) joined the mission. M. Orihuela-Quintanilla and Y. Liu assisted in the preparation of the report. The mission chief issued a press release in Dubai on November 8, 2014.

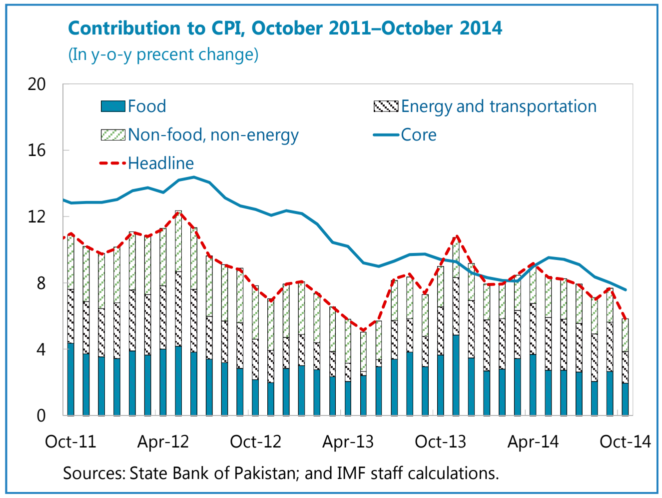
CONTENTS

TABLES

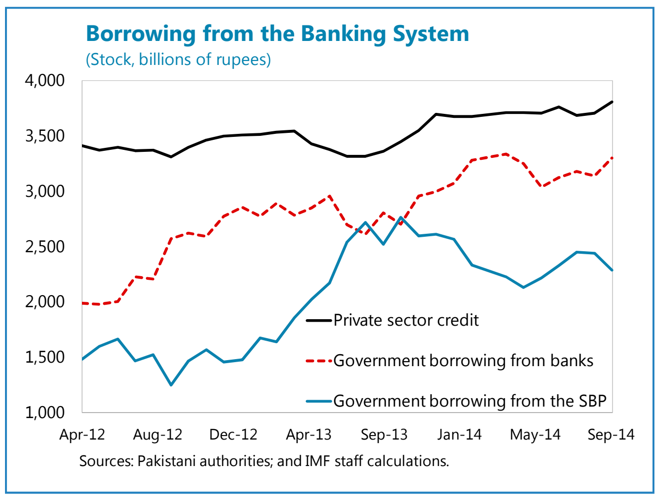
APPENDIX

INTRODUCTION

1. **Program performance was strong through the third review, but political difficulties contributed to weaker results more recently**. Demonstrations in Islamabad hampered the government's operations in August–September. Security conditions have also remained difficult due to ongoing military operations against the Pakistani Taliban, which have created a large number of internally displaced persons. Recent flooding heightened pressure on the government to relax adjustment policies. Judicial challenges to privatization, tax, and energy tariff measures have also slowed reform momentum. However, the authorities have recommitted to achieving their program targets, and have begun to address policy shortfalls.



2. **Economic activity has faced some headwinds, but growth should remain around 4 percent in FY2014/15.**[1] Provisional estimates suggest that in FY2013/14 the economy expanded by 4.1 percent driven by the manufacturing and services sectors, though that number may be revised downward.[2] Recent floods and political uncertainties are likely to depress agricultural output and may have dented confidence, but initial estimates suggest that the impact will be small and private credit growth has remained strong.[3] The balance of payments has worsened somewhat in recent months, with export growth slipping and the financial account weakening. This contributed to a slight drop in foreign reserves to US$8.9 billion by end-September. Despite a depreciation of the Rupee by 4 percent over the past quarter, the real effective exchange rate has appreciated 6 percent since the start of the program.



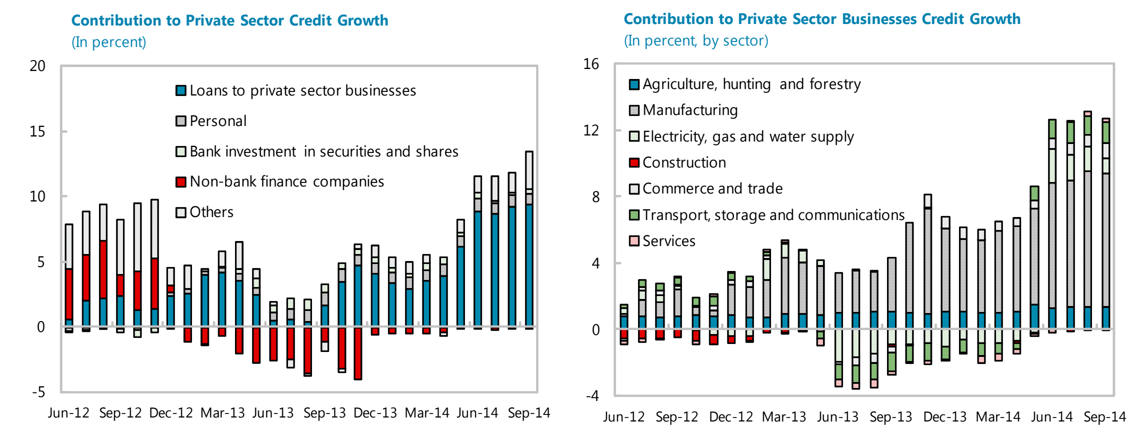
[1] Pakistan's financial year runs from July 1–June 30.

[2] Revised figures for FY2013/14 should be available in May 2015.

[3] The recent 2014 floods were less severe than the 2010 floods and the possible impact on GDP growth is estimated between 0.2 to 0.3 percentage points.

Headline inflation eased to 5.8 percent year-on-year (y-o-y) in October, with core inflation also falling (to 7.6 percent).

3. **Financial indicators continued to strengthen as of end-September 2014**. Credit growth, mainly in the manufacturing, power and utility, and transportation sectors, reached 13.4 percent, reflecting declining SBP fiscal financing, easing structural bottlenecks, and NFA growth. Banks' profitability improved due to higher net interest income, lower provision charges, and higher noninterest income. The nonperforming loan (NPL) ratio increased marginally to 13 percent and the capital adequacy ratio (CAR) increased to 15.5 percent, well-above the minimum requirement of 10 percent.



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

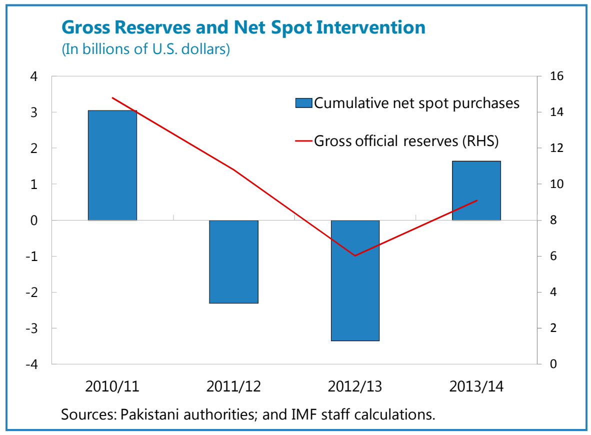
4. **Two end-June and three end-September PCs were missed and progress on Structural Benchmarks (SBs) has been uneven**. Three of the seven SBs pending since completion of the Third review were met, a fourth was completed in November, and actions for the fifth were partially completed. Specifically:

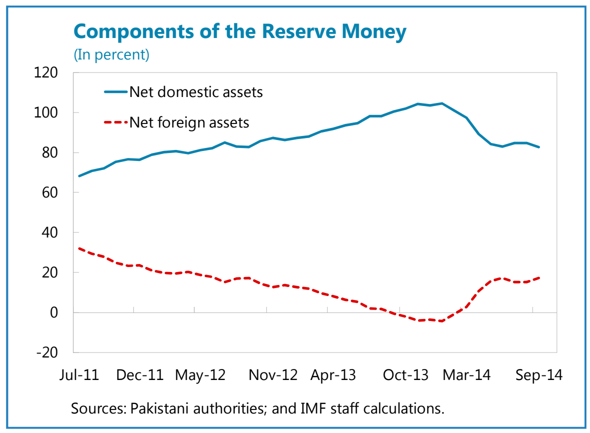
- **Federal government deficit and social spending**. The budget deficit excluding grants narrowed from 8.3 percent of GDP in FY 2012/13 to 5.5 percent in FY2013/14,[4] overperforming on the end-June PC. The end-September 2014 PCs was also met, as tax revenues came in line with projections and shortfalls (due to higher electricity subsidies and lower Gas Infrastructure Development Cess, GIDC, collections) were compensated by restraining capital expenditures. The indicative targets on cash transfers under the Benazir Income Support Program (BISP) for end-June and end-September were also met.

[4] Including grants, the overall budget deficit narrowed from 8.1 percent of GDP in 2012/13 to 4.7 percent of GDP in 2013/14.

- **Government borrowing**. The authorities missed the end-June and end-September targets on government borrowing from the SBP (by PRs 88 billion and PRs 219 billion, respectively) due to lower domestic debt issuance, delays in privatization transactions and issuance of Sukuk securities, and weak debt management.

- **Net international reserves and net swaps/forward position**. The end-June NIR target was comfortably met (by over US$1.6 billion). However, the end-September target was missed by US$630 million due to the delays in privatization emerging from political uncertainty, and in spite of SBP's purchases of US$429 million in the foreign exchange spot market. The SBP met the targets on its net short swap/forward position for both end-June and end-September.





- **Net Domestic Assets**. The authorities missed both the end-June and end-September NDA targets, reflecting government overborrowing from the SBP, and insufficient open market operations to sterilize spot foreign exchange purchases.[5]

- **Structural benchmarks**:

  - **Debt management** (MEFP ¶20). The authorities have issued an order on consolidating debt management functions (SB for end-September), but it fell short of what had been envisaged. They also appointed a director to the Debt Policy Coordination Office (DPCO).

  - **Anti-Money Laundering (AML) framework** (MEFP ¶18). The SB on amending the relevant tax laws and submitting the AML Act to the National Assembly (NA) was missed as additional coordination was required with Fund staff.

[5] NDA exceeded the ceiling by PRs 151 billion at end-June and by PRs 25 billion at end-September.

- **SBP independence** (MEFP ¶6). The SBP met the end-August benchmark on improving internal operations and adopted International Financial Reporting Standards (IFRS) as its financial reporting framework. But the authorities missed the end-June SB on central bank independence legislation, which is still pending in the NA committee and does not yet fully incorporate the recommendations of the Safeguards Assessment Report.

- **Energy sector reforms** (MEFP ¶27–34). Due to political difficulties, the targeted 7 percent electricity price increase was not implemented on July 1, despite its notification in June as a prior action for the Third review. As the political landscape has normalized and fuel prices declined, a 2.5 percent increase was instituted effective October 1, 2014 and further adjustments will take place in the coming months. The planned increase in the GIDC has been collected but has not been remitted so far due to repeated court challenges. Supply side and revenue management reforms continue and the appointment of a chairman of the power regulatory body (NEPRA) was finalized in November.

- **Privatization** (MEFP ¶37). The government completed minority share sales of United Bank Limited (UBL) and Pakistan Petroleum Limited (PPL) in June 2014 (SB) raising over $500 million in revenues. The authorities had intended to sell additional shares in OGDCL, but postponed the offer in light of adverse world energy market developments. The hiring of financial advisors for Pakistan International Airlines (PIA), Faisalabad Electric Supply Company (FESCO) and Northern Power Generation Company Limited (NPGCL) was completed in July 2014. The hiring of financial advisors for Allied Bank Limited (ABL) and Habib Bank Limited (HBL) were finalized in November.

MACROECONOMIC OUTLOOK AND RISKS

5. **The program's macroeconomic framework was maintained**. Recent floods and political uncertainties pose downside risk to growth and inflation outlook this year, but their impact is assessed to be small and should be offset by declining oil prices.

- Growth is expected to rise to around 5 percent in the medium-term due to easing fiscal adjustment and improvements in structural bottlenecks in the energy sector, public enterprises, and the investment climate.

- Average inflation is expected to ease to below 8 percent in FY2014/15 and fall further thereafter, as inflation expectations will be anchored by tight monetary policy and sustainable fiscal policy.

- Foreign exchange reserves are expected to exceed US$14 billion by end-June 2015—a coverage ratio of over three months of imports. The current account deficit is expected to widen to about 1½ percent of GDP, driven by stagnant exports while non-oil imports pick up. The sharp decline in world oil prices should help contain import growth.

Reserves accumulation will be supported by SBP intervention in the FX spot market, privatization proceeds, multilateral disbursements, and external private financing.

6. **Crisis risks have eased as program policies reduce macroeconomic imbalances, but downside risks to the growth outlook have grown since the last review**. Key risks include:

- *Slippages in policy implementation* could impede investment and weaken growth prospects, undermining progress in macro-stabilization.
- *Political and security conditi*ons remain challenging. Recent political unrest, terrorist threats with attendant military operations in the border region with Afghanistan, sectarian violence, and urban criminal activity all pose significant risks.
- *Recent floods* present additional downside risks to growth and fiscal performance.
- *External vulnerabilities* remain. Reserves levels and coverage ratios continue to be insufficient. Downside risks include weakened global economic conditions, which could impair exports and hurt remittances; and global financial volatility, which could make debt issuance more difficult and costly.
- *Sustained decline in oil prices* poses an upside risk, which may help ease balance of payments pressures and boost growth.

POLICY DEVELOPMENTS

A. Fiscal Policy

7. **The authorities remain committed to lowering the budget deficit to 4.8 percent of GDP in FY2014/15**, **and the review reached understandings about how to keep the fiscal program on track, but there are significant fiscal risks**. The delays in implementing the electricity tariff adjustment and pending court challenges against the GIDC have created potential shortfalls of 0.2 and 0.3 percent of GDP, respectively. There is also a risk that some of the tax measures approved in the FY2014/15 budget may yield less than originally envisaged, while the stock of General Sales Tax (GST) refund claims remains high at above PRs 135 billion.[6] Recent floods—albeit less severe in scale and intensity compared to the 2010 floods—have prompted additional spending in relief and rehabilitation efforts.[7]

[6] After reaching a peak of PRs 153.5 billion at the end of 2013, the flow of GST refund claims has been reversed and the stock has declined.

[7] The provincial government of Punjab has already allocated PRs 15 billion for flood relief, half of which is expected to be covered by the federal government.

8. **The authorities and staff reached understandings on measures to remain within program targets**. The authorities began implementing electricity price adjustments on October 1, 2014 and will continue in coming months (MEFP¶27). Furthermore, in the event that GIDC legal concerns are not resolved by January 2015, they will put in place specific compensatory measures on the revenue side yielding at least 0.3 percent of GDP (MEFP¶34). They will also maintain in reserve some 0.2 percent of GDP in extraordinary SBP profits from the privatization of public banks. The government will also continue to restrain expenditures in the first nine months of the fiscal year as a cushion against any revenue shortfall.

9. **The fiscal consolidation program hinges on broadening the tax base through the elimination of tax concessions and exemptions** (Box 1). The FY2014/15 budget eliminated a number of tax concessions and exemptions granted through Statutory Regulatory Orders (SROs), which are expected to yield about 0.3 percent of GDP. The government has also continued to refrain from issuing new SRO concessions or exemptions[8] and plans to remove most additional SROs over the next two years and to enact legislation to abolish the practice of granting tax concessions or exemptions through SROs in 2015. This will expand the tax base, simplify tax administration, and strengthen compliance, bringing a projected increase of 1–1½ percent of GDP in revenues.

10. **The authorities are pressing ahead with plans to improve tax administration** (MEFP ¶12–14). The FBR issued 139,110 first-time notices to potential taxpayers as of end-September 2014, ahead of the schedule for an eventual 300,000 notices. So far, 20,000 new individuals have registered and filed tax returns. At the same time, the authorities have launched a GST collection scheme for around 25,000 large retailers and over 1.3 million small retailers. The FBR is also making a greater use of information technology to broaden the tax base and to strengthen tax compliance by collecting data from multiple sources (such as property and motor vehicle transactions and international travel). In this context, to better manage tax compliance and enforcement, expansion of the FBR's information reporting processes and technologies by merging 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 is crucial.[9]

11. **Provincial governments remain crucial to the fiscal reform process, especially by improving revenue collection at the subnational level**. The most recent National Finance Commission (NFC) award granted 57.5 percent of the divisible pool of tax revenues to the provinces, up from 45 percent in 2007 and 37.5 percent in 1997. Although provincial governments are responsible for the delivery of a range of public goods and services, the mismatch between expenditure and revenue decentralization leaves the federal government with a chronic deficit. Furthermore, revenue effort at the province level is extremely low (generating only 7 percent of total

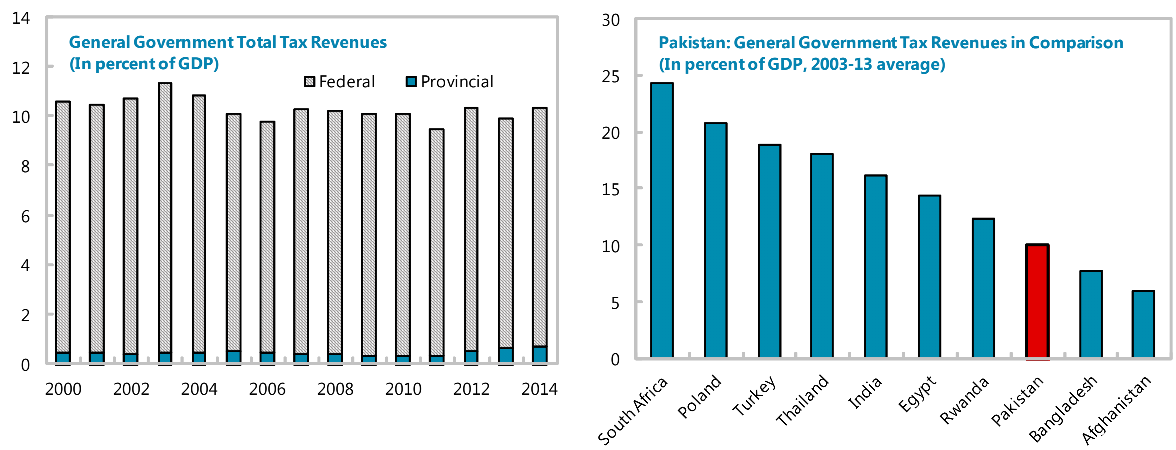
[8] The only exception was related to an emergency situation in basic food supply.

[9] Out of 3.6 million NTN-holders, only 890,000 file tax returns on a regular basis.

Box 1. Broadening the Tax Base

The tax-to-GDP ratio has hovered around 10 percent of GDP over the past decade, almost 5 percent of GDP below the average of peer countries. Previous attempts to raise the ratio have at best produced only temporary improvements. Most recently, the 2008 SBA included provisions to introduce a full-fledged VAT, but the program went off track in part because of the lack of political support. Political resistance to bold revenue reforms has also been an issue under the current program, although the authorities have taken some important initial steps. Tax revenues rose from 9.7 percent of GDP in 2012/13 to 10½ percent in 2013/14, and measures included in the current fiscal year budget are expected to raise tax revenues to around 11½ percent. Further improvement in tax collection towards the end-program target of 13 percent of GDP, however, will require a series of tax administration reforms, along with a rethinking of tax policies.

