Government of Pakistan Budget, 1961-62

Budget Estimates for 1961-62

On the basis of existing taxation, Revenue Receipts for 1961-62 are placed at Rs. 215.53 crores. With Revenue Expenditure at Rs. 191.90 crores, the surplus amounts to Rs. 23.63 crores.

The Revenue Receipts for 1961-62 show an increase of Rs. 18.79 crores over the Revised Revenue Estimates for 1960-61. With respect to Revenue Expenditure there was also an increase of Rs. 17.69 crores. The surplus on Revenue Budget for 1961-62 is expected to be higher by Rs. 1.10 crores than for 1960-61.

The estimates of Capital Expenditure for 1961-62 total to Rs. 229.94 crores which reflects a rise of Rs. 26.08 crores over 1960-61 (Revised Estimates).

In the Revenue Budget, the anticipated increase from Rs. 196.74 crores in 1960-61 to Rs. 215.53 crores in 1961-62 was expected to emerge chiefly from Customs, Central Excise Duties, and Interest Receipts. Collections under Customs Duties are expected to increase by Rs. 6.95 crores from Rs. 53.45 crores to Rs. 60.40 crores, under Central Excise Duties, by Rs. 1.36 crores from Rs. 32.33 crores to Rs. 34.07 crores and under Interest Receipts, by Rs. 4.05 crores from Rs. 8.89 crores to Rs. 12.94 crores. On the Expenditure side, the increase from Rs. 174.21 crores to Rs. 191.90 crores is largely accounted for by Non-Development Expenditure on Debt Service and Frontier Regions. A small increase of Rs. 1.76 crores is also estimated in the field of Agriculture under Development Expenditure.

In the Capital Budget, the increase in total expenditure by Rs. 26.08 crores from Rs. 203.86 crores to Rs. 229.94 crores is despite the fall of Rs. 12.88 crores on the Non-Development side. There has been an increase under Development Expenditure of Rs. 49.46 crores. Of this, Rs. 29.22 crores is additionally set aside for Direct Capital outlay by the Central Government and at the same time assistance to Provinces is also marked up by Rs. 20.26 crores. Capital Outlay under Railways will increase by Rs. 14.23 crores; under Indus Basin Replacement Works, by Rs. 6.95 crores; under New Federal Capital, by Rs. 2 crores; under Food Storage Construction, by Rs. 2.32 crores and under Agricultural Improvement and Research, by Rs. 1.44 crores.

The Capital Receipts for the year 1961-62 are estimated Rs. 59.58 crores higher at Rs. 239.62 crores. Internal Resources are placed higher by Rs. 5.60 crores at Rs. 92.64 crores with enlarged Accretions to Reserve Funds, Recoveries of Loans and Advance etc. Meanwhile External Resources are also expected to go up by Rs. 53.98 crores to Rs. 146.98 crores. While Foreign Loans are expected to increase by Rs. 31.06 crores, Foreign Grants will be stepped up by Rs. 22.92 crores. The ICA local currency releases are placed higher at Rs. 85 crores in 1961-62 against Rs. 65.35 crores in the preceding year. Considerable increases in Foreign Loans are expected from the U.K., D.L.F. and West Germany. As total Capital Expenditure is placed lower at Rs. 229.94 crores against Receipts of Rs. 239.62 crores, the balance of Rs. 9.68 crores is proposed to be utilised for the retirement of ad hoc treasury bills of the order of Rs. 7 crores created in the year 1960-61 and the rest of Rs. 2.68 crores will improve the cash balance of the Government.

The 1961-62 Budget proposes no fresh taxes. At the same time a number of tax concessions have been announced whose net effect will be a loss of revenue of Rs. 1.11 crores. The losses in customs duties and income tax are Rs. 1.32 crores and Rs. 0.45 crores respectively. However, re-adjustment in Central Excise Duties is expected to yield an additional Rs. 0.66 crore. A brief mention may be made of the areas of concessions: the marginal rate of personal taxes has been reduced; the 'investment allowance' in respect of total income has been increased; some concessions given for purchase of books and literary and artistic works in relation to tax liabilities; the rate of intercorporate tax on industrial incomes has been reduced; the scope of 'tax-holiday' to industries and the period of concessions have been expanded; some concessions granted to the mining industry; incentives provided to the construction of new houses; depreciation allowance for ship-building industry has been increased; tax-exemption granted to foreign technicians enlarged; some concessions are also given to donors to charitable institutions; number of domestic manufactures like cycles, sewing machines, hurricane lamps, insecticides, ships and barges, timber and bamboo products etc., have been exempted from sales tax; all excisable commodities produced in specified backward regions have been exempted from excise duties; excise duty has also been removed in respect of salt, electric fans etc., some reduction in import duties have also been announced.

