BUDGET 2021-22:
HIGHLIGHTS AND COMMENTARY

NASEEM FARAZ, MAHMOOD KHALID, SABA ANWAR,
SHAAF NAJIB and HANIA AFZAL

FISCAL POLICY CENTER
PAKISTAN INSTITUTE OF DEVELOPMENT ECONOMICS
ISLAMABAD

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1. INTRODUCTION

PTI government has presented its third budget. The incumbent Finance Minister was expected to spell out new directions of the government which are pro-growth and reflected with fiscal allocations that are in agreement with the Fund while encouraging the existing and new enterprises. At least from the Budget speech it appears he has been successful. However, a critical appraisal is required to qualify this stance.

Government has faced numerous economic challenges, aggravated by the Covid 19 Pandemic but the Government has successfully progressed from recovery and stabilisation to sustainable growth. Provisional GDP growth rate for FY 2021 is estimated to be 3.94 percent against the targeted growth of 2.1 percent. The Current account balance during Jul-Apr, FY 2020-21 had been in surplus of $0.8 bn (0.3 percent of GDP) against a deficit of $4.7 bn (–2.1 percent of GDP) in the corresponding year. This had been possible both by an increased export of 6.5 percent to $21.0 bn and remittances significantly growing by 29.0 percent to $24.2 bn. FBR tax collection grew by 14.4 percent to Rs 3,780 bn during Jul-Apr FY 2020-21 against Rs.3,303 bn last year and is expected to post a healthy Rs. 4,691 collection by the end of FY 2020-21. Government has posted a primary surplus for the first three quarters of FY 2020-21. This has enabled the government to resume the $6bn Extended Fund Facility and completed the second to fifth review under the program with IMF.

However the journey to growth from stabilisation along with unwarranted risks of Covid-19 is tough and requires an out of the box thinking. This is recognised by the government; Federal Minister for Finance and Revenue Mr. Shukat Tarin stated in his interview for PIDE Pre-Budget P & R Volume II, Issue VI *Tax, Expenditures, And Debt: Trica of Budget Challenges* "…Well I'm very impressed with the work that PIDE has done. We are making broad use of the recommendations which we have found over there. For instance, the growth areas, productivity, investment, vibrant cities, markets, openness, creativity, internet access and technology usage, those are the areas of growth and those are the, I would say, engines of growth". While the growth enablers are understood the approach towards these enablers still needs to step-up. PIDE Growth Commission has presented a detailed report titled "The PIDE Reform Agenda" to unleash Productivity, Investment, Vibrant Cities, Markets, Openness, Creativity, Internet Access, and Technology Usage.

2. EXPENDITURES

2.1. Current Expenditures

- Total current expenditures for the year 2021-22 are estimated at Rs 7,523 billion (see Table 4.1).
- As last year, the mark up in the current year is still driving the current expenditures with a 7.3 percent increase in 2021-22. The mark-up payments for the year 2021-22 have been estimated at Rs 3,059 billion, out of which Rs 2,757 billion would be paid on domestic debt and Rs 302 billion on foreign debt.
- The major component of the current expenditures is defense-related expenditure. This has increased to Rs 1370 billion. The growth in allocation for 2021-22 (5.7 percent) is less than the last year (11.3 percent).
- Regarding subsidies, there is a sharp rise of 58 percent for 2021-22. This is a huge burden for the government.

Table 4.1

Classification of Current Expenditures (Rs. Billion)

		Budget 2020-21	Revised 2020-21	Budget 2021-22
(i)	**Mark-up Payment**	2,946	2850	3059
	Domestic Debt	2,631	2611	2757
	Foreign Debt	315	239	302
(ii)	**Pension**	470	470	480
	Military	359	359	360
	Civil	111	111	120
(iii)	**Defense Affairs and Services**	1,286	1295	1370
(iv)	**Grants and Transfers**	904	932	1167
(v)	**Subsidies**	209	430	682
(vi)	**Pay and Pension**	0	158.4	160
Vii)	**Provision for Contingencies**	50		25
(viii)	**Running of Civil Government**	476	487	479
(ix)	**Provision of Disaster /Emergency/Covid**			100
	CURRENT EXPENDITURE (i to ix)	6,345	6560	7523

- Grants and transfers, Rs 1167 billion, have been estimated against a revised estimation of Rs 932 billion for the year 2020-21.
- For running the business of government, a lesser amount of Rs 479 billion have been estimated for the fiscal year 2021-22 against revised expenditures of Rs 487 billion in 2020-21.

