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Reforming the Federal Public Sector Development Programme

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PREFACE

Public Sector Development Programme (PSDP) is an instrument to implement the Govt's development priorities. Federal PSDP is aligned towards objectives / Targets of Annual/Five-year plans/ Vision. The Government provides infrastructure, builds up national capital, develops human capital, initiates various sectoral programme. Public investment has a multiplier effect on economic growth. It impacts the private sector investment, leverages potential of the economy for creation of much needed social goods and acts as enablers of private investment. The economically and financially viable projects are prioritised and financed under PSDP. Efforts are made to utilise scarce public resources optimally and efficiently to attain long run sustainable development goals.

However, evidence suggests that public investment could not succeed to act as a driver of economic growth. One of the key reasons for insignificant impact of PSDP on economic growth is drastic decline of development expenditure. The development expenditure was 7.5 percent of GDP in 1992, it shrunk to 2.5 percent of GDP in 2000 and further declined to 1.7 percent of GDP in 2020 and currently, it is around 1 percent of GDP. The inclusion of new projects in PSDP each year increases throw-forward effect. Thin allocation to large number of projects, resulted in cost-overrun and time overrun of the projects. Resultantly, the economically and financially viable projects become unviable due to delay in their implementation. The data indicated that among Nos. 931 on-going development projects, 16 percent (Nos. 148) development projects are subject to cost overrun. Whereas 59 percent (Nos. 551) projects are facing time overrun. Financing the PSDP through Foreign assistance, on account of resource scarcity, needs a counterpart allocation. The commitments of foreign funding for these projects, often, are not fully realised which jeopardise the overall project portfolio and increases pressure on domestic resources.

In order to support this infrastructure led development, the institutions have repeatedly been weakened and their role in policy planning reduced. There is immediate need of portfolio cleaning and other measures to make the existing portfolio smart. This study furnished its recommendations including Portfolio Cleaning, Project Completion/ Closure Facility, Creating Additional Resources for Rapid Completion of Projects etc.

Shahid Zia Cheema
Chief, Growth and Employment

INTRODUCTION

Federal Public Sector Development Programme (PSDP) is an important policy instrument for planning public investments to achieve socio-economic objectives. It enables private sector investments and creates spillover impact for leveraging potential of the economy for promotion of much needed social good. Development policy in Pakistan has been built on the development philosophy of the Haq/HAG Model. While this approach proved beneficial in initial times but over time this has resulted in an excessive focus on brick and mortar infrastructural development while the software of economy continued suffering (PIDE, 2020). The institutions have been weakened and their role in policymaking reduced, overtime.

One of key functions of Planning Commission is to formulate Annual Development Programme. Public Sector Development Programme (PSDP) which is an integral part of public sector investment and reflects Govt's economic priorities. In order to support this infrastructure led development, this instrument is aligned towards objectives / targets of annual / five year plans / vision 2025 through implementation of viable projects.

Table 1

Process of PSDP

➢ Development Budget Call Circular	(Nov. of current year)
➢ Indication of overall size of budget by FD	(Start of April)
➢ IBC for Ministries/Division	(Mid of April)
➢ Priorities Committee	(Mid of May)
➢ APCC	(8-10 days before budget)
➢ National Economic Council	(4-5 days before to budget)
➢ Approval of Annual Plan & PSDP by Cabinet	(A day before budget)
➢ Approval by the Parliament with Finance Bill	(End of May or June)

While formulating Annual PSDP, a development budget call circular is floated every year indicating the strategy to formulate PSDP for respective year (a template is Annex-I). The PSDP is formulated in accordance with the procedures and templates defined in the Manual for Development Projects. The common key feature repeated are following:

- *Basic infrastructure development;* for social service delivery (schools, hospitals etc.)
- *Human Resource Development;* how to develop, hire, motivate and retain the best human resource of the country.
- *Growth Enabler;* communication network, close coordination, alignment with policies, plans, programmes, projects and should be aligned with National Goals etc.
- *Balanced regional development;* such as spending more in backward areas.

After the introduction of *Public Financial Management (PFM) Act 2019*, no un-approved scheme will be financed through development budget which in earlier PSDP formulations have been blatantly done. As per NEC decision, a proper feasibility is required on PC-II form for projects costing over Rs 500 M. Further, it was also decided for PSDP 2021-22 that all development portfolios or investment should be reflected in

PSDP and during the Fiscal Year funds may not be transferred to non-development expenditure and maximum resources will be provided for on-going projects (not less than 80 percent), preference will be given to less developed areas of the country and those on-going projects which has 80 percent plus expenditure will be fully financed. Finally, all new projects are provided funds as per available fiscal space.[1]

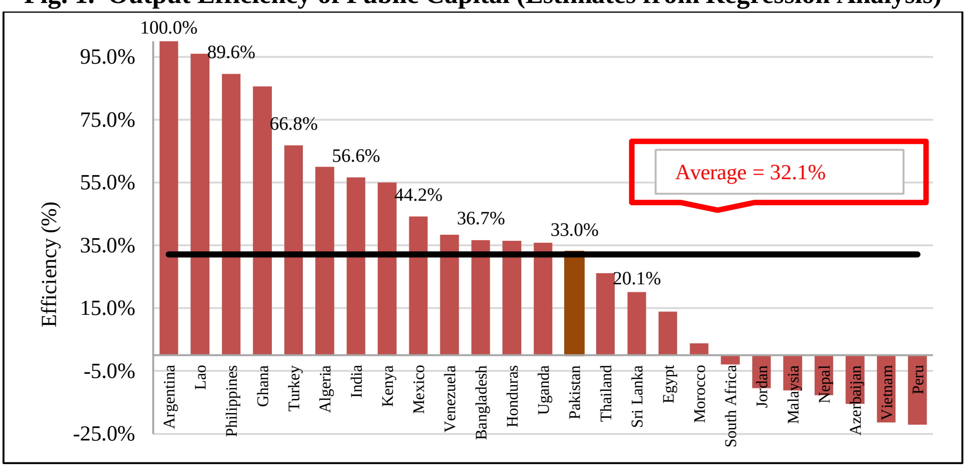
The Development Conundrum

The critical questions remain such as; I*s PSDP leading to desired economic growth? Is there adequate financing arrangements for throw forward of projects? What is the average lifecycle of projects? etc*. With the current pace of population growth rate, the country direly needs an enhanced economic growth rate, the role of PSDP becomes very important however, there is empirical evidence that Public sector investment multipliers are small and insignificant. Therefore, a project level analysis is required for answering these and other critical questions. In the present study we have analysed the federal PSDP allocations data from 2011-12 to 2020-22 to identify key areas where reforms are critically needed. Based on these, a complete road map for PSDP reforms is provided at the end of this report which can be taken as a blueprint for way forward in achieving the desired growth rates.

PUBLIC INVESTMENTS AS ENGINES OF GROWTH

Low productivity of public investment is also reflected if we compare the output efficiency of Public Capital across sample of LDCs. Pakistan appears to be around the average (33 percent only). Evidence suggests that public investment has unsuccessful to act as a driver of economic growth. As the allocations becoming more and more political than developmental, the effectiveness and efficiency of PSDP continue falling down. This has severely dented the PSDP's effectiveness.