Pakistan: General Government Tax Revenues



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

Tax administration reforms will increase revenue collection and bring a fairer and more equitable tax system. Given the low level of tax compliance and widespread evasion, the FBR is implementing a strategy to address structural flaws in the tax system, improve tax administration, and induce behavioral change among taxpayers. In particular, the authorities have: (i) issued notices to potential taxpayers and provided incentives to tax compliance; (ii) initiated the tendering of electronic volume tracking of production to improve sales tax collection; (iii) started the field surveys of potential high net worth taxpayers to broaden both the sales and income tax bases; and (iv) implemented an IT solution for tax refunds (computerized risk-based evaluation of sales tax or CREST) that identifies discrepancies in sales tax invoices at different stages and imposes an effective control mechanism for fake invoices and inadmissible refunds. These steps are expected to expand the tax base and improve tax compliance. The FBR is also intensifying actions in auditing and enforcement, including to: (i) legally charge tax evaders; (ii) temporarily close businesses and/or attach properties of tax offenders; and (iii) attach bank accounts of tax defaulters to withdraw the assessed tax liability directly from their accounts. As part of the program, the authorities have now established quarterly FBR revenue targets to improve accountability and transparency in revenue administration.

tax revenues), despite the large tax base that falls under their purview—including income tax on agriculture and sales tax on services. While provincial governments have supported fiscal consolidation by maintaining budget surpluses, balancing the devolution of revenue and expenditure responsibilities is key to attaining sustainable intergovernmental fiscal relations. In this context, the authorities will expand the scope of the upcoming round of NFC deliberations to cover all areas of fiscal management and seek technical assistance from international partners to support this process. The critical issues for long-term fiscal sustainability across all layers of government are (i) revenue mobilization by federal and provincial governments in currently undertaxed areas, such agricultural, services, and property taxes; (ii) additional financing of high-priority expenditures such as education, health, and infrastructure , and (iii) robust public financial management, debt management and procurement systems.

12. **Increasing targeted social assistance to the poor remains a key component of the program**. The authorities met both the end-June and end-September 2014 indicative targets on cash transfers through the BISP, reaching over 4.6 million households. In 2014/15, the quarterly stipends paid through the BISP was increased by 25 percent to PRs 4,500 to address poverty and inequality concerns and protect the most vulnerable from the impact of energy price adjustments and fiscal consolidation.[10] Going forward, coverage of the BISP is expected to reach around 4.8 million beneficiaries by end-2014 and 5.3 million by end-June 2015. To ensure timely payment to beneficiaries, the e-payment contracts with commercial banks have been extended, and the authorities will launch new ATM cards following the completion of competitively selected e-banking options by end-June 2015, while addressing administrative concerns in BISP operations.

13. **The government has taken corrective actions to reduce its reliance on central bank financing**. Sukuk proceeds in December 2014, and a more rigorous system of monitoring of the sources of financing brought the level of government borrowing from the SBP in line with the program target. In addition, the authorities will adhere to the issuance plan for domestic public securities in future T-bill and Pakistan Investment Bond (PIB) auctions to build cash buffers.

14. **Strengthening public debt management remains a top priority** (MEFP ¶20). Establishing a sound organizational framework for public debt management, consistent with the recommendations of the Medium-Term Debt Strategy (MTDS), to diversify the sources of financing and to reduce reliance on central bank financing are essential. The authorities have made progress in lengthening the maturity profile and improving the balance between domestic and external debt. Although the government approved an administrative order to empower the DPCO, it fell short of unifying fragmented debt management functions (which constitute an obstacle for effective debt

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[10] In partnership with the provincial governments, the authorities have also made significant progress in rolling out the education conditional program of cash transfers, and expanded the program from five pilot districts to 32 districts in all provinces.

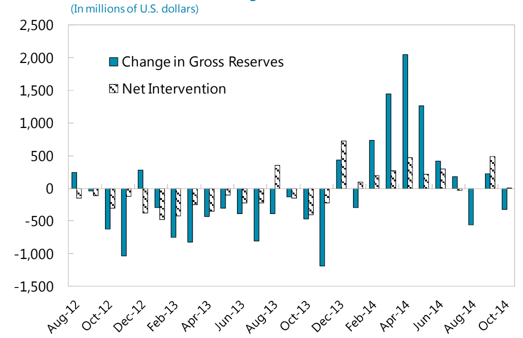
management). To this end, the authorities will: (i) provide Fund staff with a detailed financing plan for the coming 12 months (prior action) and extend the existing in-quarter issuance plan to a rolling monthly issuance program for the next three months for domestic public securities by end-November 2014; (ii) strengthen risk management and strategy functions by reorganizing the DPCO as a middle office coordinating the market risk management functions and subsequently move to credit risk management and operational risk management functions (new SB); (iii) build capacity by hiring and/or training additional staff with the help of international partners based on the September 2014 skills-gap analysis; (iv) take steps to strengthen front office management of debt issuance both in domestic and external markets by arranging a formal linkage with the DPCO and executing and communicating the borrowing plan with SBP being the agent, and strengthening the primary dealership system; and (v) draft the required rules under the Fiscal Responsibility and Debt Limitation Act 2005.

15. **Staff reiterated the importance of increased efforts to tackle tax evasion through use of the AML regime**. Staff stressed the necessity of enacting amendments to the relevant tax laws and submitting the AML Act (AMLA) to the NA for approval (SB proposed to be rescheduled to end-December 2014, MEFP ¶18). The enactment of the AMLA and its proper implementation will facilitate the detection of proceeds of tax crimes. The Financial Monitoring Unit has prepared draft guidance on the risks of abuse of the investment incentive scheme and will issue it by end-December 2014.

B. Monetary and Exchange Rate Policies

16. **While foreign exchange reserves have risen sharply under the program, efforts should continue to boost them well above three months' of imports**.[11] Foreign exchange market pressures have eased somewhat and concerns over an impending balance of payments crisis have receded. The SBP has recently stepped up spot market purchases of foreign exchange, which have netted some US$795 million so far this fiscal year as of end-November. This in staff's assessment puts the authorities on track to meet the end-December PC given other actions planned by the government (including an international sukuk and accelerating other privatization offers). The SBP is also on track to meet the end-December target on the stock of foreign exchange swap/forward contracts. Staff encouraged the authorities to further boost reserves by continuing to purchase foreign reserves and by allowing for greater exchange rate flexibility, while reducing reliance on one-off inflows (e.g., grants and privatization receipts).

Net Intervention and Change in Gross International Reserves
(In millions of U.S. dollars)



Sources: Pakistani authorities; and IMF staff calculations.

[11] Gross International Reserves are estimated to reach about US$11 billion by end-December 2014, consistent with the broader Reserve Adequacy (ARA) metric for Pakistan.

17. **The authorities have taken corrective actions to meet end-December targets on NDA and government borrowing from the SBP**. Sukuk proceeds will help the government to achieve program targets. Furthermore, the authorities will provide staff a monthly calendar of fiscal financing sources, including T-bill and PIB auctions, consistent with curtailing government borrowing from the SBP (MEFP¶19, 20). The stock of government borrowing has already been reduced to PRs 2,150 billion by end-November, bringing NDA to PRs 2,549 billion (meeting the prior actions). The SBP will develop and announce a time-bound plan to gradually improve its interest rate corridor by setting the policy rate between the floor and ceiling rates of the corridor to enhance the effectiveness of monetary policy, better manage liquidity in the interbank market, and conduct open market operations (new SB). The improved interest rate corridor will be made operational by end-September 2015.

18. **A prudent monetary policy stance should help anchor inflation expectations**. The SBP cut its policy rate by 50 b.p. in November (to 9.5 percent) in response to the improved inflation performance. The SBP remains committed to adjusting the policy interest rate in a forward-looking fashion to maintain positive real interest rates. This should help bring inflation sustainably below 7½ percent by end-June 2015 (MEFP ¶5). With core inflation still running at around 7½ percent, a neutral policy stance is appropriate going forward. The SBP will continue to use open market operations to sterilize spot market FX purchases as needed and to contain NDA within program targets.

19. **Enhanced central bank independence is key for an improved monetary policy framework**. The SB on central bank independence legislation has been delayed to end-June 2015 (proposed rescheduled SB). 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 continue working with the IMF and the NA committee to ensure that the final law incorporates the recommendations of the IMF safeguards assessment mission and Fund staff comments by end-March 2015. The law should strengthen the SBP's autonomy through (i) full operational independence in the pursuit of price stability as the primary objective, (ii) enhanced 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 monetary policy committee to design and monitor implementation.

20. **The SBP is taking further steps to enhance its operations**. While awaiting approval of the new legislation, the SBP will introduce additional measures to further improve internal operations. Specifically: (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 safeguard procedures, the Internal Audit Department will conduct reviews of the program monetary data reported to the IMF, within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff. (new SB, end-February 2015).

C. Financial Sector Policies

21. **Progress with capitalization of four banks below the minimum capital adequacy ratio (CAR) is satisfactory** (MEFP ¶22). The largest of the four banks is now in compliance with the regulatory minimum CAR of 10 percent due to improved profitability. The combined shortfall for the three remaining noncompliant banks (all private) has decreased to PRs 11.3 billion (less than 0.04 percent of GDP) as of end-September 2014. Staff stressed that SBP should closely monitor these banks' activities to ensure compliance with CAR by end-December 2014.[12]

22. **Staff supported the ongoing financial sector reforms to ensure financial stability**. The authorities are: (i) finalizing the draft legislation for the Deposit Protection Fund (DPF) in line with Fund staff advice by end-January 2015 for expected adoption by Parliament by end-June 2015; (ii) working to finalize the Corporate Restructuring Companies (CRC) Act to set up corporate restructuring frameworks to deal with bankruptcy issues; and (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) finalizing the draft Securities Bill after incorporating proposed amendments from stakeholders, and will take time to incorporate Fund staff advice (proposed rescheduled SB).

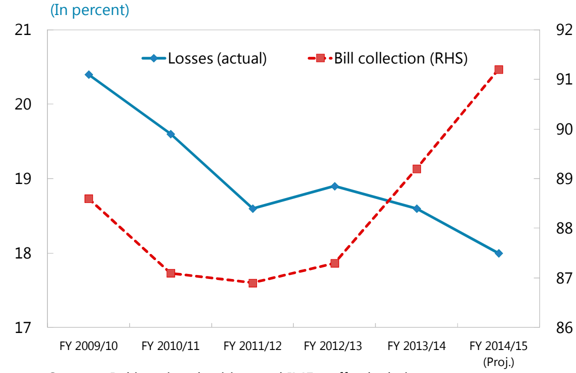
23. **The amendments to the Anti-Terrorism Ordinance of 2013 to bring it in line with the action plan agreed with the Financial Action Task Force (FATF) were enacted by the NA**. As a result, the FATF determined that Pakistan had substantially addressed its action plan at a technical level. Subject to the results of an onsite visit, Pakistan may be removed from the list of jurisdictions which have strategic AML/CFT deficiencies in February 2015.

D. Structural Issues

Energy

24. **The authorities are getting back on track to reduce electricity subsidies to 0.7 percent of GDP in FY2014/15** (MEFP ¶27). After delays in tariff increases in previous months, the authorities implemented a surcharge of PRs 0.30 from October 1, 2014 taking advantage of declining fuel prices. This adjustment implied an effective increase of 2.5 percent in electricity tariffs. The authorities are committed to make further adjustments in January and February to recover the remaining gap to reduce electricity subsidies to 0.7 percent of GDP for FY 2014/15, and limit the accumulation of circular debt.

Loss Reduction and Revenue Collection
(In percent)

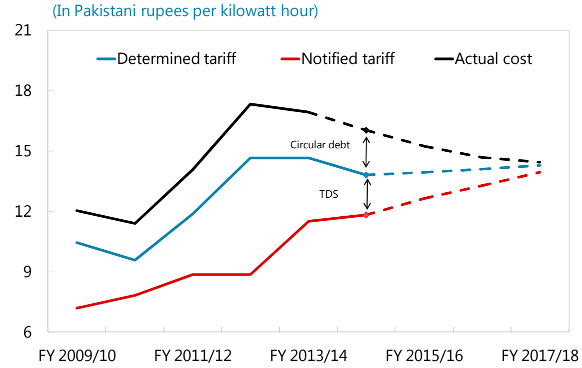


Sources: Pakistani authorities; and IMF staff calculations.

12 These banks comprise 2.7 percent of banking assets.

25. **The plan to reduce arrears in the electricity sector is progressing** (MEFP ¶28). Circular debt arrears in the power sector total nearly 2 percent of GDP and threaten the functioning of the power sector. The authorities' plan includes recovering receivables in the power sector, improving efficiency and collections, and using fiscal resources. Together with staff, the ADB, and the World Bank, the authorities have developed a monitoring system for circular debt, which will set the framework to establish a future indicative ceiling on arrears accumulation.[13] Any future government payoffs of circular debt should be strictly conditioned on accelerated energy sector reforms and on specific actions by firms and regulators to reverse arrears accumulation.

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



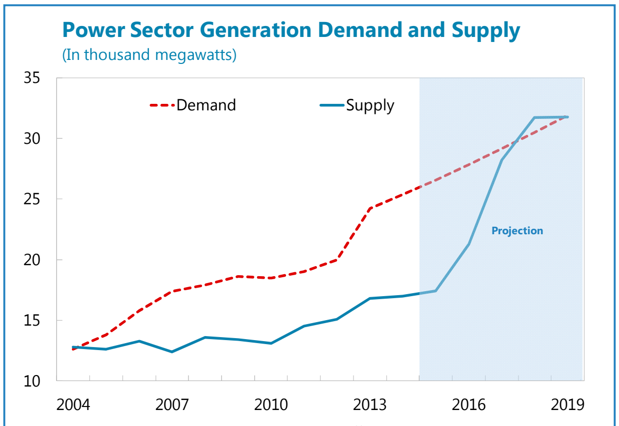
Sources: Pakistani authorities; and IMF staff calculations.

26. **Progress has continued on power sector regulatory and management reform for better functioning of the system** (MEFP ¶32). In an effort to strengthen the operations of NEPRA (the electricity sector regulator), the authorities have filled the vacancies at the NEPRA Board and the regulator is moving forward with preparations for a multi-year tariff framework. They also stepped up their efforts on monitoring, enforcement, and improvements in demand and supply management in the electricity sector (Box 2).

27. **Gas sector reforms are progressing to alleviate supply shortages and better allocate scarce gas** (MEFP ¶34). By January 2015, the authorities are committed to notifying new gas prices, which were postponed from August due to the political protests. Construction is nearing completion on a Liquefied Natural Gas (LNG) terminal which will increase total supply, with first LNG imports expected by early 2015. The authorities are 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. They will also complete the conversion of existing domestic gas concessions to new ones (under the 2012 Policy)—which will permit higher producer prices for additional production—by end-February 2015, and award additional 10-15 blocks in FY 2014/15 to increase exploration to help tackle the gas shortages.

[13] The World Bank (WB) has proposed a future ceiling on the stock of circular debt as part of the conditionality for its upcoming DPC2 energy sector loan. These numbers will be coordinated with the WB to ensure consistency.

Box 2. Energy Sector Reforms



Sources: Pakistani authorities; and IMF staff calculations.

Efforts are underway to begin to close the wide gap between supply and demand in the energy sector. Supply shortages stem from a lack of sufficient installed capacity to cover peak demand but also from the inability to keep installed plants running at peak output due to shortages of gas and of money to provide sufficient fuel oil in expensive oil-fired plants. There are also significant line losses in the distribution system due to inefficiencies and theft. In the short-run, the authorities continue to prioritize the use of gas and coal rather than fuel oil to reduce costs in the electricity generation. They are also working to rehabilitate generation plants, while upgrading electricity transmission and distribution facilities to reduce technical losses to further improve supply. The efficiency testing of fuel-based electricity generation companies and three rehabilitations (finalized last March) are expected to recover around 700 MW of capacity and increase efficiency by 1–1.5 percent. In the medium-term, the authorities will complete construction of an LNG terminal to ease gas shortages to increase electricity production, while also encouraging higher domestic gas production. They will also promote policies for private investment in 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. These expansions are expected to generate additional 2000 MW by 2016. Finally, in the longer-run they are launching the development of several major hydropower projects.

Public Sector Enterprises

28. **Staff noted progress in the privatization program, despite recent setbacks** (MEFP ¶37). While the recent offering of Oil and Gas Development Company Limited (OGDCL) was postponed in the wake of weak investor demand in an environment of sharply lower oil prices, the government is moving forward with the calendar starting with the National Power Construction Corporation (NPCC) which is due for end-March 2015. The program aims at offering and/or marketing at least one transaction in each quarter during the upcoming year (text table).

Timeline of the Privatization of PSEs			
	PSEs	Transaction	Timeline
1	Oil and Gas Development Company Limited (OGDCL)	Capital Market Transaction- GDRs/domestic sale of 7.5% shares (10 percent GoP shares)	End-December 2014
2	National Power Construction Corp. (NPCC)	Strategic & Asset Sale	End-March 2015
3	Allied Bank Limited (ABL)	Capital Market Transaction - Domestic sale of 10 percent GoP shares	End-January 2015
4	Habib Bank Limited (HBL)	Capital Market Transaction - GDRs for sale of 42 of HBL shares (100 percent GoP shares)	End-April 2015
5	Faisalabad Electric Supply Company (FESCO)	100 percent sell-out of strategic asset	End-August 2015
6	Northern Power Generation Company Limited (NPGCL)	100 percent sell-out of strategic asset	End-August 2015
7	Islamabad Electric Supply Company (IESCO)	100 percent sell-out of strategic asset	End-October2015
8	Lahore Electric Supply Company (LESCO)	Strategic & Asset Sale	End-October 2015

29. **Pakistan Steel Mills (PSM), Pakistan International Airlines (PIA), and Pakistan Railways (PR) are the major budgetary drains among PSEs**. The Expression of Interest for hiring of financial advisor for PSM was advertised in October 2014 and the authorities are on track to finalizing the hiring by end-December 2014. They will also complete the renewal of PR Board by end-December 2014. PR improved revenues by around 60 percent in FY 2013/14 and 20 percent in the first quarter of 2014/15, through rationalization of tariffs and expenditures and improved occupancy rates. They finalized a comprehensive restructuring plan for PR, which in the short-term will have a focus on improvements in freight transportation. The financial advisor for PIA was hired in July 2014 (structural benchmark) for potential offering to a strategic investor by end-December 2015 (proposed rescheduled SB).

Business Climate and Trade Policy

30. **Trade and doing business reforms are crucial to improve Pakistan's business climate**. Pakistan ranks 110 out of 189 economies on the Doing Business (DB) 2014 rankings, having lost 25 places in the past five years;[14] and 133 out of 148 economies on the WEF Global Competitiveness Rank, down 32 places in the past five years. For FY2014/15, the authorities have moved from eight import tariff slabs to six slabs by shifting most items currently at 30 and 35 percent to the 25 percent rate. Phase-out of trade related SRO's also began with this fiscal year. The elimination of most nontrade SROs which grant tax exemptions and concessions in the current fiscal year will also improve the business climate by helping to level the playing field across businesses. Based on the World Bank technical assistance (TA) mission on business climate, the authorities have produced a detailed implementation plan in October. The plan identified legislative and administrative actions, institutional roles and responsibilities, and resource requirements of the reform program. The plan focuses on six indicators—construction permits, paying taxes, enforcing contracts, starting

[14] "These indicators should be interpreted with caution due to a limited number of respondents, a limited geographical coverage, and standardized assumptions on business constraints and information availability."

businesses, trading across borders, and getting credit. Implementation has begun and the authorities will conduct a review to reduce the number of existing processes and forms of sales and income tax by end-March, 2015 (new SB).

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 establishment of end-December 2014 and end-March 2015 PCs**. On the basis of corrective actions taken (¶17), waivers are requested for the non-observance of the end-September 2014 PCs on the ceiling of the NDA, government borrowing from the SBP, and the NIR target. The authorities have completed two prior actions by end-November 2014 and are on track to meet the third prior action by December 10, 2014, five new structural benchmarks are proposed, and one structural benchmark is to be modified (Table 2). To support this request the authorities have taken corrective actions to address the missed PCs (as delineated above) and they are on track to meet the end-December targets.