Revised Estimates for 1960-61

The budgeted surplus of Revenue Receipts over Revenue Expenditure increased from Rs. 8.46 crores to Rs. 22.53 crores. There was a greater increase in Revenue Receipts from Rs. 178.32 crores to Rs. 196.74 crores than in Revenue Expenditure, from Rs. 169.86 crores to Rs. 174.21 crores.

The increase in Revenue Receipts was accounted for by Customs (+Rs. 8.30 crores) and Sales Tax (+5.98 crores), Income-Tax and Corporation Tax, and Central Excise Duties also recorded marginal increases. Liberalization of private imports and imports under Export Bonus Scheme gave rise to enlarged collections under Customs.

The increase in Revenue Expenditure was largely accounted for by Debt Services, Police, Frontier Regions, Aviation and Education.

Both Capital Receipts and Expenditure increased from Rs. 172.20 crores to 180.04 crores and from Rs. 179.19 crores to Rs. 203.86 crores. The improvement in Receipts emerged from Internal Resources (although there was a shortfall in External Resources owing to lesser utilization of

Foreign Loans) and the increase in Expenditure was on account of both Development and Non-Development Expenditure.

Meanwhile, a net amount of Rs. 10.87 crores was advanced to West Pakistan WAPDA for Indus Basin Replacement Works, and this was mainly financed by way of creating *ad hoc* treasury bills equal to Rs. 7 crores. At the same time, the cash balances were brought down to a greater extent (Rs. 16.82 crores) than originally estimated (Rs. 6.99 crores).

GOVERNMENT OF PAKISTAN BUDGET

REVENUE BUDGET

(*Rs. in lakhs*)

	1960-61 Budget	1960-61 Revised	1961-62 Budget
RECEIPTS:			
Customs ...	45,15	53,45	60,40
Central Excise Duties ...	31,94	32,33	34,07
Income Tax & Corporation Tax ...	29,88	30,63	31,06
Sales Tax ...	18,24	24,22	34,73
Railways-Net Receipts ...	5,02	5,02	—
Posts and Telegraphs-Net Receipts ...	2,94	3,19	3,65
Defence Services ...	6,14	6,42	7,50
Interest Receipts ...	9,24	8,89	12,94
Rehabilitation Taxes ...	2,40	2,79	2,90
Other Revenue ...	29,77	29,80	38,68
TOTAL RECEIPTS	1,78,32	1,96,74	2,15,53
EXPENDITURE:			
Revenue Collecting Department ...	3,95	4,16	4,27
Civil Administration ...	32,43	34,94	44,55
Defence Services ...	98,59	98,14	98,59
Civil Works & Central Road Fund ...	2,16	1,32	3,06
Special Fund for Rehabilitation ...	2,40	2,79	2,90
Servicing of Debt ...	16,64	19,45	21,95
Grants to Provincial Governments ...	2,46	2,81	2,40
Development Expenditure ...	7,77	6,86	8,81
Other Expenditures ...	3,46	3,74	3,57
TOTAL EXPENDITURE ...	1,69,86	1,74,21	1,91,90
SURPLUS ...	8,46	22,53	23,63

GOVERNMENT OF PAKISTAN BUDGET

CAPITAL BUDGET

(*Rs. in lakhs*)