Fig. 1. Output Efficiency of Public Capital (Estimates from Regression Analysis)



Source: *Doing Development Bette, 2020* (page 30).

[1] Dr. Muhmmad Afzal, Advisor MoPD & SI "Budget Formulation Process-PSDP" presentation at *Doing Development Better: Analysing the PSDP*, PIDE conference, 27th February, 2020.

Instead of a balanced approach, higher investment in few sectors have made the investment less productive or shifted to the decreasing returns to scale side position. This can be seen from the Table 2 below:

Table 2

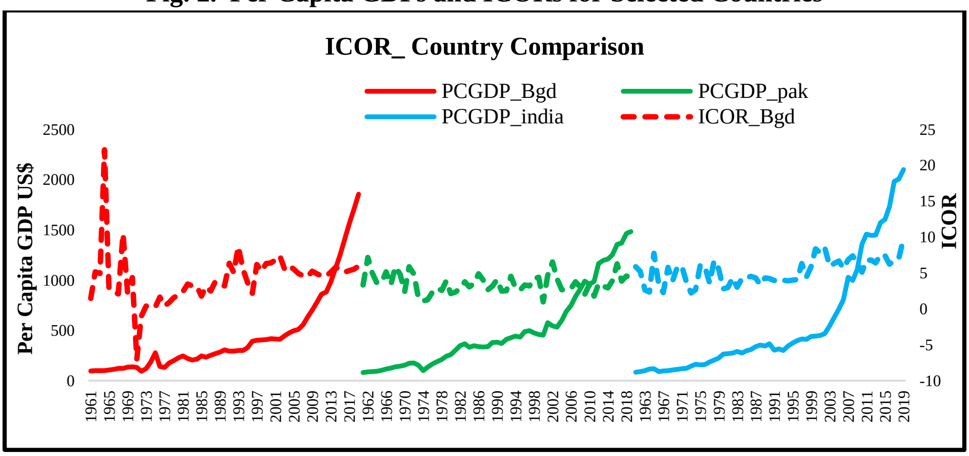
Sectoral Growth and Investment Rates (Average 2001-2017)

	Growth (%)	Investment Rate (%)	ICOR
Agriculture	2.2%	16%	7.27
Mining	2.7%	16%	5.88
Manufacturing	4.6%	18%	3.93
Electricity and Gas Distribution	0.0%	40%	830.09
Construction	3.7%	65%	17.28
Wholesale and Retail Trade	3.9%	2%	0.40
Transport and Communication	3.6%	20%	5.49
Finance and Insurance	4.0%	7%	1.85
Housing	3.3%	40%	12.10
Others	5.7%	33%	5.77
GDP	**3.5%**	**18%**	**5.33**

Source: *Doing Development Better, 2020* (p. 25).

There seems to be a disconnect in levels of investment and the corresponding ICORs. From the above table it can be inferred that lower ICOR sectors should attract higher investment for better growth outcomes, thus defining the development budget priority areas however this is not practiced.

Fig. 2. Per Capita GDPs and ICORs for Selected Countries



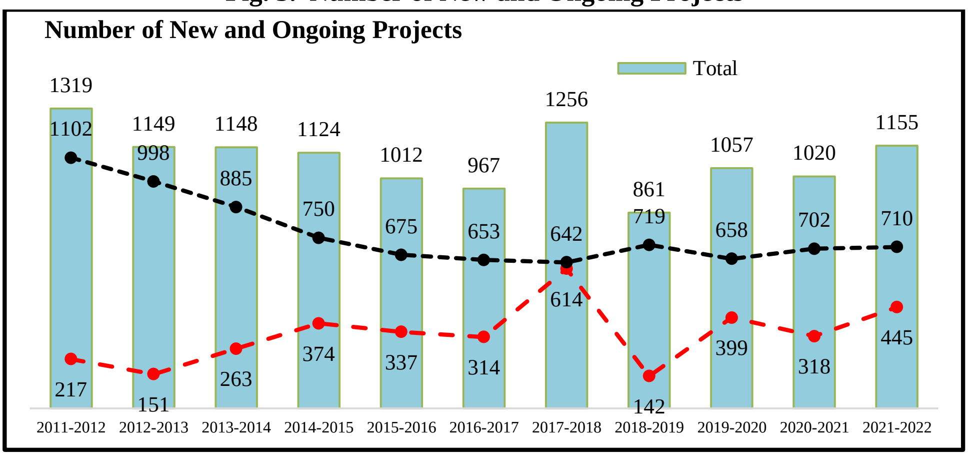
Author's estimation using WDI Data.

Pakistan ICOR has been declining overtime as compared to other countries of region. Apparently, this shows the overall miserable position of investment in Pakistan but importantly, when countries are compared for ICORs at the current level of per capita GDP, it appears that Pakistan is far below its potential. It is good for Pakistan because increasing investments can boost per capita incomes at a greater rate, compared to those countries which are at higher levels of per capita incomes/development and with higher ICORs. This represents a unique opportunity for development spending and foreign direct investment where both economic growth and higher rates of return can both be achieved, simultaneously.

PSDP Allocations Analysis—Pakistan

Overall number of projects executed has been running very high. It makes the allocations thin and project monitoring and evaluation a daunting task. In our sample of PSDPs (2011-12 to 2021-22) highest number of projects were seen in the FY 2011-12 i.e. a staggering project portfolio of 1319 projects. Further, if we see in Figure 3 below for FY2021 it was 1000+ (1020) and in FY2021 it is 1100+ (1155). One of the major reasons for such big PSDP portfolios is presence of ongoing projects. These are almost 60-70 percent of the PSDPs. Hence, leaving very small room for accommodating emerging needs for the development spending. This warrants the effectiveness and economic efficiency of PSDP. Thus, creating a need for portfolio cleaning and other measures to make the existing portfolio smart and efficient.

Fig. 3. Number of New and Ongoing Projects



On the operational side numerous PSDP projects are approved and initiated without any proper financing plan or availability of required funds. Despite allocation, government is unable to provide adequate financial support to these projects, timely which not only builds the throw-forward but also causes delay and cost overrun in the projects. Each year new projects are included even though existing throw forwards have become huge and needs a moratorium on new projects. From Figure 4 below it can be seen that at present, the throw forward is approximately 6.54 trillion rupees (FY 2022) and shows an increasing trend. Assuming an average allocation of Rs 600 Billion annually would require around 11 years for financing only the cost of ongoing projects, at current market prices and if no new project is initiated. It can also be seen a galloping trend in increase in total costs and throw forward of projects in the PSDPs but very slow increase in revised allocations for catering to the financing needs of these projects.