32. **Financing program risks and capacity to repay the Fund**. There are no significant changes to the assessment provided at the time of the last review. Pakistan's financing needs are fully covered for the next 12-months and prospects remain good for the remainder of the program. Disbursements from multilateral partners have materialized and private external financing and privatization proceeds should also provide sufficient resources in FY2014/15. The Fund's exposure to Pakistan had fallen to roughly US$3 billion (34.6 percent of gross official reserves or 4.6 percent of total external debt) by end-September, 2014. However, it is expected to increase somewhat by end-December 2014 as new extended arrangement disbursements are made (Table 11). Pakistan's capacity to repay the Fund has marginally improved and net exposure has declined, reserves are rising but still remain low, and fiscal and balance of payment pressures continue to ease. Materialization of risks to the macroeconomic outlook could still erode repayment capacity (¶7).

STAFF APPRAISAL

33. **The threat of a crisis has receded due to the authorities' efforts to address the twin fiscal and balance of payments imbalances**. Significant progress has been made in the government's first 18-months to achieve macroeconomic stability. Foreign exchange reserves are recovering, and the net foreign exchange swap/forward position is declining. Fiscal consolidation is on track, and the government has begun to improve its debt financing by diversifying sources and lengthening maturities. Macroeconomic conditions are improving. GDP growth will remain around 4 percent this year, reflecting strong manufacturing output, lower world oil prices, and a less negative fiscal impulse. Headline and core inflation have declined recently, and a prudent monetary stance should keep it lower for the remainder of FY2014/15.

34. **Risks to the recovery remain, and much still needs to be done to make the economic transformation in Pakistan more sustainable**. The challenging domestic security environment and recent political uncertainties have dampened the investment climate and seem to have—at least temporarily—weakened the government resolve and ability to aggressively press its reform agenda. More consistent implementation will be needed if Pakistan is to break its longstanding pattern of half-completed reforms which contribute to periodic crises and a stop-go development process. While the recent sharp fall in world oil prices will provide much needed savings on the import bill and will ease the impact of electricity and gas tariff adjustments, the economy remains fragile. Growth remains below what is needed to generate significant sustained improvements in living standards for all Pakistanis. Attaining the needed growth of 5–7 percent per year will require continued efforts to safeguard still fragile macroeconomic stability, but will also necessitate accelerated structural reforms to boost private investment, ease growth bottlenecks, and enhance productivity.

35. **Well designed fiscal consolidation remains a critical pillar of Pakistan's growth-enhancing reform program**. Staff welcomes the government's far-reaching efforts to restore the country's fiscal and debt sustainability while protecting well-targeted social programs for the poor and paving the way for a private sector-led inclusive growth. However, the authorities need to act preemptively to address possible shortfalls in their FY2014/15 adjustment measures. While they have taken steps to close the fiscal gap caused by the delay in implementing electricity tariff adjustments and introducing the GIDC, these need to be supported by structural fiscal reforms. In particular, bringing electricity tariffs to cost-recovery and maintaining full pass-through of any future changes in energy costs are necessary to avoid the accumulation of on- and off-budget imbalances. As Pakistan prepares for another round of negotiations on fiscal federalism, it will be critical to address imbalances between the central government and provinces that could threaten long-term fiscal sustainability.

36. **Revenue mobilization has improved under the program, but there is still great scope for increasing tax revenues, especially through tax administration reforms**. The government's efforts to raise the tax-to-GDP ratio—still standing at about half of the world average—are steps in the right direction. In particular, the elimination of some SROs is commendable and should be accompanied by strict FBR enforcement actions against tax evaders. It will be important to avoid granting new concessions and exemptions that would undermine the gains accomplished thus far. However, a broader tax administration reform strategy is needed, including the expansion the FBR's information reporting processes and technologies to better manage tax compliance and enforcement, including by using the AML tools to tackle tax crimes. Staff encouraged the authorities to continue enhancing the effectiveness of the AML/CFT framework to detect and disrupt proceeds of crimes including corruption. This will not only improve the tax-to-GDP ratio and create resources to finance much-needed spending on fixed investment and social development, but also make the taxation system more efficient, transparent and equitable. Finally, staff encouraged the authorities to build on the reform momentum and develop the GST to a modern system of indirect taxation—including services—along with an income tax regime that integrates all sources of income.

37. **Staff supports the authorities' efforts to develop the government debt market and revamp public debt management operations**. The government has made progress in reducing its reliance on central bank financing, but the targets for government borrowing from the SBP were missed partly because insufficient cash cushion and volatility in provincial withdrawals. Staff encouraged the authorities to put in place a robust organizational framework for public debt management and operationalize the MTDS to diversify the sources of financing and to reduce reliance on government borrowing from the SBP.

38. **The SBP should sustain its efforts to boost foreign exchange reserves**. The SBP should continue its interventions to accumulate reserves, so as to reduce potential external vulnerabilities and reach at least three months' of import coverage in the coming months. While stepped-up intervention may entail some downward exchange rate flexibility, it will generate lasting positive effects on competitiveness and the balance of payments.

39. **The SBP should increasingly focus on maintaining price stability, while meeting program monetary targets**. This will require improved SBP operations and enhanced autonomy. Legislation to enhance SBP independence remains a priority, and the authorities should work to ensure that the draft legislation currently in parliament fully conforms to international best practices. The authorities need to continue reducing their reliance on SBP financing, diversify financing sources of the budget, and provide market participants with clear paths for their upcoming public securities auctions. Enhancing communication with the public about SBP price objectives, improving the functioning of the interest corridor, and using effective open market operations should be given priority. Steps to improve SBP governance, risk management, and internal controls are also welcome. Staff encouraged the SBP to move toward a modern monetary framework, pursue inflation targets over time, and improve communications with the public about its framework.

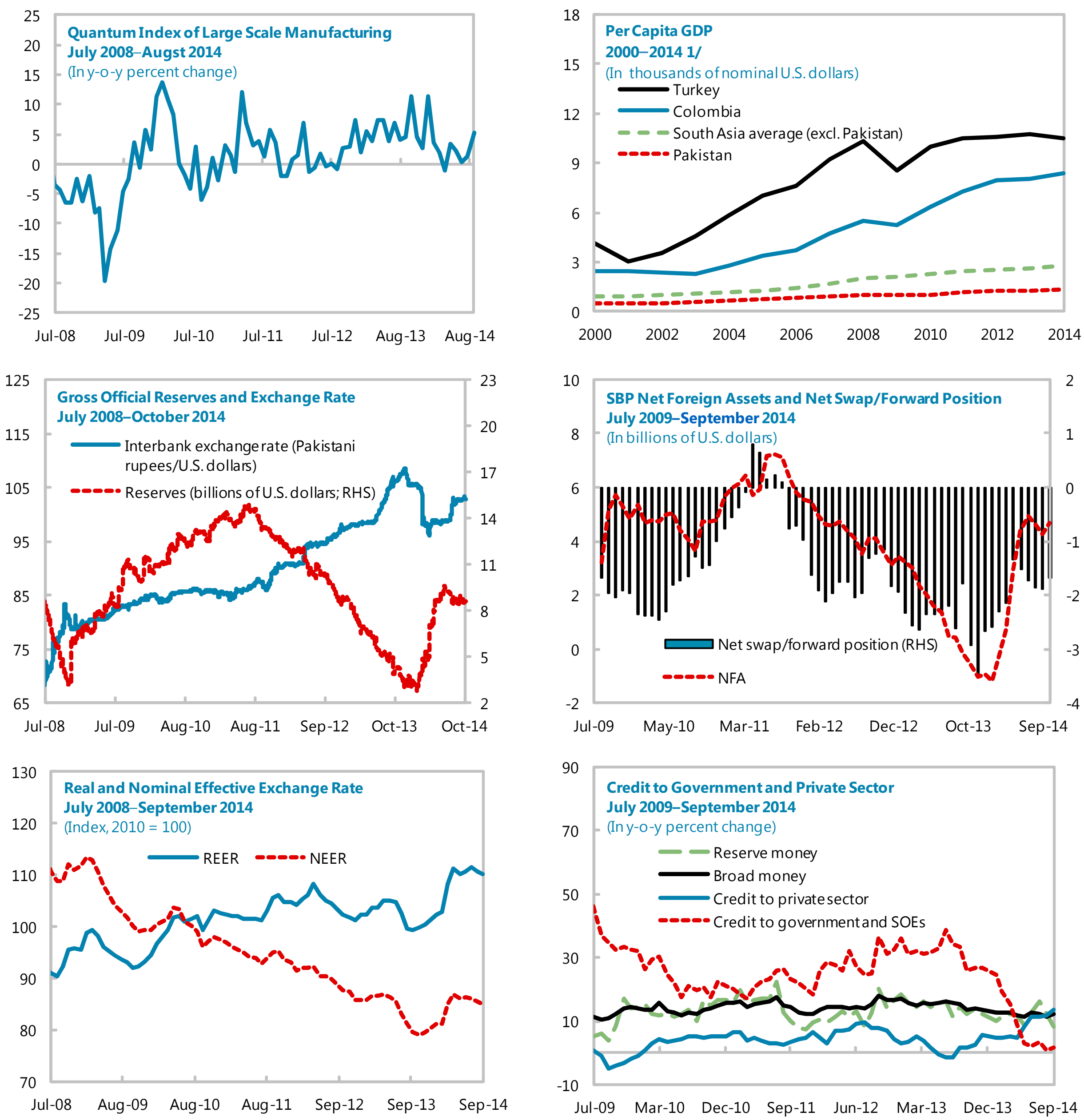
40. **Deep structural reforms remain critical for improving economic performance over time**. The authorities are moving forward with energy price adjustments, addressing the administrative constraints on the power sector's regulatory framework, continue to work on improvements in the operations and collections of energy companies, and with electricity tariff rationalizations despite the recent hiccough. The implementation of gas price rationalization should move forward with the gas levy and more favorable producer prices to better allocate the current supply and encourage new production however they need to follow up with the legal processes to achieve full implementation. The commitment to privatization of public sector enterprises (PSEs) remains strong, although the authorities may encounter further difficulties if market appetite diminishes. The government has been moving forward with trade policy implementation and is stepping up their efforts on business climate reforms.

41. **Keeping the program on track in future reviews will require strong political commitment at the highest levels, together with steadfast implementation by the government and the SBP**. 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.

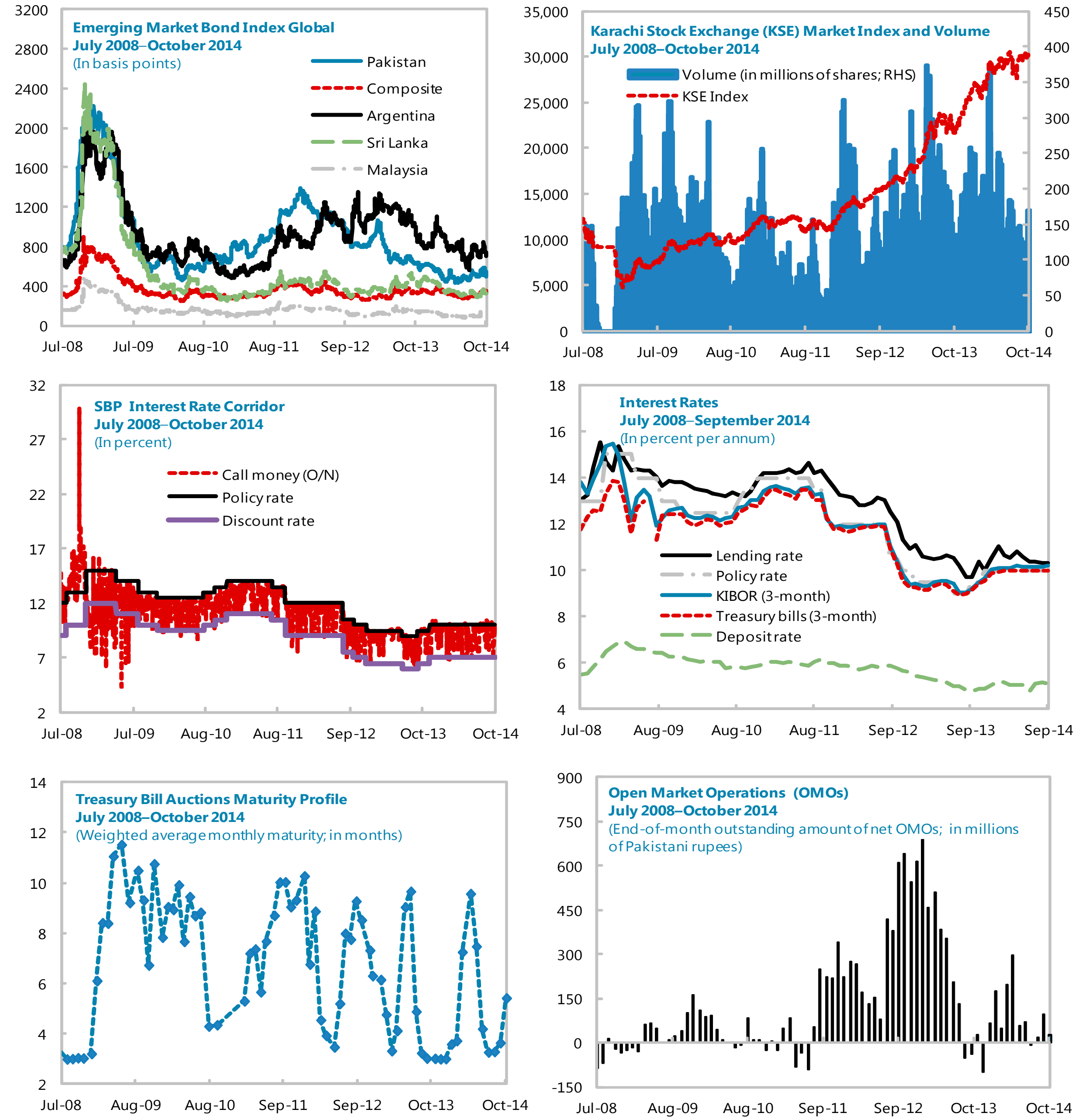
42. **On the basis of Pakistan's performance under the extended arrangement and the corrective actions outlined above (¶17, 31), staff supports the authorities' request for completion of the fourth and fifth review under the arrangement and for waivers for the nonobservance of the end-September performance criteria on NDA of the SBP, government borrowing from the SBP, and NIR**. Staff also recommends the establishment of the end-December 2014 and end-March 2015 PCs, setting of five new structural benchmarks, and the revised timelines of structural benchmarks as proposed in the attached MEFP.

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



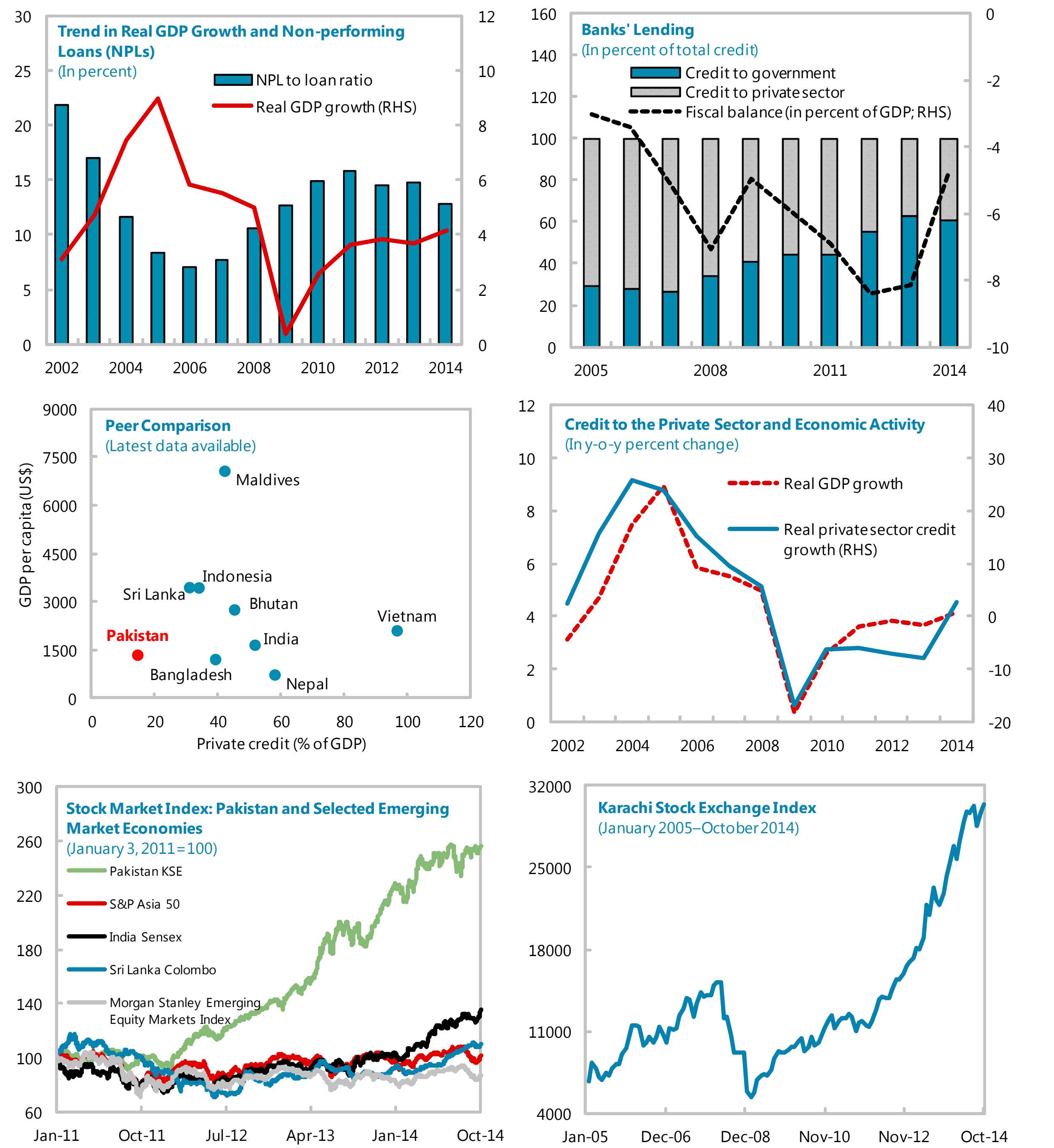
Sources: Pakistani authorities; IMF World Economic Outlook; and IMF staff calculations.
1/ 2014 per capita GDP figures for countires other than Pakistan are estimated.

