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TWELFTH AND FINAL REVIEW UNDER THE EXTENDED ARRANGEMENT, REQUEST FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA, AND PROPOSAL FOR POST-PROGRAM MONITORING—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR PAKISTAN

In the context of the Twelfth and Final Review Under the Extended Arrangement, Request for Waivers of Nonobservance of Performance Criteria, and Proposal for Post-Program Monitoring, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 28, 2016, following discussions that ended on August 4, 2016, 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 September 13, 2016.
- A **Statement by the Executive Director** for Pakistan.

The documents listed below will be separately released.

Letter of Intent sent to the IMF by the authorities of Pakistan*
*Also included in Staff Report

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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September 28, 2016

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IMF Executive Board Completes the Twelfth and Final Review Under the Extended Fund Facility for Pakistan

The Executive Board of the International Monetary Fund (IMF) on September 28, 2016 completed the twelfth and final review of Pakistan's three-year economic reform program supported by an Extended Fund Facility (EFF) arrangement. The Board's decision enables the immediate disbursement of the final tranche in an amount equivalent to SDR 73 million (about US$102.1 million). On September 4, 2013, the Executive Board approved the 36-month extended arrangement under the EFF in the amount of SDR 4.393 billion (about US$6.15 billion, or 216 percent of Pakistan's current quota at the IMF. (See Press Release No. 13/322).

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

"Pakistan's Fund-supported program has helped the country restore macroeconomic stability, reduce vulnerabilities, and make progress in tackling key structural challenges. Economic growth has gradually increased and inflation has declined. External buffers have been bolstered, financial sector resilience has been reinforced, and the fiscal deficit has been reduced, while social safety nets have been strengthened. Tax policy and administration reforms allowed for further revenue mobilization. Steps have been taken to strengthen the State Bank of Pakistan's autonomy. Energy sector reform allowed a reduction of power outages, energy subsidies, and accumulation of power sector arrears. A country-wide strategy to improve the business climate was adopted.

"Significant challenges remain for Pakistan in the post-program period, and the authorities' commitment to continue implementing strong policies to reinforce macroeconomic stability gains and advance growth-supporting reforms is to be commended. In light of the significant public debt burden, the authorities' plan to further reduce the fiscal deficit is welcome. The 2016/17 budget and the revised fiscal responsibility framework can anchor fiscal policy in support of further gradual fiscal consolidation. Further accumulating international reserves in a context of sufficient exchange rate flexibility will help strengthen confidence and competitiveness, while maintaining a prudent monetary policy stance will be key to supporting low inflation and macroeconomic stability. Swiftly addressing the remaining recommendations of the 2013 Safeguards Assessment is needed to further strengthen the central bank's autonomy. Further progress in advancing financial sector reforms will be important.

"Moving forward with key structural reforms is pivotal to foster higher and more inclusive growth. Restructuring and attracting private sector participation in public enterprises is needed to ensure their financial viability and reduce fiscal costs. Completing the power sector reform will be important to strengthen the soundness of the sector and support growth. Continuing to move forward with the implementation of the new business climate reform strategy will help increase competitiveness, foster investment, and support private-sector-led growth and job creation.

"Close Fund engagement with Pakistan will continue through policy dialogue in the context of regular consultations and post-program monitoring, along with ongoing technical assistance."

PAKISTAN

September 13, 2016

TWELFTH AND FINAL REVIEW UNDER THE EXTENDED ARRANGEMENT, REQUEST FOR WAIVERS OF NONOBSERVANCE OF PERFORMANCE CRITERIA, AND PROPOSAL FOR POST-PROGRAM MONITORING

EXECUTIVE SUMMARY

Extended Arrangement under the Extended Fund Facility (EFF): A 36 month, SDR 4,393 million (216 percent of the new quota) Extended Arrangement under the EFF was approved by the Executive Board on September 4, 2013, and the eleventh review was completed on June 27, 2016, for a total disbursement of SDR 4.32 billion.[1] The thirteenth and final tranche amounting to SDR 73 million will be available upon completion of this review. The authorities have not requested a follow-up arrangement. Fund engagement with Pakistan will continue, including through Post-Program Monitoring.

Status of the program: The authorities met most Performance Criteria (PCs) at end-June 2016 but the PCs on the budget deficit and Net Domestic Assets (NDA) of the State Bank of Pakistan (SBP) were missed by small margins. They also met all program Indicative Targets (ITs). Structural Benchmarks (SBs) on financial sector reform, (enactment of the Deposit Protection Fund Act), privatization (solicitation of expressions of interests for the disinvestment of a major power generation company) and energy sector reform (update of the power sector arrears reduction plan) were met. However, one SB on energy sector reform (notification of multi-year tariffs for FESCO, IESCO and LESCO) was not met due to an unresolved dispute with the regulator.

Key issues: Discussions focused on near-term priorities in fiscal and monetary policy in light of missed program targets in these areas, along with the economic and financial policy agenda for the post-program period. The authorities reiterated their commitment to strong policies to lock in hard-won macroeconomic stability gains and advance key growth-supporting reforms beyond the end of the program. To this end, the authorities intend to (i) continue pursuing gradual fiscal consolidation while expanding tax revenue and priority spending, (ii) further bolster their external buffers while maintaining an adequate monetary policy stance to keep inflation expectations well-anchored, (iii) strengthen financial sector resilience, and (iv) advance growth-enhancing structural reforms, including restructuring or privatizing ailing PSEs, completing the energy sector reform, and improving the business climate.

[1] Pakistan's new quota is SDR 2,031 million (previously SDR 1,033.7 million).

Approved By
Daniela Gressani and Kristina Kostial

Discussions took place in Dubai during July 27–August 4, 2016. Staff representatives comprised H. Finger (head), G. Albertin, M. Kryshko, A. Tudyka (all MCD), K. Al-Saeed (MCM), S. Cevik (FAD), M. Kim (SPR), T. Mirzoev (Resident Representative), and H. Zaidi (Resident Representative Office, Islamabad). S. Mahmood (Senior Advisor, OED) joined for the discussions. The mission issued a press release on August 4, 2016. J. Chen and M. Orihuela-Quintanilla assisted in the preparation of the report.

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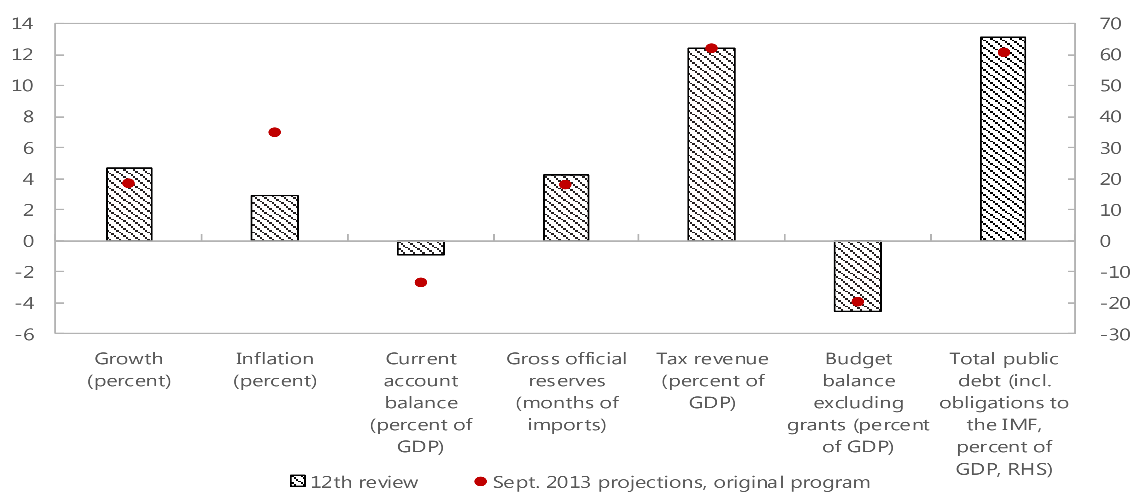
PROGRESS UNDER THE EFF-SUPPORTED PROGRAM AND CHALLENGES AHEAD

1. **Macroeconomic resilience has improved and short-term vulnerabilities have declined under the program, supported by policy discipline and the pronounced decline in oil prices**. Since the start of the program in September 2013, economic growth has gradually increased, inflation has declined, and external buffers have been bolstered, supported by the authorities' policies and the benefits of lower oil prices. Moreover, the fiscal deficit has been reduced, while social safety nets have strengthened, supporting the poor. However, public debt remains high and further fiscal consolidation is needed to reduce fiscal vulnerabilities. International reserves, while having tripled over the program period to cover 4.2 months of imports, have not yet reached comfortable levels (76 percent of the ARA metric).[2] In addition, pronounced real appreciation of the rupee over the program period, despite the SBP's significant purchases in the foreign exchange market to rebuild external buffers, has negatively affected trade competitiveness. Further accumulating foreign exchange reserves is needed to bolster external buffers, strengthen investor confidence, and support private sector-led growth.

Pakistan: Macroeconomic Performance under the Three-year EFF Program

		FY2012/13	FY2015/16
Real Sector			
Real GDP growth	↑	3.7	4.7
CPI inflation (annual average)	↓	7.4	2.9
Fiscal			
Overall fiscal balance (excluding grants, percent of GDP)	↓	-8.5	-4.6
Structural primary balance (percent of GDP)	↓	-4.5	0.4
Public debt (percent of GDP)	↑	62.3	64.8
Tax-to-GDP	↑	10.0	12.4
Energy subsidies (percent of GDP)	↓	2.0	0.6
Social Spending under BISP (per beneficiary per quarter, in rupees)	↑	3,000	4,700
Coverage of BISP (million beneficiaries)	↑	3.78	5.36
BOP and Exchange rate			
Exports (y-o-y growth)	↓	0.4	-8.6
GIR ($U.S. billions)	↑	6.0	18.1
NIR ($U.S. billions)	↑	-2.4	7.5
REER (2000=100)	↑	100.7	118.3
Monetary			
Private sector credit (y-o-y growth)	↑	-0.6	11.1
Change in borrowing from the SBP (percent of reserve money)	↓	23.2	-16.3
Financial			
Capital Adequacy Ratio	↑	15.5	16.1
Non-performing Loans to gross loans	↓	14.8	11.1

Program Achievements (FY2015/16)



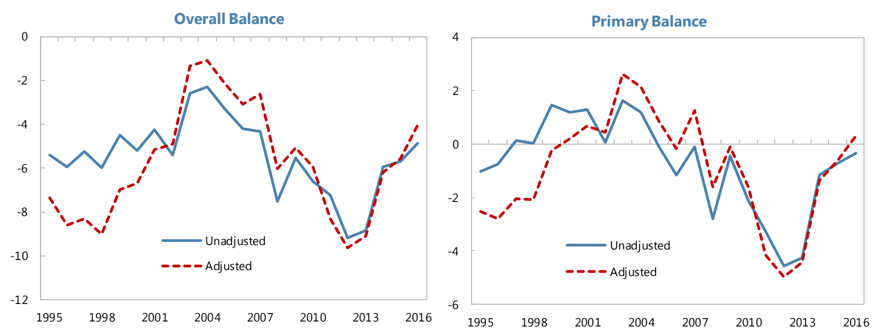
Source: Pakistani authorities; IMF staff calculations

[2] International Monetary Fund, 2016, "Guidance Note on the Assessment of Reserve Adequacy and Related Considerations," IMF Policy Paper, June (Washington: International Monetary Fund).

2. Inflation has declined, the monetary policy framework has been strengthened, and some progress has been made in strengthening the State Bank of Pakistan's (SBP's) autonomy. Headline inflation declined to 2.9 percent (on average) in FY 2015/16, from about 7½ percent in FY 2012/13, reflecting lower food and fuel prices, a prudent monetary policy stance, and reduced budget financing by the SBP. Furthermore, the authorities amended the SBP law, introduced a number of administrative measures to increase the SBP's autonomy, put in place an independent monetary policy committee, and improved the interest rate corridor and the SBP's internal operations. However, a number of important recommendations from the 2013 Safeguard Assessment remain to be addressed to further strengthen the SBP's autonomy (¶22).

3. The authorities achieved sizeable fiscal consolidation on the back of tax and energy subsidy reforms, while increasing priority social and capital spending. The overall budget deficit (excluding foreign grants) narrowed by 3.9 percent of GDP under the three-year program and the structural primary balance turned into surplus, bolstering macroeconomic resilience.[3] The tax-to-GDP ratio increased by nearly 2½ percentage points of GDP owing to a significant reduction in tax concessions and exemptions, increased withholding taxes on nonfilers of income tax returns, and improvements in tax compliance and enforcement. Moreover, the administrative authority to grant new tax concessions was markedly restricted. In parallel, energy subsidies were reduced by about 1½ percent of GDP, while capital expenditure increased by about 0.5 percent of GDP, and targeted cash transfers to the poor under the Benazir Income Support Program (BISP) were increased by about 0.1 percent of GDP.

Headline and Cyclically Adjusted Fiscal Balances
(Excluding grants, in percent of GDP)



Sources: Ministry of Finance; Federal Board of Revenue; State Bank of Pakistan; and IMF staff calculations.

4. However public debt has remained high and further fiscal consolidation is needed to ensure medium-term sustainability. Public debt increased by about 2 ½ percent of GDP over the course of the program and remains high at about 65 percent of GDP (430 percent of revenue) as of end-June 2016, well above the emerging market average.[4] Pakistan's tax-to-GDP ratio remains below comparator emerging market countries, and advancing reforms of tax policy and

[3] The underlying fiscal adjustment after accounting for clearance of circular debt in the energy sector (1.4 percent of GDP in FY 2012/13) was 2.5 percentage points of GDP over the program period.

[4]The increase in gross public debt in FY 2015/16 was more than projected mainly due to a build-up of government deposits along with exchange rate effects and a higher-than-programmed budget deficit.

administration is needed to mobilize additional revenues to support fiscal consolidation and create fiscal space for growth-supporting priority spending. Furthermore, prudently managing current nonpriority public expenditures would be important to support medium-term fiscal consolidation. The FY 2016/17 budget and recent amendments to the Fiscal Responsibility and Debt Limitation (FRDL) Act strengthen the anchor for near- and medium-term fiscal policy and can support fiscal consolidation efforts.

5. The stability and resilience of the financial sector are being reinforced. The performance of the banking sector improved, as reflected in higher profitability, strengthened liquidity indicators, robust capital adequacy, and declining (though still substantial) nonperforming loans (NPLs). The Deposition Protection Corporation Act to establish deposit insurance has been enacted (August 2016, SB), steps have been taken to strengthen the framework for NPL recovery, and the regulatory and supervisory framework is being reinforced, including through phased implementation of Basel III standards. Next steps in the reform agenda include finalizing the introduction of the deposit insurance scheme, ensuring that all banks are in compliance with regulatory requirements, and addressing the still high level of NPLs (¶¶ 23–25).[5]

6. Key structural weaknesses are being tackled, and reforms will need to continue after the program ends. The implementation of growth-supporting structural reforms has advanced, albeit with some delays. Continuing these reforms beyond the end of the program—notably in the energy sector, business climate and PSEs reform—will be key to foster higher and more inclusive medium-term growth and limit fiscal risks.

- **Power sector**. Widespread electricity outages, while still present, were gradually reduced through improved supply and demand management, and untargeted subsidies were lowered. The accumulation of arrears was significantly reduced (though a substantial stock of arrears still remains), helped by lower oil prices, improved performance of distribution companies (DISCOs), tariff rationalization, and the introduction of surcharges. However, additional efforts are needed to further reduce the accumulation of arrears and address the outstanding stock.

- **Gas sector**. Gas shortages were reduced through supply and demand measures. Supply was increased through better incentives to domestic producers and Liquefied Natural Gas (LNG) imports, tariffs were rationalized to bring them closer to cost recovery and strengthen demand management, the regulatory framework was improved, and legislation to tackle gas theft was strengthened. However, further efforts are needed to address the still high gas system losses.

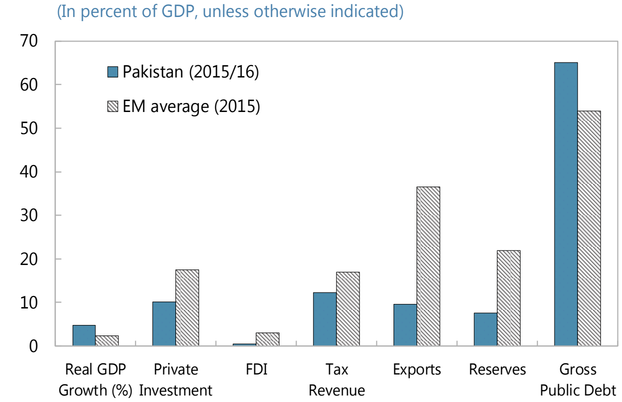
[5] Two small banks (1.5 percent of the banking assets) are marginally CAR–noncompliant, in part due to an increase in the CAR requirement, with their overall capital shortfall being less than 0.08 percent of GDP. A third small bank is below the minimum capital requirement (MCR).

- **Restructuring and privatization of PSEs**. Several capital market transactions, one strategic sale, and the corporatization of Pakistan International Airlines (PIA) have been completed, and significant preparatory work toward restructuring and seeking strategic private sector participation for a number of PSEs has been conducted. However, following labor tensions and political opposition, the authorities revisited in early 2016 their strategy for PSE reform, scaling back planned privatization transactions while continuing to seek private sector participation and implementing measures to contain PSE financial losses. Further efforts at restructuring and/or divesting PSEs are needed, as a number of them remain loss-making, absorbing scarce fiscal resources and imposing fiscal risks while operating inefficiently.

- **Business climate, governance and simplifying the trade regime**. After Pakistan slipped in the 2016 Doing Business ranking, a new comprehensive country-wide strategy to improve the business climate was developed in early 2016 and is now being implemented (Box 1). Furthermore, import tariff slabs were reduced to simplify the trade regime. Sustained efforts will be needed to improve the business climate, which will be important to promote competitiveness and attract private investment. The AML/CFT framework has been strengthened but requires further enhancement.

7. **With the program coming to an end, significant challenges remain and continued commitment to strong policies and reforms is pivotal**. Exports are small in relation to GDP and have been declining; private investment (including foreign direct investment) is too low to support higher growth; public debt is still too high; fiscal revenue, while having increased significantly, remains insufficient to support needed spending on public investment, health and education; and international reserves, despite having tripled over the course of the program, remain below comfortable levels. Unemployment remains relatively high at 6 percent (10½ percent among the youth and 9½ percent among women), the informal economy remains large, 30 percent of the population lives below the poverty line, and income and gender inequality are significant (Box 2). Reinforcing macroeconomic resilience and a strong structural reform drive will be important to make further inroads in addressing these challenges.

Pakistan Relative to Emerging Market Economies
(In percent of GDP, unless otherwise indicated)



Sources: IMF WEO Database, and SPR VEE Database.

PERFORMANCE UNDER THE TWELFTH REVIEW

8. Program performance at end-June 2016 has been satisfactory with most performance criteria, all indicative targets, and most structural benchmarks met.

- **Fiscal performance** was broadly in line with the program targets at end-June 2016, although the deficit was higher than programmed. The performance criterion (PC) on the general government budget deficit (excluding foreign grants) was missed by PRs 57 billion (0.2 percent of GDP), due to higher-than-expected expenditures at the provincial level, while the federal government compensated for a shortfall in nontax revenue by rationalizing expenditure. Tax revenue grew by more than 20 percent and the Federal Board of Revenue (FBR) met the indicative target (IT) on tax collections with a small margin. The IT on targeted cash transfers through the Benazir Income Support Program (BISP) was met with a significant margin, reflecting higher stipends and further expansion of coverage. The IT on the accumulation of power sector arrears was met with a large margin (achieving a net reduction in outstanding payables) owing to favorable oil prices and the authorities' continued efforts to improve DISCOs' performance.

- **Monetary performance** was satisfactory in the fourth quarter of FY 2015/16. The end-June PC on net international reserves (NIR) was met by a large margin, supported by the SBP's stepped-up spot purchases of US$1.4 billion. The SBP's net short position of swap/forward contracts remained within the program's bounds. Government borrowing from the SBP remained below the end-June 2016 ceiling by PRs 388 billion as the government continued to build financing buffers. However, the end-June PC on Net Domestic Assets (NDA) was missed by a small margin of PRs 6 billion (0.2 percent of NDA) due to higher-than-expected demand for currency, mostly driven by the financial transactions tax on nonfilers of income tax returns and strong precautionary demand for liquidity in advance of the Eid holidays in early July.

- **Progress with structural reforms was satisfactory with three out of four structural benchmarks (SBs) met**. The Deposit Protection Corporation Act to establish a deposit insurance was enacted (end-August 2016 SB). The authorities solicited expressions of interest for the divestment of Kot Addu Power Company (KAPCO), a major power generation company (July 15, 2016 SB). They also updated their plan to further limit the accumulation of new payables and gradually eliminate the outstanding stock of payables arrears in the power sector (July 15, 2016 SB). However, the notification of multi-year tariffs for three distribution companies (FESCO, LESCO and IESCO) was further delayed due to an ongoing dispute with the regulator over benchmark distribution losses and collection targets used in the determination of the FY 2015/16 tariff (missed end-July 15, 2016 SB; ¶30).