2.2. PSDP Expenditures

- This is a development Budget. The government has allocated Rs 900 billion under PSDP. This is an increase of 40 percent.
- The figure presents the sectoral priorities for next year's PSDP allocations.
- The focus this year will be on food security (12 bn). These include locust emergency fund (1 bn), rice, wheat, cotton (2 bn) and olives (1 bn).
- Rs 91 billion for water resources which include Daso hydro power project (57 bn), diameter bhasha dam (23 bn), mehmand dam (6 bn) , neelum jehlum (14 bn).
- Public private partnership and PSDP plus has been introduced. This would involve the private sector in 50 projects worth Rs 2000 billion. Government will contribute Rs 61 billion as grant through viability gap fund. These will include roads, railways, logistics, science and technology, water etc.
- Though it is ideal allocation under given circumstances, there must be a cost-benefit analysis of the assigned projects.
- The government should prioritise projects of soft infrastructure, including health and education, for inclusive economic growth momentum.
- Currently, the allocation to the education sector is only 4 percent, and the health and population sector is 3 percent of total PSDP allocation.

2.3. Pension

- There is a considerable burden of pension on the government budget.
- The budget allocation for pension increased by 12 percent in 2019-20. This year the allocation has slightly increased from 470 billion in 2020-21 to 480 billion in 2021-22 with the slight growth of 2.1 percent.
- The pay and pension commission is working on a sustainable pension model.