Fig. 4. Total Cost, Throw Forward, Revised Allocation (in Trillions)

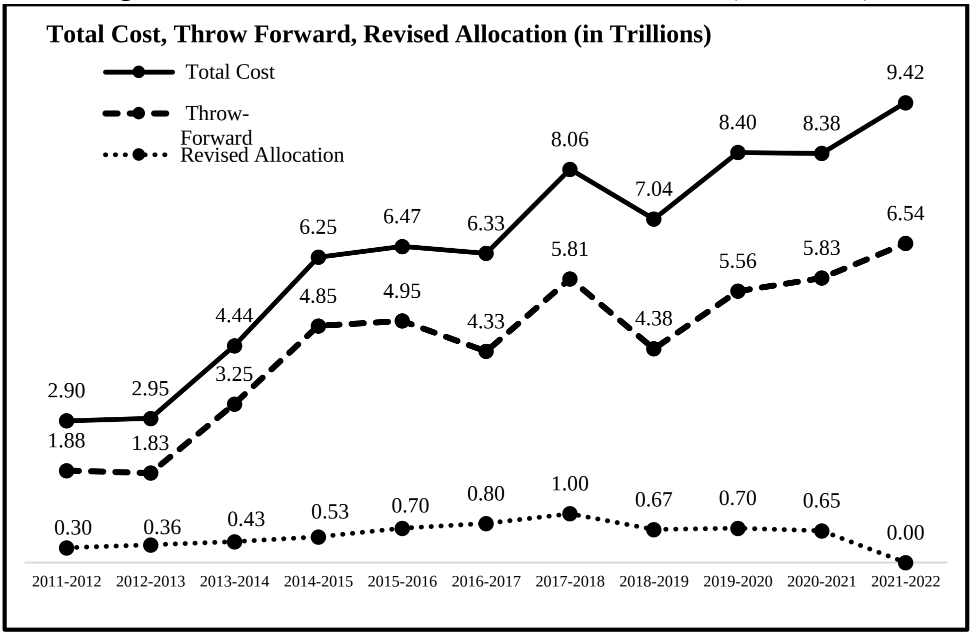


Figure 5 shows that major thrust of throw forward have been mainly driven by unmet financial needs of ongoing/older projects. Whereas, the allocations have not been keeping pace with increase in total throw forwards. Out of the 6.54 trillion total throw forward, about 4.4 trillion rupees (68 percent) is because of the ongoing projects.

Fig. 5. Throw Forward Ongoing/new Projects

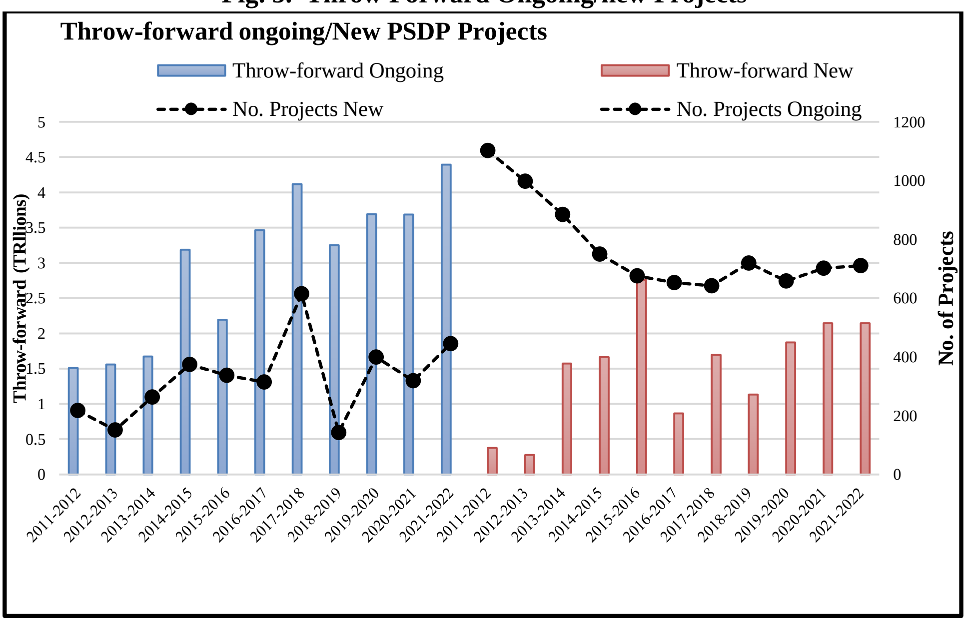
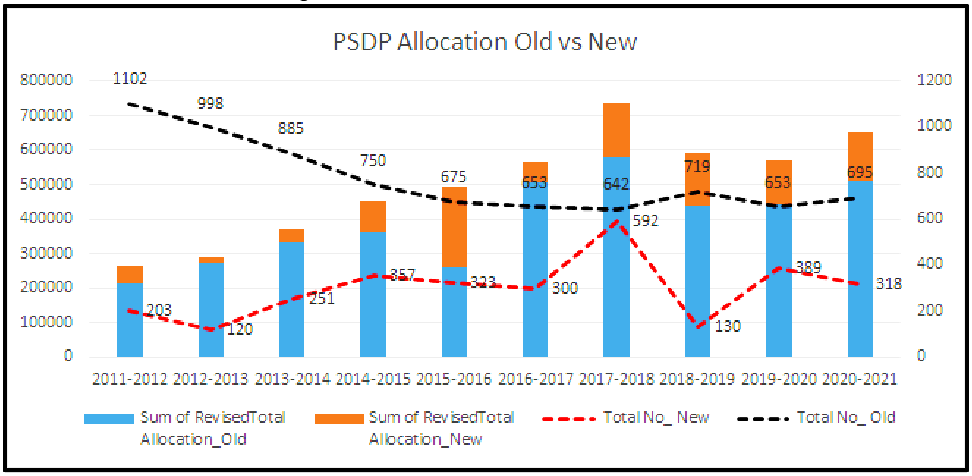


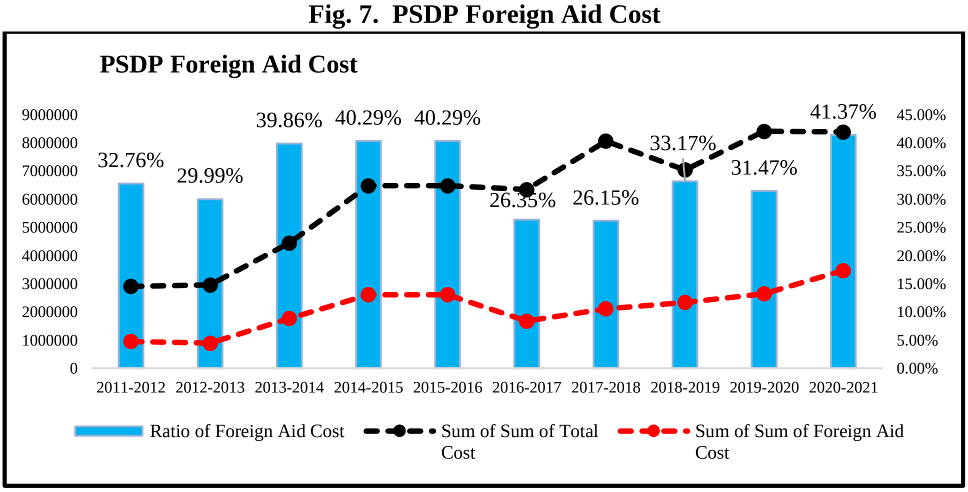
Fig. 6. PSDP Allocation Old vs. New



If we look at the allocations for ongoing and new projects then it appears the current government has been financing ongoing projects adequately vs. the previous governments in which random behaviour is seen (See Figure 6). However the number of new projects in each PSDP appears to be about around one third of total projects financed. This creates throw forwards for next years which needs to be profiled, properly, for efficient financing of these projects.