Figure 1. Pakistan: Structural Reforms under the Three-Year EFF Program

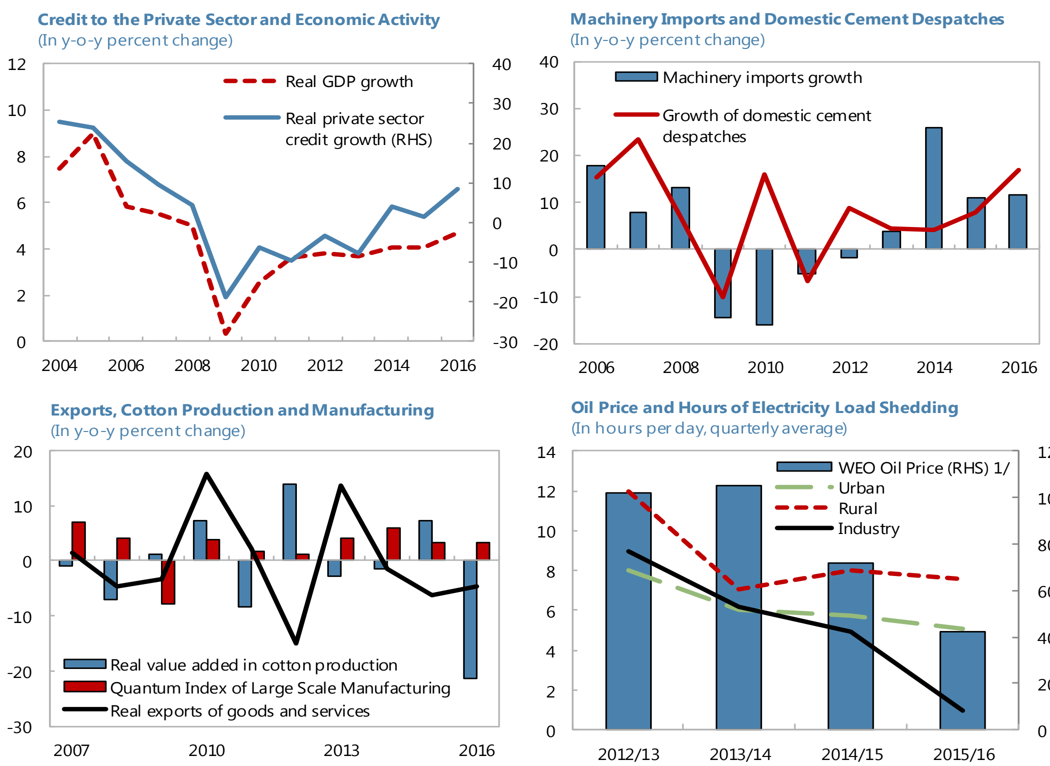
		FY2012/13	FY2015/16	Status
SBP's autonomy				
Strenghtening SBP's autonomy	↑	..	..	Amendments to the SBP's law have been adopted, a Monetary Policy Committee was established, and executive measures introduced.
Internal control at the SBP	↑	..	..	The operations of the SBP were improved and the interest rate corridor strengthened.
Tax reforms				
Tax concessions/exemptions (percent of GDP)	↓	2.0	1.3	Statutory Regulatory Orders (SROs) were reduced and the administrative authority to grant new SROs was greatly reduced.
Power sector reform				
Energy subsidies (percent of GDP)	↓	2.0	0.6	Electricity subsidies were kept only for low-end domestic consumers and agricultural users.
DISCOs' distribution losses (percent)	↓	18.9	17.9	DISCOs' distribution losses were significantly reduced. The Penal Code and Code of Criminal Procedures were amended in January 2016 to more effectively address electricty theft.
DISCOs' collection rates (percent)	↑	87.2	92.6	DISCOs' collection rates were substantially increased.
Power sector payables arrears (including PHCL, percent of GDP)	↔	2.2	2.3	This includes arrears transferred into PHCL, an SPV (PR 335 billions). Excluding this, arrears at end-June 2016 were at 1.2 percent of GDP (PR 321 billion). About ⅔ of power sector arrears were cleared in June and August 2013. While arrears have re-accumulated, the pace of accumulation has been sustantially reduced. The plan to reduce power sector arrears was updated in July 2016 to take into account the revised strategy to privatize DISCOs.
Notified Electricity Tariff (in PRs per kWh)	↑	8.8	11.9	The electricity tariff was brought closer to cost recovery by increasing the base tariff and introducing surcharges.
Power sector regulatory reform	↑	..	..	Quarterly performance targets have been set for DISCOs and multi-year tariffs have been determined for three DISCOs. Delays in the tariff notification remain, due to DISCOs' ongoing dispute with the regulator over tariff determination.
Power sector operational reform	↑	..	..	Revenue-based load shedding has been strengthened, supply capacity is being increased, and quarterly performance targets for collection and loss reduction have been set for DISCOs.
Power outages for industry (hours/per day)	↓	9	1	Power outages for industrial consumers were significantly reduced.
Power outages for urban consumers (hours/per day)	↓	8	5	Power outages for consumers in urban areas were gradually reduced.
Gas sector reform				
Gas producer price (in PRs per MMBTU)	↑	2.8-3.0	6-10	Gas price for producers was increased to provide incentives for investments and domestic gas production. More than two thirds of existing domestic gas concessions have been converted to the new prices.
Consumers gas tariff (in PRs per MMBTU)	↑	540.2	646.9	A new gas tariff was notified in August 2015 and semi-annual notification is expected to resume, despite a delay in October 2016. A Gas Infrastructure Development Cess (GIDC) was introduced in 2015 contributing to rationalizing gas prices.
LNG gas supply (MMCFD)	↑	0.0	400.0	LNG imports started in March 2015 and a long-term import contract was signed in February 2016. The contract for a 2nd LNG terminal was awarded in June 2016 and will facilitate higher LNG imports.
Unaccounted gas losses (percent)	↑	10.1	11.5	Gas distribution losses remain significant and above international standards. The Gas (Theft Control and Recovery) Act passed in March 2016 strengthens the framework to address gas theft.
Restructuring and privatization of PSEs				
PSEs restructuring and privatization	↔	..	..	Some successful capital market transactions. The restructuring and privatization strategy was re-assessed in early 2016. More limited private sector participation in PSEs is being sought while measures have been put in place reduce PSEs' financial losses.
PSEs' annual losses (percent of GDP)	↓	0.4	0.2	The accumulation of overall annual losses of PIA, PSM and Pakistan Railways declined.
PSEs' accumulated losses (percent of GDP)	↑	1.7	2.3	Cumulative losses of PIA, PSM and Pakistan Railways have further increased, but at a slower pace.
Business Climate Reform				
Improving business climate	↔	..	..	Pakistan's ranking in the WB's Doing Business declined in 2016. Several measures were put in place under the program, including the Virtual One-Stop-Shop for business registration, Alternative Dispute Resolution mechanisms, and reducing procedures for paying taxes. A new comprehensive strategy to improve business climate was adopted in February 2016 and is being implemented.

Sources: Pakistani authorities; and IMF staff calculations.

9. The authorities have agreed to implement corrective measures for the two missed end-June PCs and request waivers of nonobservance on this basis. The authorities will contain public expenditures by an additional 0.3 percent of GDP in order to achieve the agreed FY 2016/17 fiscal target (¶13) and will use the meetings of the Fiscal Coordination Committee (FCC) to monitor budget implementation at the federal and provincial levels, to achieve the government's fiscal targets (¶15). Furthermore, the authorities committed to bring the stock of NDA of the SBP below PRs 3,100 billion by end-August 2016 to address the small overrun relative to the end-June PC and ensure an appropriate pace of monetary expansion (prior action). This prior action was met with a considerable margin of PRs 288 billion.

OUTLOOK AND RISKS

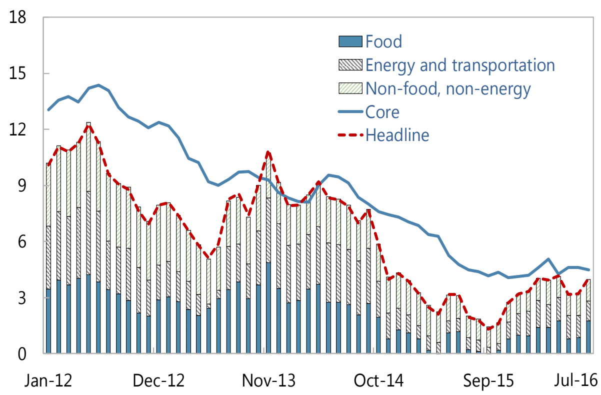
10. The economic recovery will likely continue to strengthen on the back of improved macroeconomic stability. Despite a weak cotton harvest and a continued decline in exports, growth is estimated at 4.7 percent in FY 2015/16, supported by buoyant construction activity and healthy expansion of the service sector. Strengthening domestic demand is also indicated by rising domestic machinery imports. Pakistan has been benefitting from lagged effects of the pronounced fall in oil prices and a marked reduction in domestic interest rates, which has been accompanied by strengthened private sector credit growth. Growth will likely increase moderately to 5 percent in FY 2016/17, also supported by an investment upturn related to the China Pakistan Economic Corridor (CPEC). After declining to 2.9 percent (on average) during the last fiscal year, headline inflation is expected to remain contained at 5.2 percent in FY 2016/17, well-anchored by prudent monetary policy.



Sources: Pakistani authorities; Bloomberg; and IMF staff calculations.
1/ Simple average of three spot prices: Brent, WTI, and Dubai oil prices; US$ per barrel.

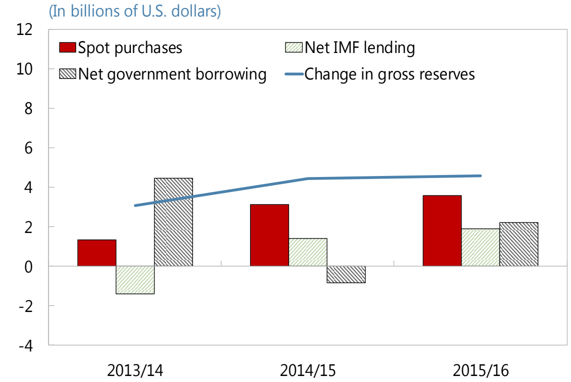
11. Despite an expected widening of the current account deficit, international reserves will likely strengthen further. The current account deficit remained contained at 0.9 percent of GDP in FY 2015/16. Pakistan's exports fell by 8.6 percent (y-o-y), reflecting lower international prices of cotton and rice, a weak business climate, and competitiveness losses from an appreciating real exchange rate. However, low oil prices and still robust remittances from the Gulf Cooperation Council (GCC) countries have offset declining exports.[6] Foreign reserves increased to about 4.2 months of imports (76 percent of the ARA metric) at end-June 2016, also reflecting SBP's increased spot purchases. The partial recovery in oil prices, higher CPEC-related imports and an expected slowdown in remittances growth will likely widen the current account deficit to about 1.5 percent of GDP in FY 2016/17. However, increased mobilization of external financing from international markets and the SBP's continued foreign exchange purchases will likely allow for further foreign reserves accumulation (to about 4.5 months of imports).

Contribution to CPI Inflation
(In y-o-y precent change)



Sources: SBP; and IMF staff calculations.

Reserve Accumulation
(In billions of U.S. dollars)



Sources: Pakistani authorities; and IMF staff calculations.

12. Risks to the outlook are tilted to the downside. Lower growth in advanced countries, such as in the UK and possibly the EU owing to the prospective Brexit, and in emerging market economies (including China and GCC) could weaken exports, remittances and FDI. Continued appreciation of the real effective exchange rate, in the context of an appreciating U.S. dollar vis-a-vis the pound and euro, would further erode export competitiveness and affect remittances. Tighter global financial conditions could have an adverse impact on capital inflows. By contrast, lower oil prices and a slower pace of increase in international interest rates, owing to the impact of Brexit on advanced economy growth, would be beneficial for Pakistan's external position and growth. Medium-to long-term risks could arise from CPEC-related repayment obligations and profit repatriation (Box 3); lower remittances if the slowdown in the GCC lasts longer than expected; and a more pronounced recovery of oil prices. Domestically, policy slippages, further delays in restructuring or privatizing PSEs, ongoing legal challenges to electricity surcharges and revenue

[6] The number of Pakistani workers employed overseas rose by more than 25 percent y-o-y in 2015 and was mostly concentrated in the GCC countries.

measures, political uncertainty, and the still difficult security conditions could affect economic activity and undermine fiscal consolidation.

POLICY DISCUSSIONS

Discussions focused on preserving hard-won macroeconomic stability gains and advancing growth-supporting structural reforms beyond the end of the program. Continuing to pursue gradual fiscal consolidation, bolstering external buffers within the context of adequate exchange rate flexibility, maintaining a prudent monetary policy stance, and strengthening the resilience of the financial sector will be key to preserve macroeconomic stability. Furthermore, moving ahead with structural reforms, especially restructuring and privatizing PSEs and the energy sector and business climate reforms will be key to foster higher and more inclusive growth.

A. Fiscal Policy

13. Fiscal consolidation needs to stay the course. The authorities remain committed to fiscal consolidation beyond the program horizon and to their budget deficit target of 3.8 percent of GDP (excluding foreign grants) in FY 2016/17, based on continued gradual consolidation both at the federal and provincial levels. The composition of fiscal adjustment is designed to boost tax revenue by ½ percent of GDP (to about 13 percent of GDP) and further rationalize noncritical current expenditures (by 0.1 percent of GDP), while creating room for an increase of 0.2 percent of GDP in development spending. In response to the latest projections which indicate a shortfall of about PRs 100 billion (or 0.3 percent of GDP) in the combined collection of the Gas Infrastructure Development Cess (GIDC) and federal nontax revenue relative to budgeted amounts, the authorities have agreed to cut nonpriority expenditures to maintain the planned fiscal stance (LOI, ¶7), while continuing to target an increase in capital expenditure from last year's level. Staff noted that the provinces' contribution to the targeted fiscal deficit could again fall short of expectations, and that there was a significant statistical discrepancy in the fiscal accounts (amounting to 0.7 percent of GDP in FY 2015/16), which, if reversed, could entail pressure on this year's deficit. The authorities agreed to manage spending prudently, coordinating closely with the provinces, to ensure the achievement of both revenue and deficit targets. They also requested IMF technical assistance to further strengthen their fiscal accounting.

14. Revenue mobilization and improving the composition of spending are central pillars in the fiscal strategy. The authorities plan to accelerate the implementation of administrative reforms and policy measures aimed at broadening the tax base and modernizing the tax system, refrain from granting concessions, exemptions, and any form of amnesty, and reduce the outstanding stock of tax refund claims to a level consistent with no more than a three-month flow.[7] Staff pointed out that

[7] The total stock of outstanding tax refund claims, increased to PRs 205 billion in June 2016, from PRs 200 billion in June 2015. As part of this total stock, outstanding GST refund claims increased to PRs 133 billion at end-June 2016, from PRs 89 billion at the end of FY2014/15. The authorities explained that this increase reflects, in part, a more systematic effort to register outstanding claims.

going forward, containing the wage bill growth, untargeted subsidies, and non-priority transfers will also be necessary to facilitate the targeted shift in the composition of expenditures towards social and capital spending across all tiers of the government.

15. Staff stressed that strengthening intergovernmental fiscal policy coordination is needed to support macroeconomic stability beyond the program. Given the extent of devolution in revenue and expenditure assignments, staff stressed the need to strengthen fiscal policy coordination across all layers of the government. To this end, the newly established FCC, comprising the provincial and federal finance secretaries, will continue to hold quarterly meetings to synchronize policy guidance and monitor budget implementation to achieve the government's fiscal targets. Furthermore, staff recommended rebalancing revenue and expenditure responsibilities between the federal and provincial governments and bring underdeveloped tax bases that are under the purview of provincial governments, such as agriculture, services, and property, more effectively into the tax base.[8] This would entail modernizing agriculture taxation by introducing a presumptive income tax, improving property tax collection by developing electronic fiscal cadasters and strengthening property valuation at the provincial level, and improve sales tax collection on services.

16. The revised fiscal responsibility framework will be key to ensure that medium-term fiscal policy is well-anchored. Recent amendments to the FRDL Act provide better operational guidance for fiscal policymaking and safeguard debt sustainability over the medium term by imposing a limit on the federal government budget deficit of 4 percent of GDP excluding foreign grants for FY 2017/18–FY 2019/20, and 3½ percent of GDP thereafter; and maintaining a limit of 60 percent of GDP on the general government debt until FY 2017/18, and adopting a 15-year transition path toward 50 percent of GDP. With these targets, fiscal policy will be anchored at a prudent stance, leading to additional gradual consolidation and strengthening long-term debt sustainability. Staff called for further strengthening the medium-term fiscal framework by improving the compilation of fiscal accounts in line with international standards, introducing an expenditure rule to avoid pro-cyclical fiscal policy, and strengthening the budget preparation and approval process in support of fiscal discipline. Staff also reiterated the importance of an independent fiscal council to enhance transparency and accountability.

17. The forthcoming public-private partnership (PPP) law can support investment and provide for appropriate management of associated fiscal risks. The draft PPP law that is under discussion at the National Assembly makes PPPs a part of the overall budget process and medium-term planning exercise and gives the Ministry of Finance an explicit role as gatekeeper in all stages of PPP projects. While the law provides the overall legal framework to manage fiscal risks originating from PPPs, staff stressed the need to develop strong secondary legislation. In this context, staff highlighted that in order to contain fiscal risks it would be important to conduct a detailed feasibility

[8] The most recent National Finance Commission (NFC) award and the 18th constitutional amendment grant 57.5 percent of most revenues to the provinces, along with devolution of spending responsibilities and sales taxation authority in services in addition to the existing taxation authority in agriculture and property. In the current round of NFC negotiations, the federal government will seek an agreement to better balance devolution of revenue and expenditure responsibilities, in a way that is consistent with the objective of macroeconomic stability.

study and value-for-money analysis for PPPs, strengthen the risk management system, bring all PPPs' contracting agencies into the regular coverage of fiscal accounts and debt statistics, establish a public register of PPP projects, and publish data on all PPP commitments to safeguard transparency and accountability.

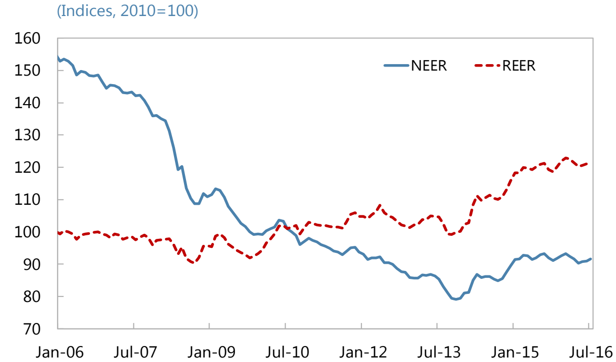
18. Further strengthening public debt management remains a priority. The authorities are committed to continue improving the effectiveness of the Debt Policy Coordination Office (DPCO) by enhancing its staffing capacity. They adopted a medium-term debt management strategy in March 2016 with target ranges for currency, refinancing, and interest rate risk. In FY 2016/17, they are envisaging to continue borrowing from external sources, including development partners and capital markets. Over the medium term, the authorities are planning a gradual reduction in external borrowing while containing the share of short-term debt. The domestic borrowing strategy is focused on lengthening the average maturity and reducing spikes in the maturity profile. Staff underscored that, despite having declined over the program period, the share of short-term debt is still elevated and reliance on short-term financing remains a vulnerability. Staff welcomed the authorities' commitment to continue diversifying domestic and external financing sources, further lengthening the maturity profile, and reducing rollover risks to reduce debt-related vulnerabilities.

19. Further expanding the coverage of BISP while strengthening its targeting and efficiency will be important to protect the most vulnerable and reduce poverty. The coverage of unconditional cash transfers (UCTs) has expanded markedly during the IMF-supported program, reaching 5.36 million beneficiaries at end-June 2016 (from 3.78 million beneficiaries in FY 2012/13) and stipends have been increased by more than 60 percent. The coverage of education-conditional cash transfers (CCTs) has also continued to expand, reaching 1.3 million children. Staff welcomed the authorities' plans to further expand the coverage of the UCT and CCT programs and to further strengthen the program's targeting and efficiency (LOI ¶13).

B. Monetary and Exchange Rate Policies

20. Staff welcomed the authorities' continued commitment to strengthen external buffers. The authorities are committed to further accumulating international reserves through the SBP's spot purchases and continuing to take advantage of still favorable oil prices. Staff emphasized that, in parallel, greater downward exchange rate flexibility would contribute to strengthening external buffers and supporting competitiveness, which has been affected by significant real effective exchange rate appreciation (about 17.5 percent over the three-year program period).

Nominal and Real Effective Exchange Rate
(Indices, 2010=100)



Sources: Pakistani authorities; and IMF staff calculations.

21. The monetary policy stance needs to remain prudent to keep inflation well-anchored and preserve macroeconomic stability. Following the accommodative policy rate cut in May 2016 (by 25 bps), the SBP should be prepared to tighten in case inflationary pressures intensify, and continue maintaining clearly positive real interest rates. Moving forward, higher foreign reserve accumulation and the normalization of deposit growth (following a decline linked to last year's introduction of a financial transactions tax for nonfilers of income tax returns) would reduce the need for ongoing SBP's liquidity injections. Staff also emphasized that the stock of government borrowing from the SBP should continue to be contained and kept in line with recently achieved prudent levels.

22. Staff stressed the need to further strengthen central bank autonomy. In August 2016, the SBP developed a time-bound legislative action plan to address remaining recommendations of the 2013 Safeguards Assessment. Staff stressed that the proposed amendments to the SBP law represent good progress towards clarifying the SBP's objectives, enhancing its financial autonomy, and limiting its scope for providing credit to the government, but several recommendations—in the areas of institutional autonomy, governance, and personal autonomy of SBP board members—are not addressed in the action plan. Staff encouraged the authorities to pursue more ambitious reforms in line with recent technical assistance and to move swiftly with implementation.

C. Financial Sector Issues

23. While the banking system continues to be profitable and well-capitalized, efforts are under way to strengthen the capitalization of some small banks. The SBP is actively engaging with three small undercapitalized banks to bring them into regulatory compliance by end-2016. To this end, one bank has received a partial capital injection and is in the process of raising additional equity, a second, publicly-owned, bank is in the divestment process, and a third bank is seeking to merge with a larger peer. Staff stressed the need for the SBP to continue engaging closely with affected banks to ensure their regulatory compliance.

24. Advancing financial sector reforms is needed to further strengthen resilience and enhance financial deepening. Following the enactment of the Deposit Protection Corporation Act, the authorities plan to make the new deposit insurance operational by end-2016, which will help enhance the stability of the banking system. Furthermore, continuing to strengthen the legal and regulatory framework for the financial sector, including with the phased implementation of Basel III capital and liquidity requirements by 2019, strengthening the supervision of systemically important banks, and developing consolidated banking supervision will be important.[9] Staff stressed that the Pakistan Development Fund—a state-owned development bank for which the authorities are aiming to mobilize the participation of international development partners—should operate on a commercial basis and have a strong governance framework to mitigate financial risks and avoid quasi-fiscal activities.

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[9] The SBP has issued industry-wide instructions which pertain to eligible capital and related deductions, capital conservation buffer, and liquidity standards of LCR and NSFR.

25. Addressing the still high level of NPLs can help support banks' credit to the economy and private sector-led growth. Enhancing the debt enforcement regime, developing an appropriate insolvency framework, and continuing to strengthen the market infrastructure for distressed debt are needed for more efficient NPL resolution. In this context, staff welcomed the enactment of the Corporate Restructuring Companies (CRC) Act and the amendments to the Financial Institutions (Recovery of Finances) Ordinance, which strengthen the NPL recovery and resolution framework and will support the provision of credit to the economy. Staff also stressed that moving ahead with the adoption of an appropriate Corporate Rehabilitation Act would be important to strengthen the bankruptcy framework.

26. Further enhancing the effectiveness of the anti-money laundering and combating the financing of terrorism (AML/CFT) framework will be important. Following the amendments to the AML Act to subject the proceeds of serious tax crimes (including income tax) to AML legislation, staff welcomed the authorities' commitment to put in place implementation measures that will bolster the reporting of suspicious transactions related to tax evasion and enhance the cooperation between the Financial Monitoring Unit and the FBR to address tax evasion. Staff stressed the importance of strengthening the effectiveness of the AML/CFT framework in line with international standards, including by tackling the proceeds of corruption and strengthening the effective implementation of the relevant United Nations Security Council Resolutions related to terrorism and terrorist financing.