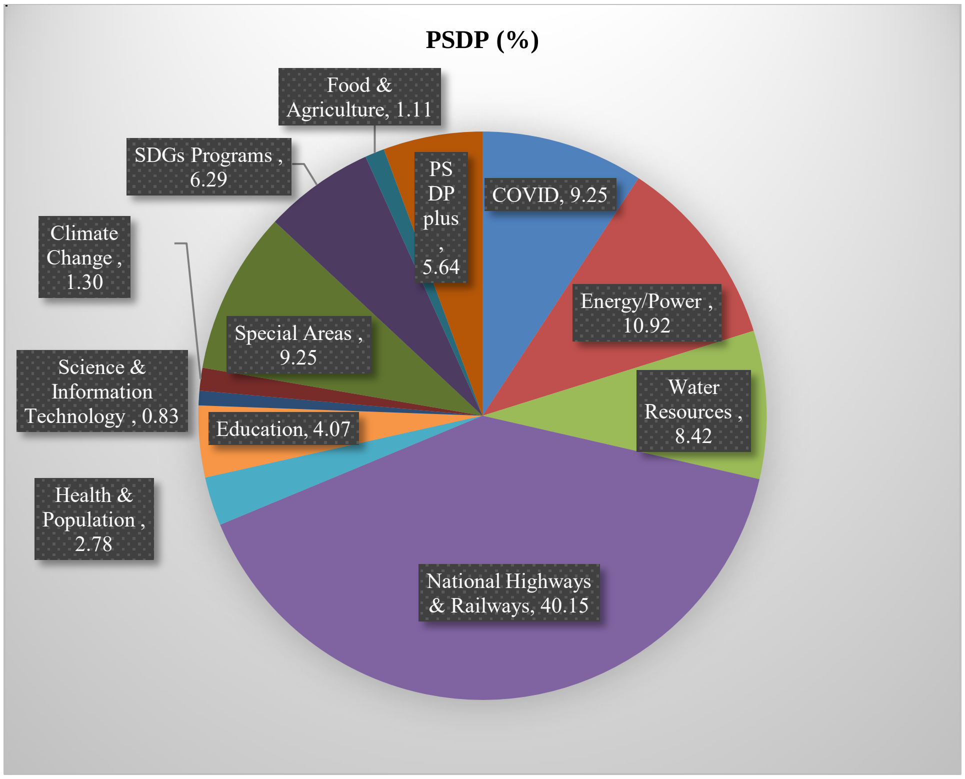
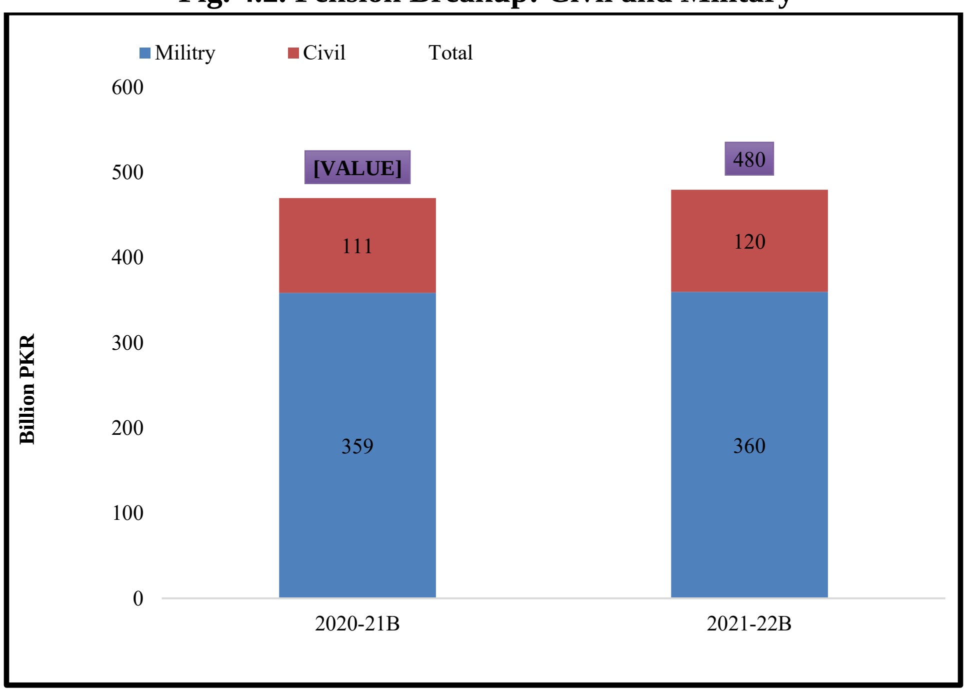


Fig. 4.2. Pension Breakup: Civil and Military



2.4. Social Protection

- The government has increased budget allocation for the Ehsaas program from 208 billion to 260 billion. The government has also allocated 68 billion to provide subsidies in energy, food, and other sectors with the focus to target the vulnerable segments only.
- To carry forward the stimulus package, the government in the current budget earmarked Rs 100 billion for Coronavirus-related schemes. The SME sector has been provided Rs 12 billion for loans and other schemes.

3. TAXES AND REVENUES

Tax and Revenues Federal Budget 2020-21 has presented an ambitious revenue plan (see Table 3.1). Considering the past performance, it is likely that the targets will be underachieved. Revenue forecasting models, if any, used by the Ministry of Finance and the FBR, always overestimate the expected revenue performance. The total tax collection grew by 6.1 percent in FY2020 against the meagre growth of 0.1 percent in the comparable period of FY2019. In absolute terms, tax collection stood at Rs 4,747.8 billion in FY2020 against Rs 4,473.4 billion in FY2019. Tax Revenue target for the FY2021 has been set at RS 5.83 trillion. Table 3.1 shows the composition of tax and non-tax revenue along with performance and target value for the next fiscal year.