Figure 2. Pakistan: Selected Financial Indicators, 2008–14



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

Figure 3. Pakistan: Selected Banking and Financial Indicators



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

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets for FY2013/14 and 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
	Actual	Fourth Review			Fifth Review			Program		Projection	Projection
		Target	Adjusted target	Actual	Target	Adjusted target	Actual				
Performance Criteria											
Floor on net international reserves of the SBP (millions of U.S. dollars)	-2,437	1,800	1,064	2,678	3,000	3,260	2,630	3,500	4,500	5,700	7,000
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,402	2,324	2,221	2,355	2,306	2,291	2,316	2,436	2,365	2,322	2,217
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	2,012	1,464	1,468	1,402	376	383	337	722	1,087	1,387	375
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	2,255	2,150	2,150	1,725	1,900	1,900	1,675	1,775	1,775	1700	1550
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3/	2,168	2,240	2,240	2,328	2,070	2,070	2,289	2,000	1,905	1,865	1,800
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	62	62	66	14	14	21	36	69	95	22
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	1,936			2,266			539	1,195	1,883	2,756	

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
Prior Actions				
1	Bring the government borrowing level from the SBP to PRs 2,150 billion.	end-November 2014		Ensure PC on Government borrowing is met (MEFP ¶19).
2	Limit the stock of Net Domestic Assets of the SBP to PRs 2,450 billion. 1/	end-November 2014		Ensure PC on NDA is met (MEFP ¶4).
3	Provide Fund staff with a detailed quarterly financing plan for the coming 12 months and extend the existing in-quarter issuance plan to a rolling quarterly issuance program published every month for domestic public securities (including local Sukuk bonds).	Five days prior to the board meeting		Bring debt management up to best international practices, and to ensure that future program targets on government borrowing from the SBP are met (MEFP ¶20).
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 budet.	end-June-2014	Met	Reduce distortions and improve revenue collection.
3	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-September 2014	Not met, rescheduled to end-December, 2014	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.
4	Approve an administrative order to consolidate the responsibilities of public debt management in the debt management office.	end-September 2014	Partially met	Strengthen the organizational framework for effective public debt management.
Monetary sector				
5	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 2014	Not met, rescheduled to end-June 2015	Prerequisite for an independent monetary policy framework.
6	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.
Financial sector				
7	Enact the Securities Bill, in line with Fund staff advice.	end-December 2014	Rescheduled to end-June, 2015	Enhance the resilience of the financial sector.
8	Enact the Deposit Protection Fund Act, in line with Fund staff advice.	end-June 2015		Enhance the resilience of the financial sector.
Structural Policies				
9	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.
10	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	
11	Conduct a diagnostic study of the regulatory framework of the power sector and prepare an interim report.	end-April 2014	Met	
12	Offer the minority shares in United Bank Limited and Pakistan Petroleum Limited to domestic and international investors.	end-June 2014	Met	
13	Fill the vacancies in the NEPRA Board.	end-July 2014	Met at end-November, 2014	
14	Privatize 26 percent of PIA's shares to strategic investors.	end-December 2014	Rescheduled to end-December, 2015	
New Structural Benchmarks				
15	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.
16	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		Improve SBPs liquidity management.
17	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 safeguard procedures, the Internal Audit Department will conduct reviews of the program monetary data reported to the IMF, within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff.	end-February 2015		Improve monetary policy framework through enhanced central bank independence.
18	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.
19	Conduct a review to reduce the number of existing processes and forms for paying sales and income taxes.	end-March 2015		Improve business climate.

1/ Prior action on NDA is subject to TMU adjustors. The adjusted target for end-November is PRs 2,655 billion.

Table 3. Pakistan: Selected Economic Indicators, 2010/11–2014/15 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	
					Third Review	Projections
			(Annual percentage change)			
Output and prices						
Real GDP at factor cost	3.6	3.8	3.7	4.1	4.0	4.3
GDP deflator at factor cost	19.5	5.7	7.6	7.0	8.1	8.0
Consumer prices (period average) 2/	13.7	11.0	7.4	8.6	8.1	7.9
Consumer prices (end of period) 2/	13.3	11.3	5.9	8.2	7.5	7.5
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	15.7	14.1
Government	-4.2	-5.1	-5.0	-1.3	-1.1	-1.2
Nongovernment (including public sector enterprises)	18.4	18.1	18.5	14.1	16.8	15.3
Gross capital formation 3/	14.1	15.1	14.6	14.0	16.9	15.6
Government	2.5	3.3	3.1	3.4	3.5	3.2
Nongovernment (including public sector enterprises)	11.6	11.7	11.5	10.6	13.4	12.4
Public finances						
Revenue and grants	12.6	13.2	13.3	15.1	14.8	15.0
Expenditure (including statistical discrepancy)	19.8	21.9	21.5	19.5	19.4	19.5
Budget balance (including grants)	-6.9	-8.4	-8.1	-4.7	-4.6	-4.5
Budget balance (excluding grants)	-7.1	-8.8	-8.3	-5.5	-4.8	-4.8
Primary balance	-3.1	-4.0	-3.7	-0.2	0.1	0.2
Total general government debt 4/	55.3	60.5	62.3	62.5	63.8	61.2
External general government debt	22.4	22.4	20.0	19.6	23.1	19.8
Domestic general government debt	32.9	38.1	42.3	42.9	40.7	41.4
			(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	3.7
Net domestic assets	6.6	23.8	19.3	8.8	8.5	8.7
Broad money (percent change)	9.4	20.9	15.9	12.5	12.2	12.4
Reserve money (percent change)	16.2	12.2	15.8	12.9	12.1	12.0
Private credit (percent change)	7.6	3.9	-0.6	11.4	9.0	14.0
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	1.4	3.5	0.9
Merchandise imports, U.S. dollars (percentage change)	14.9	12.8	-0.6	3.9	4.3	6.0
Current account balance (in percent of GDP)	0.1	-2.1	-1.1	-1.2	-1.2	-1.5
			(In percent of exports of goods and services, unless otherwise indicated)			
External public and publicly guaranteed debt	153.4	160.3	144.6	166.4	176.3	167.1
Debt service	11.7	16.0	21.1	23.5	29.8	22.9
Gross reserves (in millions of U.S. dollars) 5/	14,784	10,799	6,008	9,096	13,326	14,103
In months of next year's imports of goods and services	3.6	2.7	1.5	2.1	2.8	3.0
Memorandum items:						
Real effective exchange rate (annual average, percentage change)	4.2	3.8	1.7	-1.4	…	…
Terms of trade (percentage change)	7.2	-10.5	-0.5	-0.7	-1.4	-1.6
Real per capita GDP (percentage change)	1.5	1.7	1.6	2.1	2.0	2.3
GDP at market prices (in billions of Pakistani rupees)	18,276	20,047	22,489	25,402	28,946	28,602
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, 2010/11–2018/19

	2010/11	2011/12	2012/13	2013/14	2014/15		2015/16	2016/17	2017/18	2018/19
					Third Review	Projections	Projections			
					(Annual percentage change)					
Output and prices										
Real GDP at factor cost	3.6	3.8	3.7	4.1	4.0	4.3	4.4	4.8	5.0	5.0
Consumer prices (period average)	13.7	11.0	7.4	8.6	8.1	7.9	6.8	6.0	6.0	6.0
					(In percent of GDP)					
Saving and investment balance	0.1	-2.1	-1.1	-1.2	-1.2	-1.5	-1.6	-2.1	-2.3	-2.7
Government	-6.7	-8.4	-8.1	-4.7	-4.6	-4.5	-3.8	-3.4	-3.2	-3.0
Non-government (including public sector enterprises)	6.8	6.3	7.1	3.5	3.4	3.0	2.2	1.3	0.9	0.4
Gross national saving	14.2	13.0	13.5	12.8	15.7	14.1	14.8	15.6	16.4	17.1
Government	-4.2	-5.1	-5.0	-1.3	-1.1	-1.2	-0.4	0.2	0.3	0.6
Non-government (including public sector enterprises)	18.4	18.1	18.5	14.1	16.8	15.3	15.1	15.3	16.1	16.4
Gross capital formation	14.1	15.1	14.6	14.0	16.9	15.6	16.4	17.6	18.7	19.7
Government	2.5	3.3	3.1	3.4	3.5	3.2	3.4	3.6	3.6	3.7
Non-government (including public sector enterprises)	11.6	11.7	11.5	10.6	13.4	12.4	13.0	14.0	15.2	16.1
					(In billions of U.S. dollars, unless otherwise indicated)					
Balance of payments										
Current account balance	0.2	-4.7	-2.5	-3.0	-3.1	-4.0	-4.7	-6.2	-7.6	-9.4
Net capital flows 1/	2.3	1.4	0.5	6.8	6.1	7.4	4.9	9.5	10.9	12.8
Of which: foreign direct investment 2/	1.6	0.8	1.5	1.6	4.3	1.8	3.2	2.2	3.0	3.9
Gross official reserves	14.8	10.8	6.0	9.1	13.3	14.1	16.5	19.9	23.1	26.2
In months of imports 3/	3.6	2.7	1.5	2.1	2.8	3.0	3.3	3.7	4.0	4.2
External debt (in percent of GDP)	31.1	29.1	26.2	26.2	28.0	24.5	24.5	24.7	25.0	25.0
					(In percent of GDP)					
Public finances										
Revenue and grants	12.6	13.2	13.3	15.1	14.8	15.0	15.5	15.8	15.9	16.0
Of which: tax revenue	9.5	10.4	9.9	10.4	11.5	11.2	12.0	12.7	12.8	13.1
Expenditure (incl. stat. discr.), *of which:*	19.5	21.6	21.4	19.8	19.4	19.5	19.3	19.2	19.1	19.0
Current	16.5	17.9	16.6	16.2	15.9	16.2	15.9	15.6	15.5	15.3
Development (incl. net lending)	2.6	3.4	4.7	3.8	3.5	3.2	3.5	3.6	3.6	3.7
Primary balance 4/	-3.1	-4.0	-3.7	-0.2	0.1	0.2	0.5	0.5	0.6	0.6
Overall fiscal balance 4/	-6.9	-8.4	-8.1	-4.7	-4.6	-4.5	-3.8	-3.4	-3.2	-3.0
Total public debt (including obligations to the IMF)	59.5	64.0	64.3	63.7	65.8	61.8	60.5	58.6	56.5	54.8

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, 2010/11–2018/19

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

	2010/11	2011/12	2012/13	2013/14	2014/15						2015/16		2016/17	2017/18	2018/19
					End-Year	End-Year	Q1	Q2	Q3	Q4	Q1	End-Year			
					Third review	Projections	Actual	Projections					Projections		
Current account	214	-4,658	-2,496	-2,971	-3,055	-4,006	-1,330	-1,254	-692	-731	-1,249	-4,691	-6,249	-7,552	-9,444
Balance on goods	-10,516	-15,765	-15,431	-16,635	-17,461	-18,906	-5,868	-4,653	-4,375	-4,009	-5,031	-19,725	-21,532	-23,725	-26,291
Exports, f.o.b.	25,356	24,696	24,795	25,151	26,582	25,381	5,960	6,237	6,345	6,839	6,173	26,408	27,831	29,129	30,615
Imports, f.o.b.	35,872	40,461	40,226	41,786	44,043	44,287	11,828	10,891	10,720	10,848	11,204	46,133	49,363	52,854	56,907
Services (net)	-1,940	-3,192	-1,472	-2,534	-2,839	-2,806	-441	-731	-810	-824	-884	-3,573	-4,333	-4,484	-5,494
Services: credit	5,768	5,035	6,733	5,257	5,457	5,864	1,712	1,406	1,326	1,419	1,438	5,978	6,226	7,084	7,149
Of which: Coalition Support Fund	743	0	1,806	1,050	1,400	1,455	735	240	240	240	240	915	225	0	0
Of which: 3G Licenses	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Services: debit	7,708	8,227	8,205	7,791	8,296	8,670	2,153	2,137	2,137	2,243	2,322	9,550	10,559	11,567	12,642
Income (net)	-3,017	-3,245	-3,685	-3,915	-4,073	-4,236	-822	-1,245	-895	-1,274	-973	-4,716	-5,437	-6,341	-7,293
Income: credit	716	826	488	537	672	594	99	163	148	184	139	623	667	711	670
Income: debit	3,733	4,071	4,173	4,452	4,745	4,830	921	1,408	1,043	1,458	1,112	5,339	6,105	7,052	7,963
Of which: interest payments	1,408	1,589	1,325	1,522	1,812	2,128	335	680	434	679	454	2,301	2,656	3,259	3,768
Of which: income on direct investment	2,065	2,177	2,714	2,928	2,933	2,702	586	728	609	779	658	3,038	3,449	3,793	4,195
Balance on goods, services, and income	-15,473	-22,202	-20,588	-23,084	-24,374	-25,947	-7,131	-6,630	-6,080	-6,107		-28,013	-31,303	-34,549	-39,078
Current transfers (net)	15,687	17,544	18,092	20,113	21,318	21,941	5,801	5,376	5,388	5,376	5,639	23,322	25,054	26,997	29,634
Current transfers: credit, *of which:*	15,863	17,686	18,183	20,253	21,477	22,111	5,852	5,415	5,428	5,416	5,679	23,481	25,213	27,156	29,793
Official	845	658	412	369	683	517	129	153	192	43	65	411	411	315	855
Workers' remittances	11,201	13,186	13,922	15,832	16,708	17,340	4,695	4,207	4,113	4,326	4,619	18,628	20,134	21,903	23,735
Other private transfers	3,817	3,842	3,849	4,052	4,087	4,253	1,028	1,056	1,122	1,047	995	4,442	4,667	4,938	5,202
Current transfers: debit	176	142	91	140	159	170	51	40	40	40	40	159	159	159	159
Capital account	161	189	264	1,833	464	678	16	241	207	213	159	747	761	763	389
Capital transfers: credit	161	186	266	1,833	464	678	16	241	207	213	159	747	761	763	389
Of which: official capital grants	160	180	250	328	464	678	16	241	207	213	159	747	747	763	389
Capital transfers: debit	0	3	2	0	0	0	0	0	0	0	0	0	0	0	0
Financial account	2,103	1,275	549	5,235	5,673	6,469	741	2,271	1,296	2,160	1,313	4,149	8,774	10,157	12,401
Direct investment abroad	-44	-77	-198	-148	-15	-97	-18	-27	-26	-26	-24	-101	-102	-102	-102
Direct investment in Pakistan	1,636	821	1,456	1,631	4,317	1,809	169	212	191	1,236	1,538	3,233	2,205	3,030	3,902
Of which: privatization receipts	1	0	0	831	1,750	1,040	0	20	20	1,000	1,300	1,750	600	600	0
Portfolio investment (net), *of which:*	339	-149	26	2,766	1,380	2,710	182	1,798	90	640	-140	1,431	2,969	5,600	6,164
Financial derivatives (net)	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-200
Other investment assets	-920	9	-314	297	-267	772	611	325	36	-200	7	148	856	68	188
Monetary authorities	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
General government	-3	3	-2	2	0	-3	-3	0	0	0	0	0	0	0	0
Banks	-63	-91	-126	24	-566	185	224	205	6	-250	-3	-12	-12	-12	-12
Other sectors	-854	97	-186	271	299	590	390	120	30	50	10	160	868	80	200
Other investment liabilities	1,092	671	-421	689	258	1,275	-203	-37	1,005	510	-68	-562	2,847	1,562	2,449
Monetary authorities	-10	-105	710	145	-1,065	-1,065	0	-1,065	0	0	0	0	0	0	0
General government, *of which:*	298	998	249	1,223	-3,168	791	-167	377	561	20	-81	-922	1,357	9	-145
Disbursements	2,377	2,633	2,530	4,201	2,788	4,431	658	1,013	1,634	1,125	1,028	3,842	3,405	2,340	2,328
Amortization	1,957	1,577	2,282	2,973	5,956	3,641	825	636	1,074	1,106	1,109	4,764	2,048	2,331	2,473
Banks	52	220	-1,117	-378	809	381	176	120	25	60	10	142	187	265	72
Other sectors	752	-442	-262	-301	3,682	1,168	-212	531	419	431	2	219	1,302	1,287	2,523
Net errors and omissions	14	-81	-309	-254	0	240	240	0	0	0	0	0	0	0	0
Reserves and related items	-2,492	3,275	1,992	-3,843	-3,082	-3,380	333	-1,259	-812	-1,643	-223	-204	-3,287	-3,369	-3,345
Reserve assets	-2,225	4,430	4,530	-3,271	-4,018	-5,100	60	-2,010	-1,159	-1,991	-718	-2,360	-3,399	-3,276	-3,019
Use of Fund credit and loans	-267	-1,155	-2,538	-572	936	1,720	273	751	348	348	496	2,155	113	-93	-327
Memorandum items:															
Current account (in percent of GDP)	0.1	-2.1	-1.1	-1.2	-1.2	-1.5						-1.6	-2.1	-2.3	-3
Current account (in percent of GDP; excluding fuel imports)	5.9	4.3	5.0	4.7	4.9	3.9						3.6	3.2	2.8	3
Exports f.o.b. (growth rate, in percent)	28.9	-2.6	0.4	1.4	3.5	0.9						4.0	5.4	4.7	5
Imports f.o.b. (growth rate, in percent)	14.9	12.8	-0.6	3.9	4.3	6.0						4.2	7.0	7.1	8
Oil imports (in million US$, cif)	12,317	14,368	14,066	14,676	15,756	14,612						14,859	16,014	16,900	18,871
Terms of trade (growth rate, in percent)	7.2	-10.5	-0.5	-0.7	-1.4	-1.6						1.2	-0.5	-0.2	-1
External debt (in millions of U.S. dollars)	66,366	65,478	60,899	65,565	72,927	66,373						69,758	75,348	81,940	88,635
Gross external financing needs (in millions of U.S. dollars) 1/	1,988	6,960	4,909	8,596	10,778	9,031						10,068	9,446	10,640	14,223
End-period gross official reserves (millions of U.S. dollars) 2/	14,784	10,799	6,008	9,096	13,326	14,103	8,943	10,953	12,112	14,103	14,821	16,463	19,862	23,138	26,157
(In months of next year's imports of goods and services)	3.6	2.7	1.5	2.1	2.8	3.0	2.0	2.5	2.7	3.0	3.1	3.3	3.7	4.0	4.2
GDP (in millions of U.S. dollars)	213,626	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	
							Third Review	Projections
Revenue and grants	1,878	2,130	2,306	2,642	2,988	3,831	4,289	4,288
Revenue	1,851	2,079	2,261	2,567	2,949	3,625	4,206	4,191
Tax revenue	1,331	1,500	1,738	2,076	2,231	2,635	3,342	3,209
Federal	1,285	1,445	1,673	1,969	2,081	2,445	3,134	2,995
FBR revenue	1,157	1,329	1,558	1,881	1,936	2,266	2,810	2,756
Direct taxes	440	529	602	732	736	884	1,026	1,139
Federal excise duty	116	121	137	122	119	139	185	159
Sales tax/VAT	452	517	633	809	841	1,002	1,241	1,167
Customs duties	148	161	185	218	240	241	358	291
Petroleum surcharge	112	89	83	60	110	104	123	122
Gas surcharge and other	16	28	32	27	35	43	42	43
GIDC 1/	…	…	…	…	…	32	159	75
Provincial	46	55	65	107	151	190	208	214
Nontax revenue	520	579	523	491	717	990	863	982
Federal	436	512	461	443	646	941	788	902
Provincial	84	68	62	48	71	49	75	80
Grants	27	51	46	75	39	206	83	98
Expenditure	2,531	3,008	3,566	4,326	4,816	5,027	5,609	5,577
Current expenditure	2,093	2,482	3,012	3,579	3,742	4,123	4,592	4,637
Federal	1,547	1,855	2,227	2,611	2,647	2,950	3,242	3,292
Interest	638	642	698	889	991	1,148	1,352	1,344
Domestic	559	578	630	821	920	1,073	1,224	1,225
Foreign	79	64	68	68	71	75	128	119
Other	909	1,213	1,529	1,722	1,656	1,802	1,890	1,948
Defense	330	375	450	507	541	623	706	711
Other	579	838	1,078	1,215	1,116	1,179	1,185	1,237
Of which: subsidies 2/	244	227	493	556	305	336	229	254
Of which: grants	136	361	259	291	368	372	442	463
Provincial	546	627	786	968	1,095	1,173	1,350	1,345
Development expenditure and net lending	404	558	469	681	1,058	966	1,017	925
Public Sector Development Program	398	519	462	669	695	865	1,012	917
Federal	196	260	216	293	324	435	525	477
Provincial	202	258	246	375	372	431	486	440
Net lending	7	39	7	12	363	101	5	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	-1,404	-1,387
Overall Balance (including grants)	-653	-878	-1,260	-1,685	-1,828	-1,196	-1,320	-1,289
Financing	653	878	1,260	1,685	1828	1,196	1,320	1,289
External	75	138	62	53	24	320	-46	297
Of which: privatization receipts	1	0	0	0	0	1	195	2
Of which: IMF	0	0	0	0	0	0	0	0
Domestic	579	740	1,198	1,631	1804	876	1,367	992
Bank	351	304	727	1,102	1317	322	1,093	412
Nonbank	227	436	471	529	487	553	273	580
Memorandum items:								
Primary balance (excluding grants)	-43	-287	-608	-871	-876	-254	-52	-43
Primary balance (including grants)	-16	-236	-562	-796	-837	-48	32	55
Total security spending	330	375	450	507	541	623	706	711
Total government debt	7,387	8,448	10,112	12,130	14,021	15,880	18,468	17,497
Domestic debt	3,860	4,654	6,014	7,638	9,521	10,892	11,793	11,837
External debt 4/	3,527	3,794	4,098	4,492	4,500	4,988	6,675	5,661
Total government debt including IMF obligations	7,805	9,138	10,879	12,822	14,454	16,178	19,032	17,686
Nominal GDP (market prices)	13,200	14,867	18,276	20,047	22,489	25,402	28,946	28,602