D. Structural Issues

Public Sector Enterprises

27. Staff stressed that restructuring and attracting private sector participation in ailing PSEs will be important to restore their financial viability and reduce fiscal costs. While planned privatization transactions had been scaled back in early 2016 owing to political opposition and widespread strikes, the authorities reiterated their commitment to attract private sector participation in PSEs while continuing, in parallel, to contain their financial losses. Staff welcomed the authorities' commitment to advance their reform agenda (LOI, ¶21):

- **Pakistan International Airlines (PIA)**. While legislation requires the government to maintain a majority of shares and management control, the authorities are committed to attract private sector participation in the company and finalize the transaction structure for a minority sale by end-2016. In parallel, measures to reduce PIA's financial and operating costs will continue to be implemented.

- **Pakistan Steel Mill (PSM)**. Following inconclusive discussions with a provincial government over a transfer of ownership, the authorities resumed, in July 2016, the privatization process for PSM and aim to conclude the bidding process by end-June 2017. In parallel, the authorities will continue to implement measures to limit PSM's financial losses.

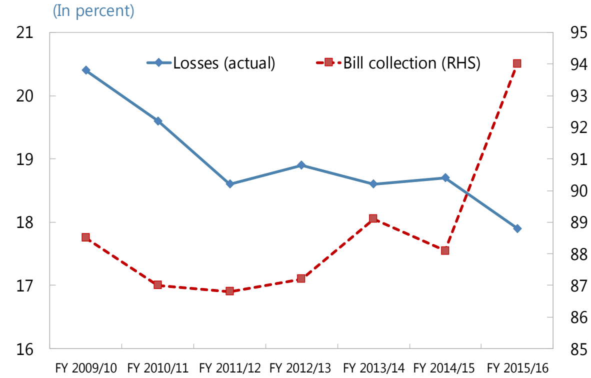
- **Pakistan Railways**. Staff welcomed further improvements in the company's revenue performance and the authorities' commitment to move forward with the restructuring plan.

- **Energy sector**. The authorities have solicited expressions of interest for the divestment of KAPCO, a major generation company (July 15, 2016 SB) and plan to finalize the transaction by March 2017. Furthermore, preparatory work has started to conduct an Initial Public Offering (IPO) for FESCO by February 2017, to be followed by IPOs for IESCO and LESCO by the end of FY 2016/17. The authorities expressed their commitment to seek strategic private sector participation in DISCOs in the medium term.

Energy Sector

28. Favorable oil prices and efforts to further strengthen DISCOs' performance have continued to contain the accumulation of new arrears in the power sector. The end-June 2016 IT on the accumulation of power sector arrears was met with a large margin, reflecting favorable oil prices, a strengthening in DISCOs' payments collection, and a reduction in distribution losses. In particular, most DISCOs met their quarterly performance targets in terms of collection and distribution losses at end-June 2016. With this, there was no new accumulation of arrears in the fourth quarter of FY 2016/17 and the stock of outstanding arrears declined slightly.

Loss Reduction and Revenue Collection
(In percent)



Sources: Pakistani authorities; and IMF staff calculations.

29. Further limiting the accumulation of power sector arrears and gradually reducing the outstanding stock is needed to ensure the soundness of the sector. The authorities have updated, in consultation with development partners, their power sector arrears reduction plan (July 15, 2016 SB) to take into account changes in the privatization strategy for DISCOs. In order to contain the accumulation of new arrears, the authorities will continue to strengthen DISCOs' performance by further reducing distribution losses, increasing payment collections, and continuing to set quarterly performance targets. Furthermore, they are seeking to revise the regulatory benchmarking for tariff determination and are working to resolve outstanding issues with regional governments. In parallel, proceeds from the planned IPOs of FESCO, IESCO and LESCO will be used to reduce the stock of outstanding arrears.

30. Moving forward with establishing a multi-year tariff framework for DISCOs will be key to attract investors and strengthen the regulatory framework. The notification of the multi-year tariffs for FESCO, IESCO and LESCO was further delayed (missed July 15, 2016 SB), owing to the DISCOs' unresolved dispute with the regulator. Notably, DISCOs have requested the regulator to revise benchmark distribution losses used for the FY 2015/16 tariff determination in order to reflect higher distribution losses. Staff reiterated the importance of establishing a multi-year tariff framework in preparation for DISCOs' IPOs and called for the swift resolution of the ongoing litigation and, subsequently, for the resumption of regular tariff notification while underscoring the importance of preserving the independence of the regulator. The authorities indicated their commitment move ahead with setting multi-year tariffs for FESCO, IESCO and LESCO, to be followed by the other DISCOs.

31. Staff called for resuming regular gas tariff notification to ensure cost recovery, avoid the build-up of losses and strengthening the regulatory framework. The authorities committed to finalize the delayed notification of the FY 2016/17 gas tariff by October 2016 and resume regular gas notification moving forward. Staff welcomed the authorities' strategy to further reduce gas shortages by stepping up imports of Liquefied Natural Gas (LNG) while continuing to fully pass through the price of imported LNG to consumers. Staff stressed that continuing efforts to reduce still high distribution losses, including by strengthening network infrastructure and tackling gas theft, is needed to improve the sector performance. Staff welcomed the authorities' plan to move ahead with restructuring and unbundling the gas sector.

Business climate, governance and trade policy

32. Moving ahead with the swift implementation of the new business climate reform strategy will be key to foster much needed investments and support private sector-led growth. Staff commended the authorities' progress in the implementation of key short-term measures to ease the process of starting new businesses, paying taxes and trading across borders, and to facilitate access to credit. Staff stressed that sustained implementation of the new business climate reform strategy beyond the end of the program will be important to effectively strengthen the business climate and attract much needed growth-supporting private sector investment. Staff also welcomed the simplification of the import tariff structure from five to four slabs in July 2016.

PROGRAM MODALITIES AND OTHER ISSUES

33. Financing and capacity to repay the Fund. Pakistan's capacity to repay the Fund remains strong, owing to supportive macroeconomic policies and increasing foreign exchange reserves. Pakistan will continue to benefit from disbursements from multilateral and bilateral partners beyond the end of the EFF-supported program and has access to international markets, which limits short- and medium-term financing risks. The Fund's exposure to Pakistan continued to increase with the purchase made upon completion of the eleventh review, reaching SDR 4.32 billion (about US$6.01 billion; Table 11) and would further increase with the final disbursement under the arrangement (Table 9). While the materialization of risks to the outlook could erode Pakistan's capacity to repay to the Fund, the debt sustainability analysis shows that external debt would remain on a medium-term downward trend under most stress scenarios, with external financing needs below the risk assessment benchmark. However, under an extreme stress scenario in which downside risks simultaneously materialize, external debt would rise over the medium-term and external financing would peak at 8 percent of GDP, above the medium-vulnerability risk benchmark (though still below the high-vulnerability risk benchmark).[10]

34. After completion of the EFF-supported program, close Fund engagement will continue through policy dialogue and technical assistance. The authorities have indicated that they will not request a follow-up arrangement after the EFF-supported program expires on September 30, 2016. Given that Pakistan's outstanding credit to the Fund exceeds 200 percent of the quota and SDR 1.5 billion, staff supports Pakistan entering into Post-Program Monitoring.[11] Staff also recommends that Pakistan returns to the 12-month cycle for Article IV Consultations. Technical assistance is planned in the areas of national accounts and price statistics, fiscal reporting, debt management, and central bank consolidated supervision and contingency planning.

35. Safeguards Assessment. An updated safeguards assessment with respect to the EFF was completed in December 2013 and concluded that legal amendments are needed to strengthen the central bank's autonomy and governance arrangements. The authorities have implemented the 2013 safeguards recommendations, except for legal amendments to the SBP Act, which were only partially addressed. The authorities are taking steps to address a number of the remaining recommendations, including in the areas of the SBP's objectives, its financial autonomy, and its limits for providing credit to the government. However, several other recommendations—in the areas of institutional autonomy, governance, and personal autonomy of SBP board members—still remain to be addressed (¶22).

STAFF APPRAISAL

36. Over the course of the program, macroeconomic stability has been restored, vulnerabilities have been reduced, and progress has been made in tackling key structural challenges. At the start of the program in September 2013, growth prospects were weak, inflation was high, fiscal imbalances were large, and international reserves were low. Over the program period, helped by policy discipline and favorable oil prices, economic growth has gradually increased, inflation has been contained, and external buffers have been strengthened. Moreover, the fiscal deficit has been reduced, social safety nets have been strengthened, and the resilience of the financial sector has been reinforced. On the structural front, tax policy and administration reforms allowed further revenue mobilization; the SBP's autonomy started to be strengthened; the AML/CFT framework was improved; the energy sector reform reduced power outages, energy subsidies, and the accumulation of new power sector arrears; and a country-wide strategy to improve the business climate started to be implemented.

[10] The extreme test scenario assumes lower remittances, higher profit repatriation, a sharp decline in FDI and equity portfolio inflows, higher external financing costs, and lower medium-term growth.

[11] Pakistan is projected to fall below the PPM thresholds by 2023.

37. However, continued efforts will be needed to strengthen macroeconomic resilience and advance growth-supporting structural reforms. Despite sizable fiscal consolidation, public debt has remained high; foreign reserves remain below comfortable levels; there has been significant appreciation of the real exchange rate; and the structural reform agenda needs to be completed. To reinforce Pakistan's macroeconomic resilience, the authorities need to continue pursuing gradual fiscal consolidation, bolstering external buffers, maintaining a prudent monetary policy stance, and strengthening the resilience of the financial sector. In addition, advancing structural reforms beyond the end of the program will be important to generate stronger and more inclusive growth. The agenda should include advancing tax reforms to mobilize revenues needed to support higher priority social and investment spending, further strengthening the SBP's autonomy and the effectiveness of the AML/CFT framework, restructuring and privatizing PSEs, completing the energy sector reform, and improving the business climate.

38. Continuing to pursue gradual fiscal consolidation is needed to firmly put debt on a downward path. Staff supports the authorities' objective to reduce the overall fiscal deficit (excluding foreign grants) to 3.8 percent of GDP in FY 2016/17 while increasing capital expenditure and strengthening social safety nets. The authorities' additional measures to achieve their fiscal target are welcome. The fiscal consolidation strategy should continue beyond this fiscal year: the authorities should enhance revenue mobilization by broadening the tax base and contain nonpriority spending to support fiscal consolidation and create fiscal space to increase priority social and investment spending. The revised fiscal responsibility framework will help anchor fiscal policy in support of medium-term fiscal consolidation, and the new PPP framework can foster investment while managing associated fiscal risks. Strengthening fiscal policy coordination between the federal and provincial governments will be important to support medium-term fiscal consolidation. Moreover, further reducing the share of short-term debt will be important to strengthen Pakistan's macroeconomic resilience.

39. Monetary and exchange rate policies should continue to focus on bolstering external buffers and maintaining price stability. The authorities should continue to accumulate international reserves at a steady pace while allowing for greater downward exchange rate flexibility. This will help strengthen macroeconomic resilience and contain real exchange rate appreciation pressures which have affected competitiveness. The monetary policy stance should remain prudent to maintain low inflation and support macroeconomic stability, and the SBP should continue maintaining clearly positive real interest rates and be prepared to tighten monetary policy in case inflationary pressures intensify. While some progress has been made in strengthening the SBP's autonomy, more ambitious steps are required to address the remaining recommendations of the 2013 Safeguards Assessment.

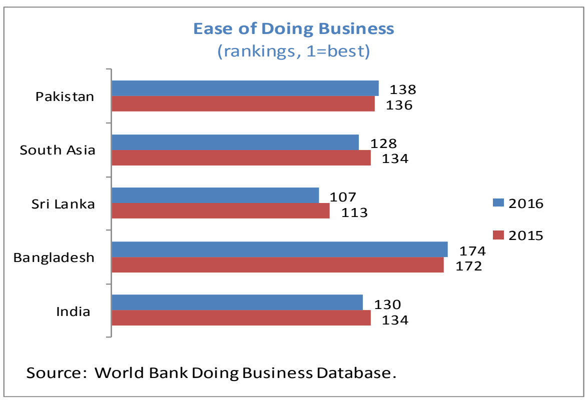
40. Financial policies should continue to focus on enhancing the sector's resilience. To this end, it will be important to make the new deposit insurance scheme operational, ensure all banks' compliance with regulatory capital requirements, further strengthen the regulatory and supervisory framework, and continue with policies to reduce the still high level of NPLs. The PDF should operate on a commercial basis to strictly limit any fiscal risks. While the expansion of the coverage of tax crimes as predicate offenses to money laundering was welcome to support the enforcement of revenue collection and strengthen governance, the authorities should continue enhancing the AML/CFT framework in line with international standards.

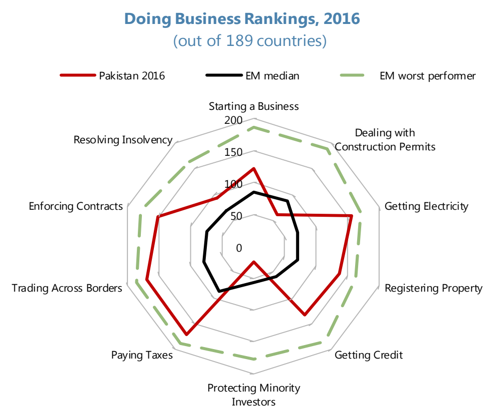
41. An acceleration in structural reforms is needed to support higher and more inclusive growth. Restructuring and seeking private sector participation in PSEs remain key to ensure their financial viability and reduce fiscal costs. Following setbacks earlier this year, the authorities' continued commitment to attract private sector participation in PSEs is welcome, while, in parallel, efforts to contain their financial losses continue. Power sector reforms need to be completed to strengthen the soundness of the sector, eliminate outages, and address the system's arrears. The updated arrears reduction plan is welcome, including the authorities' commitments to further improve DISCOs' performance and use the proceeds of planned IPOs to reduce outstanding arrears. Resuming regular tariff notification and establishing a multi-year tariff framework for DISCOs will be important to ensure cost recovery, attract private investors, and strengthen the regulatory framework. In addition, continuing with the swift implementation of the business climate reform strategy will be important to foster investment and support private-sector-led growth and job creation.

42. On the basis of Pakistan's performance under the extended arrangement and corrective actions, staff supports the authorities' request for completion of the twelfth review under the arrangement and for waivers for nonobservance of the end-June PCs on the budget deficit and NDA. Staff supports Pakistan entering into PPM and recommends a return to the 12-month cycle for Article IV Consultations.

Box 1. Strengthening the Business Climate

Pakistan's weak business climate continues to constrain private investment and economic growth. Despite several measures to improve the business climate, Pakistan's position in the World Bank Doing Business ranking further slipped to 138 in 2016 (out of 189 economies) from 136 in 2015, reflecting Pakistan's slower pace of reforms compared to other countries. Notably, Pakistan's ranking in starting a business, getting credit, and trading across borders worsened. Thus, lengthy procedures and high costs for opening a new business and paying taxes, limited access to credit notably for small and medium enterprises (SMEs), complex border trading requirements, constraints in accessing electricity, and weak contract enforcement continue to weigh on Pakistan's business climate, which ranks below the South Asia average and comparator emerging markets countries.





An Action Plan was adopted in 2014 and a number of measures to improve the business climate were implemented under the program during 2014–15. An integrated virtual One-Stop-Shop (VOSS) for investors was launched allowing to streamline procedures for new business registration and physical OSSs became operative in Lahore and Islamabad. The number of procedures for paying taxes was reduced by introducing an integrated web-based platform (IRIS) covering the full spectrum of business processes, and tax filing for traders was simplified. Pilot Alternative Dispute Resolution (ADR) mechanisms were introduced to facilitate the resolution of commercial disputes. A new National Financial Inclusion Strategy was adopted to foster the provision of credit to SMEs and marginalized segments of society, and the credit information system was strengthened. Furthermore, a web-based portal (WeBOC) was launched to facilitate the processing of export/imports documents, and an electronic export form was introduced.

Efforts to strengthen the business climate were redoubled in early 2016 with the adoption of a new strategy. Following consultation with key stakeholders and World Bank technical assistance, the authorities adopted a new and comprehensive country-wide reform strategy in February 2016. Building on the reforms undertaken under the 2014 Action Plan, the new strategy defines specific time-bound measures (short-term, medium-term and longer-term), both at the federal and provincial level, to tackle constraints to business creation, expansion and operations and targets the ten areas covered by the World Bank's Doing Business indicator. In the short term, the new strategy focuses on addressing constraints in key areas by easing procedures to start a new business and paying taxes, facilitating access to credit and trading across borders, and strengthening the regulatory framework.

Box 1. Strengthening the Business Climate (Concluded)

Key short-term measures under the new 2016 business climate reform strategy have been implemented. Notably, the utilization and accessibility of VOSS was enhanced and the fee structure was rationalized to reduce the costs to open a new business. The capacity of the IRIS web portal was strengthened and a new electronic tax filing procedure was developed. The Secured Transaction Act to use movable property as collateral for getting credit and amendments to the Credit Bureau Act 2015 were approved by the National Assembly, regulations for credit bureaus were issued, the Corporate Restructuring Companies Act to set up companies to take over assets of bankrupt firms was enacted and the Corporate Rehabilitation Act to establish a mechanism for the organization and rehabilitation of distressed companies was submitted to the parliament. Furthermore, an electronic form for imports was rolled out and the Real Time Electronic Data Exchange to facilitate trade with China has become operational.

Further advancing the new business climate reform strategy is pivotal to foster private sector investment and higher growth. Completing the automation of VOSS, expanding the physical OSSs, amending the 1984 Companies Ordinance to reduce start-up procedures for small-sized companies, consolidating payments at the provincial level and facilitating the use of digital signatures would ease the creation of new businesses. Completing the roll-out of electronic tax filing and new simplified tax forms, and implementing an associated electronic payment system would ease paying taxes. Enacting the amendments to the Credit Bureau Act 2015, licensing private credit bureaus under the new Bureau Act, and enacting and developing secondary regulations to implement the Secured Transaction Act would support better access to credit. Expediting the execution and registration of a deed, digitalizing maps and providing online access to land records would facilitate registering a property. Further expanding the use of ADR mechanisms, rolling out case management systems in district courts, establishing specialized commercial courts, and enacting the Corporate Rehabilitation Act to strengthen the bankruptcy framework would improve contract enforcement. Finally, completing the roll-out of WeBOC and strengthening the underlying IT infrastructure, implementing an integrated platform for clearance of goods, and rationalizing physical inspections would ease cross border trading.

Box 2. Improving Living Standards and Inclusiveness

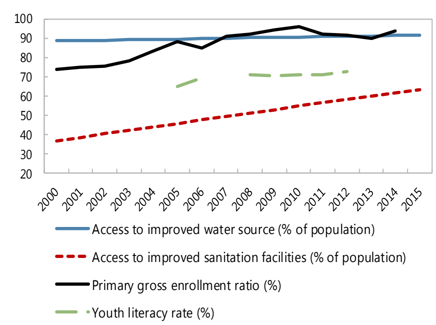
Despite improvements, poverty and unemployment remain significant. GDP growth averaged 4.3 percent during 2000–15 and, after decelerating during 2009–12, it has gradually recovered. During the same period, Pakistan's per capita income increased by 40 percent (but remains below the South Asia average), the poverty headcount dropped by more than 40 percent, and unemployment gradually decreased. However, unemployment remains high at nearly 6 percent, the informal economy is large, and about 30 percent of the population is still below the poverty line.

	2000	2005	2010	2011	2012	2013	2014		2015
							Pakistan	South Asia 1/	
GDP growth (% at constant factor costs)	3.9	9.0	2.6	3.6	3.8	3.7	4.1	6.9	4.0
GNI per capita (in 2005 US dollars)	612	729	790	800	815	833	858	1,496	..
Unemployment (% of total labor force)	7.8	7.7	5.6	6.0	6.0	6.2	6.0	3.9	5.9
Employment to population ratio (%)	47.3	48.8	51.2	51.3	51.5	51.6	51.7	54.0	..
Infant mortality rate (per 1,000 live births)	87.7	80.0	73.5	72.1	70.6	69.1	67.4	42.0	65.8
Poverty headcount ratio (% of population)	..	50.4	36.8	36.3	..	29.5	..	..	..
GINI index	..	32.7	29.6	..	..	..	..	31.4	..

Sources: World Bank; and IMF staff estimates and projections.
1/ South Asia is defined as Afghanistan, Bangladesh, Bhutan, India, Nepal, Pakistan, and Sri Lanka.

Access to education and health has improved but significant further efforts are needed. During 2000–14, the primary gross enrollment ratio and the youth literacy rate improved, reaching 94 percent and 73 percent, respectively. Infant mortality decreased to 66 per 1,000 live births, with life expectancy slightly increasing to 66.4 years. In parallel, public expenditure on education increased from 1.8 to 2.5 percent of GDP and public expenditure on health from 0.6 to 0.9 percent of GDP, although at these levels, public spending is still very low compared to other EMDCs. Access to improved water sanitation facilities increased markedly to about 60 percent of the population, with access to improved water sources reaching about 90 percent. Despite these improvements, Pakistan continues to rank low on the Human Development Index (147 out of 188 countries in 2015, unchanged from 2009).

Health and education



Source: World Bank

Gender inequality has decreased but remains high. Pakistan ranks poorly in the Gender Gap Index (144 out of 145 countries in 2015), well below comparator countries.[1] The gaps between male and female labor force participation and unemployment remain substantial, even if they slightly decreased to 58 percent and 5 percent, respectively, in 2014, while the primary gross enrollment ratio differential is high at 15 percent.

BISP, the main social safety net program, effectively contributed to reduce poverty. Launched in 2008, BISP provides a minimum income to the poorest through unconditional cash transfers (UCTs) and supports primary school enrollment and attendance through conditional education cash transfers (CCTs)**.** During the EFF-supported program, UCTs were increased by more than 60 percent and coverage was broadened to 5.36 million beneficiaries while CCTs' coverage increased to 1.3 million children. Impact evaluation analysis indicates that UCTs contribute to reduce poverty among BISP beneficiaries (20 percent reduction in the proportion of beneficiaries living below the poverty line from 2011 to 2014 in the sample) and strengthen women's empowerment by providing the cash transfer to any ever-married woman in a BISP-eligible household. However, the impact of CCTs on education remains more limited since the size of the transfer is low compared to the cost of schooling (Oxford Policy Management, 2015).

1/ The Gender Gap Index (World Economic Forum, 2015) measures the gap between men and women in four categories: economic participation and opportunity, educational attainment, health and survival and political empowerment.

Box 3. The Macroeconomic Impact of the China-Pakistan Economic Corridor

The China-Pakistan Economic Corridor (CPEC) is an opportunity for Pakistan to boost investment and growth. CPEC is a large package of investment projects in energy and transport infrastructure, financed by China. The total size of CPEC is estimated at around US$44½ billion (about 16 percent of FY 2015/16 GDP), of which more than half (US$28 billion) is allocated to "early harvest" projects over the next few years, with the remainder of the investments expected to materialize up to 2030 and beyond. Of the early harvest projects, about $10 billion is allocated to road, rail, and port infrastructure, which the government plans to execute within its regular development spending envelope. The remaining $18 billion (6 percent of GDP) will largely cover energy projects provided through FDI. Some CPEC priority projects are already under way, which contributed to a pickup in FDI, imports of machinery and industrial materials, and the government's external financing in FY 2015/16.