Table 3.1

Tax Profile

Rs in Trillion	Yearly Profile						Missed Targets %			Targeted Growth %
	2018-19 BE	2018-19 RE	2019-20 BE	2019-20 RE	2020-21 BE	2020-21 RE	2018-19	2019-20	2020-21	2021-22
Total Revenues	5.66	5.03	6.72	5.50	6.57	8.49	–11.11	–18.05	–16.43	–2.7
Share of total revenues										
Total Taxes	86.36	87.33	86.68	76.46	83.13	68.69	–10.12	–27.72	–9.49	17.44
Total Non-tax Revenues	17.40	14.38	20.17	29.22	25.00	23.57	–17.37	44.89	–1.68	29.17
FBR Revenues	78.35	82.48	82.71	71.00	75.50	67.99	–6.43	–29.65	–9.9	20.32

- The revenue collection target has been set at Rs5.83 trillion for the upcoming fiscal year 2022 and is less than the IMF recommendations of Rs6 trillion. This collection, if achieved, would be a 24 percent increase in YoY on the Rs4.7 trillion target surpassed by the revenue collection agency FBR. The non-tax collection target will be set at Rs1.42tr, an increase of 22 percent. The proportion of provincial taxation would be Rs3.41tr, thus an increase of 25 percent revenue given to provinces. The government spending would increase to Rs8.497tr from Rs7.341tr, an increase of 15 percent in the Fiscal Year 2021-22.

- The share of the total taxes in the revenues is around 75 percent. Last year it went exceptionally high to around 84 percent due to the increase of economic activity. The FBR contributes around 80 percent of the total revenues of the federal government; therefore, any miscalculation or miss targeting can severely cripple the budget, not just of the federal but the provincial governments as well.

Table 3.2

Revenue Performance and Revenue Targets

	Description of Revenue Source	Target Achievements 2018-19	2019-20	2020-21	Targeted Growth % 2021-22
Tax Revenues					
A.	FBR Revenues	–6.43	–29.65	–5.48	17.44
.	Direct Taxes	–4.38	–22.04	–12.43	6.80
	Taxes on Incomes	–3.41	–21.95	–12.42	6.85
	Workers Welfare Fund	–77.54	–49.54	81.22	102
	Capital Value Tax (CVT)	–49.73	–38.00	–81.57	–79.3
ii.	Indirect Taxes	–7.74	–34.21	–0.61	24.89
	Custom Duties	0.00	–45.43	9.37	22.65
	Sales Tax	–12.35	–32.30	0.41	30.58
	Federal Excise	0.38	–14.48	–23.83	–1.38
B.	Other Taxes	–46.24	12.46		
	Other Indirect Taxes		90.64		
	Mobile Handset Levy	–80.05	33.33	–13.79	55.17
	Airport Tax	–66.67	–51.43	20	100
	GIDC	–75.00	–63.33	66.66	766
	Natural Gas Development Surcharge	–50.00	0.00	170	260
	Petroleum Levy	–32.22	20.36	11.11	35.55
Non-Tax Revenue		–1737	44.89	5.85	29.17
A.	Income From Property and Enterprise	20.37	–9.79	–15.9	26.16
Out Of Which	Pak. Telecommunication Authority	0.00	544.90	25.21	70.46
	Total Markup	2.46	–57.59	–16.82	4.44
	Dividends	–20.75	–26.97	–33.86	48.18
B.	Receipts from Civil Administration and Other Functions	–44.21	87.87	12.68	5.96
Out of Which	Surplus Profit of SBP	–47.36	93.32	12.90	4.83
C.	Miscellaneous	–20.58	25.40	7.38	51.25

Table 3.3

Interprovincial Fiscal Relations

	Yearly Profile					Target Achievements (%)		Growth (%)
	2019-20 BE	2019-20 RE	2020-21 BE	2020-21 RE	2021-22 BE	2019-20 MT	2020-21 MT	2020-21 RE
FBR Revenues (PKR. Trillions)	5.56	3.91	4.96	–5.48	17.44	–29.65		
Provincial Share in Federal Taxes %	58.59	61.47	57.90	–5.9	18.72	–26.19		