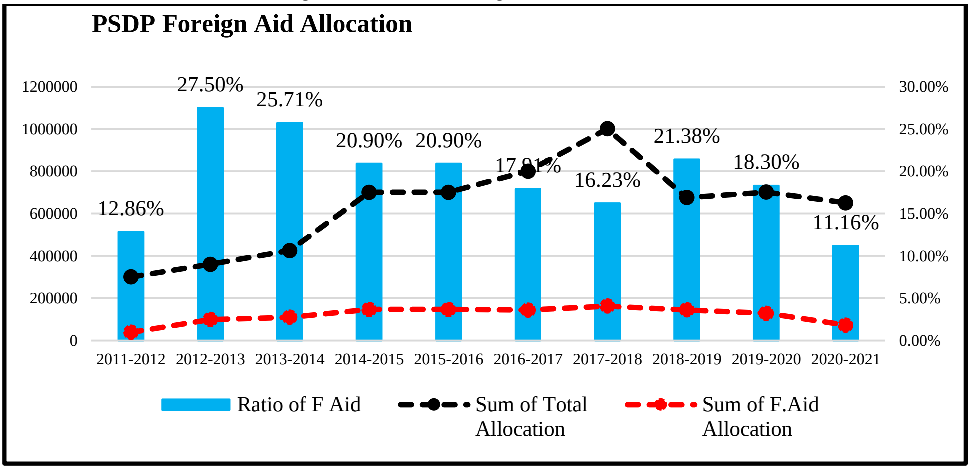
Another important issue is the financing for the PSDPs. Federal PSDP, overtime, has become dependent on Foreign Project Aid. This shows resource scarcity and lack of local ownership in overall PSDP formulation. These Projects are not fully funded by foreign resources hence needs a counterpart allocation too. Ironically the commitments in foreign funding for these projects do not fully realise. This jeopardise the overall project portfolio progress and increases charge on local resource allocations., The foreign Aid cost of projects have been increasing and it stands more than 41 percent for FY2021, as it can be seen from Figure 7.

Fig. 7. PSDP Foreign Aid Cost



When it comes to actual allocations then counterpart funds for foreign assistance fell short of commitment. This leads to time and cost overrun in projects as well as put extra pressure on already scarce domestic resource for funding these expenditures. The PSDP foreign aid allocation as compared to overall cost share has been declining for FY 2021 it was just 11 percent, as it can be seen from Figure 8.

Fig. 8. PSDP Foreign Aid Allocation



Lastly, the overall federal PSDP is focusing on too many sectors (around 40), each year, with a huge number of projects to execute with a sizeable throw forward. Few of these sectors have been devolved to the provinces after the 18th amendment but these sectors are still funded from the federal PSDP.

Fig. 9. Sectoral Allocation-Health

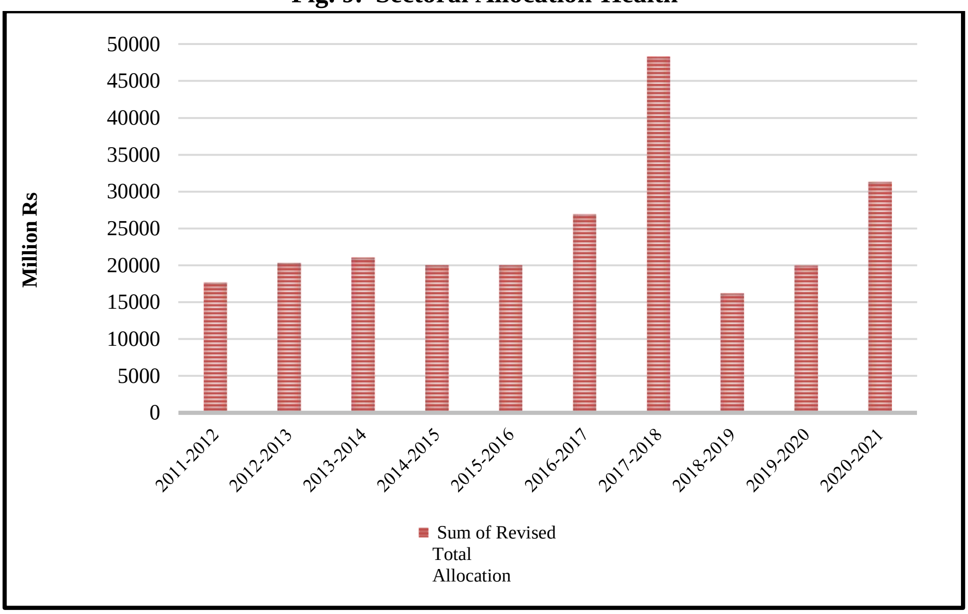
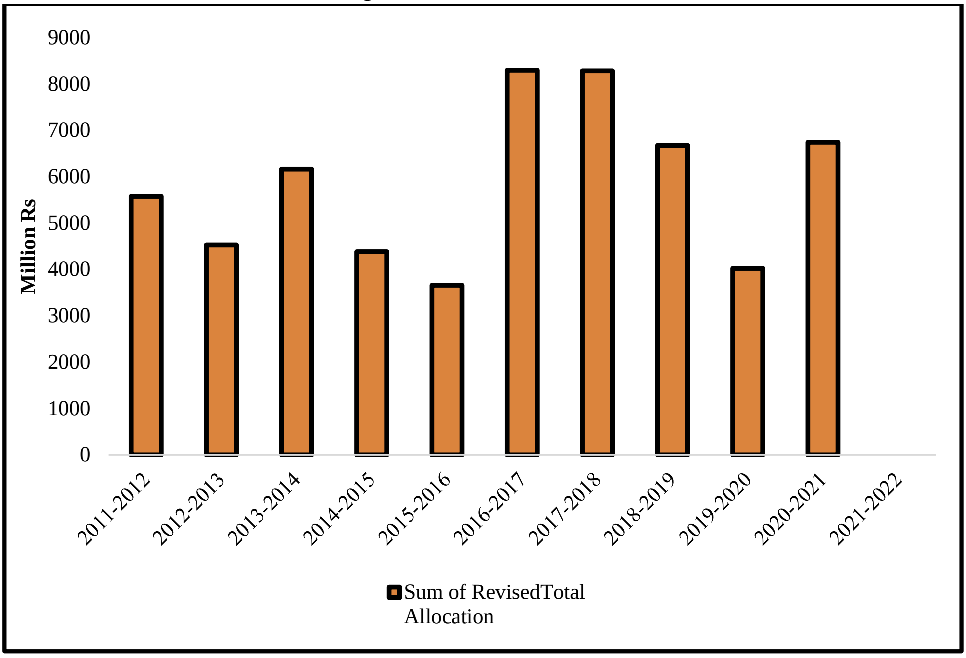


Fig. 10. Education Sector



Bucket Analysis

As described in Table 1 (process of PSDP), each year in April an Indicative Budget Ceiling (IBC) is communicated to the respective ministry. Ministry proposes a bucket of new projects along with ongoing projects as financing needs for targeting its sectoral objectives. A critical analysis is done to empirically identify the average age of these buckets comprising of new projects for a sample of three important sectors; Water, Energy and Transport and Communication for the years 2011-12, 2012-13, 2013-14 and 2014-15. Table 3 provides the Financial Analysis of these buckets.