Financing modalities vary across sectors and projects. In the energy sector, power plant projects will be funded through FDI by Chinese firms with commercial loans borrowed from Chinese banks. These firms will operate as Independent Power Producers (IPPs) and have their electricity sales guaranteed through pre-negotiated power purchase agreements including guaranteed tariffs. In the transport sector, financing will be provided by the Chinese government and state banks mostly as concessional loans. Other, smaller CPEC infrastructure projects are expected to be financed through a mix of concessional loans and grants.

Estimated Financing for "Early Harvest" Projects

US$, millions	FDI	Concessional loan	Commercial loan	Grant	Total
Energy	18,000	0	0	0	18,000
Transportation	1,247	6,465	1,620	0	9,332
Other infrastructure	0	259	0	228	487
Total	19,247	6,724	1,620	228	27,819

Sources: Pakistani authorities; various media reports; and IMF staff estimates.

The direct impacts on the external balance are expected to be substantial. During the investment phase, as the "early harvest" projects proceed, Pakistan will experience a surge in FDI and other external funding inflows. A concomitant increase in imports of machinery, industrial raw materials, and services will likely offset a significant share of these inflows, such that the current account deficit would widen, with manageable net inflows into the balance of payments. While precise quantification of these impacts is difficult due to uncertainty and lack of available information, staff projects CPEC-related capital inflows (FDI and external borrowing) to reach about 2.2 percent of the projected GDP in FY 2019/20, and CPEC-related imports to about 11 percent of the total projected imports in the same year.[1]

The broader positive impacts on the economy would be considerable. If implemented as envisaged, CPEC could go a long way towards alleviating Pakistan's long-standing supply-side bottlenecks and lifting its long-term potential output. Priority energy sector projects are expected to add significant power-generation capacity within the next few years, and subsequent energy projects could further expand the capacity over the long term. This would help mitigate Pakistan's chronic electricity load-shedding problem and provide a reliable support for domestic economic activities and exports. CPEC transport infrastructure projects (e.g. roads, railways, port facility upgrade) would allow easier and lower-cost access to domestic and overseas markets, promoting inter-regional and international merchandise trade. Service exports would also benefit from the increased trade traffic from China. Furthermore, these CPEC projects could catalyze private business investment and boost productivity—e.g., by facilitating more efficient allocation of productive inputs across regions.

Over the longer term, Pakistan will need to manage increasing CPEC-related outflows. As Chinese IPPs start their operations, profit repatriation by these companies would begin to rise in the subsequent years. While the path and the size of the repatriation would depend on factors such as the timing of project completion and the terms of power purchase agreements with the Pakistani government, it could add up to a significant level given the magnitude of the FDI. Repayment obligations to CPEC-related government borrowing, including amortization and interest payments, are expected to rise after FY 2020/21 due to the concessional terms of most of these loans. Combined, these CPEC-related outflows could reach about 0.4 percent of GDP per year over the longer run.

Box 3. The Macroeconomic Impact of the China-Pakistan Economic Corridor (Concluded)

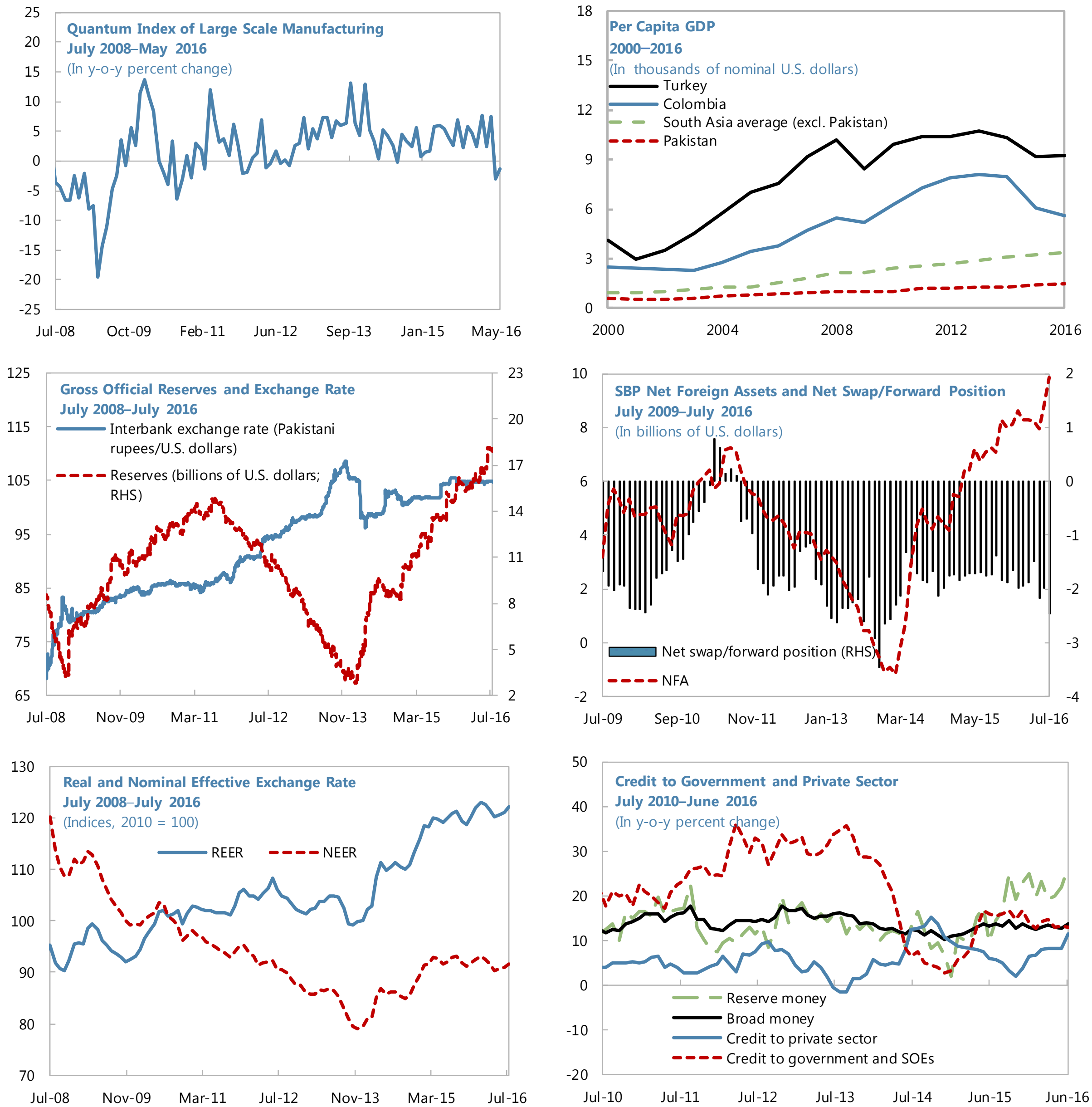
Pro-growth reforms and prudent macroeconomic policies will be essential to unlock CPEC's full potential. Supported by increased energy supply and transportation capacity, CPEC has the potential to catalyze higher private investment and exports, which would help cover the CPEC-related outflows that are expected over the longer term. Reaping the full potential benefits of CPEC will require forceful pro-growth and export-supporting reforms. These include improvements in the business climate, and strengthening governance and security. Real effective exchange rate appreciation should be contained by allowing greater downward exchange rate flexibility and keeping inflation well anchored. Finally, fiscal policy should remain prudent and debt management should be strengthened to keep the long-term public debt path sustainable. The authorities noted that additional Chinese investment over the longer term, building on CPEC as a platform, could also help cover the projected CPEC-related outflows.

Sound project management and monitoring system should be in place to ensure timely implementation and mitigate risks. There is a need to ensure sound project evaluation and prioritization mechanisms based on effective cost-benefit analysis and realistic forecasts of macroeconomic and financing conditions. The procurement process should be transparent and competitive, and there is a need to ensure transparency and accountability in project management and monitoring.[2] Power purchase agreements with Chinese IPPs should be negotiated with terms that would adequately incentivize investment while ensuring that the cost of generated power remains favorable for the distribution system and consumers. Moreover, capacity improvements in the power transmission network will be needed to keep up with the increasing supply.

[1]This baseline projection is predicated on the assumption that the completion of "early harvest" projects would extend up to FY 2020/21, given large uncertainties and Pakistan's absorptive capacity.

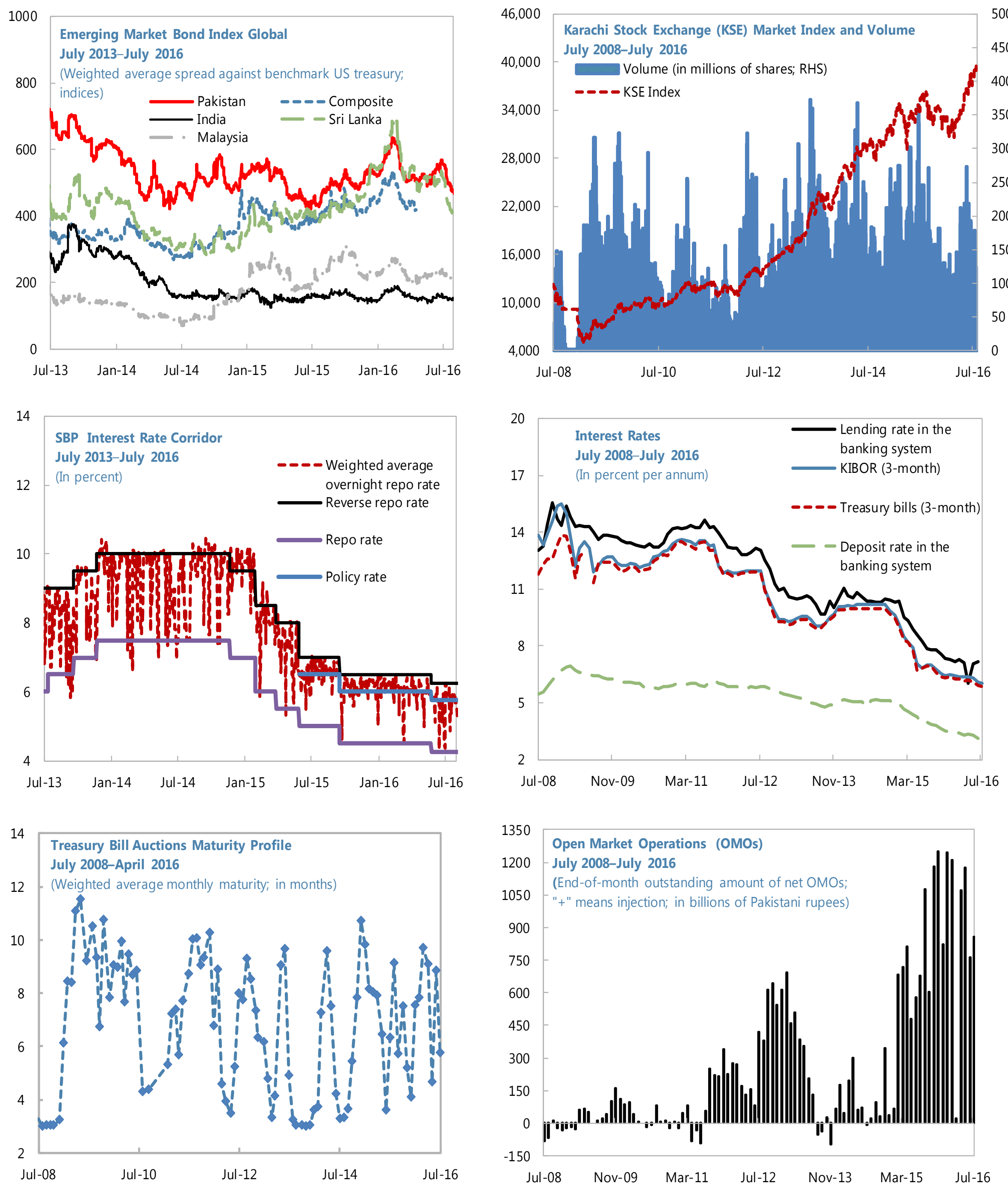
[2] International Monetary Fund, 2015, "Making Public Investment More Efficient."

Figure 2. Pakistan: Selected Economic Indicators, 2008–16



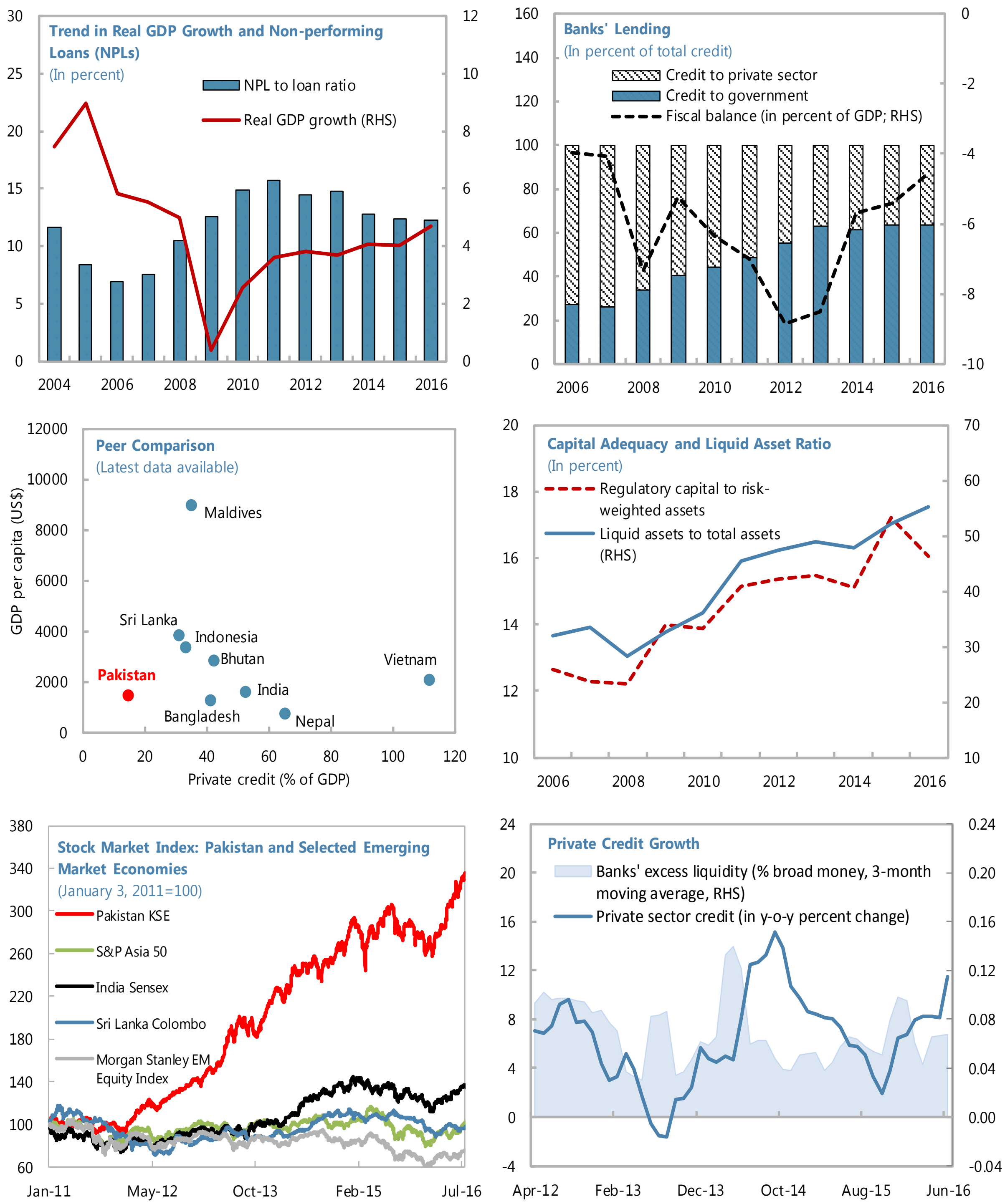
Sources: Pakistani authorities; IMF World Economic Outlook Database; and IMF staff calculations.

Figure 3. Pakistan: Selected Financial Indicators, 2008–16



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

Figure 4. Pakistan: Selected Banking and Financial Indicators



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

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets for FY 2014/15 and FY 2015/16

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

	FY2014/15	FY2015/16					
	end-June	end-September	end-December	end-March	end-June		
					Program		
					Twelfth Review		
					Target	Adj. Target	Actual
Performance Criteria							
Floor on net international reserves of the SBP (millions of U.S. dollars) 4/	5,354	6,955	6,882	6,172	11,050	6,310	7,560
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,442	2,661	2,633	2,791	2,731	3,023	3,029
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	1,489	329	541	1,009	1,292	1,292	1,349
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	1,700	1,385	1,650	1,885	2,000	2,000	1,985
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3	1,887	1,589	1,457	1,361	1,800	1,800	1,412
Continuous Performance Criterion							
Accumulation of external public payment arrears by the general government (continuous)	0	0	0	0	0	0	0
Indicative Targets							
Cumulative floor on Targeted Cash Transfers Spending (BISP) (billions of Pakistani rupees)	94	24	48	75	95	95	101
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	2,588	600	1,385	2,103	3,104	3,104	3,112
Ceiling on power sector payment arrears (flow, billions of Pakistani rupees)	57	13	0	4.9	18	18	(10)

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.
4/ Adjustors are presented on a cumulative basis since the beginning of the program (September, 2013).

Table 2. Pakistan: Structural Benchmarks, Twelfth and Last Review 2016

Item	Measure	Time Frame (by End of Period)	Status	Macroeconomic rationale
Prior Actions				
1	Bring the stock of NDA of the SBP to or below PRs 3,100 billion by end-August 2016.	end-August 2016	Met	Conduct prudent monetary policy
Structural Benchmarks				
Financial sector				
2	Enact the Deposit Protection Corporation Act, in line with Fund staff advice.	end-August 2016	Met	Enhance the resilience of the financial sector.
Structural Policies				
3	Notify multi-year tariffs for FESCO, IESCO and LESCO.	July 15, 2016	Not Met	Prepare for DISCO privatization.
4	Update the plan to further limit the accumulation of new payables and gradually eliminate the outstanding stock of payables arrears in the power sector.	July 15, 2016	Met	Strengthen the financial perfomance of the power sector.
5	Solicit expressions of interest for the divestment of Kot Addu Power Company (KAPCO).	July 15, 2016	Met	Strenghten private sector participation in the energy sector.

Table 3. Pakistan: Selected Economic Indicators, 2010/11–2016/17[1/]

Population: 189.9 million (2014/15)
Per capita GDP: US$1,510 (2014/15)
Poverty rate: 12.7 percent (2010/11)
Main exports: Textiles ($13.5 billion, 2014/15)
Unemployment: 5.9 percent (2014/15)

	2012/13	2013/14	2014/15	2015/16		2016/17
				Eleventh Review	Actual	Proj.
			(Annual percentage change)			
Output and prices						
Real GDP at factor cost	3.7	4.1	4.0	4.7	4.7	5.0
GDP deflator at factor cost	7.1	7.4	4.6	2.0	2.0	5.2
Consumer prices (period average)	7.4	8.6	4.5	3.0	2.9	5.2
Consumer prices (end of period)	5.9	8.2	3.2	4.0	3.2	5.3
Pakistani rupees per U.S. dollar (period average)	8.4	6.4	-1.5			
			(In percent of GDP)			
Saving and investment						
Gross saving	13.9	13.4	14.5	14.2	14.3	14.2
Government	-5.1	-1.4	-1.6	-0.6	-0.7	0.2
Nongovernment (including public sector enterprises)	19.0	14.7	16.1	14.8	15.0	14.0
Gross capital formation 2/	15.0	14.6	15.5	15.2	15.2	15.7
Government	3.2	3.5	3.7	3.5	3.7	3.8
Nongovernment (including public sector enterprises)	11.7	11.1	11.8	11.7	11.5	11.9
Public finances						
Revenue and grants	13.5	15.2	14.5	15.6	15.2	16.0
Expenditure (including statistical discrepancy)	21.9	19.8	19.1	19.5	18.9	19.6
Budget balance (including grants)	-8.4	-4.9	-5.2	-4.1	-4.3	-3.6
Budget balance (excluding grants)	-8.5	-5.7	-5.4	-4.4	-4.6	-3.8
Primary balance	-3.9	-0.3	-0.5	0.2	-0.1	0.5
Total general government debt	62.3	62.5	62.0	62.7	64.8	62.9
External general government debt	19.6	19.2	17.7	18.9	18.7	18.8
Domestic general government debt	42.8	43.3	44.3	43.8	46.0	44.1
			(Annual changes in percent of initial stock of broad money, unless otherwise indicated)			
Monetary sector						
Net foreign assets	-3.4	3.7	2.1	2.4	1.7	2.3
Net domestic assets	19.3	8.8	11.1	10.1	11.9	9.9
Broad money (percent change)	15.9	12.5	13.2	12.5	13.7	12.2
Reserve money (percent change)	15.8	12.9	9.8	17.0	26.5	12.0
Private credit (percent change)	-0.6	12.5	5.9	9.0	11.1	13.0
Six-month treasury bill rate (period average, in percent)	9.8	9.7	8.8			
External sector						
Merchandise exports, U.S. dollars (percentage change)	0.4	1.1	-3.9	-8.8	-8.6	3.5
Merchandise imports, U.S. dollars (percentage change)	-0.6	3.8	-0.9	-4.4	-2.0	7.4
Current account balance (in percent of GDP)	-1.1	-1.3	-1.0	-1.0	-0.9	-1.5
			(In percent of exports of goods and services, unless otherwise indicated)			
External public and publicly guaranteed debt	140.7	161.2	159.7	192.0	192.9	199.4
Debt service	21.6	26.2	22.5	24.2	22.1	29.9
Gross reserves (in millions of U.S. dollars) 3/	6,008	9,096	13,534	18,378	18,129	20,847
In months of next year's imports of goods and services	1.5	2.2	3.4	4.3	4.2	4.6
Memorandum items:						
Real effective exchange rate (annual average, percentage change)	-1.3	0.9	10.9			
Terms of trade (percentage change)	-1.9	0.2	7.0	9.6	10.7	-0.6
Real per capita GDP (percentage change)	2.1	2.6	2.0	3.0	3.0	3.3
GDP at market prices (in billions of Pakistani rupees)	22,386	25,169	27,493	29,598	29,598	33,130
GDP at market prices (in billions of U.S. dollars)	231.2	244.4	271.0			

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

1/ Fiscal year ends June 30.
2/ Including changes in inventories.
3/ Excluding gold and foreign currency deposits of commercial banks held with the State Bank of Pakistan.