- Provinces get around 59 percent of the FBR revenues as fiscal transfers. Such a small figure has resulted in the underperformance of FBR in the past two consecutive years. The provinces suffer immensely if the federal transfer is lower than expected. In case of lower federal transfers and limited or no options of borrowing Provincial service delivery suffers badly.
- This year the FBR revenue targets are expected to grow to RS 5.8 trillion that is 23percent higher as compared to the estimated collection of Rs 4.7 trillion in FY 20-21

Salient Features

- On the revenue front, targets are once again ambitious and stringent, possibly leading to an increased debt burden. The government is expected to achieve this by focusing on broadening the tax base through augmented documentation as opposed to introducing various new major taxes.
- The government has reduced sales tax on locally manufactured cars from 17 percent to 12.5 percent. The government has also exempted Federal Excise Duty (FED) on 850cc cars and will slash duty on electric cars.
- The government was introducing third-party audits which would thwart the FBR harassing any individual or business entity. Those who are found guilty of evading taxes or deliberately hiding their income will be fined severely.
- Through the Finance Bill, 2021, the threshold of monthly electricity bill has been reduced from Rs75,000 to Rs25,000 for the purpose of levying withholding tax at the rate of 7.5 percent. However, this tax will not be applied on persons who filed their

annual income tax returns and are on the ATL issued by the Federal Board of Revenue.

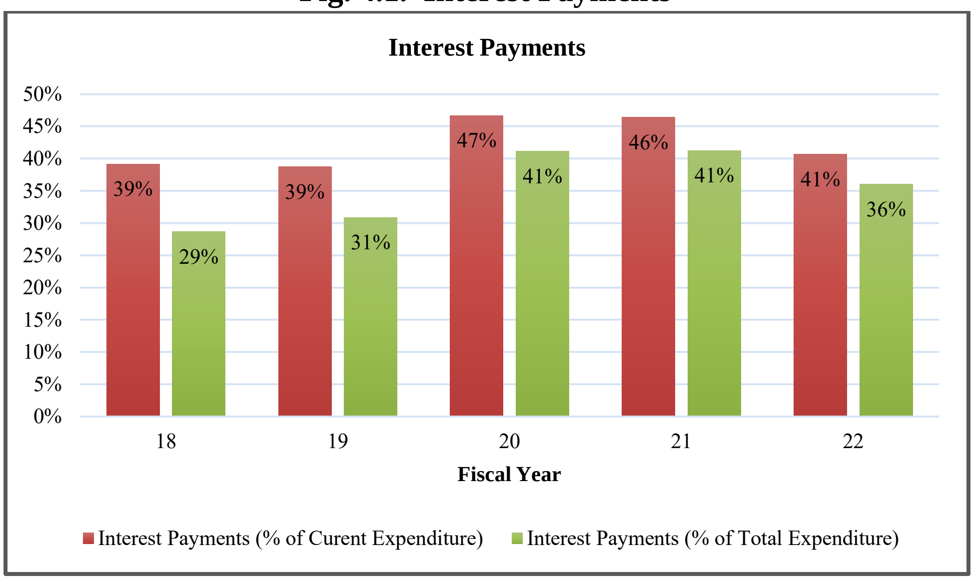
- The finance bill proposed to tax profit on the debt component of GP fund and other such funds. The finance bill also proposed to withdraw personal income tax exemptions.
- The specified goods when supplied within the limits of the Border Sustenance Markets, established in cooperation with Iran and Afghanistan, will be completely exempted from the sales tax.
- withholding taxes on mobile phones, will be reduced to 10 percent at first and then 8 percent later from 12.5 percent
- The rich will be asked to pay taxes in accordance with their wealth, So the salaries class will not be burdened with additional taxes.
- Custom duty from vaccine and medicines of livestock abolished to promote the livestock sector.
- Tax exemption on paper used for Quran publication, auto-disable syringe, and oxygen cylinders.
- Tax collections saw an 18 percent increase last year as the country crosses the limit of Rs4000 tax collection. 75 percent more tax refunds were made this year.
- Provincial share in the federally collected taxes to stand at Rs3,411 billion. Provinces share in NFC increased, to receive extra Rs707bn.
- Sugar included in the third schedule of sales tax act, helping in the elimination of artificial hike in prices of the commodity.
- The Federal Board of Revenue (FBR) has been tasked to collect an additional revenue of over Rs1 trillion in budget 2021-22 over the current fiscal year’s collection. This additional revenue will be achieved through the withdrawal of exemptions in sales tax, income tax, minimising concessionary tax rates as well as through growth in economy and inflation.