	1960-61 Budget	1960-61 Revised	1961-62 Budget
DIRECT OUTLAY ON CENTRAL GOVERNMENT			
Development Expenditure:			
Railways (as per Railway Budget) ...	20,80	20,37	34,60
Posts and Telegraphs ...	5,80	5,74	6,68
Irrigation ...	5	1,42	8,37
Agricultural Improvement and Research ...	1,61	1,31	2,75
Industrial Development ...	17,16	19,77	18,04
Civil Aviation ...	4,36	4,32	4,41
Civil Works ...	11,01	8,65	7,06
Electricity Schemes ...	2,00	2,00	30
Food Storage and other Works ...	3,45	2,66	4,98
Miscellaneous Investments ...	2,55	2,10	3,62
Other Expenditures ...	3,65	3,64	10,97
Expenditure from Reserve Fund ...	1,23	1,88	1,30
Loans to Local Bodies, etc. ...	8,05	8,44	8,43
Loans and Grants to Provincial Governments ...	99,87	1,00,99	1,21,25
Less Likely Shortfall in Expenditure	—10,00	—4,50	—15,00
TOTAL-DEVELOPMENT EXPENDITURE ...	1,71,59	1,78,79	2,17,76
Add NON-DEVELOPMENT EXPENDITURE ...	7,60	25,07	12,18
TOTAL-CAPITAL EXPENDITURE ...	1,79,19	2,03,86	2,29,94
Financed by:			
Revenue Surplus ...	8,46	22,53	23,63
Permanent Debt-Internal (Net) ...	10,00	14,29	7,00
Floating Debt (Net) ...	—29	12,58	—7,31
Unfunded Debt (Net) ...	10,24	8,43	9,50
Recovery of Loans and Advances ...	4,42	3,02	4,24
Other Capital Receipts ...	4,65	3,72	5,06
Accretions to Reserve Funds ...	23,75	22,97	34,52
Deposits and Remittances (Net) ...	2,50	6,50	90,00
Foreign Loans ...	58,28	39,44	70,50
Foreign Grants ...	50,19	53,56	76,48
Cash Balance Utilization ...	6,99	16,82	—2,68
TOTAL-CAPITAL RESOURCES ...	1,79,19	2,03,86	2,29,94

(A.M.G.)

Excerpts from White Paper on the Central Budget, 1961-62

The White Paper seeks to review and analyse broadly the results of the economic and fiscal policies pursued by Government during the preceding year.

The year 1960-61 (July 1960—June 1961) saw the country's economy gather further strength. Industrial and agricultural production went up. Exports touched new heights. Gold, dollar and sterling reserves were further reinforced. The supply position of goods in general improved. Price controls were progressively lifted. The food situation remained under control. The cost of living rose only slightly. The monetary expansion slowed down.

Foreign Exchange

The foreign exchange position continued to improve during the year 1960. The gold, dollar and sterling reserves increased by Rs. 6.68 crores. The balance of payments on current account, however, showed a deficit of Rs. 62 lakhs. This was not the outcome of any weakness of the country's foreign exchange position. It resulted from the Government's policy of liberalising imports with a view to ensuring greater utilization of the existing industrial capacity, giving an impetus to private investment, improving the supply of consumer goods, counteracting the prevailing inflationary pressures and keeping the rising prices under check.

Larger payments were, to a great extent, offset by larger receipts arising partly out of the successful operation of the Export Bonus Scheme. Payments during the year ending 31st December, 1960 amounted to Rs. 224.23 crores against Rs. 167.66 crores in the preceding year. The payments on private account amounted to Rs. 158.26 crores and on Government and invisible accounts to Rs. 65.95 crores.

The receipts during 1960 aggregated Rs. 223.59 crores compared with those of Rs. 191.96 crores in 1959, constituting an improvement of Rs. 31.63 crores. This was a record level for the past many years. Particularly sharp increases were noticed in the earnings from the export of raw jute and raw cotton which rose by Rs. 12.61 crores and Rs. 6.73 crores respectively. Both jute and cotton manufactures also fetched more foreign exchange to the extent of Rs. 3.95 crores and Rs. 1.10 crores respectively.

The improvement in the foreign exchange reserves was ascribable partly to an increase in the net capital inflow. Direct foreign capital investment during the year 1960 amounted to Rs. 2.4 crores showing an increase of 147 per cent over the investment during 1959.

The reserves maintained their rise in the first quarter of 1961. They are, however, likely to show some decline in the following quarter due to the full impact of the liberalised import policy and seasonal factors. The table given below indicates the position of reserves since September, 1958:

(*Rs. in crores*)

September, 1958	72.62
December, 1958	76.58
December, 1959	122.72
December, 1960	129.4
March, 1961	143.00

Foreign Aid

The total aid allocated to Pakistan up to the end of March, 1961 amounted to $ 1875.56 million. The following table gives its source-wise break-up:—

(*In million US $*)

Country/Agency	Total allocations upto 31st March 1961	Allocations during 1959-60 April-March	Allocations during 1960-61 April-March
United States	1435.84	205.07	265.25
Canada	129.07	15.14	15.00
Australia	22.73	0.87	0.00
United Kingdom ...	4.78	0.59	N.A.
New Zealand	5.62	0.57	0.00
Germany	0.71	—	0.71
Japan	0.19	0.04	N.A.
Sweden	0.50	—	—
United Nations (including Special Fund)... ...	16.39	5.56	3.57
World Bank (including I.F.C.)	242.73	24.90	90.00
Ford Foundation ...	17.00	3.20	1.98
TOTAL ...	1875.56	255.94	376.51
CRORE Rs. ...	892.76	121.90	179.11