Table 3

Financial Analysis

Sector	Bucket	Total Cost (Billion Rs)	Annual Decay (Billion Rs)*	Age of Bucket (Years)*	SD	CV	Project Min Cost (Billion Rs)	Project Maximum Cost (Billion Rs)
Transport & Communication	2011-12	104.04	8.77	11.24	29.85	0.65	0.215	24.137
	2012-13	170.59	20.02	9.19	62.66	0.85	0.053	55.488
	2013-14	172.84	8.75	12.24	44.53	0.70	0.001	60.590
	2014-15	997.73	142.18	7.35	372.40	0.92	0.010	353.960
Energy Sector	2011-12	16.5	1.173	15.34	4.51	0.41	0.08	8.90
	2012-13	0.12	0.089	2.40	0.06	0.8	0.04	0.08
	2013-14	1240.4	41.63	29.87	116.37	0.11	0.04	958.73
	2014-15	430.43	35.345	3.90	142.15	1.80	0.03	150.00
Water Sector	2011-12	159.16	14.29	11.09	50.90	0.70	0.005	61.067
	2012-13	45.63	4.6797	8.13	17.54	1.42	0.006	32.778
	2013-14	57.54	4.43	7.23	18.11	1.83	0.230	32.778
	2014-15	27.71	1.3095	11.56	12.56	0.42	0.013	1.124

* Annual Decay is the slope of trend line fitted and Age of the Bucket is the Y-intercept (years on which trend line is 0). Details are provided in Annexure.

It is apparent from the table above that there is no clear trend of annual decay (reduction in throw forward) for the three sectors or the bucket years. It is the highest for the 2014-15 Bucket of Transport and Communications sector (142.18 Billion rupees per annum) apparently due to higher initial cost of the bucket itself. The lowest is for energy sector 2012-13 bucket with a drop rate of just 0.089 Billion rupees (mainly again due to very small bucket for the same year).

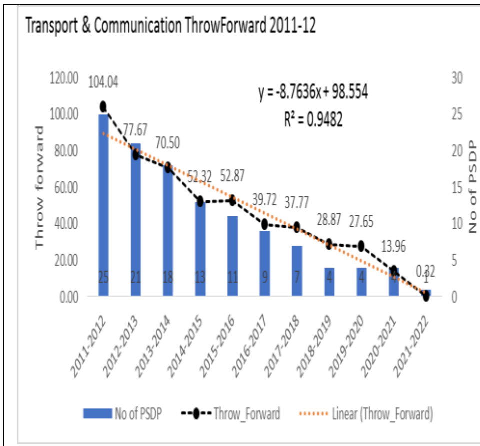
Average age of the energy sector bucket for 2013-14 is the highest (29.87 years). It means that on average it will take almost 30 years to fully execute the bucket introduced for this sector in 2013-14 until and unless some drastic measures to complete these projects or simply wiping them out from PSDP portfolio is not done. On the other hand, for year 2012-13 for the same sector, it has the lowest expected execution of the bucket introduced (2.4 years). Transport and communications and Water on the other hand have lesser variations in the age of their respective year wise buckets. For example for Transport and Communications the highest age of executing financial sanction would be 12.24 years for 2013-14 bucket and 7.35 years for 2014-15 bucket (this is also reflected by the smaller coefficient of variation (CV) values for transport and communication sector). Similar analysis was done using the Number of projects for the same sample of buckets. The results are reported in Table 4 below.

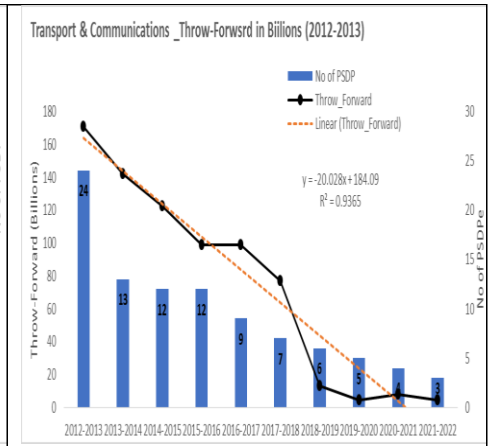
Table 4

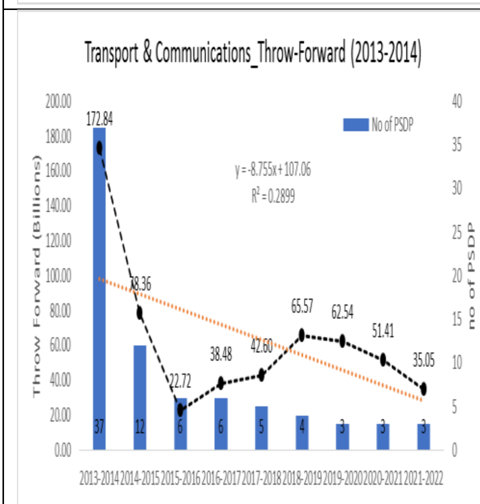
Aging of Bucket Projects

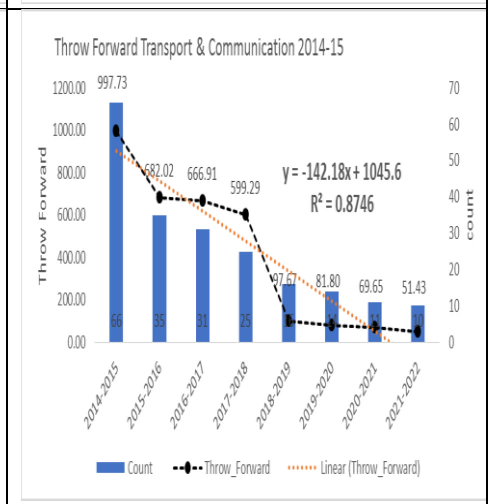
Sector	Bucket	No of Projects	Annual Project Completion	Age of Bucket (Years)
Transport and Communication	2011-12	25	2.30	10.43
Transport and Communication	2012-13	24	1.86	10.61
Transport and Communication	2013-14	37	2.85	8.08
Transport and Communication	2014-15	66	6.81	8.32
Energy Sector	2011-12	6	0.46	11.07
Energy Sector	2012-13	2	1.00	3.00
Energy Sector	2013-14	20	1.90	9.68
Energy Sector	2014-15	24	2.81	7.61
Water Sector	2011-12	18	1.53	11.24
Water Sector	2012-13	14	1.375	8.63
Water Sector	2013-14	11	0.733	10.00
Water Sector	2014-15	18	1.310	11.56

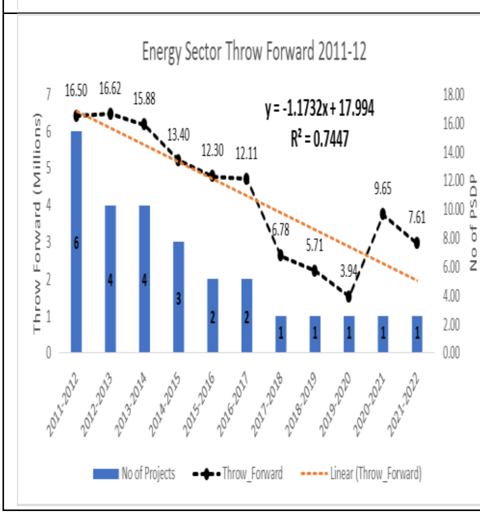
Bucket wise analysis is also presented in the following graphs. It appears that in almost all the buckets significant number of projects is taken out of the bucket in the first year (mostly smaller projects). However the throw forward does not fall on the same rate and even increases in some cases due to cost escalation.