4. DEBT AND FINANCING

- The federal government's total debt and liabilities reached a staggering PKR 37,078.5 billion by the end of April 2021. This is just an under PKR 2000 billion increase from June 2020, when the federal government total debt and liabilities amounted to PKR 35107.1 billion.

- Against the total planned expenditure of PKR 8487 billion in Fiscal year 22, PKR 3060 billion have been allocated for interest payments. As a result, 41 percent of the government's Current Expenditure (PKR 7523 billion) will be spent on interest payments. This equals 36 percent of the total expenditure for the year.
- Interest payments take up a massive portion of the budget expenditure, however, a 5 percentage point proposal of decrease can be seen in interest payments share in current expenditure as well as a 5 percentage point decrease as a share of total expenditure, as shown in figure 4.1 for the upcoming budget FY 2021-22. This will allow the federal government a fiscal space to allocate more funds on development expenditures and other growth-oriented measures of the budget. However, given our debt now has significant long term commitments the interest cost may not fall. Last year saw a substantial decrease owing to G20 relief and lowered interest rates.

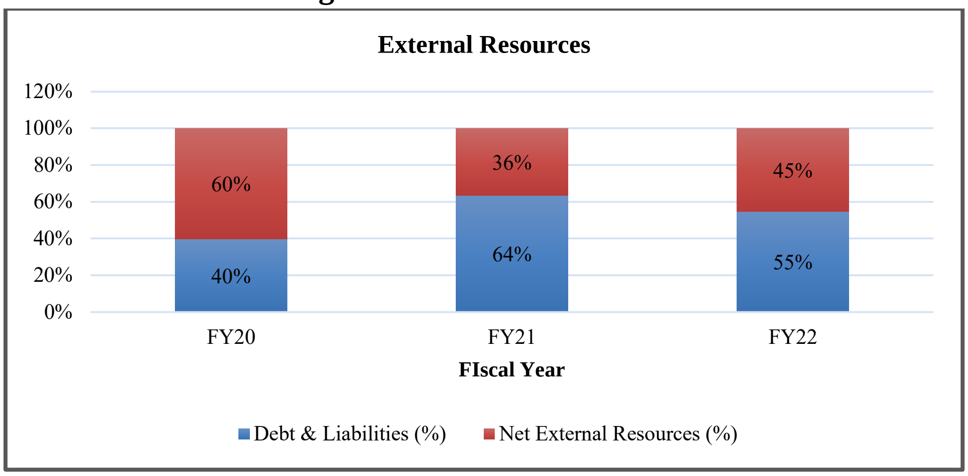
Fig. 4.1. Interest Payments



- The federal government expects to raise over PKR 2.7 trillion from external resources, including PKR 2.69 trillion from external loans. This will increase the gross external resources in the upcoming fiscal year by over PKR 0.5 trillion.