During this period some more credit arrangements were made with certain countries. Two new loan agreements of £ 5 million and £ 3 million respectively were signed with U.K. The former credit is earmarked for the purchase of jute looms by the PIDC and of equipment by the East Pakistan WAPDA. The latter credit is meant for the procurement of Railway equipment. A line of credit of $30 million has been obtained from Russia for financing oil prospecting operations. The Federal Republic of Germany has agreed to supply a further credit of DM 150 million both for the private and public needs. The Japanese offer of a credit of $20 million for the purchase of textile machinery has also been accepted. A protocol was signed with Yugoslavia for a loan of $10 million for financing private and public projects. The Export-Import Bank approved a loan of $ 6.4 million for the purchase of cotton ginning and delinting machinery.

An important development was the formation of a Consortium of a number of countries and institutions interested in the development effort of Pakistan. The Consortium was organized by the International Bank for Reconstruction and Development in order to provide these countries and institutions an opportunity to meet and discuss with the representatives of Pakistan, the requirements of aid in foreign exchange for the implementation of Pakistan's Second Five-Year Plan. The first meeting of the Consortium was held on 6th and 7th October, 1960, in Washington. In addition to the World Bank, the Governments of Canada, Germany, Japan, the United Kingdom and the United States of America sent participants. The Governments of France and Italy and the International Monetary Fund were represented by observers. The Consortium considered Pakistan's Second Five-Year Plan and decided to meet again after a detailed appraisal of the Plan had been carried out by a World Bank team. The World Bank team visited Pakistan in January-February, 1961 and submitted its report in May, 1961.

The Consortium met again from 5th to 7th June, 1961. The meeting was attended by the representatives of the Governments of Canada, France, Germany, Japan, United Kingdom and the United States of America. The representatives of the International Bank for Reconstruction and Development and the International Development Association also attended. The Government of Denmark, Norway and Sweden and the International Monetary Fund sent observers.

The Consortium noted the successful efforts made by the Government of Pakistan to create conditions in the country favourable to economic development and endorsed their policies for freeing the economy progressively from administrative controls and for preventing generation of further inflationary pressures. The Consortium recognized that the successful continuation of these policies depended, among other things, on an uninterrupted flow of assistance from abroad. The Consortium members announced additional aid commitments amounting to 320 million dollars for the second year of the Plan beginning July 1, 1961. The Consortium also agreed to hold another meeting later in 1961-62 to decide on the extent and the nature of assistance for the second and third years of the Plan taken together.

Export

The export performance of the country during the period under report has been very satisfactory. It was due both to an increase in the demand overseas for Pakistan's principal exportable commodities and the continued success of the Export Bonus Scheme. The total exports during 1960, valued Rs. 193.23 crores compared with Rs. 166.70 crores of 1959 indicating a use of 15.8 per cent. In this the share of the principal exportable commodities was to the tune of Rs. 168.84 crores. At Rs. 193.23 crores, the exports reached a record height since the Korean War boom year of 1951.

The earnings of raw jute in the year stood at Rs. 84.79 crores—Rs. 12.6 crores more than the preceding year's receipts. This was notwithstanding the fact that the total quantity of jute exported in 1960 was smaller than that exported in 1959. A negligible carry-forward and smaller crops both in Pakistan and India than originally anticipated coupled with late arrivals pushed up the jute prices. At one time Export Firsts and Narayanganj Cuttings were quoted as high as Rs. 425 and Rs. 280 per bale compared with Rs. 185 and Rs. 60 per bale a year earlier.

Raw cotton and wool also made larger contributions. At Rs. 21.97 crores the exports earnings of raw cotton recorded an increase of Rs. 6.73 crores over the preceding year's collections. The duty on Staple and Desi varieties of cotton remained unchanged though the duty on Comilla cotton was cut down from Rs. 40 to Rs. 20 per bale with a view to encouraging its cultivation and making it competitive with similar varieties of foreign cotton. Another notable development in this field was the removal of condition of prior opening of Letters of Credit by the foreign buyers of cotton. This step was intended to make cotton more attractive in the foreign markets. Wool fetched Rs. 9.10 crores against Rs. 7.98 crores in the preceding year. This improvement was the result of a rise both in the quantity and the price of wool exported. A factor responsible for the increase in wool exports was the rigid insistance on wool being graded and qualitatively certified prior to its export under the Wool Grading Scheme. With a view further to improving the quality of wool a scheme has been drawn up by the Government of West Pakistan for the establishment of Sheep Centres at different places. These centres will provide for scientific shearing of wool and its proper sorting before export, thereby enhancing the confidence of the foreign buyer in the quality of Pakistani wool. A similar scheme has been prepared by the Government of East Pakistan also.