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 Third Review	2014/15 Projections
Revenue and grants	14.3	12.6	13.2	13.3	15.1	14.8	15.0
Revenue	14.0	12.4	12.8	13.1	14.3	14.5	14.7
Tax revenue	10.1	9.5	10.4	9.9	10.4	11.5	11.2
Federal	9.7	9.2	9.8	9.3	9.6	10.8	10.5
FBR revenue	8.9	8.5	9.4	8.6	8.9	9.7	9.6
Direct taxes	3.6	3.3	3.7	3.3	3.5	3.5	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	4.3	4.1
Customs duties	1.1	1.0	1.1	1.1	0.9	1.2	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	0.1
GIDC 1/	…	…	…	…	0.1	0.6	0.3
Provincial	0.4	0.4	0.5	0.7	0.7	0.7	0.7
Nontax revenue	3.9	2.9	2.4	3.2	3.9	3.0	3.4
Federal	3.4	2.5	2.2	2.9	3.7	2.7	3.2
Provincial	0.5	0.3	0.2	0.3	0.2	0.3	0.3
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	19.4	19.5
Current expenditure	16.7	16.5	17.9	16.6	16.2	15.9	16.2
Federal	12.5	12.2	13.0	11.8	11.6	11.2	11.5
Interest	4.3	3.8	4.4	4.4	4.5	4.7	4.7
Domestic	3.9	3.4	4.1	4.1	4.2	4.2	4.3
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	6.5	6.8
Defense	2.5	2.5	2.5	2.4	2.5	2.4	2.5
Other	5.6	5.9	6.1	5.0	4.6	4.1	4.3
Of which: subsidies 2/	1.5	2.7	2.8	1.4	1.3	0.8	0.9
Of which: grants	2.4	1.4	1.5	1.6	1.5	1.5	1.6
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	3.5	3.2
Public Sector Development Program	3.5	2.5	3.3	3.1	3.4	3.5	3.2
Federal	1.8	1.2	1.5	1.4	1.7	1.8	1.7
Provincial	1.7	1.3	1.9	1.7	1.7	1.7	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	-4.8
Overall Balance (including grants)	-5.9	-6.9	-8.4	-8.1	-4.7	-4.6	-4.5
Financing	5.9	6.9	8.4	8.1	4.7	4.6	4.5
External	0.9	0.3	0.3	0.1	1.3	-0.2	1.0
Of which: privatization receipts	0.0	0.0	0.0	0.0	0.0	0.7	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	4.7	3.5
Bank	2.0	4.0	5.5	5.9	1.3	3.8	1.4
Nonbank	2.9	2.6	2.6	2.2	2.2	0.9	2.0
Memorandum items:							
Primary balance (excluding grants)	-1.9	-3.3	-4.3	-3.9	-1.0	-0.2	-0.1
Primary balance (including grants)	-1.6	-3.1	-4.0	-3.7	-0.2	0.1	0.2
Total security spending	2.5	2.5	2.5	2.4	2.5	2.4	2.5
Total government debt 4/	56.2	55.3	60.5	62.3	62.5	63.8	61.2
Domestic debt	31.0	32.9	38.1	42.3	42.9	40.7	41.4
External debt 4/	25.2	22.4	22.4	20.0	19.6	23.1	19.8
Total government debt including IMF	60.8	59.5	64.0	64.3	63.7	65.8	61.8
Nominal GDP (market prices, billions of Pakistani rupees)	14,867	18,276	20,047	22,489	25,402	28,946	28,602

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 Budget, 2011/12–2015/16

(In billions of Pakistani rupees)

	2011/12	2012/13	2013/14	2014/15						2015/16
				End-Year	End-Year	Q1	Q2	Q3	Q4	Q1
				Third Review	Projections	Actual	Projections			Projections
Revenue and grants	2,642	2,988	3,831	4,289	4,288	842	1,000	1,080	1,366	1,002
Revenue	2,567	2,949	3,625	4,206	4,191	840	965	1,044	1,341	957
Tax revenue	2,076	2,231	2,635	3,342	3,209	628	753	779	1,048	746
Federal	1,969	2,081	2,445	3,134	2,995	583	697	729	986	697
FBR revenue	1,881	1,936	2,266	2,810	2,756	539	656	688	873	656
Direct taxes	732	736	884	1,026	1,139	190	258	307	383	238
Federal excise duty	122	119	139	185	159	25	39	39	57	35
Sales tax/VAT	809	841	1,002	1,241	1,167	259	287	272	349	309
Customs duties	218	240	241	358	291	65	71	70	84	74
Petroleum surcharge	60	110	104	123	122	28	30	30	33	32
Gas surcharge and other	23	32	39	37	37	8	9	9	12	8
GIDC 1/	…	…	32	159	75	7	0	0	67	0
Provincial	107	151	190	208	214	45	57	50	62	49
Nontax revenue	491	717	990	863	982	212	212	265	293	211
Federal	443	646	941	788	902	200	194	244	264	194
Provincial	48	71	49	75	80	12	18	21	29	17
Grants	75	39	206	83	98	2	35	36	25	45
Expenditure	4,326	4,816	5,027	5,609	5,577	1,177	1,350	1,409	1,641	1,333
Current expenditure	3,579	3,742	4,123	4,592	4,637	1,074	1,159	1,181	1,223	1,193
Federal	2,611	2,647	2,950	3,242	3,292	796	825	842	828	889
Interest	889	991	1,148	1,352	1,344	395	345	360	243	365
Domestic	821	920	1,073	1,224	1,225	376	312	337	200	331
Foreign	68	71	75	128	119	19	33	24	43	35
Other	1,722	1,656	1,802	1,890	1,948	401	480	482	585	524
Defense	507	541	623	706	711	165	178	178	190	171
Other	1,215	1,116	1,179	1,185	1,237	236	302	304	395	353
Of which: subsidies 2/	556	305	336	229	254	58	61	58	77	91
Of which: grants	291	368	372	442	463	75	111	116	161	118
Provincial	968	1,095	1,173	1,350	1,345	278	334	338	395	304
Development expenditure and net lending	681	1,058	966	1,017	925	98	176	228	423	140
Public Sector Development Program	669	695	865	1,012	917	93	174	226	424	138
Federal	293	324	435	525	477	40	86	112	239	58
Provincial	375	372	431	486	440	53	88	115	185	80
Net lending	12	363	101	5	8	5	2	2	-1	2
Statistical discrepancy ("+" = additional expenditure) 3/	67	16	-62	0	0	5	0	0	-5	0
Overall Balance (excluding grants)	-1,760	-1,867	-1,402	-1,404	-1,387	-337	-386	-365	-300	-377
Overall Balance (including grants)	-1,685	-1,828	-1,196	-1,320	-1,289	-335	-351	-329	-275	-332
Financing	1,685	1828	1,196	1320	1,289	335	351	329	275	332
External	53	24	320	-46	297	-30	205	64	58	12
Of which: IMF	0	0	0	0	0	0	0	0	0	0
Domestic	1,631	1804	876	1367	992	365	146	265	217	320
Bank	1,102	1317	322	1093	412	155	87	143	27	171
Nonbank	529	487	553	273	580	210	58	122	190	149
Memorandum items:										
Primary balance (excluding grants)	-871	-876	-254	-52	-43	58	-40	-4	-57	-11
Primary balance (including grants)	-796	-837	-48	32	55	60	-5	32	-32	34
Total security spending	507	541	623	706	711	165	178	178	190	171
Total government debt	12,130	14,021	15,880	18,468	17,497					
Domestic debt	7,638	9,521	10,892	11,793	11,837					
External debt 4/	4,492	4,500	4,988	6,675	5,661					
Total government debt including IMF obligations	12,822	14,454	16,178	19,032	17,686					
Nominal GDP (market prices)	20,047	22,489	25,402	28,946	28,602					

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, 20010/11–2015/16

	2010/11	2011/12	2012/13	2013/14	2014/15					2015/16
					Q1	Q2	Q3	Q4	End-Year	Q1
					Actual	Projections			Third Review	Projections
	(In billions of Pakistani rupees, unless otherwise indicated)									
Monetary survey										
Net foreign assets (NFA)	780	527	270	601	570	706	793	971	926	995
Net domestic assets (NDA)	5,915	7,115	8,588	9,367	9,392	9,850	9,758	10,236	10,247	10,187
Net claims on government, *of which: 1/*	2,983	4,197	5,629	5,710	5,713	6,064	6,158	6,351	6,876	6,498
Budget support, *of which:*	2,523	3,667	5,125	5,448	5,588	5,676	5,818	5,845	6,395	6,016
Banks	1,369	2,005	2,957	3,121	3,300	3,676	3,913	3,980	4,551	4,216
Commodity operations	397	436	468	492	469	388	339	505	481	482
Credit to nongovernment	3,547	3,653	3,664	4,102	4,149	4,525	4,554	4,645	4,262	4,723
Private sector	3,159	3,395	3,376	3,760	3,807	4,196	4,220	4,286	3,938	4,340
Public sector enterprises	388	257	288	342	342	329	334	359	324	384
Privatization account	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3
Other items, net	-612	-732	-702	-442	-467	-736	-951	-757	-889	-1,031
Broad money	6,695	7,642	8,858	9,968	9,962	10,556	10,551	11,207	11,172	11,182
Currency outside scheduled banks	1,501	1,674	1,938	2,178	2,262	2,358	2,359	2,500	2,495	2,508
Rupee deposits	4,819	5,528	6,405	7,191	7,082	7,543	7,537	8,011	8,008	7,981
Foreign currency deposits	375	440	515	599	618	655	654	695	669	694
State Bank of Pakistan (SBP)										
NFA	614	389	134	489	482	617	705	883	834	907
NDA	1,352	1,800	2,401	2,372	2,310	2,436	2,365	2,322	2,319	2,217
Net claims on government	1,184	1,665	2,156	2,236	2,115	1,852	1,746	1,772	1,767	1,657
Of which: budget support	1,155	1,662	2,168	2,328	2,289	2,000	1,905	1,865	1,844	1,800
Claims on nongovernment	-6	-5	-6	-5	-6	-6	-6	-6	-6	-6
Claims on scheduled banks	315	289	448	500	505	696	705	720	642	729
Privatization account	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3
Other items, net	-139	-146	-195	-356	-302	-103	-78	-161	-82	-161
Reserve money, *of which:*	1,966	2,189	2,535	2,861	2,791	3,054	3,069	3,205	3,153	3,124
Banks' reserves	349	396	476	531	380	405	405	430	564	429
Currency	1,606	1,784	22,489	2,317	2,397	2,649	2,665	2,775	2,589	2,695
	(Annual percentage change, unless otherwise indicated)									
Broad money	15.9	20.9	15.9	12.5	12.2	12.5	12.4	12.4	12.2	12.2
NFA, banking system (in percent of broad money) 2/	4.1	-3.0	-3.4	3.7	5.3	6.9	6.7	3.7	3.5	4.3
NDA, banking system (in percent of broad money) 2/	11.8	66.0	19.3	8.8	6.9	5.5	5.7	8.7	8.7	8.0
Budgetary support (in percent of broad money) 2/	10.2	17.1	19.1	3.7	3.0	0.7	2.7	4.0	13.4	4.3
Budgetary support	30.4	45.3	39.7	6.3	5.0	1.2	4.6	7.3	26.2	7.7
Private credit	4.0	16.9	-0.6	11.4	13.4	13.5	13.7	14.0	9.0	14.0
Currency	15.9	70.4	15.8	12.4	14.0	13.0	11.4	14.8	12.6	10.9
Reserve money	17.1	47.9	15.8	12.9	8.2	12.1	12.1	12.0	12.1	11.9
Memorandum items:										
Velocity	2.7	2.6	2.5	2.7	3.0	2.9	2.9	2.7	2.7	2.7
Money multiplier	3.4	3.5	3.5	3.5	3.6	3.5	3.4	3.5	3.5	3.6
Currency to broad money ratio (percent)	22.4	21.9	21.9	21.8	22.7	22.3	22.4	22.3	22.3	22.4
Currency to deposit ratio (percent)	28.9	28.0	28.0	28.0	29.4	28.8	28.8	28.7	28.8	28.9
Foreign currency to deposit ratio (percent)	7.2	7.4	7.4	7.7	8.0	8.0	8.0	8.0	7.7	8.0
Reserves to deposit ratio (percent)	6.7	6.6	6.9	6.8	4.9	4.9	4.9	4.9	6.5	4.9
Budget bank financing (change from the beginning of the fiscal year; in Rs billions), *of which:*	589	1,144	1,458	324	140	227	370	397	1,330	171
By commercial banks	606	636	952	164	179	555	793	859	1,726	235
By SBP	-17	508	506	160	-39	-328	-423	-463	-396	-65
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	0.8	1.6	3.2	2.1	0.1
NFA of commercial banks (millions of U.S. dollars)	1,937	1,464	1,377	1,130	861	819	823	815	776	805
NDA of commercial banks (billions of Pakistani rupees)	4,563	5,315	6,187	6,995	7,082	7,413	7,393	7,913	7,928	7,970

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–September 2014)

	Dec. 2010	Dec. 2011	Dec. 2012	Mar. 2013	Jun. 2013	Sep. 2013	Dec. 2013	Mar. 2014	Jun. 2014	Sep. 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
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
Capital to total assets	9.8	9.6	9.0	8.9	8.9	9.3	8.9	8.9	8.8	9.0
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
Provisions to NPLs	66.7	69.3	71.8	71.9	73.2	76.5	78.4	77.8	79.5	77.6
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
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
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
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
Noninterest expenses to gross income	52.7	51.1	53.9	57.5	56.4	56.8	57.4	56.8	54.6	54.9
Liquidity										
Liquid assets to total assets	36.1	45.5	47.4	47.4	49.0	46.7	47.3	48.3	47.8	48.3
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
Loans/Deposits	61.4	53.6	51.5	51.6	48.1	48.7	48.6	49.2	47.7	48.2

Source: State Bank of Pakistan.
1/ As of December 2013, CAR indicators are reported under Basel II

Table 9. Pakistan: Indicators of Fund Credit, 2013–18
(In millions of SDR unless otherwise specified)

		Projections				
	2013	2014	2015	2016	2017	2018
		(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
Of which:						
ECF, SBA, and ENDA	1,576.8	303.0	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
In percent of end-period gross official reserves	101.8	34.5	37.2	38.7	32.1	26.6
As a share of external debt	5.8	5.9	8.2	9.4	8.7	7.7
		(Projected Debt Service to the Fund based on Existing and Prospective Drawings) 1/				
Total	2,355.1	232.4	339.2	63.5	72.2	223.0
Of which:						
Principal	2,313.5	228.8	303.0	0.0	0.0	150.0
Interest and charges	41.7	3.6	36.2	63.5	72.2	73.0
SBA and ENDA Principal		228.8	303.1	0.0	0.0	0.0
Extended Fund Facility Principal		0.0	0.0	0.0	0.0	150.0
In percent of end-period gross official reserves	104.4	3.3	3.5	0.6	0.5	1.4
As a share of total external debt service	50.8	5.0	6.8	1.7	1.8	4.0
Memorandum items						
Quota (millions of SDRs)	1,033.70	1,033.70	…	…	…	…

Source: IMF staff projections.
1/ Excludes current year obligation paid up to October 16 , 2014.

Table 10. Pakistan: Selected Vulnerability Indicators, 2010/11–2018/19

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19
					Projections				
Key economic and market indicators									
Real GDP growth (factor cost, in percent)	3.6	3.8	3.7	4.1	4.3	4.4	4.8	5.0	5.0
CPI inflation (period average, in percent) 1/	13.7	11.0	7.4	8.6	7.9	6.8	6.0	6.0	6.0
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	-1.5	-1.6	-2.1	-2.3	-2.7
Net FDI inflows (percent of GDP)	0.7	0.3	0.5	0.6	0.6	1.1	0.7	0.9	1.1
Exports (percentage change of U.S. dollar value; GNFS)	25.0	-4.5	6.0	-3.6	2.8	3.7	5.2	6.3	4.3
Gross international reserves (GIR) in billions of U.S. dollars	14.8	10.8	6.0	9.1	14.1	16.5	19.9	23.1	26.2
GIR in percent of ST debt at remaining maturity (RM) 2/	332.8	273.7	106.5	137.5	196.5	194.8	453.6	992.5	1057.8
GIR in percent of ST debt at RM and banks' foreign exchange (FX) deposits 2/	169.3	125.4	55.3	71.6	103.8	108.4	171.7	230.1	242.7
Total gross external debt (ED) in percent of GDP, *of which:*	31.1	29.1	26.2	26.2	24.5	24.5	24.7	25.0	25.0
ST external debt (original maturity, in percent of total ED)	1.0	0.6	0.0	1.1	2.3	-0.2	-0.1	-0.1	-0.1
ED of domestic private sector (in percent of total ED)	10.8	10.8	10.4	13.2	16.9	19.2	23.2	29.5	35.5
ED to foreign official sector (in percent of total ED)	89.2	89.2	89.6	86.8	83.1	80.8	76.8	70.5	64.5
Total gross external debt in percent of exports	213.2	220.2	193.2	215.6	212.4	215.4	221.2	226.3	234.7
Gross external financing requirement (in billions of U.S. dollars) 3/	1.7	6.7	5.3	6.4	8.0	10.0	9.4	10.5	13.9
Public sector 4/									
Overall balance (including grants)	-6.9	-8.4	-8.1	-4.7	-4.5	-3.8	-3.4	-3.2	-3.0
Primary balance (including grants)	-3.1	-4.0	-3.7	-0.2	0.2	0.5	0.5	0.6	0.6
Debt-stabilizing primary balance 5/	-7.8	1.4	-1.6	-3.1	-0.6	-1.2	-1.6	-1.6	-1.5
Gross PS financing requirement 6/	26.9	32.5	35.9	34.6	29.5	28.0	25.7	24.3	22.8
Public sector gross debt 7/	55.3	60.5	62.3	62.5	61.2	59.1	57.3	55.2	53.7
Public sector net debt 8/	52.0	57.2	59.5	60.2	59.2	57.4	55.9	54.0	52.7
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	11.4	...	...	...	...	...
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
September 2, 2014	360	35	Fourth review and end-June 2014 performance /continuous criteria
December 2, 2014	360	35	Fifth review 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.