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

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16		2016/17	2017/18	2018/19	2019/20
						Eleventh Review	Actual	Projections			
						(Annual percentage change)					
Output and prices											
Real GDP at factor cost	3.6	3.8	3.7	4.1	4.0	4.7	4.7	5.0	5.2	5.5	5.5
Consumer prices (period average)	13.7	11.0	7.4	8.6	4.5	3.0	2.9	5.2	5.0	5.0	5.0
						(In percent of GDP)					
Saving and investment balance	0.1	-2.1	-1.1	-1.3	-1.0	-1.0	-0.9	-1.5	-2.2	-2.2	-1.9
Government	-6.7	-8.6	-8.4	-4.9	-5.2	-4.1	-4.3	-3.6	-2.9	-2.7	-2.5
Non-government (including public sector enterprises)	6.8	6.6	7.3	3.6	4.3	3.1	3.5	2.1	0.7	0.5	0.6
Gross national saving	14.2	13.0	13.9	13.4	14.5	14.2	14.3	14.2	13.9	14.4	15.1
Government	-4.2	-5.3	-5.1	-1.4	-1.6	-0.6	-0.7	0.2	1.0	1.3	1.8
Non-government (including public sector enterprises)	18.4	18.3	19.0	14.7	16.1	14.8	15.0	14.0	12.9	13.1	13.3
Gross capital formation	14.1	15.1	15.0	14.6	15.5	15.2	15.2	15.7	16.0	16.6	17.0
Government	2.5	3.4	3.2	3.5	3.7	3.5	3.7	3.8	3.8	4.0	4.3
Non-government (including public sector enterprises)	11.6	11.7	11.7	11.1	11.8	11.7	11.5	11.9	12.2	12.6	12.7
						(In billions of U.S. dollars, unless otherwise indicated)					
Balance of payments											
Current account balance	0.2	-4.7	-2.5	-3.1	-2.6	-2.9	-2.5	-4.7	-7.1	-7.6	-7.1
Net capital flows 1/	2.3	1.4	0.5	7.0	5.3	5.8	5.1	7.4	8.4	8.0	7.3
Of which: foreign direct investment 2/	1.6	0.7	1.3	1.6	0.8	1.3	1.3	2.6	3.3	4.4	6.0
Gross official reserves	14.8	10.8	6.0	9.1	13.5	18.4	18.1	20.8	22.0	21.8	21.2
In months of imports 3/	3.6	2.7	1.5	2.2	3.4	4.3	4.2	4.6	4.5	4.2	4.0
External debt (in percent of GDP)	31.1	29.2	26.3	26.7	24.0	25.6	25.7	25.1	24.9	24.2	22.7
Terms of trade (annual percentage change)	7.3	-9.7	-1.9	0.2	7.0	9.6	10.7	-0.6	-0.9	-0.2	-0.9
Real effective exchange rate (annual percentage change)	6.1	3.0	-1.3	0.9	10.9						
						(In percent of GDP)					
Public finances											
Revenue and grants	12.6	13.0	13.5	15.2	14.5	15.6	15.2	16.0	16.7	17.0	17.3
Of which: tax revenue	9.5	10.4	10.0	10.5	11.0	12.3	12.4	12.9	13.6	13.9	14.3
Expenditure, *of which:*	19.3	21.7	21.8	20.1	19.7	19.8	19.6	19.6	19.6	19.6	19.8
Current	16.5	17.9	16.8	16.4	16.6	16.5	16.6	15.8	15.7	15.7	15.5
Development and net lending	2.6	3.5	5.0	4.0	3.8	3.5	3.7	3.8	3.8	4.0	4.3
Primary balance (including grants)	-2.9	-4.2	-3.9	-0.3	-0.5	0.2	-0.1	0.5	1.5	1.7	1.6
Primary balance (excluding grants)	-3.2	-4.4	-4.1	-1.1	-0.7	0.0	-0.3	0.3	1.3	1.6	1.6
Overall fiscal balance (including grants)	-6.7	-8.6	-8.4	-4.9	-5.2	-4.1	-4.3	-3.6	-2.9	-2.7	-2.5
Overall fiscal balance (excluding grants)	-7.0	-8.9	-8.5	-5.7	-5.4	-4.4	-4.6	-3.8	-3.0	-2.8	-2.5
Total public debt (including obligations to the IMF)	58.9	63.3	64.2	63.7	63.6	64.3	66.9	64.2	61.7	59.3	56.4

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.

Table 5. Pakistan: Balance of Payments, 2013/14–2019/20
(In millions of U.S. dollars, unless otherwise indicated)

	2013/14	2014/15	2015/16		2016/17					2017/18	2018/19	2019/20
			Eleventh Review	Actual	Q1	Q2	Q3	Q4				
					Projections							
Current account	-3,130	-2,627	-2,885	-2,480	-1,053	-1,409	-1,346	-874	-4,684	-7,079	-7,645	-7,063
Balance on goods	-16,701	-17,318	-17,622	-18,567	-5,257	-5,381	-5,107	-5,034	-20,779	-22,260	-23,356	-22,965
Exports, f.o.b.	25,068	24,083	21,961	22,003	5,322	5,681	5,780	5,984	22,767	24,116	26,071	29,027
Imports, f.o.b.	41,769	41,401	39,583	40,570	10,579	11,063	10,887	11,018	43,547	46,376	49,426	51,992
Services (net)	-2,551	-2,842	-2,424	-2,285	-456	-569	-661	-438	-2,124	-3,170	-3,210	-3,769
Services: credit	5,322	5,876	5,000	5,455	1,451	1,378	1,284	1,606	5,719	5,386	5,864	6,320
Of which: Coalition Support Fund	1,050	1,452	937	937	364	186	175	400	1,125	0	0	0
Services: debit	7,873	8,718	7,424	7,740	1,907	1,946	1,945	2,044	7,843	8,557	9,074	10,089
Income (net)	-3,943	-4,565	-5,014	-4,745	-1,101	-1,327	-1,280	-1,364	-5,072	-5,705	-6,165	-7,108
Income: credit	541	681	604	585	138	157	142	178	615	646	678	735
Income: debit	4,484	5,246	5,618	5,330	1,239	1,484	1,422	1,542	5,686	6,352	6,843	7,842
Of which: interest payments	1,552	1,936	2,125	2,114	507	575	661	568	2,310	2,776	2,956	3,269
Of which: income on direct investment	2,932	3,308	3,483	3,202	732	909	761	974	3,376	3,575	3,887	4,573
Balance on goods, services, and income	-23,195	-24,725	-25,059	-25,597	-6,814	-7,277	-7,048	-6,836	-27,975	-31,136	-32,731	-33,842
Current transfers (net)	20,065	22,098	22,174	23,117	5,761	5,867	5,702	5,962	23,291	24,057	25,086	26,779
Current transfers: credit, *of which:*	20,222	22,337	22,305	23,263	5,800	5,907	5,741	6,002	23,450	24,216	25,245	26,938
Official	380	349	540	527	137	143	49	104	433	327	12	12
Workers' remittances	15,837	18,720	19,186	19,915	5,000	5,044	4,932	5,186	20,162	20,900	22,049	23,529
Other private transfers	4,005	3,268	2,579	2,821	664	720	761	711	2,856	2,989	3,183	3,397
Current transfers: debit	157	239	131	146	40	40	40	40	159	159	159	159
Capital account	1,857	378	426	342	66	77	59	93	295	436	291	222
Capital transfers: credit	1,857	378	432	348	66	77	59	93	295	436	291	222
Of which: official capital grants	352	367	426	342	66	77	59	93	295	436	291	222
Capital transfers: debit	0	0	6	6	0	0	0	0	0	0	0	0
Financial account	5,553	5,004	5,687	4,764	1,068	2,208	2,033	1,774	7,083	7,932	7,662	7,058
Direct investment abroad	-128	-72	-38	-15	-4	-3	-4	-3	-14	-13	-13	-13
Direct investment in Pakistan	1,700	852	1,385	1,282	522	665	594	816	2,597	3,343	4,410	6,010
Of which: privatization receipts	310	764	0	0	0	0	0	0	0	0	0	0
Portfolio investment (net), *of which:*	2,760	1,903	46	-430	85	836	87	337	1,345	678	135	-969
Financial derivatives (net)	0	0	0	0	0	0	0	0	0	0	0	0
Other investment assets	211	102	219	-82	-33	-33	-33	-23	-120	102	138	145
Monetary authorities	0	0	0	0	0	0	0	0	0	0	0	0
General government	5	-31	-41	-46	0	0	0	0	0	0	0	0
Banks	8	-63	460	169	17	17	17	17	70	70	70	70
Other sectors	198	196	-200	-205	-50	-50	-50	-40	-190	32	68	75
Other investment liabilities	1,010	2,219	4,076	4,009	498	743	1,389	646	3,276	3,822	2,993	1,886
Monetary authorities	146	563	3	4	0	0	0	0	0	0	0	0
General government, *of which:*	1,610	893	4,237	3,626	466	663	1,351	434	2,913	3,614	2,876	1,647
Disbursements	4,349	3,704	7,630	6,339	1,614	1,403	2,801	2,417	8,234	9,350	8,702	8,734
Amortization	2,734	2,809	3,393	2,713	1,148	740	1,450	1,983	5,321	5,736	5,827	7,087
Banks	-293	480	32	374	15	16	17	17	65	79	96	116
Other sectors	-453	283	-196	5	17	64	22	195	298	130	22	123
Net errors and omissions	-422	-119	-315	14	0	0	0	0	0	0	0	0
Reserves and related items	-3,858	-2,636	-2,912	-2,640	-81	-876	-745	-993	-2,695	-1,289	-308	-218
Reserve assets	-2,464	-4,044	-4,830	-4,547	-166	-855	-724	-973	-2,718	-1,124	146	603
Use of Fund credit and loans	-1,394	1,408	1,918	1,907	84	-20	-20	-20	24	-165	-454	-821
Memorandum items:												
Current account (in percent of GDP)	-1.3	-1.0	-1.0	-0.9	...	...	...	...	-1.5	-2.2	-2.2	-1.9
Current account (in percent of GDP; excluding fuel imports)	4.8	3.5	1.9	1.8	...	...	...	...	1.6	1.0	1.3	1.8
Exports f.o.b. (growth rate, in percent)	1.1	-3.9	-8.8	-8.6	...	...	...	...	3.5	5.9	8.1	11.3
Imports f.o.b. (growth rate, in percent)	3.8	-0.9	-4.4	-2.0	...	...	...	...	7.4	6.5	6.6	5.2
Oil imports (in million US$, cif)	14,774	12,167	8,150	7,668	...	...	...	...	9,654	10,462	12,205	13,954
Terms of trade (growth rate, in percent)	0.2	7.0	9.6	10.7	...	...	...	...	-0.6	-0.9	0	-1
External debt (in millions of U.S. dollars)	65,365	65,103	71,870	72,978	...	...	...	...	76,925	81,876	85,346	85,843
o/w external public debt	51,998	51,935	56,210	59,023	...	...	...	...	60,832	63,779	64,683	62,171
Gross external financing needs (in millions of U.S. dollars) 1/	9,536	7,445	7,297	6,440	...	...	...	...	10,901	13,176	15,746	17,475
End-period gross official reserves (millions of U.S. dollars) 2/	9,096	13,534	18,378	18,129	18,295	19,150	19,874	20,847	20,847	21,971	21,825	21,222
(In months of next year's imports of goods and services)	2.2	3.4	4.3	4.2	4.2	4.3	4.4	4.6	4.6	4.5	4.2	4.0
GDP (in millions of U.S. dollars)	244,361	271,050		284,185	...	...	...	...				

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, 2008/09–2016/17
(In billions of Pakistani rupees)

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16		2016/17
								Eleventh Review	Actual	Projection
Revenue and grants	1,878	2,130	2,306	2,611	3,011	3,837	3,984	4,625	4,512	5,293
Revenue	1,851	2,079	2,261	2,567	2,982	3,631	3,937	4,556	4,447	5,248
Tax revenue	1,331	1,500	1,738	2,076	2,231	2,640	3,024	3,643	3,660	4,265
Federal	1,285	1,445	1,673	1,969	2,081	2,450	2,818	3,377	3,377	3,921
FBR revenue	1,157	1,329	1,558	1,881	1,936	2,272	2,594	3,104	3,112	3,621
Direct taxes	440	529	602	732	736	884	1,029	1,284	1,192	1,461
Federal excise duty	116	121	137	122	119	145	170	183	191	245
Sales tax/VAT	452	517	633	809	841	1,002	1,089	1,262	1,324	1,498
Customs duties	148	162	185	218	240	241	306	375	406	417
Petroleum surcharge	112	89	83	60	110	104	131	135	149	150
Gas surcharge and other	16	28	32	27	35	43	35	38	36	40
GIDC	0.0	0.0	0.0	0.0	0.0	32	57	100	80	110
Provincial	46	55	65	107	151	190	206	265	283	344
Nontax revenue	520	579	523	491	751	990	913	913	786	983
Federal	436	511	461	443	680	941	838	823	693	874
Provincial	84	68	62	48	71	49	76	90	93	110
Grants	27	50	46	45	29	206	47	69	66	45
Expenditure	2,544	3,024	3,536	4,341	4,885	5,058	5,426	5,848	5,796	6,498
Current expenditure	2,093	2,481	3,012	3,579	3,757	4,123	4,556	4,882	4,907	5,248
Federal	1,547	1,853	2,227	2,611	2,647	2,950	3,169	3,402	3,357	3,554
Interest	638	642	698	889	991	1,148	1,304	1,289	1,263	1,362
Domestic	559	578	630	821	920	1,073	1,208	1,170	1,151	1,231
Foreign	79	64	68	68	71	75	96	119	113	132
Other	909	1,211	1,529	1,722	1,656	1,802	1,866	2,113	2,093	2,192
Defense	330	375	450	507	541	623	698	781	758	860
Other	579	836	1,078	1,215	1,116	1,179	1,168	1,332	1,336	1,332
Of which: subsidies 1/	244	227	493	556	368	336	265	165	218	154
Of which: grants 2/	136	359	259	291	305	372	401	616	563	581
Provincial	546	627	786	968	1,110	1,173	1,387	1,480	1,550	1,694
Development expenditure and net lending	417	571	477	696	1,112	997	1,047	1,040	1,102	1,250
Public Sector Development Program	398	518	465	675	721	878	1,013	1,040	1,089	1,255
Federal	196	260	216	299	348	435	489	510	496	620
Provincial	202	258	249	376	373	443	524	530	592	635
Net lending	20	53	12	21	391	119	34	0	13	-5
Statistical discrepancy ("+" = additional expenditure)	34	-28	46	67	16	-62	-178	-74	-212	0
Overall Balance (excluding grants)	-693	-944	-1,276	-1,775	-1,903	-1,427	-1,489	-1,292	-1,349	-1,250
Overall Balance (including grants)	-666	-894	-1,230	-1,730	-1,873	-1,221	-1,442	-1,223	-1,284	-1,205
Financing	666	894	1,230	1,730	1873	1,221	1,442	1,223	1,284	1,205
External	86	158	144	60	38	351	166	493	331	424
Of which: privatization receipts	1	0	0	0	0	1	2	0	0	0
Of which: IMF	0	0	0	0	0	0	0	0	0	0
Domestic	580	736	1,086	1,670	1836	870	1,276	730	953	782
Bank	353	305	614	1,140	1457	322	910	511	780	547
Nonbank	227	431	471	529	378	548	366	219	173	234
Memorandum items:										
Primary balance (excluding grants)	-56	-302	-577	-886	-912	-279	-185	-3	-86	112
Primary balance (including grants)	-28	-252	-532	-841	-882	-73	-138	66	-21	157
Total security spending	330	375	450	507	541	623	698	781	758	860
Energy sector circular debt clearance	0	0	0	391	322	0	0	25	16	19
Total government debt	7,313	8,331	10,005	12,008	13,948	15,730	17,059	18,562	19,165	20,836
Domestic debt	3,860	4,654	6,017	7,638	9,571	10,902	12,188	12,956	13,619	14,621
External debt	3,453	3,677	3,988	4,370	4,376	4,828	4,871	5,606	5,546	6,215
Total government debt including guarantees	n.a.	8,934	10,584	12,540	14,573	16,291	17,695	...	...	...
Total government debt including IMF obligations	7,731	9,020	10,773	12,699	14,380	16,028	17,477	19,043	19,797	21,278
Nominal GDP (market prices)	13,200	14,867	18,276	20,047	22,386	25,169	27,493	29,598	29,598	33,130

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

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

2/ Additional spending on security and internally-displaced people is recorded under transfers ("grants") instead of development expenditure as reported in the original FY2015/16 budget.

Table 6b. Pakistan: General Government Budget, 2009/10–2016/17

(In percent of GDP, unless otherwise indicated)

	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16 Eleventh Review	2015/16 Actual	2016/17 Projection
Revenue and grants	14.3	12.6	13.0	13.5	15.2	14.5	15.6	15.2	16.0
Revenue	14.0	12.4	12.8	13.3	14.4	14.3	15.4	15.0	15.8
Tax revenue	10.1	9.5	10.4	10.0	10.5	11.0	12.3	12.4	12.9
Federal	9.7	9.2	9.8	9.3	9.7	10.2	11.4	11.4	11.8
FBR revenue	8.9	8.5	9.4	8.6	9.0	9.4	10.5	10.5	10.9
Direct taxes	3.6	3.3	3.7	3.3	3.5	3.7	4.3	4.0	4.4
Federal excise duty	0.8	0.8	0.6	0.5	0.6	0.6	0.6	0.6	0.7
Sales tax	3.5	3.5	4.0	3.8	4.0	4.0	4.3	4.5	4.5
Customs duties	1.1	1.0	1.1	1.1	1.0	1.1	1.3	1.4	1.3
Petroleum surcharge / Carbon tax	0.6	0.5	0.3	0.5	0.4	0.5	0.5	0.5	0.5
Gas surcharge and other	0.2	0.2	0.1	0.2	0.2	0.1	0.1	0.1	0.1
GIDC	…	…	…	…	0.1	0.2	0.3	0.3	0.3
Provincial	0.4	0.4	0.5	0.7	0.8	0.7	0.9	1.0	1.0
Nontax revenue	3.9	2.9	2.4	3.4	3.9	3.3	3.1	2.7	3.0
Federal	3.4	2.5	2.2	3.0	3.7	3.0	2.8	2.3	2.6
Provincial	0.5	0.3	0.2	0.3	0.2	0.3	0.3	0.3	0.3
Grants	0.3	0.2	0.2	0.1	0.8	0.2	0.2	0.2	0.1
Expenditure	20.3	19.3	21.7	21.8	20.1	19.7	19.8	19.6	19.6
Current expenditure	16.7	16.5	17.9	16.8	16.4	16.6	16.5	16.6	15.8
Federal	12.5	12.2	13.0	11.8	11.7	11.5	11.5	11.3	10.7
Interest	4.3	3.8	4.4	4.4	4.6	4.7	4.4	4.3	4.1
Domestic	3.9	3.4	4.1	4.1	4.3	4.4	4.0	3.9	3.7
Foreign	0.4	0.4	0.3	0.3	0.3	0.3	0.4	0.4	0.4
Other	8.1	8.4	8.6	7.4	7.2	6.8	7.1	7.1	6.6
Defense	2.5	2.5	2.5	2.4	2.5	2.5	2.6	2.6	2.6
Other	5.6	5.9	6.1	5.0	4.7	4.2	4.5	4.5	4.0
Of which: subsidies 1/	1.5	2.7	2.8	1.6	1.3	1.0	0.6	0.7	0.5
Of which: grants 2/	2.4	1.4	1.5	1.4	1.5	1.5	2.1	1.9	1.8
Provincial	4.2	4.3	4.8	5.0	4.7	5.0	5.0	5.2	5.1
Development expenditure and net lending	3.8	2.6	3.5	5.0	4.0	3.8	3.5	3.7	3.8
Public Sector Development Program	3.5	2.5	3.4	3.2	3.5	3.7	3.5	3.7	3.8
Federal	1.7	1.2	1.5	1.6	1.7	1.8	1.7	1.7	1.9
Provincial	1.7	1.4	1.9	1.7	1.8	1.9	1.8	2.0	1.9
Net lending	0.4	0.1	0.1	1.7	0.5	0.1	0.0	0.0	0.0
Statistical discrepancy ("+" = additional expenditure)	-0.2	0.3	0.3	0.1	-0.2	-0.6	-0.2	-0.7	0.0
Overall Balance (excluding grants)	-6.4	-7.0	-8.9	-8.5	-5.7	-5.4	-4.4	-4.6	-3.8
Overall Balance (including grants)	-6.0	-6.7	-8.6	-8.4	-4.9	-5.2	-4.1	-4.3	-3.6
Financing	6.0	6.7	8.6	8.4	4.9	5.2	4.1	4.3	3.6
External	1.1	0.8	0.3	0.2	1.4	0.6	1.7	1.1	1.3
Of which: privatization receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: IMF	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic	4.9	5.9	8.3	8.2	3.5	4.6	2.5	3.2	2.4
Bank	2.1	3.4	5.7	6.5	1.3	3.3	1.7	2.6	1.7
Nonbank	2.9	2.6	2.6	1.7	2.2	1.3	0.7	0.6	0.7
Memorandum items:									
Primary balance (excluding grants)	-2.0	-3.2	-4.4	-4.1	-1.1	-0.7	0.0	-0.3	0.3
Primary balance (including grants)	-1.7	-2.9	-4.2	-3.9	-0.3	-0.5	0.2	-0.1	0.5
Total security spending	2.5	2.5	2.5	2.4	2.5	2.5	2.6	2.6	2.6
Energy sector circular debt clearance	0.0	0.0	2.0	1.4	0.0	0.0	0.1	0.1	0.1
Total government debt	56.0	54.7	59.9	62.3	62.5	62.0	62.7	64.8	62.9
Domestic debt	31.3	32.9	38.1	42.8	43.3	44.3	43.8	46.0	44.1
External debt	24.7	21.8	21.8	19.6	19.2	17.7	18.9	18.7	18.8
Total government debt including guarantees	60.1	57.9	62.6	65.1	64.7	64.4	…	…	…
Total government debt including IMF	60.7	58.9	63.3	64.2	63.7	63.6	64.3	66.9	64.2
Nominal GDP (market prices, billions of Pakistani rupees)	14,867	18,276	20,047	22,386	25,169	27,493	29,598	29,598	33,130

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

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

2/ Additional spending on security and internally-displaced people is recorded under transfers ("grants") instead of development expenditure as reported in the original FY2015/16 budget.