Tea remained a source of concern during the year under report. Consequent upon severe drought afflicting the tea-growing areas in East Pakistan, tea production fell by 26.7 per cent in spite of an increase of 1.2 per cent in the acreage devoted to tea-growing. Against an estimated production of 57,000,000 lbs., the actual yield of tea did not exceed 42,000,000 lbs. Since there was no likelihood of the domestic consumption of tea going down in the face of shorter supplies, it was decided to stop exports in September, 1960. By then only 1.9 million lbs. of tea had been exported yielding an exchange of bare Rs. 96 lakhs. This resulted in a fall of nearly Rs. 3.74 crores in the earnings from tea during 1960 as compared with those in 1959. Among the measures adopted to secure an increase in the output of tea in the years to come the East Pakistan WAPDA has been requested to undertake a survey of the ground and surface water resources in the district of Sylhet with a view to making arrangements for artificial irrigation of tea estates thereby lessening their dependence on rains. In addition, efforts are being made to procure tea seeds from abroad, arrangements are in hand for the supply of fertilizers to tea gardens and licences have been granted for the import of machinery and equipment for the tea industry.

The Export Bonus Scheme came in for a comprehensive review during the course of the year. It was noticed that the scheme had acted as a powerful incentive for exports and had added many a new item to the export list. It had also created an export consciousness all around and had brought a number of persons with new ideas into the export line. A major feature of this policy was the change it brought about in the system of issue of repeat licences. Industrial consumers and commercial importers were allowed with effect from the January—June, 1961, shipping period to apply for repeat licences on production of bills of lading duly certified by a scheduled bank and accompanied by invoices showing a minimum of 75 per cent utilization of the earlier licence instead of waiting for 100 per cent utilization of the earlier licence and producing complete bills of entry under the old procedure. The object was to enable an efficient importer to get at least two consignments within one shipping period.

This policy further sought to establish a relationship between industrial licensing and the export performance of industries in order to underline the fact that further progress along the path of liberalisation was possible only if exports were expanded. Special treatment in the matter of licensing for replacement, balancing and modernisation of machinery and equipment was promised to those units under 12 specified industries which have done reasonably well on the export side or which possessed export potential capable of being developed. To emphasise the export bias of the policy it was provided that in admitting new-comers to the import trade preference should be shown to such persons as have some export performance to their credit.

In the middle of the shipping period January—June, 1961, Government took another step in the direction of further liberalisation of imports. They decided to place 11 items on a regulated Open General License. These comprised iron and steel, drugs and medicines, tractors, typewriters and office machines, milk food for infants, cement (for East Pakistan) and parts and accessories of automotive vehicles, etc. This reflected Government's anxiety to abolish rigid import controls with all possible speed.

Food Situation

Food for all at reasonable prices remains the ultimate aim of Government's food policy. It was in pursuance of this objective that a new wheat policy was launched in West Pakistan early in 1960. The idea was to provide an incentive to the wheat grower by offering him an economic price for his produce without placing too much burden on the consumer and to free the wheat trade from the years old controls and to give it back to private hands in accordance with the dictates of a free economy. The operation of this policy during the period under review has established its usefulness. The situation remained under control even when prospects of the new Rabi crop looked bleak due to the lack of rains at the time of sowing. Generous issues from Government stocks of imported wheat dispersed all over the country counter-balanced the short supply from indigenous sources. The bulk of the home grown wheat was lifted at higher than the floor rate of Rs. 13.50 per maund by private buyers. The Government procurement was negligible. The prices of indigenous wheat acquired a stability never seen in the past many years.

In East Pakistan also the policy of partial decontrol of rice trading worked well. No abnormal price variations were registered. No unusual demands were made on Government reserves.

Development

The opening year of Pakistan's Second Five-Year Plan which commenced from the 1st July, 1960, witnessed a more animated development activity in the country, setting a stage for accelerated progress in the years to come. The current year's Annual Development Programme for the public sector was kept at Rs. 222 crores. Due provisions were made for its implementation in the Budgets of the Central and the Provincial Governments. Nearly 70 per cent of the Programme consisted of ongoing projects leaving the balance of 30 per cent for new ones. In this Programme emphasis was placed on the development of productive sectors and the creation of infra-structure. Of the total expenditure envisaged, Agriculture, Village AID, Water and Power were allocated 45 per cent. Transport and Communications 21 per cent, Industries, Fuel and Minerals 10 per cent and the balance was earmarked for Housing and Settlement, Education and Training, Health, Social Welfare and Manpower Development. The foreign exchange element of the Programme was of the order of Rs. 111 crores. Most of this was expected to come through aid. To provide resources for the rupee portion of the Programme, additional taxes of Rs. 10.50 crores were levied in accordance with Government's policy of maximum mobilization of domestic resources for financing country's development effort.