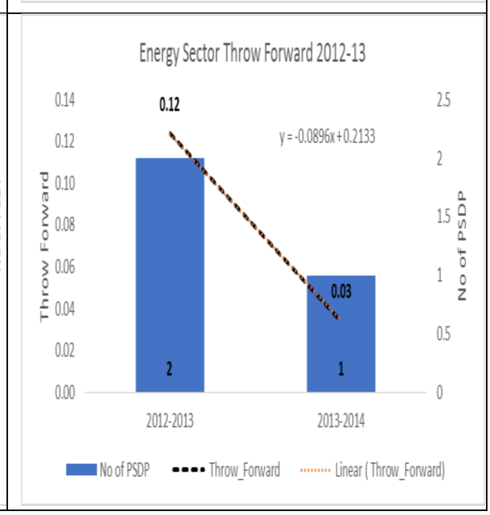

Transport & Communication ThrowForward 2011-12
y = -8.7636x + 98.554
R² = 0.9482
Throw forward
No of PSDP
104.04
77.67
70.50
52.32
52.87
39.72
37.77
28.87
27.65
13.96
0.22
2011-2012
2012-2013
2013-2014
2014-2015
2015-2016
2016-2017
2017-2018
2018-2019
2019-2020
2020-2021
2021-2022
No of PSDP
Throw_Forward
Linear (Throw_Forward)

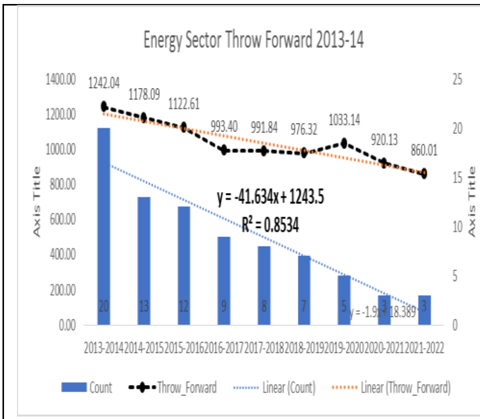

Transport & Communications _Throw-Forwsrd in Billions (2012-2013)
No of PSDP
Throw_Forward
Linear (Throw_Forward)
y = -20.028x + 184.09
R² = 0.9365
Throw-Forward (Billions)
No of PSDPs
2012-2013 2013-2014 2014-2015 2015-2016 2016-2017 2017-2018 2018-2019 2019-2020 2020-2021 2021-2022

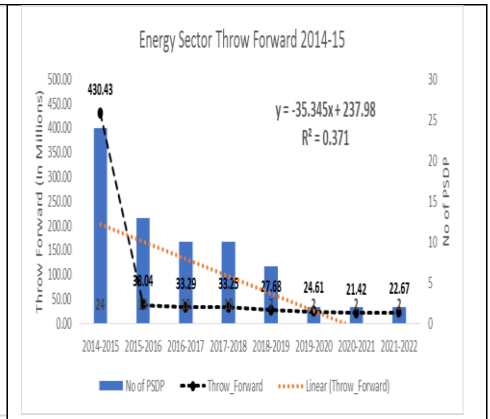

Transport & Communications_Throw-Forward (2013-2014)
No of PSDP
y = -8.755x + 107.06
R² = 0.2899
Throw Forward (Billions)
no of PSDP
172.84
78.36
22.72
38.48
42.60
65.57
62.54
51.41
35.05
2013-2014 2014-2015 2015-2016 2016-2017 2017-2018 2018-2019 2019-2020 2020-2021 2021-2022

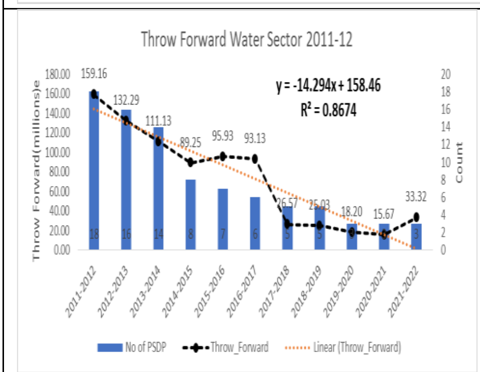

Throw Forward Transport & Communication 2014-15
y = -142.18x + 1045.6
R² = 0.8746
Throw Forward
count
997.73
682.02
666.91
599.29
97.67
81.80
69.65
51.43
2014-2015
2015-2016
2016-2017
2017-2018
2018-2019
2019-2020
2020-2021
2021-2022
Count
Throw_Forward
Linear (Throw_Forward)

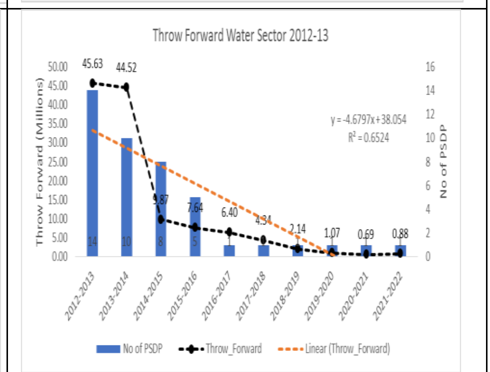

Energy Sector Throw Forward 2011-12
y = -1.1732x + 17.994
R² = 0.7447
Throw Forward (Millions)
No of PSDP
16.50
16.62
15.88
13.40
12.30
12.11
6.78
5.71
3.94
9.65
7.61
2011-2012
2012-2013
2013-2014
2014-2015
2015-2016
2016-2017
2017-2018
2018-2019
2019-2020
2020-2021
2021-2022
No of Projects
Throw_Forward
Linear (Throw_Forward)

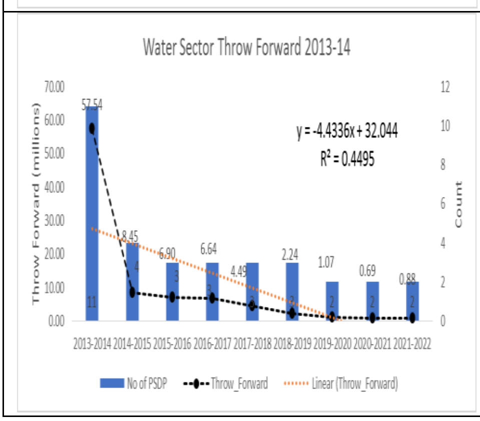

Energy Sector Throw Forward 2012-13
y = -0.0896x + 0.2133
Throw Forward
No of PSDP
0.12
0.03
2012-2013
2013-2014
No of PSDP
Throw_Forward
Linear (Throw_Forward)

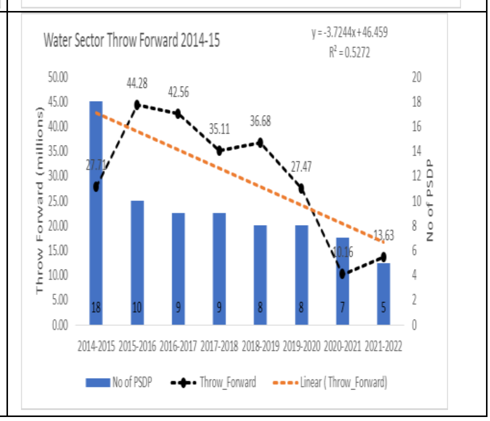












OUTLINE OF FUTURE STRATEGY

Medium term budgetary framework provides the government with fiscal arrangements that extend beyond a single year towards a multiyear budget. However, this exercise is not conducted in letter and spirit. Performance audits and development needs' assessment, which is aligned with a national-level Growth Strategy, do not form the basis for budgetary allocations for current and development expenditures.