Table 6c. Pakistan: General Government Budget, 2013/14–2016/17

(In billions of Pakistani rupees)

	2013/14	2014/15	2015/16		2016/17				
			End-Year		Q1	Q2	Q3	Q4	End-Year
			Eleventh Review	Actual	Projection				
Revenue and grants	3,837	3,984	4,625	4,512	1,022	1,339	1,228	1,704	5,293
Revenue	3,631	3,937	4,556	4,447	1,013	1,328	1,217	1,690	5,248
Tax revenue	2,640	3,024	3,643	3,660	823	1,079	989	1,373	4,265
Federal	2,450	2,818	3,377	3,377	757	992	910	1,263	3,921
FBR revenue	2,272	2,594	3,104	3,112	699	916	840	1,166	3,621
Direct taxes	884	1,029	1,284	1,192	282	370	339	471	1,461
Federal excise duty	145	170	183	191	47	62	57	79	245
Sales tax/VAT	1,002	1,089	1,262	1,324	289	379	347	482	1,498
Customs duties	241	306	375	406	80	105	97	134	417
Petroleum surcharge	104	131	135	149	29	38	35	48	150
Gas surcharge and other	39	26	34	33	7	9	8	11	35
GIDC	32	57	100	80	21	28	26	35	110
Provincial	190	206	265	283	66	87	80	111	344
Nontax revenue	990	913	913	786	190	249	228	317	983
Federal	941	838	823	693	169	221	203	281	874
Provincial	49	76	90	93	21	28	25	35	110
Grants	206	47	69	66	9	11	10	15	45
Expenditure	5,058	5,426	5,848	5,796	1,254	1,644	1,508	2,092	6,498
Current expenditure	4,123	4,556	4,882	4,907	1,013	1,328	1,218	1,690	5,248
Federal	2,950	3,169	3,402	3,357	686	899	825	1,145	3,554
Interest	1,148	1,304	1,289	1,263	263	345	316	439	1,362
Domestic	1,073	1,208	1,170	1,151	237	311	285	396	1,231
Foreign	75	96	119	113	25	33	31	42	132
Other	1,802	1,866	2,012	2,093	423	555	509	706	2,192
Defense	623	698	781	758	166	218	200	277	860
Other	1,179	1,168	1,232	1,336	257	337	309	429	1,332
Of which: subsidies 1/	336	265	165	218	30	39	36	49	154
Of which: grants 2/	372	401	616	563	112	147	135	187	581
Provincial	1,173	1,387	1,480	1,550	327	429	393	545	1,694
Development expenditure and net lending	997	1,047	1,132	1,102	241	316	290	403	1,250
Public Sector Development Program	878	1,013	1,136	1,089	242	318	291	404	1,255
Federal	435	489	510	496	120	157	144	200	620
Provincial	443	524	530	592	123	161	147	204	635
Net lending	119	34	0	13	(1)	(1)	(1)	(2)	(5)
Statistical discrepancy ("+" = additional expenditure)	-62	-178	-74	-212	-	-	-	-	-
Overall Balance (excluding grants)	-1,427	-1,489	-1,292	-1,349	(241)	(316)	(290)	(403)	(1,250)
Overall Balance (including grants)	-1,221	-1,442	-1,223	-1,284	(233)	(305)	(280)	(388)	(1,205)
Financing	1,221	1,442	1,223	1,284	233	305	280	388	1,205
External	351	166	493	331	82	107	98	136	424
Of which: IMF	0	0	0	0	-	-	-	-	-
Domestic	870	1,276	730	953	151	198	181	252	782
Bank	322	910	511	780	106	138	127	176	547
Nonbank	548	366	219	173	45	59	54	75	234
Memorandum items:									
Primary balance (excluding grants)	-279	-185	-3	-86	22	28	26	36	112
Primary balance (including grants)	-73	-138	66	-21	30	40	36	51	157
Total security spending	623	698	781	758	166	218	200	277	860
Energy sector circular debt clearance	0	0	25	16	...	...	...	...	19
Total government debt	15,730	17,059	18,562	19,165	...	...	...	...	20,836
Domestic debt	10,902	12,188	12,956	13,619	...	...	...	...	14,621
External debt	4,828	4,871	5,606	5,546	...	...	...	...	6,215
Total government debt including IMF obligations	16,028	17,477	19,043	19,797	...	...	...	...	21,278
Nominal GDP (market prices)	25,169	27,493	29,598	29,598	...	...	...	...	33,130

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

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

2/ Additional spending on security and internally-displaced people is recorded under transfers ("grants") instead of development expenditure as reported in the original FY2015/16 budget.

Table 7. Pakistan: Monetary Survey, 2013/14–2016/17

	2013/14	2014/15	2015/16				2016/17			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
							Projections			
	(In billions of Pakistani rupees, unless otherwise indicated)									
Monetary survey										
Net foreign assets (NFA)	601	813	924	963	897	1,008	1,016	1,111	1,192	1,301
Net domestic assets (NDA)	9,367	10,469	10,478	10,799	11,063	11,817	11,925	12,168	12,226	13,088
Net claims on government, *of which: 1/*	6,027	6,958	7,115	7,108	7,394	7,820	7,771	7,909	8,036	8,212
Budget support, *of which:*	5,448	6,330	6,469	6,513	6,868	7,117	7,223	7,361	7,488	7,664
Banks	3,121	4,443	4,887	5,056	5,507	5,705	5,423	5,561	5,688	5,864
Commodity operations	492	564	570	523	464	637	548	548	548	548
Credit to nongovernment	4,153	4,456	4,447	4,752	4,792	5,013	5,018	5,400	5,432	5,594
Private sector 4/	3,798	4,021	3,995	4,317	4,345	4,469	4,474	4,856	4,888	5,050
Public sector enterprises	355	435	452	435	447	544	544	544	544	544
Privatization account	-3	-41	-41	-41	-41	-41	-41	-41	-41	-41
Other items, net	-809	-904	-1,044	-1,021	-1,082	-974	-824	-1,101	-1,202	-677
Broad money	9,968	11,282	11,402	11,762	11,960	12,825	12,941	13,279	13,419	14,389
Currency outside scheduled banks	2,178	2,555	2,970	2,880	3,013	3,334	3,365	3,453	3,489	3,669
Rupee deposits	7,191	8,130	7,838	8,277	8,354	8,904	8,981	9,235	9,339	10,127
Foreign currency deposits	599	598	593	605	593	587	595	592	591	593
State Bank of Pakistan (SBP)										
NFA	490	722	873	902	864	1,033	1,042	1,137	1,218	1,326
NDA	2,372	2,420	2,611	2,574	2,712	2,941	3,178	2,927	2,873	3,124
Net claims on government	2,395	1,919	1,611	1,481	1,384	1,430	1,700	1,700	1,700	1,700
Of which: budget support	2,328	1,887	1,582	1,457	1,361	1,412	1,800	1,800	1,800	1,800
Claims on nongovernment	-5	-6	-6	-6	-5	-5	-5	-5	-5	-5
Claims on scheduled banks	500	401	387	422	423	407	417	416	413	416
Privatization account	-3	-41	-41	-41	-41	-41	-41	-41	-41	-41
Other items, net	-515	146	661	718	951	1,148	1,107	857	805	1,054
Reserve money, *of which:*	2,861	3,142	3,484	3,476	3,576	3,974	4,220	4,064	4,091	4,450
Banks' reserves	531	413	335	419	383	392	416	401	403	439
Currency	2,317	2,715	3,135	3,043	3,177	3,563	3,804	3,663	3,687	4,012
	(Annual percentage change, unless otherwise indicated)									
Broad money	12.5	13.2	14.5	13.0	13.5	13.7	13.5	12.9	12.2	12.2
NFA, banking system (in percent of broad money) 2/	3.7	2.1	3.6	3.0	1.5	1.7	0.8	1.3	2.5	2.3
NDA, banking system (in percent of broad money) 2/	8.8	11.1	10.9	10.0	12.0	11.9	12.7	11.6	9.7	9.9
Budgetary support (in percent of broad money) 2/	3.7	8.8	8.8	8.3	9.0	7.0	6.6	7.2	5.2	4.3
Budgetary support	6.3	16.2	15.8	15.3	16.1	12.4	11.6	13.0	9.0	7.7
Private credit 4/	12.5	5.9	3.3	6.4	8.3	11.1	12.0	12.5	12.5	13.0
Currency	12.4	17.3	31.3	25.1	24.9	30.5	13.3	19.9	15.8	10.1
Reserve money	12.9	9.8	24.8	25.0	19.2	26.5	21.1	16.9	14.4	12.0
Memorandum items:										
Velocity	2.7	2.6	2.6	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Money multiplier	3.5	3.6	3.3	3.4	3.3	3.2	3.1	3.3	3.3	3.2
Currency to broad money ratio (percent)	21.8	22.6	26.1	24.5	25.2	26.0	26.0	26.0	26.0	25.5
Currency to deposit ratio (percent)	28.0	29.3	35.2	32.4	33.7	35.1	35.1	35.1	35.1	34.2
Foreign currency to deposit ratio (percent)	7.7	6.8	7.0	6.8	6.6	6.2	6.2	6.0	6.0	5.5
Reserves to deposit ratio (percent)	6.8	4.7	4.0	4.7	4.3	4.1	4.3	4.1	4.1	4.1
Budget bank financing (change from the beginning of the fiscal year; in Rs billions), *of which:*	324	882	139	183	538	787	893	1,031	1,158	1,334
By commercial banks	164	1,323	444	612	1,064	1,262	980	1,118	1,245	1,421
By SBP	160	-441	-304	-429	-526	-475	-87	-87	-87	-87
NFA of SBP (change from beginning of the year; in billions of U.S. dollars) 3/	3.6	2.1	1.3	1.5	1.2	2.8	-0.2	0.6	1.3	2.3
NFA of commercial banks (millions of U.S. dollars)	1,130	887	489	584	312	-243	-236	-234	-234	-232
NDA of commercial banks (billions of Pakistani rupees)	6,995	8,050	7,867	8,224	8,351	8,877	8,747	9,241	9,354	9,964

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.

4/ Items pertaining to Islamic Financing previously reported under "Other assets" have been reclassified as "Credit to private sector" beginning March 2016.

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

(December 2013–June 2016)

	Dec. 2013	Mar. 2014	Jun. 2014	Sep. 2014	Dec. 2014	Mar. 2015	Jun. 2/ 2015	Sep. 2/ 2015	Dec. 2/ 2015	Mar. 2/3/ 2016	Jun. 2/ 2016
Capital adequacy 1/											
Regulatory capital to risk-weighted assets	15.1	14.8	15.1	15.5	17.1	17.4	17.2	18.2	17.3	16.3	16.1
Tier I capital to risk-weighted assets	12.8	12.5	12.5	13.6	14.3	14.2	14.1	15.0	14.4	13.2	13.0
Capital to total assets	8.9	8.9	8.8	9.0	10.0	10.0	8.3	8.5	8.4	7.9	7.5
Asset composition and quality											
Nonperforming loans (NPLs) to gross loans	13.3	13.4	12.8	13.0	12.3	12.8	12.4	12.5	11.4	11.7	11.1
Provisions to NPLs	78.4	77.8	79.5	77.6	79.8	80.2	80.8	81.8	84.9	83.6	82.4
NPLs net of provisions to capital	13.0	14.0	12.5	13.6	10.1	9.8	10.9	10.0	7.7	8.9	9.7
Earnings and profitability											
Return on assets (after tax)	1.1	1.3	1.4	1.4	1.5	1.7	1.6	1.5	1.5	1.5	1.3
Return on equity (after tax)	12.4	14.1	15.4	15.9	16.1	17.0	15.9	15.7	15.6	16.3	14.4
Net interest income to gross income	70.3	69.9	70.5	71.4	71.3	68.4	67.5	69.1	70.4	70.0	70.6
Noninterest expenses to gross income	57.4	56.8	54.6	54.8	53.3	47.0	46.1	46.9	47.8	50.6	51.0
Liquidity											
Liquid assets to total assets	47.3	48.3	47.8	54.8	49.2	51.9	52.3	53.7	53.8	55.9	55.2
Liquid assets to total deposits	60.0	63.7	60.6	61.4	64.5	70.4	69.5	74.8	73.3	77.3	77.0
Loans/Deposits	48.6	49.2	47.7	48.2	48.2	46.9	45.7	46.7	46.6	46.3	47.0

Source: State Bank of Pakistan.

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

2/ As required by Basel requirements, the authorities used regulatory capital instead of balance sheet capital to calculate FSI figures.

3/ Changes in the accounting treatment in capital in one bank resulted in a downward revision in regulatory capital to risk-weighted assets and Tier 1 capital to risk weighted assets. This change is not expected to affect other banks.

Table 9. Pakistan: Indicators of Fund Credit, 2015–23
(In millions of SDR unless otherwise specified)

	Projections								
	2015	2016	2017	2018	2019	2020	2021	2022	2023
(Projected Level of Credit Outstanding based on Existing Drawings and Prospective Drawings)									
Total	3,600.0	4,393.0	4,393.0	4,243.0	3,823.0	3,163.0	2,400.8	1,698.7	966.5
Of which:									
ECF, SBA, and ENDA	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Extended Fund Facility	3,600.0	4,393.0	4,393.0	4,243.0	3,823.0	3,163.0	2,400.8	1,698.7	966.5
In percent of end-period gross official reserves	37.4	33.8	29.4	26.9	24.4	20.8	14.5	11.6	7.2
As a share of external debt	7.8	8.4	8.0	7.2	6.2	5.1	3.9	2.9	1.7
(Projected Debt Service to the Fund based on Existing and Prospective Drawings)									
Total	338.1	27.2	58.1	207.0	470.1	699.2	793.7	726.0	748.4
Of which:									
Principal	303.0	0.0	0.0	150.0	420.0	660.0	762.2	702.2	732.2
Interest and charges	35.1	27.2	58.1	57.0	50.1	39.2	31.5	23.9	16.2
SBA and ENDA Principal	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Extended Fund Facility Principal	0.0	0.0	0.0	150.0	420.0	660.0	762.2	702.2	732.2
In percent of end-period gross official reserves	3.5	0.2	0.4	1.3	3.0	4.6	4.8	5.0	5.6
As a share of total external debt service	7.0	0.6	1.0	3.3	5.9	7.1	7.8	7.8	9.2
Memorandum items									
Quota (millions of SDRs)	1,034	2,031	2,031	2,031	2,031	2,031	2,031	2,031	2,031
Gross official reserves (millions of U.S. dollars)	13,534	18,129	20,847	21,971	21,825	21,222	23,108	20,395	18,731
Total External Debt (millions of U.S. dollars)	65,103	72,978	76,925	81,876	85,346	85,843	84,795	80,674	80,480
Total External Debt Service (millions of U.S. dollars)	6,754	6,074	8,528	8,873	11,056	13,681	14,148	13,057	11,398

Source: IMF staff projections.

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

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
							Projections			
Key economic and market indicators										
Real GDP growth (factor cost, in percent)	3.6	3.8	3.7	4.1	4.0	4.7	5.0	5.2	5.5	5.5
CPI inflation (period average, in percent) 1/	13.7	11.0	7.4	8.6	4.5	2.9	5.2	5.0	5.0	5.0
Emerging market bond index (EMBI) secondary market spread (basis points, end of period)	857	1,136	703	501	...	...	...	...	...	...
Exchange rate PRs/US$ (end of period)	85.8	94.3	98.7	98.6	...	...	...	...	...	...
External sector										
Current account balance (percent of GDP)	0.1	-2.1	-1.1	-1.3	-1.0	-0.9	-1.5	-2.2	-2.2	-1.9
Net FDI inflows (percent of GDP)	0.7	0.3	0.5	0.6	0.3	0.4	0.8	1.0	1.2	1.6
Exports (percentage change of U.S. dollar value; GNFS)	25.0	-4.5	6.0	-3.6	-1.4	-8.3	3.7	3.6	8.2	10.7
Gross international reserves (GIR) in billions of U.S. dollars	14.8	10.8	6.0	9.1	13.5	18.1	20.8	22.0	21.8	21.2
GIR in percent of ST debt at remaining maturity (RM) 2/	306.6	209.5	75.4	106.1	177.1	233.6	185.3	178.2	151.8	115.6
GIR in percent of ST debt at RM and banks' foreign exchange (FX) deposits 2/	160.9	109.9	45.6	62.1	100.2	135.6	125.1	121.0	106.1	84.9
Total gross external debt (ED) in percent of GDP, *of which:*	31.1	29.2	26.3	26.7	24.0	25.7	25.1	24.9	24.2	22.7
ST external debt (original maturity, in percent of total ED)	1.9	2.5	2.1	4.1	5.1	6.2	5.1	4.3	5.1	4.9
ED of domestic private sector (in percent of total ED)	10.8	10.8	10.4	13.4	15.7	15.7	17.6	18.3	18.7	19.4
ED to foreign official sector (in percent of total ED)	89.2	89.2	89.6	86.6	84.3	84.3	82.4	81.7	81.3	80.6
Total gross external debt in percent of exports	213.2	220.2	193.2	215.1	217.3	265.8	270.0	277.5	267.2	242.9
Gross external financing requirement (in billions of U.S. dollars) 3/	2.3	6.7	5.3	6.5	6.2	6.3	10.8	13.0	15.3	16.7
Public sector 4/										
Overall balance (including grants)	-6.7	-8.6	-8.4	-4.9	-5.2	-4.3	-3.6	-2.9	-2.7	-2.5
Primary balance (including grants)	-2.9	-4.2	-3.9	-0.3	-0.5	-0.1	0.5	1.5	1.7	1.6
Debt-stabilizing primary balance 5/	-7.7	1.4	-1.3	-2.8	-0.2	0.0	-2.2	-1.5	-1.1	0.0
Gross PS financing requirement 6/	27.0	33.0	36.8	35.8	31.8	31.5	30.4	28.8	27.6	26.8
Public sector gross debt 7/	54.7	59.9	62.3	62.5	62.0	64.8	62.9	60.4	58.2	55.6
Public sector net debt 8/	51.7	55.9	58.6	57.1	57.0	58.5	56.6	54.1	51.9	49.2
Financial sector 9/										
Capital adequacy ratio (in percent)	15.1	15.4	15.5	15.1	17.2	...	...	...	...	...
Nonperforming loans (NPLs) in percent of total loans	15.7	14.5	14.8	12.8	12.4	...	...	...	...	...
Provisions in percent of NPLs	69.3	71.8	73.2	79.5	80.8	...	...	...	...	...
Return on assets (after tax, in percent)	1.5	1.4	1.1	1.4	1.6	...	...	...	...	...
Return on equity (after tax, in percent)	15.1	14.9	12.4	15.4	15.9	...	...	...	...	...
FX deposits held by residents (in percent of total deposits)	7.2	7.4	7.4	7.7	6.8	...	...	...	...	...
Government debt held by FS (percent of total FS assets)	44.6	55.2	64.3	60.5	61.7	...	...	...	...	...
Credit to private sector (percent change)	4.0	7.5	-0.6	12.5	5.9	...	...	...	...	...
Memorandum item:										
Nominal GDP (in billions of U.S. dollars)	213.6	224.4	231.2	244.4	271.0	284.2				

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 1/	Amount of Purchase: Millions of SDRs	Amount of Purchase: Percent of Quota 2/	Conditions
September 4, 2013	360	18	Approval of arrangement
December 2, 2013	360	18	First review and end-September 2013 performance/continuous criteria
March 2, 2014	360	18	Second review and end-December 2013 performance /continuous criteria
June 2, 2014	360	18	Third review and end-March 2014 performance /continuous criteria
December 2, 2014	720	35	Fourth and Fifth reviews and end-June and end-September 2014 performance /continuous criteria
March 2, 2015	360	18	Sixth review and end-December 2014 performance /continuous criteria
June 2, 2015	360	18	Seventh review and end-March 2015 performance /continuous criteria
September 2, 2015	360	18	Eighth review and end-June 2015 performance /continuous criteria
December 2, 2015	360	18	Ninth review and end-September 2015 performance/continuous criteria
March 2, 2016	360	18	Tenth review and end-December 2015 performance /continuous criteria
June 2, 2016	360	18	Eleventh review and end-March 2016 performance /continuous criteria
August 1, 2016	73	4	Twelfth review and end-June 2016 performance /continuous criteria
Total	4393	216	

Source: IMF staff estimates.

1/ Date in which resources become available.

2/ Based on Pakistan's new quota of SDR 2,031 million.

Appendix I. Letter of Intent

September 9, 2016

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

Dear Ms. Lagarde,

1. **Over the past three years, we have been able to significantly reduce economic vulnerabilities and advance key growth-supporting structural reforms under our home-grown economic reform program supported by the IMF**. We have rebuilt our external buffers, contained inflation, and reduced fiscal imbalances while strengthening social safety nets to protect the most vulnerable. In parallel, we have strengthened our monetary policy framework, improved the resilience of the financial sector, strengthened our public financial management and tax administration, reduced tax concessions and exemptions and untargeted energy subsidies, significantly reduced the accumulation of power sector arrears, simplified our trade regime and began implementing our strategy to improve the business climate. Despite some delays and slippages, we also advanced in our work toward restructuring and divestment of ailing public sector enterprises (PSEs).

2. **Our performance on the twelfth and last review under the three-year EFF-supported program has been satisfactory**:

Quantitative performance criteria and indicative targets (Table 1). We met most end-June 2016 quantitative performance criteria (PCs) but the PCs on the budget deficit and Net Domestic Assets (NDA) of the State Bank of Pakistan (SBP) were missed by small margins. We met the indicative targets at end-June 2016 on tax revenue, social spending under the Benazir Income Support Program (BISP), and the accumulation of power sector arrears. We have taken adequate adjustments in our budgetary spending and are stepping up coordination with the provinces to ensure achieving our fiscal deficit target for FY2016/17 (¶¶7 and 11). Moreover, we have adopted measures to ensure a pace of monetary expansion within safe limits (¶15). We request waivers of nonobservance for the two missed performance criteria on this basis.

Structural benchmarks (Table 2). We met most structural benchmarks for the twelfth review: we have enacted the Deposit Protection Corporation Act, solicited expressions of interests for the disinvestment of the power generation company KAPCO, and updated the power sector arrears reduction plan. However, the notification of multi-year tariffs for three power distribution companies has been further delayed due to the continued dispute with the regulator over FY2015/16 determined tariffs (¶23).

3. We will continue to strengthen macroeconomic stability and advance our structural reform agenda going forward. With the overall objective to consolidate macroeconomic stability gains achieved in the last three years, we aim to achieve higher, sustainable, and more inclusive growth, which is needed to absorb new entrants in the labor market and improve living standards. We will continue to pursue gradual fiscal consolidation to ensure medium-term debt sustainability, our monetary and exchange rate policies will aim at further bolstering external buffers and preserving low inflation, and we will continue to enhance financial sector stability. In parallel, we will advance our growth-supporting structural reform agenda. We will continue to widen the tax net to generate resources to step up priority spending in areas such as infrastructure, health, and education. In addition, we will further strengthen the performance of the power sector and resolutely address the outstanding stock of arrears. We intend to restructure and attract private sector participation in PSEs to ensure their viability, reduce fiscal risks and improve efficiency. We will continue implementing our strategy to strengthen the business climate to attract private investment, and we will further strengthen our institutional set-up, including by reinforcing the autonomy of the central bank.