It was originally contemplated that the Second Five-Year Plan would entail a total expenditure of Rs. 1,900 crores during the period 1960-61 to 1964-65. Its revised size is Rs. 2,300 crores. This upward revision has been necessitated by a variety of reasons. In the first place, prices, both internal and external, have been rising since the Plan was first conceived and this trend is likely to continue during the rest of the Plan period. Secondly, in a number of instances the first estimates were based on incomplete data and had to be revised in the light of further information made available subsequently. Thirdly, changes in the scope and character of certain projects have increased their cost. Fourthly, the throw-forward of expenditure in respect of development projects initiated during the First Five-Year Plan period proved to have been appreciably under-estimated. Finally, the Plan has been expanded to include some new projects not earlier included and had to take into account the extra works incidental to the execution of the Indus Basin Development Plan. The increase of Rs. 400 crores in the outlay of the Plan is shared by both the public and private sectors. The expenditure in the public sector now stands at Rs. 1,462 crores compared with the original estimates of Rs. 1,150 crores and in private sector at Rs. 838 crores against the earlier estimates of Rs. 750 crores. The revised phasing of the expenditure is as follows:—

		(*Rs. in crores*)
1960-61	...	310
1961-62	...	407
1962-63	...	472
1963-64	...	520
1964-65	...	591
Total	...	2,300

It would be unrealistic to consider this phasing as final. It is based on certain assumptions which subsequent events may not confirm necessitating alterations here and there. Such alterations will be reflected in the Annual Development Programmes which allocate the available resources in the next 12 months among competing demands keeping in view the current performance of schemes and the interest of the country's economy as a whole.

The revised Second Five-Year Plan aims at increasing the national income by 22 per cent with consequential rise of 10 per cent in the per capita income notwithstanding a larger size of the population as revealed by the preliminary Census reports.

Credit and Monetary Policy of the State Bank of Pakistan

The following are excerpts from the speech delivered by the Governor of the State Bank of Pakistan at the Annual General meeting of the shareholders of the Bank, held on 8th September, 1961:

Perhaps the most important development in the monetary field during the year 1960-61 (July-June) was the nominal increase in money supply. It recorded an increase of only Rs. 2.61 crores to Rs. 588.19 crores during the year ended June, 1961. This was against an increase of Rs. 29.60 crores in 1959-60 and Rs. 19.79 crores in 1958-59 respectively. The lowest figure of annual increase in money supply so far had been for the year 1952-53 when it rose by Rs. 5.67 crores. This clearly indicates that the rate of monetary expansion in the economy has slowed down.

The slower rate of monetary expansion was notwithstanding the fact that Government sector, even after taking into account the offsetting effect of counterpart funds, exercised an expansionary influence of Rs. 10.79 crores during the year ended June, 1961 against a contractionary effect of Rs. 3.39 crores last year. The main reasons for the slower monetary expansion are:

(1) The accumulation of counterpart funds of the order of Rs. 26.41 crores.

(2) The increase in time deposits of Rs. 28.15 crores.

(3) The contraction in the foreign sector of the order of Rs. 11.95 crores against an expansion of Rs. 22.02 crores last year.

It is significant that money supply maintained a sharply upward trend during the first half of the year. In fact it rose at a faster rate during this period of the year than in the corresponding period of the preceding year. It went up by Rs. 30.64 crores in July-December, 1960 against Rs. 20.21 crores in the second half of 1959. During January-March, 1961 it remained virtually unchanged and in the last quarter registered a steep decline of Rs. 27.56 crores under the impact of a contraction in the foreign and private sectors. As against this the Government sector exercised a net expansionary influence of Rs. 11.88 crores during the quarter.