Planning Commission's 'Manual for Development Projects', issued in 2021, and Public Financial Management (PFM) Act, 2019 require provision for maintenance of assets. The PFM Act also requires establishment of sovereign wealth fund through an act of parliament to act as holding institution for sound management of public assets and maximising returns. Implementation of the PFM Act, 2019 alone would improve the PIM system efficiency but it would require thorough effort at the granular level.

I. Proposals for Portfolio Cleaning

There are chronic issues associated with financial sustainability and economic efficiency of the current PSDP portfolio. Each fiscal year, huge allocations are made for new projects. At times, re-appropriations of funds allocated for implementation of ongoing projects is made to meet funding requirements for new additions to projects pipeline. As a result, a systemic bias is created which leads to cost over-runs and delayed implementation period of ongoing PSDP portfolio. Therefore, there is a need to undertake a systematic portfolio cleaning exercise to identify those projects which have outweighed their economic costs over the benefits, the projects whose scope can be curtailed and can be taken off from the portfolio for saving funding costs of borrowed public resources. In this regard, the following Portfolio Cleaning guidelines could be adopted:

Pruning the Portfolio of Development Projects

The size of the PSDP be reduced by 20-25 percent, and the number of ongoing projects by up to 50 percent, by eliminating low-priority projects or components, projects which have serious implementation problems, or projects which do not have the strong support of implementation agencies. This should include foreign-funded projects.

Moratorium on Approval of New Projects

A two-year moratorium on approval of all large new infrastructure projects, other than exceptional high-return quick-gestation projects that would contribute directly to exports, government revenues, or strategic goals.

Cap on Share of Infrastructure Projects

Investment in physical infrastructure projects—which by nature do not contribute to government revenues or export receipts, except indirectly, after a long gestation period—should be capped at a reasonable completion stage/ proportion of total development expenditure. Loans on offer, in excess of this cap, should be declined.

Prioritise Rehabilitation and Upgrade of Existing Public Assets

Over the years, the O&M budgets of both physical and social infrastructure assets have been under-resourced. As a result, quality of public assets has depreciated or de-graded and their intended economic impact have been severely compromised. Scaling up of O&M budget will lead to economic impact restoration of depilated public physical and social infrastructure, will rapidly create labour-intensive employment opportunities, and will likely have low import-content as well. Further, PSDP allocations can be prioritised to rehabilitate or upgrade existing physical and social infrastructure assets.

Protection of Priority Projects

While the bulk of social spending has been devolved on the provinces by the 18th amendment to the Constitution, a number of legitimate projects and programmes remain in the federal jurisdiction. These should be protected and their share in total PSDP should be allowed to grow. However, a strict review of projects and programmes (and their components) should be conducted to eliminate those that are no longer permitted to the federal government.

II. Consolidation of Development Expenditures and Proposals for Immediate Savings

The PSDP now consists of over 1, 100 projects, costing more than Rs 8 trillion, with an annual average allocation of Rs 600 billion and a throw-forward of Rs 6.54 trillion. [2] Essentially, the whole-of-government is unable to efficiently manage the current size of PSDP portfolio and follow the projects' implementation guidelines of Planning Commission's Manual for Development Projects. As a ratio of GDP, the PSDP has declined from over 5 percent of GDP in 1985-86 to 2.5 percent in 1998-99 and 1.7 percent in 2019-20.

A great deal of foreign debt has been contracted at the initiative of multilateral lending institutions, with little scrutiny by government or attention to project returns, or national interest or priorities. The present pipeline of undisbursed foreign loans exceeds $15 billion, while the number of foreign-funded projects exceeds the management and implementation capacities of executing agencies. This is reflected in the fact that while Rs. 353 billion were released for federal development expenditure in 2020-21 (9-months), only Rs. 300 billion were spent [1].

Rationalisation of Development Expenditures

The entire allocation to the Higher Education Commission (Rs.29.5 billion, including foreign loans of Rs.1.4 billion) should be scaled back to a reasonable level. Equally, provincial projects being executed by the National Highway Authority (NHA) and other federal agencies should be transferred to the provincial ADP. Such savings should be searched and realised by a close review of the PSDP to identify other projects of devolved sectors and spending thereon, should be cut by shifting them to the respective provinces/areas.

Cancel Unproductive Foreign Debt

As part of Portfolio Cleaning exercise, a critical review of foreign-funded projects should be undertaken and those projects should be closed and their foreign agreements should be cancelled that no longer make sense or on which incremental returns on further drawdown of undisbursed amounts have become negative. An immediate review of some fifty projects, each with an undisbursed balance of over $100 million, and late of other projects, may yield savings of perhaps $1 billion, which should be identified and in consultation of executing agencies, realised.

Policy Based Foreign Borrowing

A comprehensive policy for foreign borrowing should be formulated. Only the foreign borrowing should be for exceptional projects, justified by their contribution to government revenues, foreign exchange earnings and/or export promoted, or by their strategic nature).

Project Completion / Closure Facility

An allocation of around Rs.10 billion be provided in the next budget for a Project Completion Facility, to fund project closure costs incurred by loan cancellation, if necessary, for viable projects that government decides to continue.

III. Creating Additional Resources for Rapid Completion of Projects

Many projects face cost overrun and time over run due to lack of funding at appropriate stages. Over the past many decades, the funding strategy of PSDP projects has not evolved and, in fact, has become a major source of growing public sector indebtedness and deepening fiscal imbalances. A major focus of improving PSDP projects' economic impact is related to the associated with designing the most financially feasible funding strategy. Adopting such a principle will help in approving projects with greater economic value and impact but at a lower financial cost.

After the Portfolio Cleaning exercise is completed, and depending on the categorisation of projects, a number of distinct funding strategies can be considered for mobilising adequate resourcing for those projects that are retained. Some of the possible options are proposed below.

Develop Indicative Eligible Projects Assets Class

There is need to breakdown projects' portfolio impact breakdown by (i) location, (ii) social infrastructure, (iii) physical infrastructure, (iv) environmental or green infrastructure, (v) revenue and non-revenue generation, (vi) software of growth such as productivity catch-up (such as labour force skilling, IT infrastructure etc.), and (vii) export diversification measures. Templates for distinct funding strategies can be developed ranging from outright budgetary grants, local or regional user poll tax, philanthropy and crowd funding, financing for results modalities (F4R), co-funding under PPP modalities (particularly the BOT & VGF variety) and Medium Term Sukuk Notes (MTSN) programme.