Macroeconomic Near-term Outlook

4. Pakistan's near-term macroeconomic performance is expected to remain robust. Real economic growth increased to 4.7 percent in FY2015/16 and is expected to further accelerate to 5.7 percent in FY2016/17, supported by buoyant construction activity, strengthened private sector credit growth, and an investment upturn related to the China Pakistan Economic Corridor (CPEC). However, in the context of the program, we maintain a growth projection of 5 percent. We expect end-year inflation to remain contained at 5.3 percent in FY2016/17, well-anchored by prudent monetary policy. The current account deficit, which reached 0.9 percent of GDP in FY2015/16, is expected to increase to 1.5 percent of GDP, reflecting rising growth, higher oil prices, and CPEC-related imports. Having reached US$18.1 billion at end-June 2016, we expect foreign exchange reserves of the SBP to continue increasing to $20.8 billion in FY2016/17 (covering 4.5 months of prospective imports), also reflecting our further efforts to bolster external buffers.

Economic Policies

A. Fiscal Policy

5. Over the course of the program, our fiscal consolidation efforts have supported macroeconomic stabilization and public debt sustainability. The FY2015/16 deficit target of 4.4 percent of GDP (including an adjustor of 0.3 percent of GDP for exceptional spending on security and resettlement of internally-displaced persons) was missed by PRs 57 billion (or 0.2 percent of GDP) as the surplus from provincial governments was lower than we expected. The federal government partly compensated for this by containing federal spending despite a shortfall in federal nontax revenue collection. More broadly, over the last three years, we have achieved significant fiscal adjustment (3.9 percent of GDP or 4.2 percent of GDP after excluding exceptional expenditures of 0.3 percent of GDP). This has helped strengthen our public finances and bolster our macroeconomic resilience.

6. **We plan to continue a steady pace of fiscal consolidation to further strengthen public finances and improve debt sustainability**. As we approach the end of the program, our fiscal policy strategy continues to aim to bring the budget deficit to a sustainable level through revenue mobilization and expenditure rationalization. This will allow us to rebuild fiscal buffers against shocks, put the debt-to-GDP ratio on a downward path, and increase growth-enhancing and poverty-alleviating expenditures.

7. **We continue to target a deficit of 3.8 percent of GDP (excluding foreign grants) in FY2016/17**. This reflects a baseline deficit of 3½ percent of GDP and extraordinary spending of 0.3 percent of GDP on security and resettlement of internally-displaced persons. However, against the backdrop of slower growth in the collection of the Gas Infrastructure Development Cess (GIDC) and federal nontax revenue, we will manage budgetary spending very prudently and reduce noncritical current and capital expenditures as necessary to achieve our fiscal deficit target (Table 3). In case of any further deviation, we would take additional measures in order to achieve our revenue and budget deficit targets.

8. **Revenue mobilization has been—and will continue to be—the most important pillar of our fiscal policy strategy**. Over the last three years, our tax revenue-to-GDP ratio increased by 2.4 percent of GDP to 12.4 percent in FY2015/16--the highest level since 1999. The elimination of tax concessions and exemptions made a significant contribution, and, after we significantly restricted the legal authorization to grant tax concessions and exemptions through Statutory Regulatory Orders (SROs), we will maintain a rule-based and transparent framework for tax expenditures. Through a variety of efforts, including the introduction of differential tax rates for filers and nonfilers of income tax and sending of more than 300,000 first notices to nonfilers, the number of tax filers increased by 30 percent over the last three years to more than 1 million. Recently, we also introduced rationalized valuation for real estate taxes. Despite the progress, the full potential of the tax system has still to be realized and requires to generate additional resources to step up critical physical infrastructure, human capital, and social expenditures. To this end, we will refrain from granting concessions, exemptions and any form of amnesty, enhance tax policy measures, and accelerate administrative reforms aimed at broadening the tax base and modernizing our tax system. Over the coming years, we will aim at:

- **Tax policy measures**. (i) Broadening the tax base; (ii) modernizing the General Sales Tax (GST) regime on goods and services with few exceptions in close coordination with the provinces; and (iii) establishing a tax policy research and analysis unit outside the FBR.

- **Tax administration reforms**. (i) Improving FBR's access to third-party information; (ii) ensuring data matching between domestic taxes and customs to identify noncompliant taxpayers and minimize under-declarations; (iii) accelerating the implementation of risk-based auditing with a focus on high net worth individuals and large companies; (iv) building a centralized fiscal cadastre (to facilitate market value-based real estate tax); (v) putting in place additional governance and anti-corruption measures at the FBR; (vi) seeking parliamentary approval of the legislation against "benami" transactions by December 2016; and (vii) reducing the outstanding stock of tax refund claims to no more than a three-month flow.

9. We will continue to improve the composition of expenditures to support growth. As part of our multi-year fiscal consolidation strategy, we reduced poorly targeted energy subsidies by about 1 percentage point to 0.6 percent of GDP in FY2015/16, while expanding cash transfers to low-income households by 0.12 percentage points to 0.4 percent of GDP and increasing capital spending by 0.5 percent of GDP. Going forward, as indicated by the FY2016/17 budget, we will lower energy subsidies to 0.4 percent of GDP and continue to rationalize current expenditures across all layers of the general government, while continuing to increase targeted social assistance in real terms and further improving the share of development spending.

10. We have strengthened our public financial management framework to provide better policy guidance and anchor debt sustainability. We have already amended the Fiscal Responsibility and Debt Limitation (FRDL) Act with a limit on the federal government budget deficit and a gradual reduction in the general government debt ratio. We have also submitted to parliament a new public-private partnership (PPP) law to support investments and provide for transparency and better management of associated fiscal risks. The new PPP law makes PPPs a part of the overall budget process and medium-term planning exercise and gives the Ministry of Finance an explicit role as gatekeeper in all stages of PPP projects. While the PPP law provides the overall legal framework to manage fiscal risks originating from PPPs, we will provide detailed guidance through rules and regulations. Going forward, we will continue to enhance our medium-term budget framework and further improve the fiscal accounts across all levels of government.

11. We will strengthen intergovernmental fiscal policy coordination to ensure the sustainability of public finances. Given the extent of devolution in revenue and expenditure assignments, strengthening fiscal policy coordination across all layers of the government is needed. To this end, the newly established Fiscal Coordination Committee (FCC), comprising the provincial and federal finance secretaries, will continue to hold quarterly meetings to synchronize policy guidance and budget implementation. Furthermore, we will seek an agreement to balance devolution of revenue and expenditure responsibilities in a way that allows for internalizing the objectives of macroeconomic stability and fiscal sustainability across all layers of the general government. To this end, we are encouraging provincial governments to enhance their own revenue mobilization by bringing underdeveloped tax bases such as agriculture, services, and property, more effectively into the tax net and improve taxpayer compliance with a particular focus on identifying misdeclarations in agricultural income.

12. We will continue to strengthen debt management. We created the Debt Policy Coordination Office (DPCO) and integrated it in the Ministry of Finance as a middle office. We adopted a medium-term debt strategy and began monitoring it through preparation of quarterly risk reports. We lengthened the average maturity of the domestic debt portfolio and are continuing to diversify our domestic and international financing sources to reduce rollover risks. Looking ahead, we will strive to further lengthen the maturity of our debt profile and increase staffing capacity of the DPCO.

13. We will continue supporting the most vulnerable through BISP and strengthen the targeting and the efficiency of the program. Over the course of our program, we have expanded the coverage of unconditional cash transfers (UCTs) from 3.78 million beneficiaries in June 2013 to 5.36 million at end August 2016. Similarly, we have increased the amount of cash transfers from PRs 3,000 (per beneficiary, per quarter) in June 2013 to PRs 4,700 in FY2015/16 and we will further increase quarterly stipends in line with inflation in FY2016/17, through additional financing mobilized from development partners. We have increased the annual budget allocation to BISP from PRs 75 billion in FY2013/14 to PRs 115 in FY2016/17. We will continue to expand UCT coverage to reach 5.45 million beneficiaries by end-March 2017. In addition, we have strengthened service delivery, reduced costs, and improved the program's efficiency. We have also rolled out education-conditional cash transfers in 32 districts and expanded coverage to reach 1.3 million children at end-June 2016. We are piloting a biometrics-based transaction system to reduce the possibility for fraud and are updating the BISP beneficiaries' database (National Socio Economic Registry) by mid-2018 to strengthen the program's targeting. We will also extend coverage of the CCT to 1.6 million children in FY 2016/17.

B. Monetary and Exchange Rate Policies

14. We have rebuilt our external buffers, contained inflation, and strengthened SBP's autonomy. On the back of our supportive macroeconomic policies, an improved current account helped by declining oil prices and strong remittances, SBP's spot purchases in the foreign exchange market, and sustained international official disbursements, we increased our gross international reserves from US$6 billion in FY2012/13 to US$18.1 billion at end-June 2016, covering more than four months of prospective imports. Furthermore, inflation was reduced to less than 3 percent (on average) in FY2015/16 from more than 7 percent in FY 2012/13, reflecting our prudent monetary policy stance and reduced government's budgetary borrowing from the SBP, and helped also by lower food and fuel prices. We amended the SBP law and put in place a number of administrative measures to increase the SBP's autonomy, established an independent monetary policy committee, and strengthened the interest rate corridor and the internal operations of the SBP. In this respect, we have already delegated the SBP Board the authority to appropriate and distribute profits, and prohibited the distribution of unrealized gains.

15. Our monetary and exchange rate policy will continue to aim at building external buffers and preserving price stability. We will continue to take advantage of the oil windfall and build reserves while supporting exchange rate flexibility. The increased buffers would help mitigate potential external risks. We will also continue to improve our trade competitiveness, eroded by real effective exchange rate appreciation over the last three years. We will continue to maintain a prudent monetary policy stance to preserve low inflation. To this end, following the minor overrun in NDA relative to our end-June PC, we have brought the stock of NDA to below PRs 3100 billion by end-August 2016 (subject to program adjustors; prior action). We will remain vigilant to any signs of additional inflationary pressures in coming months and will continue to maintain positive real interest rates by setting the policy rate on a forward-looking basis. Furthermore, we will move forward in implementing certain remaining recommendations of the 2013 Safeguards Assessment to further strengthen the SBP's autonomy. In addition, the SBP will remain autonomous in its decisions regarding profit appropriation, which was delegated to the SBP Board in March 2016.

16. We aim to implement an inflation targeting framework over the medium-term. To this end, we will strengthen the SBP's analytical capabilities in support of a flexible inflation targeting framework, improve transparency, and disseminate information about inflation expectations and forecasts.

C. Financial Sector

17. In the last three years, we strengthened the resilience and stability of the financial sector and enabled the recovery of credit to the private sector. The performance of the banking system has steadily improved as reflected in higher profitability, robust capital adequacy, strengthening liquidity indicators, declining ratios-and better provisioning-of nonperforming loans (NPLs), and a revival of credit to the private sector. We enacted the Deposit Protection Corporation Act to establish a deposit protection scheme to enhance the stability and soundness of the banking system (end-August 2016 SB). Furthermore, we enacted the Corporate Restructuring Companies (CRC) Act and amended the Financial Institutions (Recovery of Finances) Ordinance to improve recovery and resolution of NPLs and support the provision of credit to the economy. We have also strengthened our regulatory and supervisory framework, among others through the phased implementation of Basel III capital and liquidity requirements.

18. We will continue to protect the stability of the banking sector, further reinforce the regulatory and supervisory framework, and aim to deepen the financial industry. We will implement a broad set of financial reforms elaborated in our strategic plan "SBP Vision 2020" aiming to improve the banking sector's resilience, enhance supervisory vigilance and improve the risk management framework. We will ensure that three remaining undercapitalized banks are brought into regulatory compliance. To this end, one bank has already injected part of the required capital and is in the process of raising additional equity through a rights issue by end-September. Another publicly owned bank is in the divestment process, expected to be completed by end-2016, while one small bank is seeking to merge with a larger peer, also expected to be completed by end-September 2016. We will also continue to strengthen the legal and regulatory framework for the financial sector and improve macro-prudential measures. In this context we will strengthen the supervision of systemically important banks and develop consolidated banking supervision. Furthermore, we will continue with the phased implementation of Basel III regulatory norms, continue our efforts to resolve NPLs, and work towards early enactment of the Corporate Rehabilitation Act. We will make the new deposit insurance operational by end-December 2016. Furthermore, we will operate the Pakistan Development Fund to finance infrastructure projects on a commercial basis and mobilize the participation of international development partners for the purpose of gaining technical expertise, financing, and ensuring good governance.

19. We will continue enhancing the effectiveness of the anti-money laundering and combating the financing of terrorism (AML/CFT) framework. After amending the AML Act to subject the proceeds of serious tax crimes to AML legislation, we will work on implementation measures that will bolster the reporting of suspicious transactions related to tax evasion by financial and nonfinancial institutions, and enhance the proper use of financial intelligence and sharing of information and cooperation between the Financial Monitoring Unit and the FBR to address tax evasion while improving the enforcement of revenue collection. We will also continue strengthening the effectiveness of the AML/CFT framework in line with international standards to prepare for the upcoming mutual evaluation that will be conducted by the Asia Pacific Group for money laundering in 2018, including by tackling the proceeds of corruption and strengthening the effective implementation of the relevant United Nations Security Council Resolutions related to terrorism and terrorist financing.

D. Reforming Public Sector Enterprises

20. We have made progress in the implementation of our reform agenda to restructure and attract private sector participation in public sector enterprises (PSEs). We resumed our divestment program after a significant gap and raised PRs 173 billion from our divestments, including over US$ 1.1 billion from foreign investors. Transactions included the sale of minority stakes in United Bank Limited (UBL), Allied Bank Limited (ABL), Habib Bank Limited (HBL) and Pakistan Petroleum Limited (PPL), and the strategic sale of National Power Construction Co. (NPCC). We solicited expressions of interest (EOIs) for the disinvestment of the government's residual stake in Kot Addu Power Company (KAPCO), a major power generation company (July 15, 2016 SB). Alongside, we have completed a significant amount of preparatory work toward restructuring and seeking strategic private sector participation for a number of PSEs. However, owing to labor tensions and political opposition, we revised our strategy for PSEs in early 2016 and amended the timeline and mode of the planned divestment transactions, including for PIA, PSM, and DISCOs. We are implementing a comprehensive restructuring plan for Pakistan Railways and have already significantly improved the company's revenues by improving freight services, rationalizing tariffs, and strengthening expenditure controls and governance. We solicited EOIs for strategic private sector participation in SME Bank. Furthermore, the bill to corporatize State Life Insurance Corporation (SLIC) has been passed by the National Assembly.

21. We express our resolve to restructure and attract private sector participation in PSEs in order to reduce fiscal costs, ensure their medium-term financial viability, and improve efficiency.

- **Pakistan International Airlines** (PIA). While the government will maintain a majority of shares and management control of PIA, we intend to attract private sector participation. To this end, we are in the process of separating PIA's core and noncore activities and will approve the transaction structure for offering a minority stake to a strategic partner and/or the general public by end-December 2016 and complete the bidding process by August 2017. We will continue to work with PIA management to further contain financial losses by: (i) increasing performance by route rationalization and fleet modernization and expansion, (ii) reducing financial and operational costs, and (iii) providing better services to gain customers' confidence.

- **Pakistan Steel Mills**. In the absence of an agreement with the provincial government of Sindh regarding the transfer of PSM's ownership, we have resumed in July 2016 the process to attract strategic private sector participation. To this end, we will finalize the transaction structure by September 2016, aiming to conclude the bidding process by end-June 2017. In parallel, we will continue to limit PSM's financial losses.

- **Pakistan Railways**. We will continue to implement our restructuring plan, including further improving freight and passenger services, increasing and diversifying revenues by actively participating in new ventures, strengthening the internal organization, and improving the company's financial accounting practices to gradually converge toward International Financial Reporting Standards (IFRS).

- **Energy sector**. We will move forward with the divestment in KAPCO and finalize the transaction by March 2017. Furthermore, we will conduct an IPO in the capital market for FESCO by February 2017, to be followed by IPOs for IESCO and LESCO by the end of FY 2016/17. We will utilize the IPOs' proceeds to reduce the stock of outstanding circular debt in the power sector. In parallel, we will continue to improve DISCOs' performance and reduce the system financial losses. We will continue to divest our stakes in the DISCOs in the medium term.

- **Other companies**. We will finalize the transaction of SME Bank by end-December 2016, the divestment of government's shares in Mari Petroleum Limited (MPCL) to existing shareholders by October 2016 and the IPO for SLIC by end-March 2017.

E. Energy Sector Reforms

22. **Over the last three years, we have advanced in tackling key structural weaknesses in the power sector**. We reduced unscheduled electricity outages, increased electricity supply by adding new generation capacity and rehabilitating existing generation plants, improved demand management, and strengthened the regulatory framework and governance. We reduced budgetary subsidies and significantly contained the accumulation of new payable arrears in the power sector by (i) improving DISCOs' performance, (ii) rationalizing tariffs and introducing surcharges to bring prices closer to cost recovery (while maintaining a uniform tariff across the country), and (iii) reducing delays in tariff determination. On the back of a net reduction in payables in the fourth quarter, the stock of circular debt declined to PRs 321 billion at end-June 2016. The stock of debt held in PHCL was maintained at PRs 335 billion. In order to improve DISCOs' performance, we signed performance contracts, set quarterly performance targets, improved monitoring and enforcement, strengthened legislation to pursue electricity theft, upgraded the electricity transmission and distribution network, improved revenue-based load management and the provision of incentives to collectors. As a result, we reduced DISCOs' distribution losses to 17.9 percent in FY 2015/16 from 18.9 percent in FY 2012/13 and increased collection rates to 92.6 percent in FY 2015/16, from 87.2 percent in FY 2012/13.

23. **We will move further ahead with our reform efforts to ensure the soundness of the power sector which is key to support higher medium-term growth**. We intend to further contain the accumulation of new arrears in the power sector and gradually reduce the outstanding stock. To this end, we updated our circular debt reduction plan in consultation with our development partners to reflect the changes in the divestment strategy for DISCOs (July 15, 2016 SB). In line with this plan, we will continue to improve the performance of DISCOs by further reducing losses and increasing recoveries, reduce the system financial losses, use the proceeds from DISCOs' IPOs and successive divestment to reduce the stock of outstanding circular debt, and will, by September 2016, resolve outstanding issues with Azad Jammu and Kashmir (AJK). Furthermore, after several DISCOs entered in litigation against NEPRA over the determination of FY 2015/16 tariffs, we will continue our dialogue with NEPRA to revise regulatory benchmarking for tariff determination in relation to recoveries and losses, while preserving the integrity of the regulatory framework. We will notify the delayed FY 2015/16 tariffs at the earliest, which will include notification of the multi-year tariffs for FESCO, IESCO and LESCO (missed July 15, 2016 SB). This will be necessary for attracting private sector participation and moving forward with the gradual setting up of a multi-year framework for the remaining DISCOs. Following the notification, we will ensure the resumption of the timely and regular tariff notification process. Finally, we will more than double our electricity generation capacity in the medium term, including through CPEC projects. In this regard, we will ensure to maintain a regulatory framework allowing for cost recovery, strong governance and monitoring of CPEC and other generation projects, and manage associated risks.

24. **We have advanced in the implementation of our comprehensive gas sector reform**. In order to reduce gas shortages, we implemented a strategy to increase gas supply through gas imports and encouraging domestic production which led to 500 MMCFD (or 13 percent) increase. We started importing Liquefied Natural Gas (LNG) in March 2015 and are in the process of launching LNG terminals and expanding the transportation network. We are passing through the full cost of LNG imports to end-consumers. We improved incentives for local gas production by implementing the Petroleum Policy 2012 and raising producer prices by 50 percent (on average), and we awarded new exploration licenses and converted existing ones. Furthermore, we rationalized the end-user gas price to bring it closer to cost recovery and better guide demand. We started tackling gas system losses (unaccounted-for gas) by formulating and implementing gas loss reduction plans in the two gas utility companies and enacting the Gas (Theft Control and Recovery) Act to better pursue gas theft offenses. We also conducted a comprehensive review of the rules for third party access to the gas network and strengthened governance by publishing periodic monitoring and evaluation reports on performance of the oil and gas sector. We completed a study to examine options for unbundling gas companies and opening up the gas market.

25. **We are resolved to move further ahead to address remaining challenges in this sector**. We will resume our practice of regular semi-annual gas tariff notification to ensure cost-recovery, avoid the build-up of losses for gas companies, and strengthen the regulatory framework. To this end, we will complete the FY 2016/17 tariff determination by early October 2016 to be followed by notification of the revised tariff, and continue to fully pass through the price of imported LNG to consumers. Furthermore, we will continue to increase LNG imports and required transport

infrastructure. We will ensure appropriate incentives to increase domestic production and revise the incentives in nonconventional gas policies. We will reduce system gas losses through network investment measures, managerial, technical and administrative improvements. We will also amend the rules for third party access to the gas transmission system by December 2016 to increase competition. Furthermore, we will unbundle the gas sector within FY 2017–18.

F. Improving the Business Climate and Liberalizing Trade

26. We have made progress towards improving the business climate. After implementing several measures under our 2014 Action Plan, we began implementing in early 2016 a new and comprehensive country-wide reform strategy to improve the business climate with time-bound measures at the federal and provincial level. To this end, we facilitated starting a new business, paying taxes and getting credit, strengthened the regulatory framework and simplified trading across borders. Notably, we introduced one-stop-shops and rationalized the fee structure for opening new businesses. We reduced the number of procedures for paying taxes, introduced Alternative Dispute Resolution (ADR) mechanisms to facilitate the resolution of commercial disputes, and adopted a new National Financial Inclusion Strategy. We also improved credit information systems and the collateral framework, enacted the amendments to the Credit Bureau Act 2015, and issued regulations for credit bureaus. We launched a web-based portal to simplify trade documentation.

27. We will further accelerate the implementation of our new business climate reform strategy to foster private sector investment and higher and more inclusive growth. We will further facilitate the creation of new businesses by completing the automation of the OSSs, and reducing start-up procedures for small-sized companies. Furthermore, we will further improve the electronic payment system to ease paying taxes. We will license private credit bureaus under the new Credit Bureau Act and develop regulations to strengthen the collateral framework. We will continue to encourage provinces to expedite the execution and registration of deeds, digitize maps, and provide online access to land records to facilitate property registration. We will further expand the availability of ADR mechanisms, increase case management systems in district courts, and establish specialized commercial courts. Finally, we will further simplify procedures for trade documentation.

28. We have simplified the import tariff structure and strengthened trade relations, and we will continue to maintain an open trade regime to support economic growth. We have gradually reduced import tariff slabs from seven to four and phased-out trade-related SROs. We took advantage of the three-year Generalized System of Preferences Plus benefits with the European Union from January 2014 and we will start negotiations for its extension.

G. Conclusions

29. Based on our successful program performance and remedial actions, we propose completion of the twelfth and last review under the Extended Arrangement. We express our appreciation to the Fund for their partnership over the last three years in support of our reform agenda for the purpose of turning around the macroeconomic instability, which prevailed in Pakistan in 2013 and to achieve macroeconomic stability. Having concluded the EFF program, we will pursue our consultation and policy dialogue. We are pleased to share our resolve in following prudent economic policies to preserve and consolidate hard-earned macroeconomic stability gains and continue advancing growth-supporting structural reforms. We authorize the International Monetary Fund to publish this Letter of Intent and its attachments, and the related staff report.