Appendix I. Letter of Intent

December 2, 2014
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 fourth and fifth reviews was mostly satisfactory. We have met some of the performance criteria for the fourth and fifth program reviews and continue to move forward on our ambitious structural reform agenda. While further effort is needed in some areas, we are committed to the corrective actions described in the attached Memorandum of Understanding of Economic and Financial Policies (MEFP). Despite recent floods and uncertainties, there are signs of improvement in economic conditions and balance of payments pressures have been contained. 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 maintenance of fiscal, monetary, and financial sector buffers to safeguard against risks.

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

- *Quantitative performance criteria and indicative targets.* The end-June 2014 quantitative performance criteria (PCs) were observed with the exception of the targets on Net Domestic Assets (NDA) and on government borrowing from the State Bank of Pakistan (SBP), which were missed. Although NEPRA tariff determination and notification were accomplished as per the prior action for the Third Review, the increase in electricity tariffs scheduled for 1st July 2014 did not go into effect due to last minute difficulties. Three PCs were missed for end-September 2014 (on Net International Reserves, on NDA, and on government borrowing from the SBP). We have since taken action to address these shortcomings and are on track to meet the end-December 2014 targets as outlined in the attached MEFP. The indicative target on transfers under the Benazir Income Support program (BISP) was met.

- *Corrective actions for missed targets :*

  - To address the shortfall in electricity prices, we adjusted tariffs by PRs 0.30/kWh effective from October 1, 2014, taking advantage of a decline in the automatic fuel surcharge due to lower world oil prices. We will use continue to use the downward trend in oil prices to make further adjustments while maintaining consumer prices constant (MEFP ¶27).

- ➢ We also stepped up the accumulation of international reserves through interventions in the foreign exchange market, and accumulated additional reserves with the successful issuance of international Sukuk securities (¶5).

- ➢ We have improved our debt management practices and public debt issuance calendar, and are strengthening the Debt Policy Coordination Office (DPCO) to better manage the government borrowing target from the SBP (MEFP ¶20).

- ➢ We have taken steps to keep the stock of NDA at PRs 2,450 billion by end-November, 2014, and we will also improve the SBP interest rate corridor to better manage liquidity (new structural benchmark, MEFP ¶4).

- *Structural Benchmark (SBs).* Performance on SBs was mixed. Of the seven SBs pending since the completion of the third review, three were met—elimination of the exemptions and concessions granted through SROs; improving the internal operations of the SBP; and offering minority shares of UBL and PPL. Others remain outstanding—amending the relevant tax laws on anti-money laundering (AML); consolidating the responsibilities of the public debt management office; filling the vacancies in the NEPRA Board; and enacting the amendments to SBP's law to give SBP more independence. We remain committed to secure the completion of these SBs.

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 five 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 waivers on the three end-September performance criteria, and the completion of the fourth and fifth reviews under the Extended Arrangement.

We believe that the policies set forth in this letter and in the letters of August 19, 2013, December 11, 2013, March 6, 2014, and June 19, 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/	/s/
Ishaq Dar	Ashraf Wathra
Minister of Finance	Governor of the State Bank of Pakistan
Pakistan	Pakistan

Attachment I. Memorandum of Economic and Financial Policies

Recent Economic Developments and Outlook

1. **Economic activity is gradually improving**. Provisional national accounts estimates show that GDP grew 4.1 percent in FY2013/14, primarily driven by the services and manufacturing sectors. For program purposes, we now expect that GDP growth reach about 4.3 percent in FY 2014/15 though the government retains its goal of achieving a growth of 5.1 percent. Risks to growth are tilted to the downside due to the recent floods, but initial assessments suggest that the macroeconomic impact will be small. Downside risks will be mitigated by easing oil prices, which should help increase energy supply and provide a cushion against external vulnerabilities. Headline inflation for end-October 2014 fell to 5.8 percent over October 2013, and we now expect it to ease to around 7½ percent by the end of this fiscal year (7.9 percent annual average), helped by prudent monetary policy and a favorable global commodity price outlook.

2. **The external current account deficit was slightly higher than projected over the past two quarters**. This reflects lower goods exports and higher imports, which were partially compensated by strong workers' remittances. The capital and financial account was stronger than expected in FY2014Q4, helped by the US$2 billion Eurobond placement, bilateral and multilateral inflows, and privatization receipts. However, this performance was not sustained in FY2015Q1 due to delays in privatization and Sukuk transactions in international markets and fewer multilateral disbursements. As a result, the rapid build-up of gross reserves seen from US$5.4 billion at end-March to US$9.1 billion by end-June 2014 lost momentum due to political disruption and uncertainty. Reserves edged down to US$8.9 billion by end-September 2014. The rupee was relatively flat during the last quarter of FY2013/14, but weakened since end-June by about 3.3 percent against the dollar. For the remainder of FY2014/15, we expect the current account to show some further weakening, driven by a larger trade deficit, which will continue to be partly compensated by stronger workers' remittances. External financing will continue to be supported by significant program disbursements, debt issuance, and the government privatization program. This will help to sustain an improvement in the reserve coverage ratio, which is now expected to exceed 3-months of imports by end FY2014/15.

A. Monetary and Exchange Rate Policies

Economic Policies

3. **Monetary aggregates continued to grow broadly in line with program objectives in the last two quarters**. The SBP continued to accumulate foreign reserves, which helped the stock of Net Foreign Assets (NFA) to recover to well above pre-program levels. The growth rate of broad money declined to 12.2 percent y-o-y in September 2014. Reserve money growth also declined by 4.7 percent y-o-y compared to the previous quarter and it remained well below the previous year's growth rate of 14.3 percent. Private sector credit continued to accelerate (reaching 13.4 percent

y-o-y growth by end-September 2014) driven mainly by businesses, and in particular manufacturing and power generation.

4. **Performance under the monetary targets was mixed**. The end-June PC on Net International Reserves (NIR) was met by a wide margin (US$1.6 billion), due in part to Eurobond issuance and spot market purchases. But the SBP missed the end-September target by US$630 million due to delays in privatizations, despite significant foreign exchange spot purchases. The ceiling on the net swap/forward position was also met both at end-June and end-September and the SBP is on track to meet the end-December target as well. However, we missed both end-June and end-September targets on government borrowing from the SBP due to the delays in privatization and Sukuk issuance. Since then, we have taken corrective actions to bring down the stock of government borrowing from the SBP to end-December program targets (¶19). For the same reasons, the SBP also missed the end-June and end-September ceilings on Net Domestic Assets (NDA) by PRs 151 billion and PRs 25 billion, respectively. The SBP has since taken steps to keep the stock of NDA at PRs 2,450 billion by end-November, 2014 (prior action) and is on track to achieve the end-December NDA program target. To enhance the effectiveness of monetary policy, better manage liquidity in the interbank market, and conduct open market operations, the SBP will embark on a plan to gradually improve its interest rate corridor by setting the policy rate between the floor and ceiling rates of the corridor. To this end, the SBP will announce its time-bound plan by end-February 2015 (new structural benchmark) and make the improved interest rate corridor operational by end-September 2015.

5. **Monetary and exchange rate policies continue to be geared toward rebuilding SBP reserves and maintaining price stability**. Headline and core inflation have been on a declining path in the past few months. However, we believe that preserving this momentum requires a continued prudent monetary policy stance to anchor inflation expectations. To this end, the SBP will use monetary policy tools as needed to bring inflation sustainably below 7½ percent by the end of FY2014/15. In particular, the central bank will adhere to program NDA targets, improve the functioning of the interest rate corridor (¶4), and set the policy rate in a forward-looking fashion to maintain positive real interest rates in line with its desired inflation path. The SBP will continue its purchases of foreign exchange in the spot market to build reserves. The SBP will pursue inflation goals for monetary policy and improve communications with the public about its framework.

6. **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, not meeting the end-June 2014 structural benchmark to enact the legislation. 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 revise the

draft law in the NA committee and have the committee report the legislation to the full assembly by end-March 2015. Enactment of the legislation is now expected for end-June 2015 (structural benchmark proposed to be rescheduled).

7. **We are taking steps to enhance SBP operations**. The SBP has met the structural benchmark for end-August on improving its internal operations. In addition, it adopted International Financial Reporting Standards (IFRS) as its financial reporting framework and accordingly the financial statements for FY2013/14 are prepared and audited in accordance with requirements of full IFRS/IAS for the first time. While awaiting the amendments to the SBP law, we will introduce additional non-legislative measures, in line with the recommendations in the Safeguard Assessment Report, to further improve internal operations of the SBP. Specifically: (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 safeguard procedures, the Internal Audit Department will conduct reviews of the program monetary data reported to the IMF, within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff. (new structural benchmark end-February 2015).

B. Fiscal Policy

8. **Fiscal consolidation remains a crucial objective of the government's economic program**. We remain committed to achieving fiscal consolidation of around 4–4½ percent of GDP over the three year program, which will lower the deficit to around 3½ percent of GDP and place the debt-to-GDP ratio on a firmly declining path. The negative impact of fiscal consolidation on economic activity has been—and will continue to be—ameliorated by implementing structural reforms to boost growth, expanding targeted assistance programs to protect the most vulnerable, and developing a more efficient and equitable tax system to create fiscal space to finance development spending and foster inclusive growth.

9. **Fiscal performance in FY2013/14 was stronger than planned, achieving a reduction in the budget deficit (excluding grants) from 8.3 percent to 5.5 percent of GDP**. Once grants are included, the overall deficit fell even further to 4.7 percent of GDP. Tax revenues and spending were broadly in line with expectations. The tax-to-GDP ratio increased by 0.5 percentage points despite the nonrecovery of GIDC arrears, while non-tax revenues overperformed, rising by 0.7 percentage points due to higher-than-projected SBP profits. As planned, during the last quarter of the FY 2013/14 we were able to scale up capital spending (which had been kept low in the first nine months of the year as a precaution against shortfalls in revenue). At the same time, the provinces ran budget surpluses consistent with achieving the envisaged year-end fiscal outturn.

10. **The approved FY2014/15 budget is consistent with program objectives, aiming to lower the deficit (excluding grants) to 4.8 percent of GDP**. The envisaged fiscal adjustment in the current year is underpinned by tax revenue measures and further rationalization of energy subsidies. However, the delay in implementing the electricity tariff adjustment and the court order

against the Gas Infrastructure Development Cess (GIDC) have created risks to the fiscal outlook. To address these concerns, we have developed a new electricity tariff strategy (¶27), and in the event that GIDC legal concerns are not resolved by January 2015 (¶34) we stand ready to take compensatory measures as agreed, including adjustment on the revenue side, to reach our fiscal targets.

11. **We remain committed to our plan to broaden the tax base through the elimination of tax exemptions and loopholes**. We have issued no new Statutory Regulatory Orders (SROs) granting exemptions or concessions in recent months with only one exception (related to an emergency situation in basic food supply). We reaffirm our commitment not to issue any new tax concessions or exemptions through SROs, which narrow the tax base, complicate tax administration, and weaken tax compliance. We will prepare the necessary draft legislation by end-March 2015 at the latest (new structural benchmark) to permanently prohibit the practice and we expect approval of the legislation on or before end-December 2015. The FY2014/15 budget included the necessary legislation to eliminate SRO exemptions and concessions totaling 0.34 percent of GDP, plus additional tax policy measures to broaden the tax base amounting to 0.2 percent of GDP. Moreover, the FY2014/15 budget included a detailed list of the remaining tax expenditures, which we will continue to publish in future budgets. Our plan for eliminating most SROs granting tax exemptions or concessions (finalized in December 2013) is expected to ultimately increase tax revenues by 1-1½ percent of GDP, with all designated SROs eliminated in no more than three years. These steps will facilitate gradually moving the GST to a full-fledged integrated modern indirect tax system with few exemptions, along with an integrated income tax, by FY2016/17.

12. **Tax administration reforms will gradually deliver further improvements in revenue collection**. In view of the low level of tax compliance and widespread evasion, 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 have initiated the tendering of electronic volume tracking of production to improve sales tax collection. We will award the contract for the systems by end-December 2014.

b. We have started the field surveys of potential high net worth taxpayers to broaden both the sales and income tax bases. In all, we have already issued investigation/contravention reports worth ¼ percent of GDP.

c. We have begun the implementation of an IT solution for tax refunds (computerized risk-based evaluation of sales tax or CREST) that has already pointed out discrepancies in sales tax invoices at different stages and put an effective check on many fake invoices and inadmissible refunds, leading to fiscal savings. So far, this system has allowed us to reject false claims worth some PRs 10 billion.

d. We have introduced risk-based e-registration in sales tax to manage new registrations.

e. We have revised valuation rulings in customs duties to mitigate wrong declarations and underinvoicing.

f. We have appointed an information technology member to the FBR to revamp and integrate FBR IT systems.

g. We have started the electronic data interchange (EDI) connectivity to streamline trade with Afghanistan.

13. **We are committed to implementing strong actions in enforcement and auditing as part of our tax compliance program**. Using the powers entrusted under tax laws, the FBR is stepping up actions, including to: (i) legally charge tax evaders; (ii) temporarily close businesses and/or attach properties of tax offenders; and (iii) attach bank accounts of tax defaulters to withdraw the assessed tax liability directly from their accounts. In mid-February, we published a tax directory of all current parliamentarians at both the federal and provincial levels and the full directory of all taxpayers at end-April in an effort to foster a culture of transparency and compliance. The number of nonfiling parliamentarians (at both the federal and provincial level) has since fallen from 8 percent to 2.5 percent, and it should fall to zero by next fiscal year. In addition, we increased the number of tax audits to 5 percent of declarations (from 2.2 percent last year). We have completed around 90 percent of selected audits, which created additional revenue demands of almost PRs 16 billion. Moreover, we are reviewing the internal system of incentives. To further strengthen the enforcement capability of the FBR, we set up an integrity and performance unit to encourage high achievers and punish corruption in the tax service, and a fiscal management cell to target nontaxpayers with an ostentatious lifestyle.

14. **We will expand and improve the information technology infrastructure at the FBR to enhance our tax compliance efforts**. We are building a monitoring system to track progress and set quarterly objectives on tax policy and administration initiatives (as described in the TMU). We already issued 140,000 first notices through end-September 2014, and we are ahead of schedule on our plan for 300,000 notices, out of which 20,000 individuals have so far registered and filed returns. With our scheme for differential taxation between filers and non-filers, we will encourage more taxpayers into the tax base. We have also initiated a sales tax collection scheme for retailers that identified over 25,000 large retailers and estimated over 1.3 million small retailers as new potential sales tax payers. Furthermore, we have established quarterly FBR revenue targets and propose including them as indicative targets (as defined in the TMU) under the IMF program. At the same time, we will continue to strengthen our database by collecting information from multiple sources including urban property transactions, motor vehicle procurement, and international travel. In addition, we plan the following further tax administration actions:

a. We will target nonfilers who have the potential to contribute at least the average tax paid by currently registered taxpayers.

b. We will streamline the online filing scheme, which will facilitate registration and filing of personal income tax returns by simplifying the tax return form.

c. We will expand the coverage of tax audits to 7.5 percent of filed tax returns and improve their quality to generate a revenue demand of approximately PRs 25 billion. The balloting will also cover elected representatives, key public figures, sports persons, performing artists, etc., demonstrating the government's resolve on tax collections.

d. We will continue to seek technical assistance on tax administration from our international partners.

15. **Beyond the current fiscal year, further revenue and expenditure measures will be implemented to achieve a sustainable deficit of around 3½ percent of GDP by the end of the program**. This will require further fiscal consolidation of 1–1¼ percent of GDP in FY2015/16, with the remainder in FY2016/17. Well over half of the adjustment should come from the revenue side, mainly through further widening of the tax base (including from the elimination of the remaining designated SROs), with some contribution from improved tax administration. With enhanced revenue collection and a broader tax base, we hope to avoid the need for further increases in GST or income tax rates while achieving our overall deficit targets. On the expenditure side, further reductions in untargeted subsidies will be undertaken in FY2015/16, along with steps to streamline public administration, including wage and salary costs.

16. **Provincial governments remain crucial in the fiscal reform process, especially by improving revenue collection at the provincial level**. Under successive constitutional amendments (most recently the 18th), Pakistan has moved decisively to 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 a substantial devolution of spending responsibilities and taxation authority in agriculture, property and services. To assure achievement of our fiscal targets in FY2014/15, and following last year's agreement under the Council of Common Interest, the provincial finance secretaries agreed to maintain provincial budget surpluses consistent with the program. Going forward, the government will seek an agreement that will find a balance between devolution of revenue and expenditure responsibilities and is consistent with the imperatives of macroeconomic stability. In preparation for these negotiations, we will seek technical assistance from our international partners to reflect best practices by undertaking studies with the goal of achieving sustainable federal-provincial fiscal relations.

17. **We continue our support to the poor and most vulnerable segments of the population through the Benazir Income Support Program (BISP)**. We have reached around 4.6 million families paid by end-September 2014 and achieved the indicative targets for transfer payments for both end-June and end-September 2014. We remain on track to reach around 4.8 million beneficiaries by end-December 2014. To ensure timely payments, we are extending the current contracts with commercial banks making e-banking payments and will phase-in the rollout of new ATM cards following the completion of competitively selected e-banking options. We will approve the new e-payment mechanism by end-June 2015 to start implementation early July 2015. This transition may temporarily affect the timeliness of beneficiary payments, but we will assure that all beneficiaries will receive their payments before the quarter ends. To protect the vulnerable segments of society from reduction in untargeted electricity subsidies, inflation, and fiscal adjustment measures, we have increased the stipends paid to the poorest families from PRs 3,600 to PRs 4,500 per quarter starting from FY2014/15. We will also expand coverage through stepped-up

outreach efforts, with a target of reaching an additional 0.7 million eligible families by end-June 2015. In partnership with the provincial governments, we have also made significant progress in the rollout of the education conditional cash transfers. This will allow us to expand the program from five pilot districts to 32 districts in all provinces by end-January 2015. To improve the administrative functioning of the BISP, all vacant positions in the Board have now been filled. Under instructions issued by Government and in compliance with BISP Act 2010, we will resolve administrative and decision-making issues so as to ensure its smooth functioning.

18. **In order to enable the use of anti-money laundering (AML) tools to combat tax evasion, we have started preliminary work to include tax crimes in the Schedule of Offenses of the 2010 Anti-Money Laundering Act (AMLA)**. The FBR has identified a list of serious tax offenses. In order to ensure that serious tax crimes are predicate offences to money laundering, we will enact amendments to the relevant tax laws (as defined in the TMU) and submit amendments to the AMLA to Parliament by end-December 2014 (structural benchmark is proposed to be rescheduled). We will also ensure that the AML framework is properly implemented to facilitate detection of potential cases of abuse of the investment incentive scheme to launder criminal proceeds. In this regard, proper guidance will be provided by the Financial Intelligence Unit to financial institutions and the FBR by end-December 2014. Finally, the Anti-Terrorism (Amendment) Ordinance 2013 has been enacted as a permanent law, in line with the action plan agreed with the Financial Action Task Force (FATF).

C. Fiscal Financing

19. **We are committed to taking measures to contain budget financing from the SBP within program targets**. The successful US$2 billion Eurobond issue helped the government to diversify budget financing, as it continued to shift from short-term domestic financing and borrowing from the SBP to longer-term domestic and external bond financing. However, despite reducing gross government borrowing from the SBP, we missed the end-June target by PRs 88 billion and end-September target by PRs 218 billion for reasons already explained (¶4). The government has since taken corrective actions, including by bringing in Sukuk proceeds, and monitoring monthly stocks of government borrowing, to bring the level to PRs 2,150 billion by end-November, 2014 (prior action) and we are on track to reduce it to the end-December program target. In addition the government will adhere to the domestic public securities plan in upcoming T-bill and Pakistan Investment Bond (PIB) auctions to build buffers for budget financing, and will continue to diversify financing sources (¶20).[1]

[1] The IMF will also provide technical assistance on further developing the local Sukuk market.