Develop Medium Term Sukuk Notes (MTSN) Programme

Both under the SBP Act and the ongoing IMF's Extended Fund Facility, the Government is prohibited from direct borrowing from the central bank. Consequently, the Government will have to recourse to commercial banks for borrowing and then fund the increasingly annual PSDP envelope. Such a situation will adversely impact both the cost and flow of credit to the private sector, which will dampen the prospects of overall push for economic growth revival in the country. Instead, developing a structured multi-tranche Medium Term Sukuk Notes (MTSN) programme will essentially side-step the rather complicated and time-consuming process of Sukuk issuance. Eligible institutions that can participate in the MTSN programme could be limited to Islamic commercial banks, pension funds, insurance institutions and the Central Directorate of National Savings (CDNS). There are two major distinct advantages of this arrangement: ensuing competition among the participating institutions will ensure that the borrowing costs are lower than the alternative and will also avoid the potential crowding-out of credit to the private sector. However, realisation of these positive impact is contingent on developing a robust system of estimation and projection of multi-tranche cash requirements of PSDP projects portfolio under implementation.

Reducing the Government Footprint

Increased public investment programme (PIP i.e., both Federal PSDP & Provincial ADPs) will inevitably increase government footprint in the economy, crowd out and discourage private investment. It is, therefore, necessary to reduce government footprint in the current and future PSDP projects portfolio. Depending upon specifics, outright privatisation of partially completed projects could be considered subject to safeguarding provision of public goods interests. Another alternative could be to increasingly deploy Public-Private Partnership arrangements (particularly the BOT & VGF variety) in implementation of revenue generating PSDP projects. As a result, government will have more funds to allocate to projects where private sector cannot be involved for any reason. The recently established PPP Authority (P3A) in the Planning Commission needs to be legally empowered and adequately resourced to fulfil its mandate. Policies' review is needed to facilitate the private sector by reducing government footprint.

Commercialisation of Projects

Acknowledging the fact, that not all development projects could be revenue generating projects, it is important to differentiate between such projects that can be revenue generating and those that cannot be. For the latter, the proposal should include any possible way of making commercial use of project as source of revenue generation. These could range from advertisement spaces to rental spaces for commercial activities such as street vendors etc. Although, revenue from such streams might not be sufficient to contribute to even a small portion of project cost, the revenue from these could be utilised for O&M costs of such projects in the long-run.

IV. Enhancing Capacity for Project Development

Capacity gaps need to be filled for strict compliance of procedures, enlisted in the Manual for Development Projects and Public Finance Management (PFM) Act 2019, throughout the project cycle. All the stages of project cycle starting from needs assessment and project identification to project completion and impact evaluation must be ensured by CDWP and ECNEC.

CDWP/ECNEC should be authorised to fix the responsibility on the defaulters of the procedures, rules and regulations while implementing the projects. There is a need to classify projects into core/national/mega and non-core projects depending on their size, scope, complexity in design and implementation and cross nature of work that lies beyond one agency or the impact that extends beyond a single province.

V. Refocusing the PSDP

The PSDP focus should be shifted away from higher allocations for brick-mortar and physical infrastructure. According to PIDE, evidence suggests that public investment has failed to act as a driver or crowding-in of private investment and growth in Pakistan. This is also why the developing and now developed countries have shifted their focus from infrastructural development to development of software of economy.

Instead, the PSDP should be refocused to a more Result Based Management system, where the focus shall be on developing the software of economy. Ensuring greater compliance and effectiveness of the PSDP need not be limited to the completion of projects but by focusing on projects and plans that encourage economic growth in the economy.

VI. Institutional Reforms for Effective Monitoring and Evaluation Studies of PSDP

Increased resource allocation to conduct M&E studies for the proposed and ongoing PSDP projects on the level of line ministries as well as an overall check and balance regarding the planning, budgeting, implementation and evaluation by the Planning Commission. These M&E reports are essential for future better allocation and planning of the PSDP projects.

VII. Adopt the World Bank and the IMF PIM Evaluation Methodology

The Planning Commission can adopt the World Bank’s Public Investment Management (PIM) Evaluation Methodology, which has identified 8 characteristics to evaluate any PIM system in the world.

IMF has also designed a Public Investment Management Index (PIMI). The purpose of PIMI is to quantitatively evaluate the PIM systems globally, by averaging the scores of four sub-indices appraisal, selection, implementation and evaluation.

This proposal is also in line with the PIDE recommendation: “IMF’s PIMI and World Bank’s PIM evaluation method should both be used for evaluating Pakistan’s Federal PSDP system time to time. The reform measures to the PSDP shall be updated and refocused on the basis of these evaluations with the objective to ensure effectiveness and efficiency of the PSDP system in Pakistan.”

VIII. Establishment of Development Dashboard for Federal PSDP and Provincial ADP Portfolios

Performance monitoring and impact assessment is critical for improved policy making. The PFM Act 2019 also provides for quality assurance reports done independently, for projects over a PC determined threshold. It is proposed to create an all-Pakistan level “development dashboard”, which will transparently feature the project details and performance indicators. It will also provide information on slow moving projects and those which are at different stages of their progress. It will help better monitor and intervene for overall alignment of PIP with the national economic priorities.

IX. Re-defining Legal Framework for the PSDP

Enacting a legal framework/law for the PSDP with the primary objective of establishing mandatory set of principles and procedures that every year’s PSDP must follow in order to ensure greater effectiveness and increased compliance of the programme.

The legal framework must also define the jurisdiction of PSDP, regarding what projects can or cannot be directly funded by the federal government. This is necessary to reduce the politicisation of PSDP while also preventing an overlap of development projects/expenditures among tiers of governments, especially those that must be responsibility of LG.

X. Reducing Burden on the PSDP by Empowering Local Authorities

By defining the jurisdiction of direct funding through PSDP, the burden on PSDP could be reduced. This, however, could prove effective only when the local authorities i.e., local governments, municipal corporations/authorities and district administration are empowered and supported to operate within their clearly defined respective jurisdictions. As a result, not only the entire development plan through various government agencies will be far more effective and far-reached, but will also reduce the burden on federal government to directly fund through PSDP thus reducing project time and costs.

XI. Tighten the Approval Procedures

The gaps in planning and approval stages of the PSDP programme/procedures must be eliminated. This will be possible only through tightening of procedures and ensuring compliance to those. No project shall be approved which do not follow the set-out procedures.

A third-party review of design and appraisal may be instituted along the lines of public hearings done by some regulators such as NEPRA. The appraisals should go beyond the usual technical and economic parameters and develop a project appraisal scorecard. The signatories of the scorecard must be held responsible for any lapses. Risk assessment has been made mandatory in the PFM Act for all projects exceeding a certain threshold and the Planning Commission would determine the threshold separately for different kinds of projects in various sectors.

NOTES

[1] In addition to capacity limits, the fear of arbitrary prosecution may have inhibited spending. In either case, the matter needs investigation.

[2] "The National Economic Council (NEC) in its meeting of June 10, 2020 approved the National Outlay at Rs. 1,324 billion. The size of Federal PSDP is set at Rs. 650 billion including foreign assistance of Rs. 72.5 billion. Public Private Partnership Authority has been activated leveraging Rs. 50 billion private sector investment to complement public resources. The current PSDP 2020-21 is part of a three years rolling plan to carry forward vision of the government." PSDP 2020-21, Preface.

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