/s/
Senator Mohammad Ishaq Dar
Minister of Finance
Pakistan

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

Table 1. Pakistan: Quantitative Performance Criteria and Indicative Targets for FY 2014/15 and FY 2015/16

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

	FY2014/15	FY2015/16					
	end-June	end-September	end-December	end-March	end-June		
					Program		
					Twelfth Review		
					Target	Adj. Target	Actual
Performance Criteria							
Floor on net international reserves of the SBP (millions of U.S. dollars) 4/	5,354	6,955	6,882	6,172	11,050	6,310	7,560
Ceiling on net domestic assets of the SBP (stock, billions of Pakistani rupees)	2,442	2,661	2,633	2,791	2,731	3,023	3,029
Ceiling on overall budget deficit (cumulative, excluding grants, billions of Pakistani rupees) 2/	1,489	329	541	1,009	1,292	1,292	1,349
Ceiling on SBP's stock of net foreign currency swaps/forward position (millions of U.S. dollars)	1,700	1,385	1,650	1,885	2,000	2,000	1,985
Ceiling on net government budgetary borrowing from the SBP (stock, billions of Pakistani rupees) 1/, 3	1,887	1,589	1,457	1,361	1,800	1,800	1,412
Continuous Performance Criterion							
Accumulation of external public payment arrears by the general government (continuous)	0	0	0	0	0	0	0
Indicative Targets							
Cumulative floor on Targeted Cash Transfers Spending (BISP) (billions of Pakistani rupees)	94	24	48	75	95	95	101
Floor on net tax revenues collected by the FBR (cumulative, billions of Pakistani rupees)	2,588	600	1,385	2,103	3,104	3,104	3,112
Ceiling on power sector payment arrears (flow, billions of Pakistani rupees)	57	13	0	4.9	18	18	(10)

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.
4/ Adjustors are presented on a cumulative basis since the beginning of the program (September, 2013).

Table 2. Pakistan: Structural Benchmarks, Twelfth and Last Review 2016

Item	Measure	Time Frame (by End of Period)	Status	Macroeconomic rationale
Prior Actions				
1	Bring the stock of NDA of the SBP to or below PRs 3,100 billion by end-August 2016.	end-August 2016	Met	Conduct prudent monetary policy
Structural Benchmarks				
Financial sector				
2	Enact the Deposit Protection Corporation Act, in line with Fund staff advice.	end-August 2016	Met	Enhance the resilience of the financial sector.
Structural Policies				
3	Notify multi-year tariffs for FESCO, IESCO and LESCO.	July 15, 2016	Not Met	Prepare for DISCO privatization.
4	Update the plan to further limit the accumulation of new payables and gradually eliminate the outstanding stock of payables arrears in the power sector.	July 15, 2016	Met	Strengthen the financial perfomance of the power sector.
5	Solicit expressions of interest for the divestment of Kot Addu Power Company (KAPCO).	July 15, 2016	Met	Strenghten private sector participation in the energy sector.

Table 3. Pakistan: General Government Budget, 2008/09–2016/17
(In billions of Pakistani rupees)

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16		2016/17
								Eleventh Review	Actual	Projection
Revenue and grants	1,878	2,130	2,306	2,611	3,011	3,837	3,984	4,625	4,512	5,293
Revenue	1,851	2,079	2,261	2,567	2,982	3,631	3,937	4,556	4,447	5,248
Tax revenue	1,331	1,500	1,738	2,076	2,231	2,640	3,024	3,643	3,660	4,265
Federal	1,285	1,445	1,673	1,969	2,081	2,450	2,818	3,377	3,377	3,921
FBR revenue	1,157	1,329	1,558	1,881	1,936	2,272	2,594	3,104	3,112	3,621
Direct taxes	440	529	602	732	736	884	1,029	1,284	1,192	1,461
Federal excise duty	116	121	137	122	119	145	170	183	191	245
Sales tax/VAT	452	517	633	809	841	1,002	1,089	1,262	1,324	1,498
Customs duties	148	162	185	218	240	241	306	375	406	417
Petroleum surcharge	112	89	83	60	110	104	131	135	149	150
Gas surcharge and other	16	28	32	27	35	43	35	38	36	40
GIDC	0.0	0.0	0.0	0.0	0.0	32	57	100	80	110
Provincial	46	55	65	107	151	190	206	265	283	344
Nontax revenue	520	579	523	491	751	990	913	913	786	983
Federal	436	511	461	443	680	941	838	823	693	874
Provincial	84	68	62	48	71	49	76	90	93	110
Grants	27	50	46	45	29	206	47	69	66	45
Expenditure	2,544	3,024	3,536	4,341	4,885	5,058	5,426	5,848	5,796	6,498
Current expenditure	2,093	2,481	3,012	3,579	3,757	4,123	4,556	4,882	4,907	5,248
Federal	1,547	1,853	2,227	2,611	2,647	2,950	3,169	3,402	3,357	3,554
Interest	638	642	698	889	991	1,148	1,304	1,289	1,263	1,362
Domestic	559	578	630	821	920	1,073	1,208	1,170	1,151	1,231
Foreign	79	64	68	68	71	75	96	119	113	132
Other	909	1,211	1,529	1,722	1,656	1,802	1,866	2,113	2,093	2,192
Defense	330	375	450	507	541	623	698	781	758	860
Other	579	836	1,078	1,215	1,116	1,179	1,168	1,332	1,336	1,332
Of which: subsidies 1/	244	227	493	556	368	336	265	165	218	154
Of which: grants 2/	136	359	259	291	305	372	401	616	563	581
Provincial	546	627	786	968	1,110	1,173	1,387	1,480	1,550	1,694
Development expenditure and net lending	417	571	477	696	1,112	997	1,047	1,040	1,102	1,250
Public Sector Development Program	398	518	465	675	721	878	1,013	1,040	1,089	1,255
Federal	196	260	216	299	348	435	489	510	496	620
Provincial	202	258	249	376	373	443	524	530	592	635
Net lending	20	53	12	21	391	119	34	0	13	-5
Statistical discrepancy ("+" = additional expenditure)	34	-28	46	67	16	-62	-178	-74	-212	0
Overall Balance (excluding grants)	-693	-944	-1,276	-1,775	-1,903	-1,427	-1,489	-1,292	-1,349	-1,250
Overall Balance (including grants)	-666	-894	-1,230	-1,730	-1,873	-1,221	-1,442	-1,223	-1,284	-1,205
Financing	666	894	1,230	1,730	1873	1,221	1,442	1,223	1,284	1,205
External	86	158	144	60	38	351	166	493	331	424
Of which: privatization receipts	1	0	0	0	0	1	2	0	0	0
Of which: IMF	0	0	0	0	0	0	0	0	0	0
Domestic	580	736	1,086	1,670	1836	870	1,276	730	953	782
Bank	353	305	614	1,140	1457	322	910	511	780	547
Nonbank	227	431	471	529	378	548	366	219	173	234
Memorandum items:										
Primary balance (excluding grants)	-56	-302	-577	-886	-912	-279	-185	-3	-86	112
Primary balance (including grants)	-28	-252	-532	-841	-882	-73	-138	66	-21	157
Total security spending	330	375	450	507	541	623	698	781	758	860
Energy sector circular debt clearance	0	0	0	391	322	0	0	25	16	19
Total government debt	7,313	8,331	10,005	12,008	13,948	15,730	17,059	18,562	19,165	20,836
Domestic debt	3,860	4,654	6,017	7,638	9,571	10,902	12,188	12,956	13,619	14,621
External debt	3,453	3,677	3,988	4,370	4,376	4,828	4,871	5,606	5,546	6,215
Total government debt including guarantees	n.a.	8,934	10,584	12,540	14,573	16,291	17,695	...	...	...
Total government debt including IMF obligations	7,731	9,020	10,773	12,699	14,380	16,028	17,477	19,043	19,797	21,278
Nominal GDP (market prices)	13,200	14,867	18,276	20,047	22,386	25,169	27,493	29,598	29,598	33,130

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

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

2/ Additional spending on security and internally-displaced people is recorded under transfers ("grants") instead of development expenditure as reported in the original FY2015/16 budget.

Attachment. Performance of the Power Sector

1. Stock and flow of payables in the power sector. The stock of payment arrears includes the payables of PRs 321 billion, and the stock of PHCL of PRs 335 billion at end-June 2016. The evolution of the stock and the flow of payables, including its components, for FY 2014/15 and FY 2015/16 are given in the following table:

(In Billion PRs)1/	2015/16								2014/15	2015/16
	Q1		Q2		Q3		Q4			
	Target	Actual	Target	Actual	Target	Actual	Target	Actual	Total	Total
Non-recoveries	16	37	12	(6)	16.00	3.0	19	12	104	46
Accrued Markup	-	-	-	-	-		-	-	23	
Excess Line Losses	11	22	(3)	(8)	0.40	(2.7)	4	5	50	17
GST Non Refund	-	-	-	-	-		-		14	
Late Payment Surcharge	1		1				1		8	
Delay Determinations	3	-	3	-	-		-		11	
Flow (under arrears plan)	**31**	**59**	**13**	**(13)**	**16**	**0.3**	**23**	**17**	**210**	**63**
Operational deficit/surplus of the system		10		15		36	3	(18)	n.a.	43
Impact of oil prices		(56)		(20)	(2)	(29)	(8)	(14)	n.a.	(119)
Others 1/		(4)		18		12		19	n.a.	45
Stock clearance	47	4	63	-	-	(14)	-	(15)	n.a.	(25)
Total flow		13		0	15	5	18	(10)	48	8
Total (Stock)	**297**	**326**	**287**	**326**	**341**	**331**	**350**	**321**	**313**	**321**

1/Includes STFC arrears due to court stay, LNG payment arrears due to delay in tariff determination and other costs not recovered.

2. Performance of DISCOs. In October 2015, quarterly quantitative targets have been determined by MWP and each DISCO for distribution losses, and collection. The performance of DISCOs against targets are given in the tables below:

Target Bill Collection (In percent)	Q1	Q2		Q3		Q4		FY 2015/16	
	Actual	Target	Actual	Target	Actual	Target	Actual	Target	Actual
LESCO	95.4	107.4	108.7	111.3	112.1	76.4	92.7	96.2	99.7
GEPCO	95.7	103.2	107.5	110	111.3	80.8	93.6	95.7	99.7
FESCO	95.9	107.1	113.6	105.5	105.9	88.4	95.5	98.5	100.4
IESCO	79.4	98.3	103.7	89.1	90.1	86.9	95.3	87.6	91.1
MEPCO	92	105.7	113.3	112.4	106.8	88.6	96.5	98.1	100.6
PESCO	81.7	90.9	94.9	96.6	87.7	81.5	91.3	87.1	88.7
TESCO	8.8	8.7	12.3	9.1	11.3	414.9	585.8	75.4	444.5
HESCO	52.8	81.7	90.7	93.9	90.9	72.8	69.7	72.6	72.4
SEPCO	42	51.3	64.7	77.6	70.6	64.7	56.5	56.2	55.0
QESCO	105.1	22.9	74.3	27	83.3	49.5	34.5	57.5	67.1
TOTAL DISCOs	**86.9**	**95.6**	**101.5**	**98.5**	**97.3**	**83.1**	**93.9**	**90.2**	**94.6**

Losses target (In percent)	Q1	Q2		Q3		Q4		FY 2015/16	
	Actual	Target	Actual	Target	Actual	Target	Actual	Target	Actual
LESCO	15.2	9.1	9	9.1	9.8	18.4	19.1	14.1	13.9
GEPCO	14.3	3.1	2.4	7.1	7	14.0	14.4	10.7	10.6
FESCO	11.9	5.3	2.4	6.7	5.8	15.4	15.5	10.9	9.8
IESCO	9.6	1.5	1.8	3.1	5.2	18.3	16.3	9.4	9.1
MEPCO	21.5	10	9.4	10	9.8	19.5	20.3	16.7	16.4
PESCO	41.7	26.2	27.2	26.1	27.8	35.2	34.8	34.0	33.8
TESCO	21.1	17.8	17.5	14.1	16.6	28.3	20.4	20.6	19.0
HESCO	29.2	18.7	20.4	23.2	22.7	30.3	30.4	26.5	26.5
SEPCO	42.6	30.6	30.8	30.5	30.6	41.8	41.6	38.1	37.9
QESCO	24.9	19.4	21.8	23.5	22.9	27	25.7	23.9	23.9
TOTAL DISCOs	**21.1**	**12.4**	**11.9**	**13.2**	**13.4**	**22.2**	**22.0**	**18.0**	**17.9**

Statement by Jafar Mojarrad, Executive Director for Pakistan, Mohammed Daïri, Alternate Executive Director, and Shahid Mahmood, Senior Advisor to Executive Director
September 28, 2016

On behalf of our Pakistani authorities we would like to thank staff for their hard work and constructive interactions during the 12th and final review of the three-year EFF-supported program, as well as for a well-written and balanced report. Our authorities broadly agree with staff assessment and policy advice. They are also grateful to the Executive Board and management for their guidance and support throughout the program period.

Program Implementation

Program discussions in 2013 were held in the backdrop of macroeconomic imbalances, structural weaknesses, power shortages, and security and political concerns which were holding back the economy and adversely impacting macroeconomic and financial stability. The program was designed on a rich reform agenda encompassing fiscal consolidation, including by strengthening revenue, reducing inflation, rebuilding foreign exchange reserves, enhancing financial sector stability, addressing energy bottlenecks, liberalizing trade, restructuring or divesting public sector enterprises, improving the business climate, and further protecting the most vulnerable segments of the population. In addition to a number of performance criteria and indicative targets, the program was monitored through an array of structural benchmarks (SBs) which over the three-year period totaled 47 and included enactment of 18 laws by parliament.

While program implementation was faced with some difficulties initially, mainly as result of a challenging political and security environment, it has significantly strengthened more recently. Indeed, stronger ownership has allowed a marked improvement in macroeconomic performance, steady reduction in vulnerabilities, and progress in growth-supporting structural reforms. In this respect, the major objectives of the program were achieved.

Performance under the 12th and last review continued to be satisfactory. All end-June 2016 performance criteria (PCs) and indicative targets were met, except two PCs on the overall budget deficit and Net Domestic Assets (NDA) of the State Bank of Pakistan (SBP), which were missed by small margins. Necessary corrective measures were taken to limit NDA by end-August to ensure an appropriate pace of monetary expansion and to cut non-priority expenditures so as to achieve the fiscal targets. The strong growth (20 percent) in tax revenue, although partially offset by a shortfall in nontax revenue, and the large over performance with respect to targeted cash transfers under the BISP and power sector arrears are noteworthy. Similarly, all SBs were met, except for notification of the multi-year tariff for three power distribution companies (DISCOs), which was delayed because of the continuing dispute with the regulator over the FY 2015/16 determined tariffs.

Economic Developments and Outlook

Macroeconomic performance and resilience has significantly improved under the program with growth reaching 4.7 percent in FY 2015/16 (highest in eight years). While staff is projecting growth to increase to 5 percent in FY 2016/17, the authorities have a more ambitious target of 5.7 percent, based on buoyant construction activity, higher growth in private sector credit, and greater contribution from the China-Pakistan Economic Corridor. Inflation has declined to low single digits, reflecting prudent monetary policy and lower oil and other commodity prices, and is expected to remain contained at 5.3 percent at end-FY 2016/17. Gross international reserves grew almost threefold from 1.5 months of imports in FY 2012/13 to 4.2 months in FY 2015/16 and are likely to reach 4.6 months of imports in FY 2016/17. After a continuous strong performance over the last three years, Pakistan's equity market MSCI Pakistan index has been reclassified to Emerging Markets status, effective May 2017.

Fiscal Policy

Fiscal consolidation has been at the heart of the program. The authorities have curtailed the budget deficit by 3.9 percentage points of GDP over the program period, to reach 4.6 percent of GDP (excluding grants) in FY 2015/16, and are targeting a deficit of 3.8 percent of GDP in FY 2016/17. This has been achieved through a number of measures to improve revenue collection and rationalize expenditure.

Through a combination of tax policy and administration measures, the tax-to-GDP ratio has improved by 2.4 percentage points over the program period. Major progress in this area include reducing tax concessions and exceptions and prohibiting new ones through issuance of SROs, unless under exceptional circumstances and special approval procedures, and differential taxation of filers and non-filers, as well as improvement in taxpayer identification and broadening of the tax base. To buttress efforts toward reducing tax evasion and avoidance, Pakistan recently became a signatory to the joint initiative of the Council of Europe and the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters on September 14, 2016. The authorities are targeting an increase in the tax-to-GDP ratio to 14.5 percent by FY 2019/20, and to this effect are working on a range of tax policy and administration measures in close coordination with the provinces.

As part of the fiscal consolidation strategy, the authorities have also kept a sharp focus on improving the composition of expenditures to support growth. Energy subsidies have been significantly reduced along with containment of other non-priority expenditures to create space for critical social and capital spending. The new public-private partnership (PPP) law, which has been submitted to the parliament, will provide a framework for greater private sector participation in infrastructure investment and will reduce the need for budget financing while limiting moral hazard and contingent liabilities. While gross public debt declined slightly since the onset of the program to reach 62 percent of GDP in FY 2014/15, it increased to 64.7 percent of GDP in FY 2015/16, including as a result of a buildup of government deposits. The authorities have adopted a medium-term debt management strategy under which they plan a gradual reduction in external borrowing while lengthening average maturity in domestic borrowing.

To strengthen long-term debt sustainability and to provide a rule-based fiscal policy the authorities have taken steps to further bolster public financial management by amending the Fiscal Responsibility and Debt Limitation Act 2005 to: (a) cap the federal budget deficit at 4 percent of GDP (excluding grants) for the next three fiscal years and 3.5 percent thereafter; (b) reduce the debt-to-GDP ratio to 60 percent by FY 2017/18 and bring it down gradually to 50 percent over a 15-year transition period; (c) define strong and clear escape clauses; and (d) establish explicit enforcement procedures and corrective mechanisms for treatment of deviations. The newly established Fiscal Coordination Committee will synchronize policy guidance and budget monitoring across provincial and federal governments.

The authorities have continued to expand the coverage of the BISP. The number of beneficiary households for unconditional cash transfers has increased by 42 percent during the program period, along with an increase in stipends by 57 percent. The education-related conditional cash transfers have so far reached 1.3 million school-going children and its coverage will continue to increase.

Monetary and Exchange Rate Policies

Monetary and exchange rate policies were successful in maintaining price stability and building foreign reserves, including through the SBP spot purchases, with the objective of strengthening buffers against shocks. The authorities will maintain exchange rate flexibility and continue to improve trade competitiveness. The SBP will also continue to set the policy rate in a forward-looking fashion to maintain positive real interest rates and anchor inflation. Following the policy rate cut in May 2016, the SBP remains prepared to increase the policy rate should inflationary pressures reemerge.

Significant progress has been made in strengthening the autonomy and governance of the SBP during the program period including by amending the SBP law. The independent Monetary Policy Committee (MPC) of the central bank is now holding its meetings regularly, and its minutes are being published. In order to further strengthen the SBP’s autonomy the authorities will continue with implementation of remaining recommendations of the 2013 Safeguards Assessment. SBP's analytical capabilities are also being enhanced in support of introduction of a flexible inflation targeting framework in the medium-term along with improved policy transparency and greater dissemination of information about inflation expectations and forecasts.

Financial Sector

The banking sector remains well-capitalized and profitable, liquidity indicators are strengthening, and although NPLs remain high, they are on the decline and well-provisioned. Important reforms have been carried out in the regulatory and supervisory framework during the program period to foster financial sector performance and resilience, which has allowed the much needed increase in credit to the private sector. Private sector credit grew by 11.1 percent in FY 2015/16 compared to an average growth rate of 5.9 percent during the period FY 2011/12-2014/15. The authorities remain committed to enhancing the stability of the banking sector and further deepening the financial system. They will also continue in particular with the phased implementation of Basel III regulatory norms with the aim of completing it by 2019.

Structural Reforms

The authorities attach high priority to completing the public sector enterprises (PSEs) reform, which is crucial for fiscal consolidation and for improving economic growth performance. They had initiated an ambitious restructuring and divestment plan to improve PSE performance and to attract private sector participation. After initial successes, labor tensions and political opposition led the authorities to revisit plans for private sector participation resulting in revised timelines and mode of divestment for Pakistan International Airlines (PIA), Pakistan Steel and the power distribution companies. The transaction structure for PIA is being finalized while the Pakistan Steel privatization process, which had slowed down after expression of interest by the provincial authorities, has resumed following inconclusive discussions. In the interim, steps have, however, been taken to restructure the identified PSEs so as to make them more efficient, with improved service delivery, and by curtailing losses. After undergoing an intensive restructuring plan the Pakistan Railways, in particular, has shown significant improvement in freight and passenger services which has had a positive impact on the company's revenues and service delivery.

Continuing the energy sector reform is crucial in view of the serious issues at stake for the fiscal, economic and social landscape. Sustained efforts have helped in reducing budgetary subsidies and containing the accumulation of arrears, and have brought about important operational improvements in the performance of DISCOs. Stringent monitoring and enforcement, upgraded electricity transmission and distribution network, enhanced revenue-based load management and incentives to collectors have resulted in reduction in distribution losses and higher collection over the program period. With these improvements the DISCOs, starting with FESCO at first and followed by IESCO and LESCO, would now be offered for sale in the stock market through IPOs. The authorities have completed considerable preparatory work in this regard, and the proceeds from these IPOs would be utilized to reduce the stock of outstanding circular debt.

Gas sector reforms have proceeded well with tariff incentives to the gas production companies resulting in a 13 percent increase in the domestic gas supply and LNG imports, significantly contributing to the overall improvement in the supply situation. Unbundling of gas transmission system is also designed to improve competition in the sector.

After reversals in 2015, when Pakistan slipped by two positions in the World Bank Doing Business rankings, the authorities have adopted a comprehensive country-wide reform strategy with assistance from the World Bank in February 2016. Initial success has already been achieved, including rationalization of the fee structure to reduce costs of opening a new business, development of a new electronic tax filing procedure, legislation to allow use of movable property as collateral for getting credit, amendments to Credit Bureau Act and issuance of related regulations, and enactment of the Corporate Restructuring Companies Act to set up companies to take over assets of bankrupt firms. The authorities are now working towards implementation of comprehensive business climate reforms to enhance growth performance while improving inclusion through greater access to resources to the marginalized sections of the population.

Conclusion

After successful completion of the EFF-supported program, the authorities remain resolved to continue with prudent economic policies and structural reforms to preserve the hard-won economic gains and achieve their growth and job creation objectives. They look forward to continued close cooperation and policy dialogue with the Fund and to continue to benefit from its valuable technical assistance. On behalf of our authorities we request completion of the twelfth and last review of the EFF-supported program, and for waivers for nonobservance of the end-June PCs on the budget deficit and NDA.