20. **Enhancing the quality and effectiveness of public debt management continues to be a priority**. In April 2014, we published the Medium Term Debt Strategy (MTDS) FY2013/14–FY2017/18. Efforts to continue to diversify financing from both domestic and external sources are underway. We have 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 intend to issue Sukuk in international debt markets. We approved an administrative order on September 30, 2014 (structural benchmark) to strengthen the DPCO. While the order, for administrative difficulties, did not unify debt management functions, we are strengthening our organization, staffing, and procedures to bring our debt management up to best international practices, and to ensure that future program targets on government borrowing from the SBP are met. Specifically: (i) we have begun to provide Fund staff with a detailed quarterly financing plan for the coming 12 months and extend the existing in-quarter issuance plan to a rolling quarterly issuance program published every month for domestic public securities (including local Sukuk bonds), by end-November 2014 (prior action), (ii) we are taking steps to strengthen risk management and strategy functions by reorganizing the Debt Policy Coordination Office (DPCO) as a middle office responsible for updating the MTDS and monitoring its implementation, coordinating the credit risk management functions by end-March 2015 (new structural benchmark), 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 of the existing DPCO, we have recruited a Director General to lead the DPCO and build capacity by hiring and/or training additional 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 and executing and communicating the borrowing auctions with the SBP being the agent, and strengthening the primary dealership system. We are also drafting the required rules under the Fiscal Responsibility and Debt Limitation Act 2005. These actions should lead to savings in, and more effective decision-making for, government borrowing.

D. Financial Sector

21. **The performance of the banking sector remains strong, as reflected in financial soundness indicators**. Profitability increased by 44 percent (y-o-y), mainly attributed to an increase in net interest income, declining provisioning charges, and higher non-interest income. Total credit grew by 2.5 percent from June to September 2014. As of end-September 2014, the nonperforming loan (NPL) ratio increased marginally to 13.0 percent, with net NPLs to net loans ratio of 3.2 percent. The capital adequacy ratio (CAR) increased to 15.5 percent, well above the minimum requirement of 10 percent. To further enhance the assessment of the health and soundness of the financial sector, the SBP continues to work on developing a preliminary "encouraged" set of the Financial Soundness Indicators (FSIs) and will work with the IMF on dissemination of some additional FSIs to the public for transparency purposes by mid-2015.

22. **Progress is being made on dealing with the few banks that fall below the minimum capital requirement**. The number of banks that fell short of the minimum CAR of 10 percent has been reduced from four to three, with the largest of the four now in compliance. This state-owned

bank's CAR has improved to 10.01 percent as of end-September 2014, mainly due to improved profitability. The combined shortfall for the three remaining non-compliant banks (all private) has decreased to PRs 11.3 billion (less than 0.04 percent of GDP) as of end-September 2014. The risk to the banking system seems to be negligible, as they encompass only 2.7 percent of banking assets. The SBP is maintaining close monitoring on their activities to ensure conformity with the minimum CAR by end-December 2014. In particular, one bank has received a Letter of Commitment from a strategic foreign investor for a capital injection of US$70 million through a rights issue, which will fully meet the CAR shortfall by end-December 2014. The sponsors of the second bank have injected an additional PRs 2 billion and are committed to meeting the remaining capital shortfall by end-December 2014. The SBP is actively engaged with the last bank regarding its capitalization and is looking at various options for its effective resolution by end-December 2014.

23. **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 stakeholders, and it has been shared with the IMF. It will be submitted to the Parliament by end-December 2014; with enactment expected by end-June 2015 (structural benchmark is proposed to be rescheduled).

b. The revised SECP Act to enhance the regulatory power of the SECP will be discussed with the IMF in November 2014 and will be considered by the Council of Common Interest (CCI) before being submitted to Parliament by end-December 2014.

c. The Futures Trading Bill is being finalized and will be placed before the Parliament for expected approval in mid-2015.

d. The SBP-SECP joint task force (JTF) continues to hold regular meetings to ensure cooperation on the supervision of financial groups. A sub-committee of the JTF finalized its recommendation for an early warning system for financial conglomerates and will develop detailed procedural guidelines for the effective implementation of the system. These guidelines once finalized and integrated into the existing framework, will facilitate effective supervision of financial conglomerates. The preliminary work on consolidated supervision TA has been initiated.

24. **Consultation with major stakeholders on a deposit insurance scheme is underway**. The draft Deposit Protection Fund (DPF) Act has been shared with the IMF for review under the IMF Contingency Planning technical assistance and the draft will be finalized by end-January 2015. We expect the legislation to be enacted by Parliament by end-June 2015 (structural benchmark).

25. **New bankruptcy legislation is being prepared**. The draft Corporate Restructuring Companies (CRC) Act, which is extracted from certain non-controversial sections of the draft Corporate Rehabilitation Act (CRA), will be of pivotal importance in cleaning up banks' balance sheets and allowing them to focus on their core areas of operation. The draft CRC will be finalized

by end-February 2015. After reviewing the company rehabilitation law of different jurisdictions, the SECP is preparing a concept note for developing the CRA, which will be shared with stakeholders by end-June 2015.

Energy Sector Reforms

26. **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.

27. **Price Adjustments**. We have prepared the third round identified in the three-year plan for phasing out the Tariff Differential Subsidy (TDS) to continue to bring tariffs to cost recovery level. In this round, 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, taking advantage of a decline in the automatic fuel surcharge due to lower world oil prices. As world oil prices continue to decline, we will use this downward trend to make further adjustments in the surcharge (as defined in the TMU) to close any remaining gap to stay within the FY2014/15 budgeted electricity subsidy of 0.7 percent of GDP, while maintaining consumer prices constant. We will continue to protect the most vulnerable consumers. Subsequently, NEPRA will determine the FY2014/15 tariffs by February 2015 and we will finalize their notification at rates consistent with our objective of reducing electricity subsidies further to 0.3 percent of GDP for FY2015/16.

28. **Arrears**. The technical and financial audit of the system which was finalized in early-May identified the stock and flow of payables at all levels of the energy sector (including Power Sector Holding Company Limited, PHCL). Building on this audit, we are moving forward with the roadmap to limit the accumulation of payables arrears and to gradually reduce the stock:

a. The stock of arrears at the PHCL in the syndicated term credit finance (STCF) facility stood at around PRs 270 billion at end-September 2014. We have levied a surcharge (as defined in the TMU) to service part of the facility, and the tariff adjustments specified in ¶27 will be sufficient to fully service the remainder of the debt.

b. The payables in the power sector reached around PRs 256 billion at end-September 2014 of which around PRs 60 billion constitute current payables. The remainder comprises: (i) a residual leftover from payables clearance of May and July 2013; (ii) A disputed amount with the Independent Power Producers (IPP); (iii) Distribution Companies (DISCOs) non-recovery and penalties levied on past nonpayment (as defined in the TMU), and (iv) transmission and distribution losses that are not recognized by the regulator.

c. We will continue to reduce losses and improve collections through capital expenditures and revenue-based load management. We reduced losses by 0.3 percentage points (to 18.6 percent) and increased collections by around 1.6 percentage points in FY 2013/14. We will further improve performance in FY2014/15.

d. We have developed a monitoring mechanism to track the stock and flow of payables (as defined in the TMU).

29. **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 with the performance contracts, 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. The ordinance has been submitted to the Parliament for ratification, and the President extended the promulgation by another 120 days to August 27, 2014. Currently, the Bill stands at the Senate Committee after the clearance of the National Assembly. We expect it to be enacted before end-December, 2014. 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 by end-November 2014 and will be submitted to the CCI by end-December 2014. We declared the session courts (district level courts) as Utility Courts as defined in the Penal Code. Utility Courts will build on investigation systems and fast track mechanisms to improve enforcement by end-2014. In order to minimize losses from low payment rates, all state-owned DISCOs are now implementing revenue-based load shedding, which has begun to increase collections.

30. **Demand Side Management**. To encourage energy conservation, we will use pricing (¶27) and other market-based instruments to improve resource allocation and energy efficiency. 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 Act for placement to the Parliament by mid-December 2014. The act will include equipment performance standards, and would cover key electrical and gas equipment and appliances which are not yet covered.

31. **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. Three rehabilitations completed in March 2014 recovered around 700 MW of capacity while increasing efficiency by 1–1.5 percent. Moreover, 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 generate an additional 2000 MW by 2016.

32. **Governance, Regulatory, and Transparency Improvements**. We continue to place high priority on improving energy sector governance and transparency. We have already hired entry and middle management positions to enhance the technical capacity of the regulatory body, the National Electric Power Regulatory Authority (NEPRA). In order to begin addressing administrative and technical constraints, we conducted a diagnostic study of the regulatory framework of the power sector and prepared an interim report in April 2014 (structural benchmark). We have appointed a Board member with financial skills to NEPRA; however, the appointment for the Chairman was not made due to legal challenges. These challenges have been since been resolved and we have now appointed the chairman. 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 by end-September 2015. We have set-up the Central Power Purchasing Agency (CPPA) by separating it from the National Transmission and Despatch Company (NTDC) and have amended the Articles of Association. To make CPPA operational, we issued the standard operating procedures for payments and settlements and key CPPA staff will be in place by end-December 2014. We have finalized agency agreements between CPPA and the DISCOs to purchase power on their behalf.

33. **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) through corporatization and commercialization, 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 CPPA for all power purchased from WAPDA Hydel. We have included several DISCOs in our privatization plans for the coming 2–3 years and we are committed to introducing competitive pricing and direct contracting between power producers and wholesale customers in the power sector.

34. **Oil and Gas Sector**

- **Supply**. To help tackle gas shortages, we have started efforts to import Liquefied Natural Gas (LNG) and we are on track to receiving the first LNG imports by early 2015. We are 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. 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**. We are closely following the gas price rationalization plan of December 2013 to encourage new investment, promote efficiency in gas use, and assure that there will continue to be no fiscal cost from the gas sector:

  - We are implementing the Petroleum Exploration and Production Policy 2012 (2012 Policy) with amendments for enhanced production from existing and new fields and to further improve producer incentives. With price increases ranging from 2.8–3 U.S. dollars per

MMBTU to 6–10 U.S. dollars per MMBTU, we are incentivizing producers to enhance production from existing fields as well as to initiate new exploratory efforts. We have finalized the concession agreements for the 43 new blocks for exploration in new fields, and will complete the conversion of existing concessions to the 2012 Policy by end-February 2015 with support from international partners. During FY2014/15 we will award an additional 10–15 blocks. As new production and additional gas supply from imports come on line, the cost of this gas will continue to be fully reflected in the base tariff on a semiannual basis. The recent difficulties and oil-indexed decline in gas prices delayed the first gas price notification of FY2014/15 (due in August). We will notify and implement the next adjustment in the beginning of 2015, and will make further adjustments as needed when the imported gas comes online.

- To better allocate gas consumption, we adjusted the weighted average consumer prices at end-December 2013 through the application of the GIDC, which 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 GIDC has been suspended despite the Presidential Ordinance which was issued following the previous Supreme Court decision. We will actively pursue the ongoing litigation for an early decision to ensure full recovery of the GIDC. In the meantime, we have prepared and reached understandings with the IMF on contingency measures which we will implement to achieve a similar outcome if the GIDC legal challenges are not resolved by January 2015.

- We are 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-March 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 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. The current level of unaccounted for gas losses (UFG) is on average 12.5 percent due to commercial and technical losses. We are working with the World Bank on the Natural Gas Efficiency Project (NGEP) in coordination with other IFIs. We are pursuing companies at the highest level to reduce losses benchmarking international standards through investment measures, managerial and administrative improvements, and through building the capacity of the gas distribution companies. In January 2014, the President has promulgated the Gas (Theft Control and Recovery) Ordinance 2014, which was sent to the Parliament for expected approval by end-

December 2014. Finally, we affirm our commitment to enhance the capacity of Oil and Gas Regulatory Authority (OGRA).

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.

35. **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, complicated 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.

- ***Contract enforcement***. We completed in March 2014 a study to identify the needs of corporations to speed up rehabilitation of weak but viable companies. Based on the findings of the study, we will expedite the liquidation of the insolvent entities through two tracks: (i) the Corporate Restructuring Companies Act, which envisages setting up private Corporate Restructuring Companies to take over assets of bankrupt companies; and (ii) the Corporate Rehabilitation Act (¶28). In addition, we have established Alternative Dispute Resolution (ADR) Mechanisms in Karachi and Lahore. This 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).

- ***Start-ups***. The FBR, in coordination with SECP, Employees Old-Age Benefits Institute, and other stakeholders (including provinces) have approved a plan to simplify procedures and costs for setting up businesses. The implementation has begun through streamlining overlapping procedures, and establishing database sharing and a common portal for registering businesses.

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

- ***Access to credit***. Access to finance for poor and marginalized segments 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, is developing a comprehensive National Financial Inclusion Strategy (NFIS) to implement financial sector reforms to meet their financing needs. The SBP has completed the stocktaking exercise under NFIS and conducted consultations with stakeholders in September 2014 to identify policy reforms and interventions to enhance market information, infrastructure, and financial capability of the consumers. We are preparing the draft strategy document, which will be shared with all stakeholders for their input and buy-in before finalizing the NFIS by end-December 2014.

36. **Trade Policy**. Trade 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.[2] 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 reducing the tariff slabs and the next round of SRO elimination with the next 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 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.

37. **Public Sector Enterprises**. 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 in 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.

- ***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 hired three financial advisors for United Bank Limited (UBL), Pakistan Petroleum Limited (PPL) and Oil and Gas Development Company Limited (OGDCL) in May 2014 and successfully sold minority stakes in UBL and PPL in June 2014 (structural benchmark). In November, we hired financial advisors for Allied Bank Limited (ABL) and Habib Bank Limited (HBL) to market minority stakes within six months.

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

- ***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. We will finalize the sale of Heavy Electric Complex (HEC) by early-December 2014. We hired financial advisors for National Power Construction Co. (NPCC) in July 2014 to finalize the offer by end-March 2015. We also appointed financial advisors for share sales of Faisalabad Electric Supply Company (FESCO) and Northern Power Generation Company Limited (NPGCL) in July 2014 and plan to complete the transactions by end-August 2015. For Islamabad Electric Supply Company (IESCO) and Lahore Electric Supply Company (LESCO), we have hired financial advisors in November 2014 for expected completion of transactions by end-October 2015.

- ***Restructuring***. We are developing medium-term action plans to restructure Pakistan International Airlines (PIA). We have developed restructuring plans for Pakistan Steel Mills (PSM) and Pakistan Railways (PR). 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 company by end-December 2015 (revised structural benchmark).

  - **Pakistan Steel Mills**. We have appointed a professional board and a new chief executive officer and approved a comprehensive restructuring plan in April 2014 to prepare for potential strategic private sector participation in the company. We requested expressions of interest for financial advisors in October 2014 and will finalize the hiring by end-December 2014.

  - **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 60 percent through rationalization of tariffs and expenditures and improved occupancy rates. We further increased revenues by over 20 percent in the first quarter 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 institutional framework, financial stability, and service delivery. In the short-term we will focus on improvements in freight transportation through creation of a freight company, and adding more locomotives and wagons that is projected to double revenues from freight operations before the end of the current fiscal year. We are also in the process of reviving the Railway Board and will finalize the appointment of Board members by end-December 2014.

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets for FY2013/14 and 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
	Actual	Fourth Review			Fifth Review			Program		Projection	Projection
		Target	Adjusted target	Actual	Target	Adjusted target	Actual				
Performance Criteria											
Floor on net international reserves of the SBP (millions of U.S. dollars)	-2,437	1,800	1,064	2,678	3,000	3,260	2,630	3,500	4,500	5,700	7,000
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,402	2,324	2,221	2,355	2,306	2,291	2,316	2,436	2,365	2,322	2,217
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	2,012	1,464	1,468	1,402	376	383	337	722	1,087	1,387	375
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	2,255	2,150	2,150	1,725	1,900	1,900	1,675	1,775	1,775	1700	1550
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3/	2,168	2,240	2,240	2,328	2,070	2,070	2,289	2,000	1,905	1,865	1,800
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	62	62	66	14	14	21	36	69	95	22
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	1,936			2,266			539	1,195	1,883	2,756	

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
Prior Actions				
1	Bring the government borrowing level from the SBP to PRs 2,150 billion.	end-November 2014		Ensure PC on Government borrowing is met (MEFP ¶19).
2	Limit the stock of Net Domestic Assets of the SBP to PRs 2,450 billion. 1/	end-November 2014		Ensure PC on NDA is met (MEFP ¶4).
3	Provide Fund staff with a detailed quarterly financing plan for the coming 12 months and extend the existing in-quarter issuance plan to a rolling quarterly issuance program published every month for domestic public securities (including local Sukuk bonds).	Five days prior to the board meeting		Bring debt management up to best international practices, and to ensure that future program targets on government borrowing from the SBP are met (MEFP ¶20).
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 budet.	end-June-2014	Met	Reduce distortions and improve revenue collection.
3	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-September 2014	Not met, rescheduled to end-December, 2014	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.
4	Approve an administrative order to consolidate the responsibilities of public debt management in the debt management office.	end-September 2014	Partially met	Strengthen the organizational framework for effective public debt management.
Monetary sector				
5	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 2014	Not met, rescheduled to end-June 2015	Prerequisite for an independent monetary policy framework.
6	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.
Financial sector				
7	Enact the Securities Bill, in line with Fund staff advice.	end-December 2014	Rescheduled to end-June, 2015	Enhance the resilience of the financial sector.
8	Enact the Deposit Protection Fund Act, in line with Fund staff advice.	end-June 2015		Enhance the resilience of the financial sector.
Structural Policies				
9	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.
10	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	
11	Conduct a diagnostic study of the regulatory framework of the power sector and prepare an interim report.	end-April 2014	Met	
12	Offer the minority shares in United Bank Limited and Pakistan Petroleum Limited to domestic and international investors.	end-June 2014	Met	
13	Fill the vacancies in the NEPRA Board.	end-July 2014	Met at end-November, 2014	
14	Privatize 26 percent of PIA's shares to strategic investors.	end-December 2014	Rescheduled to end-December, 2015	
New Structural Benchmarks				
15	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.
16	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		Improve SBPs liquidity management.
17	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 safeguard procedures, the Internal Audit Department will conduct reviews of the program monetary data reported to the IMF, within two months after each test date, for accuracy and compliance with the TMU and share the findings with IMF staff.	end-February 2015		Improve monetary policy framework through enhanced central bank independence.
18	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.
19	Conduct a review to reduce the number of existing processes and forms for paying sales and income taxes.	end-March 2015		Improve business climate.

1/ Prior action on NDA is subject to TMU adjustors. The adjusted target for end-November is PRs 2,655 billion.

Attachment II. Technical Memorandum of Understanding (TMU)

December 2, 2014

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 July 3, 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 (¶27 of the MEFP)**

(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 will be levied to increase weighted average tariffs by 4 percent as defined in (i). The current effective notified tariff is PRs 11.82/kWh. This will be adjusted subject to negative Fuel Price Adjustments (FPA) as defined in the following Table to maintain the consumer prices constant.