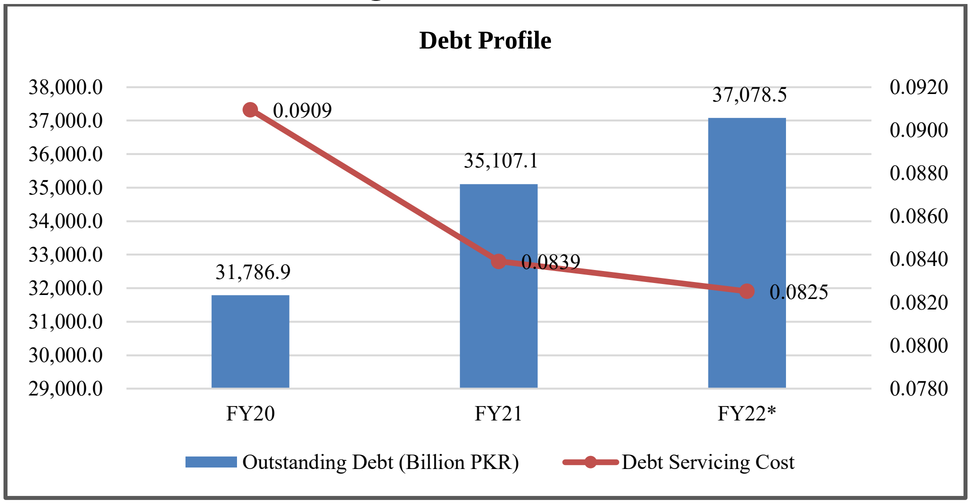
- 55 percent of the external resources raised will, however, be used for repayment of foreign loans and credits. This represents a 9-percentage point decrease in external resources share set aside for foreign loans and credit repayments. Although it is still higher than the share in Fiscal Year 2020, when 40 percent of external resources were used for foreign loans and credit repayments. That was possible primarily due to rescheduling of debt payments following the coronavirus pandemic. (Figure 4.2).
- This also is an indicator of better fiscal space available to the government in the upcoming fiscal year, which is evident through other policy reliefs provided in the budget as well as an increased development expenditure.

Fig. 4.2. External Resources



- As mentioned above, Pakistan's debt and liabilities increased by nearly PKR 2000 billion (2 trillion) in the 10-month period from July 20- Apr 21. It is expected to further increase by the end of the current fiscal year on 30 June 2021. Despite increasing debt and liabilities, Pakistan's debt servicing cost is on a downward trend, as shown in Figure 4.3. The final debt servicing cost for the upcoming year should further drop once the debt and liabilities figures for the entire Fiscal Year 21 are known.
- This represents a decreasing cost of debt despite increase in debt, providing the federal government some sigh of relief allowing them to improve spending on other developmental avenues.

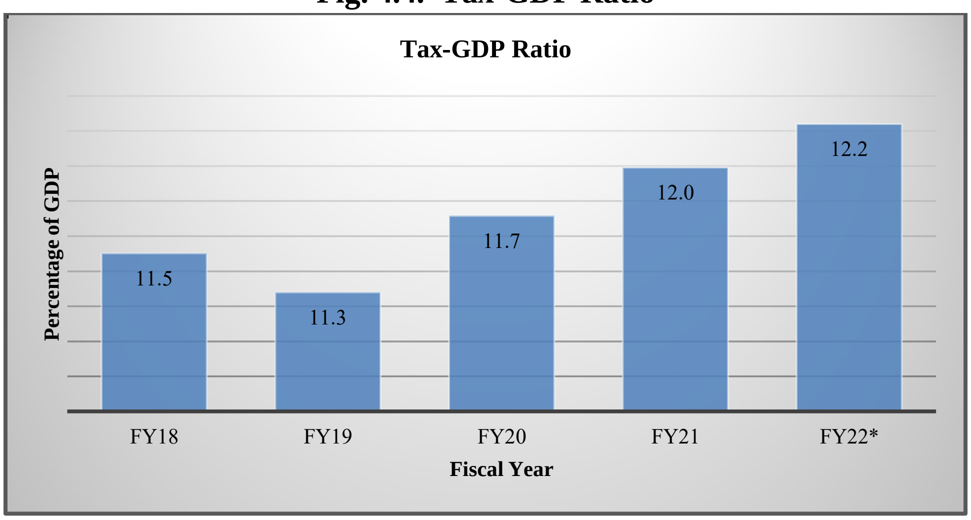
Fig. 4.3. Debt Profile



*Estimated using data up till April 2021.