The slower rate of monetary expansion relative to the improvement in the availabilities is a highly welcome development. In fact this has been a principal objective of Government policy designed to meet the situation arising out of the persistent and protracted money creation process which had gone on in the earlier years. The growth of inflationary pressures in the past was associated with a sharp rise in money supply unaccompanied by a commensurate improvement in the supply of goods and services. The problem of excess demand was in fact two-fold; namely the stock problem and the flow problem. The stock problem had emerged from the fact that money creation in the economy had been excessive leading to acute scarcity conditions. The excessive monetary expansion was also affecting the balance of payments position. Excess demand in the home market tended to absorb the output which would have been otherwise exported. Inflation was also exerting pressure on the country's balance of payments by lowering the marketable surplus of foodgrains and by intensifying the propensity to consume and hold stocks. It further reduced the country's ability to export by pushing up the costs. Rising prices of domestic items entering into cost of production of export industries weakened their competitive power in export markets. In so far as resort was had to domestic price control and to the intensification of exchange restrictions the excess demand condition was not fully reflected in the price situation or in the balance of payments. Basically, both the rise in the domestic price level and the fall in the foreign exchange reserves sprang from the same source. The problem could only be solved by working off the excess purchasing power through improved availabilities. The flow problem which related to the subsequent rate of monetary expansion was tackled by adopting a policy of restraint in the fiscal field. The overall claims were adjusted to the available resources so as to ensure that money supply increased at a slower pace allowing availabilities to catch up. It must be realised, therefore, that what is being experienced today is not accidental. It is the result of deliberate Government policy which is bearing fruit.

The slower rate of monetary expansion has afforded material relief. In the first place it has made possible the relaxation of controls and a notable movement towards a "free economy". The liberal economic policies of which we feel so proud could not have been implemented without serious short-run repercussions, if the rate of monetary expansion had not slowed down and the excess demand had not been worked off adequately. With the basic improvement in the supply and demand situation, the rising trend in prices appears to have been halted and in certain cases reversed. The external situation has also been greatly helped by the slower rate of monetary expansion both by way of larger exports and lower import demand. It may even be argued that if the monetary expansion had continued at the rate it did in the past years, the degree of liberalisation which we have introduced might have caused a greater strain on the reserves. Domestic balance in supply-demand relationship exercised a natural restraint on import demand during the period when import policy was being progressively liberalized. Export situation was helped as domestic absorption of exportable items did not rise. If the monetary expansion had continued at the rate of past years, the liberalization of import policy could not be carried out without a substantial drain on reserves.

Lately, however, there have been some complaints from the business sector that demand is weakening and that business is not brisk. It is evidently concerned with such sensitive sectors as the stock market and import trade. Judging from the available indicators there is no clear evidence to suggest that the aggregate demand in the economy is on the decline. The prices of the cash crops, particularly those of jute, ruled high whereas the producers of the food crops continued to benefit from the price rise which became effective consequent upon the freeing of the food trade. On the industrial side, investment activity has been maintained at a very high level. Having regard to all these factors it seems likely that what we are experiencing today is in the nature of an adjustment. The adjustment process which was long overdue has been reinforced by a drop in the rate of monetary expansion and the sharp increase in availabilities by way of increased production and expanded flow of imports. The economic climate is thus undergoing a change as a result of these developments. While the situation seems to depict some resistence on the part of traders and producers to reduce prices, pressures are emerging from improved supplies. Inventories are said to have grown in an effort to stem the tide. On the other hand, there are indications that the psychology of the purchaser is gradually changing in view of the improved production and larger imports. As expectations are being reversed, possible consumption is being somewhat postponed in the hope of further price declines.

The State Bank has constantly advocated the avoidance of deficit financing and excessive creation of money and we are happy to note the outcome. I would, however, like to state that we do not suggest holding down monetary expansion for all times and under all circumstances. As the excess demand in the economy is absorbed by rising production and increased imports, the situation will have to be examined afresh. Money supply must expand normally to keep pace with the increasing requirements of a growing economy. As real incomes expand and transactions grow, money supply will have to increase to permit the functioning of the economy at its full capacity. We must appreciate that the achievement of monetary balance is a highly delicate operation. Just as too rapid a rate of monetary expansion tends to undermine economic stability, an unduly slow rate of monetary expansion, if continued for long, adversely affects growth impulses. Our ultimate objective is to achieve a well sustained and increasing rate of growth. For this we have to steer clear of both inflationary and deflationary pressures in the economy.

While we should keep a careful watch on future trends so that we make timely adjustments in our policy, a hasty move in the opposite direction can set at naught the progress which we have made towards a freer economy. It needs no emphasis that an orderly functioning of the economic system presupposes active competition and a return which is in proportion to risk-bearing, enterprise and efficiency. Abnormally high profits out of tune with the economic functions performed by entrepreneurs cannot survive the fresh air of economic freedom and competition. Prices should not always be expected to rise as in the past. They may move in both directions depending upon the forces of supply and demand.