(PRs/kWh)	November 2014	December 2014	January 2015	February 2015
Estimated change in FPA /1	-0.61	-0.63	-0.42	-0.21
Notified tariff	11.82		12.43	

1/ Energy mix is calibrated from 2013/14

(iv) Syndicated Term Credit Finance (STCF) Surcharge "Debt Servicing Surcharge" (¶28) of PRs 0.30/kWh is included in the electricity tariff (excluding lifeline consumers, 0–50kWh) to service debt incurred by Power Sector Holding Company Limited. The STCF Surcharge is defined as follows:

STFC Surcharge = Total Annual Debt Service of STCF/Estimated volume of electricity sales in FY 2014/15.

	Q1	Q2	Q3	Q4	FY 2014/15
STFC Debt Service (PRs millions)	8,611	6,247	7,840	5,413	28,111

STFC Surcharge = PRs 28,111(millions)/68000(GW) = PRs 0.41/kWh

- The balance = PRs 0.41/kWh–PRs 0.3/kWh =PRs 0.11/kWh will be part of the January 1, 2015 increase in the "Debt Servicing Surcharge."
- 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 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 PHPL and utilized for debt service. In both cased, the excess or deficit will be remedied as a prior year adjustment in the next notification.

18. **Monitoring mechanism to track stock and flow of payables (¶29)**

Overdue payables (over 45 days) stand at **PRs 196 billion** as of end-September 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**	**2014/15Q3**	**2014/15Q4**	**2015/16Q1**
Overdue Payables (cumulative)	207	237	283	372
of which				
Excess T&D Losses	27	5	20	36
Under collection	43	17	18	42
Penalties	7	8	9	10

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
- 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 Investment Ltd—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
	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

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	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 categorize all grants and loans by program/project, and the amounts received/expected in cash and in kind.	Quarterly	Within 15 days of the end of each quarter
	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

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	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
	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

Reporting Agency	Type of Data	Description of Data	Frequency	Timing
	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
		Revised Projection 3/	Actual				
Multilateral and bilateral disbursement	2,853	1,584	767	1,358	1,984	1,361	1,232
of which: in cash 2/	2,608	1297	407	879	1,579	1,151	950
International debt issuance	2,000	0	0	1,500	0	500	0
Coalition Support Fund	375	350	735	240	240	240	240
Other 1/	831	0	0	20	20	1,000	1,300
Gross Inflows	6,059	1934	1,502	3,118	2,244	3,101	2,772
of which: in cash	5,814	1647	1,142	2,639	1,839	2,891	2,490
Debt service	907	1026	990	963	1,274	1,511	1,368
Memorandum items							
Gross International Reserves	9,096	10325	8,943	10,953	12,112	14,103	14,821
Program Net International Reserves	1,800	3000	3,000	3,500	4,500	5,700	7,000

1/ Includes privatization and 3G licenses.
2/ Numbers need to be confirmed with the MoF.
3/ As of November 6

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

	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15
Non Tax revenue	322	353	891	735	240	240	240	540
Of which: Coalition Support Fund	322	353	375	735	240	240	240	240
Grants	100	1538	150	129	153	192	43	65
External interest payments	215	162	212	165	327	200	405	260
Net external debt financing	50	-115	3499	866	1621	2371	1473	-81
Disbursements	645	760	4711	866	2257	3445	2578	1028
of which budgetary support	309	285	2042	84	244	1117	784	529
Amortization	594	875	1212	0	636	1074	1106	1109
Privatizations	0	0	5	0	20	20	1000	1000
Memorandum item								
Program financing	409	1823	2197	213	417	1330	1827	1594

Table 4. Government Sector (Budgetary Support)

(End-of-period stocks/PRs. Millions)

Item	June 30, 2013	Prov. June 30, 2014	Prov. September 30, 2014
Central Government	**5,561,994**	**6,059,496**	**6,228,645**
Scheduled Banks	**3,320,870**	**3,491,821**	**3,685,778**
Government Securities	1,117,115	2,413,134	2,525,537
Treasury Bills	2,611,512	1,550,476	1,647,244
Government Deposits	-407,757	-471,789	-487,003
State Bank	**2,241,124**	**2,567,674**	**2,542,866**
Government Securities	3,127	2,786	2,786
Accrued Profit on MRTBs	44,959	82,070	49,962
Treasury Bills	2,275,183	2,852,274	2,635,524
of which: MTBs created for replenishment of cash balances	2,274,675	2,851,765	2,635,015
Treasury Currency	8,653	8,654	8,654
Debtor Balances (Excl. Zakat Fund)			
Government Deposits	-96,260	-383,571	-159,522
(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**	**-556,077**
Scheduled Banks	**-287,393**	**-352,258**	**-351,874**
Advances to Punjab Gov Advances to Punjab Government for Cooperatives	1,024	1,024	1,024
Government Deposits	-288,417	-353,282	-352,898
State Bank	**-28,214**	**-157,880**	**-204,203**
Debtor Balances (Excl. Zakat Fund)	13,715	802	2,232
Government Deposits (Excl.Zakat Fund)	-41,930	-158,682	-206,435
Net Govt. Budgetary Borrowings			
from the Banking system	**5,246,387**	**5,549,357**	**5,672,568**
Through SBP	2,212,910	2,409,794	2,338,664
Through Scheduled Banks	3,033,477	3,139,563	3,333,904
Memorandum Items			
Accrued Profit on SBP holding of MRTBs	**44,959**	**82,070**	**49,962**
Scheduled banks ' deposits of Privitization Commission	**-5,433**	**-6,438**	**-6,562**
Outstanding amount of MTBs (Primary market; discounted value)	**2,529,412**	**1,525,175**	**1,606,367**
Net Govt. Borrowings (Cash basis)			
From Banking System	**5,124,762**	**5,448,424**	**5,588,291**
From SBP	2,167,951	2,327,724	2,288,702
From Scheduled Banks	2,956,811	3,120,700	3,299,589

PAKISTAN

December 11, 2014

FOURTH AND FIFTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR WAIVERS OF NONOBSERVANCE 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 December 2, 2014**. The additional information does not change the thrust of the staff appraisal.

2. **The authorities met the remaining prior action for this review**. They have provided Fund staff with a detailed quarterly financing plan for the coming 12 months and issued a rolling quarterly issuance program for domestic securities. These steps will facilitate achievement of future program targets on government financing.

3. **Gross official reserves rose to US$9.3 billion as of December 10, 2014**. The State Bank of Pakistan (SBP) has continued to purchase foreign exchange in the spot market, with purchases in the quarter (through December 10) totaling US$680 million, placing the SBP on track to meet the end-December Net International Reserves target. Reserve accumulation was aided by the inflow of US$1 billion from an international Sukuk issue. The rupee has remained roughly stable at around PRs 101–102 per U.S. dollar so far in December. The net short position in foreign exchange swap/forward contracts remains below the end-December program ceiling.

4. **The government initiated a restructuring plan for KASB Bank—one of the three remaining banks below the minimum capital adequacy ratio**. The Federal Government placed KASB Bank under moratorium for a period of six months to protect the interest of depositors and other stakeholders, with expected reconstruction or amalgamation of the bank in this period.

5. **Revenue collection at the federal level was weaker in November than expected**, but the authorities are making gradual progress in improving tax administration and remain on track to meet the end-December fiscal target due to tight expenditure control.

6. **Staff will discuss with the authorities the impacts of falling global oil and commodity prices during the next mission**. Broadly staff expects a net positive impact on growth, inflation, and the balance of payments. GDP effects will be limited in the remainder of FY2014/15, but now staff anticipates higher growth for the next fiscal year. Savings on oil imports will be partially offset by weaker commodity prices for Pakistan's exports (particularly cotton) and by expected slower remittance inflows from oil exporting countries. Sharp declines in food and energy prices are expected to continue easing inflation pressures, which has helped headline inflation to decline to 4 percent y-o-y in November, while core inflation has remained relatively high at 7.4 percent. Staff has revised the headline inflation forecast for FY2014/15 downward by 1 percent.

Press Release No. 14/583
FOR IMMEDIATE RELEASE
December 17, 2014

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fourth and Fifth Reviews Under Extended Fund Facility Arrangement for Pakistan, and Approves US$1.05 Billion Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the fourth and fifth reviews of Pakistan's economic performance under a three-year program supported by an Extended Fund Facility (EFF). The conclusion of the review enables the release of an amount equivalent to SDR 720 million (about US$1.05 billion), bringing total disbursements under the arrangement to SDR 2.2 billion (about US$3.2 billion).

In completing the fourth and fifth reviews, the Executive Board also approved the authorities' request for waivers of non-observance of performance criteria on the basis of the corrective measures taken, including prior actions on net domestic assets and on government borrowing from the State Bank of Pakistan.

The Executive Board approved on September 4, 2013 the EFF for Pakistan in the amount of SDR 4.393 billion (about US$6.44 billion, or 425 percent of Pakistan's quota at the IMF) (see Press Release No. 13/322).

Following the Executive Board's discussion on Pakistan, Mr. David Lipton, First Deputy Managing Director and Acting Chair issued the following statement:

"Macroeconomic conditions are improving, but significant risks to the recovery remain. The measures taken by the authorities to address short-term macroeconomic vulnerabilities and implement structural reforms are bearing fruit, but continued efforts are needed to make the economic transformation more sustainable.

“Fiscal consolidation is broadly on track, but the authorities must be prepared to take further action to address possible revenue shortfalls. There is still ample scope for increasing tax revenues, especially through tax administration reforms. The government has reduced its reliance on central bank financing, but a robust organizational framework for public debt management needs to be implemented.

“Efforts to boost international reserves should continue, including through spot purchases and allowing greater exchange rate flexibility. Monetary policy remains prudent, focused on meeting program monetary targets and achieving a sustained reduction in inflation. Legislation to enhance central bank independence is crucial and should conform to international best practices. It should be complemented by enhanced communication of the central bank price stability objective, improved functioning of the interest rate corridor, and effective open market operations.

“The financial sector remains stable and profitable. Ongoing financial sector reforms and remedial actions in the few banks that don’t reach minimum capital requirements will ensure the system’s continued health.

“Structural reforms are progressing. Addressing the administrative constraints on the power sector’s regulatory framework, improving the operations and collections of energy companies, and electricity tariff reform should continue. The implementation of gas price rationalization should move forward with the gas levy and more favorable producer prices to better allocate the current supply and encourage new production. Commitment to privatization of public sector enterprises is strong, but potential difficulties are related to market conditions. Trade policy and business climate reforms are progressing.

“Finally, the Executive Board, management and staff of the Fund express their deepest condolences to the people of Pakistan for the loss of innocent life in the recent horrific attack on a school in Peshawar.”

Statement by Jafar Mojarrad, Executive Director for Pakistan and Abdelali Jbili, Senior Advisor to Executive Director
December 17, 2014

Our Pakistani authorities thank staff for their hard work, and management and the Executive Board for their continued support, and appreciate the high quality engagement with the Fund under the EFF-supported program.

Program implementation

The strong momentum in program implementation since its inception on September 4, 2013 ran into headwinds lately, in connection with floods, political demonstrations in Islamabad, security-related operations, and judicial challenges to privatization, tax, and energy tariff measures. Inevitably, program implementation since June 2014 was adversely affected, but the economy was resilient. The authorities' flexible and well calibrated policy response aimed at overcoming the temporary difficulties and laying the groundwork for continued program implementation going forward. In this regard, steps have been taken to address the missed targets and preserve macroeconomic stability, while advancing the structural reform agenda.

The status of program implementation is laid out in detail in the report and the MEFP. The performance criterion (PC) on the overall budget deficit was met for end-June and end-September 2014, and the indicative target on cash transfers under the Benazir Income Support Program (BISP) was observed for the two consecutive periods. However, due to delays in privatization and Sukuk issuance, and lower domestic debt issuance, the end-June and end-September PCs on net domestic assets (NDA) and government borrowing from the State Bank of Pakistan (SBP) were missed. The PC on Net International Reserves (NIR) was met with a comfortable margin in June, but was missed for end-September. The SBP met the end-June and end-September targets on its net short swap/forward position. The authorities have taken corrective actions to address the missed PCs, including completion of three prior actions, and are on track to meet the end-December targets.

Performance on structural benchmarks (SB) was mixed for the reasons outlined above. The authorities have proposed five new SBs and remain committed to securing completion of all SBs (Table 2). Our authorities request waivers for non-observance of three PCs for end-September 2014, and completion of the fourth and fifth reviews under the program.

Recent economic developments and outlook

Provisional estimates by the National Income Accounts show that real GDP grew by 4.1 percent in FY 2013/14, primarily driven by better performance of manufacturing and services sectors. For 2014/15, growth is projected at 4.3 percent for program purposes, taking into account lingering effects of the floods, but the authorities retain their goal of achieving a growth rate of 5.1 percent. Reflecting prudent monetary policy and lower commodity prices, headline inflation declined to 4.0 percent year-on-year in November 2014, and average inflation is expected to ease to 7.0 percent in 2014/15 from 8.6 percent in 2013/14. Despite a slight deterioration, the external current account deficit is expected to remain small (1½ percent of GDP in 2014/15), with reserves strengthening to the equivalent of three months of imports.

The medium-term outlook is generally favorable, with trend improvement in growth and inflation and reduced external vulnerabilities, as shown in the report. Falling oil prices, strengthening reform implementation, and improved confidence could very well offset the downside risks indicated in the report (¶6). The ongoing energy sector reform, the buildup of fiscal and external buffers, and the improvement in the business climate will help strengthen confidence and attract foreign direct investment.

Fiscal policy

Progress in fiscal consolidation has been stronger than expected, in line with the authorities' commitment to restore fiscal and debt sustainability over the medium term. The fiscal deficit (excluding grants) was brought down to 5.5 percent of GDP in 2013/14, or a reduction of 2.8 percent of GDP compared to the previous year. Efforts on the revenue and expenditure sides were important contributing factors, as were the budget surpluses achieved by the provinces. In parallel, capital spending was increased toward the end of the year to make up for slower execution during the first half, and cash transfers to the poor under the BISP increased in line with the program target.

The 2014/15 budget seeks to reduce the deficit further to 4.8 percent of GDP, which is in line with the objective of achieving a sustainable fiscal deficit of about 3½ percent of GDP by the end of the program. Enhanced revenue mobilization and expenditure restraint will help offset potential revenue shortfall caused by the delay in raising electricity tariffs and the court order against the Gas Infrastructure Development Cess (GIDC). The authorities have already taken steps to this effect, including the increase in electricity tariffs starting October 1, 2014, taking advantage of the decline in the automatic fuel surcharge as result of lower international oil prices. Further adjustment in the fuel surcharge will be made if oil prices were to continue to decline, as needed to stay within the budgeted electricity subsidy for 2014/15 (0.7 percent of GDP).

Other important revenue efforts include the elimination of a number of tax concessions and exemptions granted through the Statutory Regulatory Orders (SROs), while refraining from issuing new SROs; improvement in tax administration and collection, by issuing a large number of first-time tax notices and using information technology by the Federal Bureau of Revenue (FBR) to enhance tax compliance; and other steps toward implementing a comprehensive tax administration strategy (MEFP ¶11-14). Anti-money laundering tools will be used to combat tax evasion, as will be reflected in the amendments of the relevant tax laws to be submitted to parliament by end-December 2014.

While provincial budget surpluses will continue to support fiscal consolidation, the upcoming renewal of the agreement with the provinces will provide an opportunity to find a better balance between devolution of revenue and expenditure responsibilities, consistent with macroeconomic stability.

Support to the most vulnerable segments of the population through the BISP is expected to reach 4.8 million beneficiaries by end-2014. Enhancements to the payment system are being made by extending existing contracts with commercial banks, and a new e-payment system will be approved by mid-2015. Moreover, the stipend paid to the poorest families has been increased from PRs 3600 to PRs 4500 per quarter starting from FY 2014/15, and efforts are underway to reach an additional 0.7 million families by the end of June 2015.

Significant progress is being made in enhancing the effectiveness of debt management. Following the finalization and publication of the Medium-Term Debt Strategy (MTDS) in April 2014, efforts have focused on lengthening the maturity profile of domestic debt and improving the balance between domestic debt and external debt through the placing of a US$2 billion sovereign loan, which was oversubscribed, and issuance of US$1 billion Sukuk in international debt markets. This has helped reduce government borrowing from the SBP. Further steps are being taken to strength the Debt Policy Coordination Office (DPCO) and enhance its risk management and strategy functions (MEFP ¶20).

Monetary and exchange rate policies

Monetary policy continues to be geared toward reducing inflation and building reserves. Developments during the last two quarters have been in line with the program's objectives, and core and headline inflation have been on a declining trend. With the easing of balance of payments pressure, the SBP has increased its spot market purchases of foreign exchange and is on track to meeting the end-December 2014 NIR target. The SBP stands ready to take actions as and when needed to bring inflation below 7½ percent by the end of 2014/15. Gradually improving its interest rate corridor will help enhance the effectiveness of monetary policy and the management of liquidity through open market operations.

Financial sector

Pakistan's banking sector remains healthy with adequate liquidity, improving profitability, and generally stable asset quality. Capital adequacy has increased to above 15.5 percent, well above the minimum requirement, and the number of banks that fall below the requirement has declined from four to three. Two banks have made additional injections for meeting capital requirements during the last quarter of 2014. With regard to the third bank, the Federal Government, on application of State Bank of Pakistan, placed KASB Bank under moratorium for a period of six months with effect from close of business as of November 14, 2014. The Federal Government has also advised SBP to consider reconstruction or amalgamation of the bank within six months, under section 47 of the Banking Companies Ordinance, 1962. Work is advancing on a deposit insurance scheme under IMF TA, with the relevant legislation expected to be enacted by Parliament by end-June 2015; new bankruptcy legislation is expected to be finalized by end-February 2015; and steps are being taken to strengthen the regulatory and supervisory framework.

In line with the authorities' commitment to enhance the independence of the SBP, amendments to the SBP Act have been submitted to Parliament aimed at ensuring full operational independence of the SBP in pursuit of price stability, establishing an independent decision-making monetary policy committee, and prohibiting any form of new direct government borrowing from the SBP. In the interim, the authorities will take steps to enhance the SBP operations, in line with the recommendations in the IMF Safeguard Assessment Report (MEFP ¶7).

Structural reforms

Structural reforms are critical for achieving high and sustainable growth, and the authorities' reform agenda is moving forward, focusing in particular on energy sector reform, public enterprises, import tariffs, and the business climate. The comprehensive energy sector reform is addressing long standing issues of price distortions, costly subsidies, collection problems, supply and distribution deficiencies, and governance and regulatory weaknesses. As detailed in the report and the MEFP, the authorities are on track to reduce the electricity subsidy to 0.7 percent of GDP in FY 2014/15, through the surcharge implemented in October 2014 and tariffs adjustments planned for January and February 2015. This, together with improved efficiency and collection, will also help reduce the circular debt arrears. For the gas sector, construction of a liquefied natural gas terminal is nearly completed, which will improve supply and help reduce the cost of electricity generation. New gas prices will be announced by January 2015.

The authorities' commitment to privatization of public sector enterprises (PSEs) remains strong as indicated in the report. They are moving forward with the offering of a number of PSEs for privatization, and plan to accelerate the pace of offerings/transactions in the coming year. Trade reform is focusing on simplifying tariff rates, shifting most items to a lower rate, and eliminating trade SROs that establish special rates and/or nontariff barriers.

Efforts are underway to improve the business climate, and the authorities have finalized a detailed plan to this effect, identifying the required legislative and administrative actions, as well as the resources to implement it.

Conclusion

Despite the unforeseen developments that hindered stronger program implementation, the authorities have skillfully addressed the related adverse effects, kept the program on track, and moved forward with their reform agenda of preserving macroeconomic stability and implementation of wide-ranging structural reforms. Their commitment to the program remains strong, and they look forward to continued fruitful cooperation with the Fund and their development partners.