- Tax Revenue-GDP Ratio has remained constant over the past few years, as shown in Figure 4.4.
- Tax Revenue target has been set at PKR 5839 billion, while the GDP is expected to grow at 4.8 percent. This will take the nominal GDP to PKR 47, 709 billion by the end of the upcoming financial year.
- If both these are achieved, the tax-revenue-GDP ratio is expected to increase to 12.2.

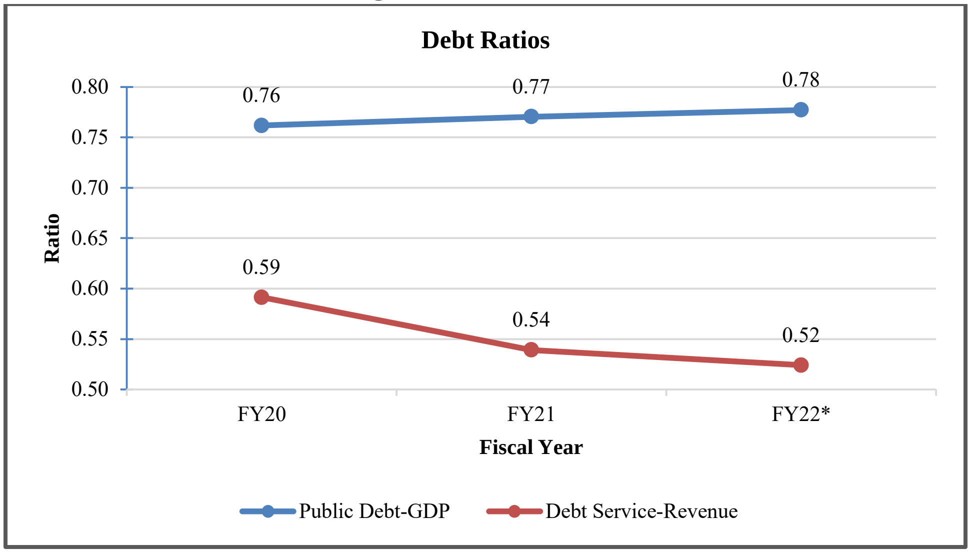
Fig. 4.4. Tax-GDP Ratio



*Projected for upcoming financial year.

- Government's debt policy statement identifies sustaining Public Debt-GDP and Debt Service-Revenue ratios important for sustained growth.
- It aims to do the above by a combination of measures including revenue mobilisation, rationalisation of current expenditure and efficient utilisation of debt.
- As shown in Figure 4.5, the Public Debt-GDP ratio is rather constant, but the Debt Service-Revenue ratio is showing a downward trajectory. This, coupled with a slightly improving tax-GDP ratio along with a falling debt servicing cost is a good beginning to sustain debt levels in coming years.

Fig. 4.5. Debt Ratios



*Public Debt-GDP Estimated using data up till April 2021.

- The government has indicated not only aiming to sustain the growth, but to also aim for high levels of growth rate in the economy. PIDE's Reform Agenda for Accelerated and Sustained Growth also highlights the need to grow at higher rates to be able to sustain debt levels as well as create opportunities for the new entrants in the labour force.
- While there is still a lot to be done to achieve a sustainable high level of growth for a longer period, on the debt front the initial indicators suggest that we are moving in the right direction and must continue improving in this aspect as well.

5. CONCLUSION

Government has faced numerous economic challenges, aggravated by the Covid 19 Pandemic but the Government has successfully progressed from recovery and stabilisation to sustainable growth. Provisional GDP growth rate for FY 2021 is estimated to be 3.94 percent against the targeted growth of 2.1 percent. The Current account balance during Jul-Apr, FY 2020-21 had been in surplus. The FBR tax collection grew by 14.4 percent during Jul-Apr FY 2020 and is expected to post a healthy collection by the end of FY 2020-21. Government has posted a primary surplus for the first three quarters of FY 2020-21. This has enabled the government to resume the $6bn Extended Fund Facility and completed second to fifth review under the program with IMF. However, the journey to growth from stabilisation along with unwarranted risks of Covid-19 is tough and requires an out of the box thinking.