Our approach regarding monetary expansion needs to be cautious but flexible. We should make sure that adequate funds are made available to the private sector to carry out its expansion plans smoothly. Activity should not be retarded in any way for lack of funds or purchasing power. We must, however, move with caution for two reasons. Firstly, the economy has just found some relief from inflationary pressures. Secondly, with the introduction of liberal economic policies, the economy has become much more open. If any pressures develop again, they would be reflected in the balance of payments situation and cause a drain on foreign exchange reserves. In the absence of domestic price control and with the operation of a liberal import policy, monetary pressures are likely to work themselves off through a rise in imports and increased domestic consumption of exportable goods. We must be careful that whatever we do in not going to endanger our progress towards a free economy. In short, our economic policies should be framed recognising the fact that our paramount need is to create conditions conducive to the maximum rate of economic growth in the framework of monetary stability and freedom from controls.

It is sometimes suggested that the present situation is simply the result of a credit squeeze imposed by the State Bank of Pakistan. This view seems to be based on a misunderstanding of the situation. It denotes a lack of appreciation of the fact that the present state of our economy has to be viewed in terms of the overall rate of monetary expansion and liberalized imports rather than an individual factor such as credit supply. The fact is that there has been a record expansion of bank credit during the past two years mounting upto Rs. 90 crores or 69 per cent above the level of June, 1959. The policy of the State Bank of Pakistan has continued to be liberal and realistic in overall terms. While seeking to ensure that credit expansion is not excessive and the monetary policy remains in harmony with the fiscal policy of Government, the State Bank has done all it could to see that the needs of our developing economy are adequately met and productive activity is fully financed. For this purpose, it has very materially increased its assistance to the commercial banks which attained a high level of Rs. 47.8 crores during the season. At the end of June, 1961 the State Bank of Pakistan loans to commercial banks stood as high as Rs. 33.7 crores compared to Rs. 1.1 crores at the end of June last year. These figures speak for themselves. The Bank has already decided that the credit limits of the banks under the Bill Discounting Scheme should be liberalised, particularly with a view to meeting the seasonal demand.

Our credit and monetary policy can by no stretch of imagination be termed restrictive. Reserve requirements specified by the State Bank are low, two per cent for time liabilities and five per cent for demand liabilities. The Bank Rate has not been raised despite the unprecedented demand for bank credit. It continues at 4 per cent since January, 1959. Even in respect of the selective credit controls which were imposed with a view to diverting credit to more essential sectors and to checking speculative activity rather than restrict the overall level of bank credit, the State Bank has maintained a most flexible approach. Some of these controls were relaxed last April in the case of East Pakistan. More recently the State Bank has abolished the restrictions on bank advances against stocks and shares of existing companies.

The State Bank has also sought to bring about a wider dispersal of bank credit so as to attack the problem of credit concentration and to ensure an adequate availability of funds for the small borrower. We have constantly encouraged credit institutions in this direction. It is gratifying to note that at least one major bank has adopted a scheme of small advances not exceeding Rs. 10,000 to a party at a concessional rate of 4 per cent. Under the scheme, a sum of about Rs. 1 crore has been loaned. It is my earnest hope that the other credit institutions of the country will follow this example and divert a larger flow of credit to this sector so as to meet the glaring inadequacy of credit for the small man. Government are also giving active consideration to a proposal for setting up a People's Finance Corporation with a view to providing increased credit facilities for small business men and traders.

While the State Bank has constantly worked for the rapid expansion and improvement of credit facilities to assist economic growth, the slower rate of monetary expansion has certain obvious implications for the banking system in an expanding economy. With the growth in the economy, demand for credit must expand. The banks can satisfy this demand only if their primary reserves continue to increase. However, a smaller rate of monetary expansion means a smaller flow of primary reserves to the banking system. Primary reserves are created either as a result of the monetization of the balance of payments surplus or through Government borrowing from, the Central Bank. If these two sectors become neutral or contractionary the banks must naturally seek to mobilise larger deposits from the public to be able to meet the credit demand. The only alternative to this effort would be for the banks to borrow increasingly from the State Bank. It is true that State Bank can provide funds but it must be recognised that like all Central Banks it is the lender of last resort. Undue dependence of the commercial banks on the Central Banks is by no means a desirable phenomenon. The banks have a great responsibility in the matter and should do their utmost to mobilise deposits resources on an increasing scale. In fact in extending future assistance to the banks and in determining its scale, the State Bank would, as a matter of policy, keep in view the efforts banks make and the success they achieve in attracting fresh deposits.