

Growth and Investment

I. INTRODUCTION

Pakistan's economy weathered an unprecedented set of challenges during 2008-09. The outgoing fiscal year witnessed the culmination of four separate, and severe, shocks that Pakistan has had to endure over the course of the past two years. The first negative shock to the economy emanated from a severe macroeconomic crisis that resulted from policy-induced imbalances of the past several years that had assumed unsustainable proportions by 2007-08. This was reinforced by a second shock involving a large deterioration in Pakistan's net external terms of trade as a result of the spike in world commodity prices that had occurred during 2007 and a large part of 2008. Largely as a result, the economy suffered a significant supply shock, especially in the case of provision of energy. In addition to the foregoing, a third shock Pakistan has had to grapple with emanated from the adverse effects of the turmoil in global financial markets which has resulted in a collapse of external demand for its exports, and a sharp decline in the availability of external capital to finance its fiscal and current account deficits.

A spill-over effect of the global financial crisis was felt on market and investor confidence in many developing countries, including Pakistan, as banking systems and asset markets came under periods of stress. Finally, 2008-09 witnessed the intensification of an unprecedented domestic security challenge which has exacted an extremely high cost on the economy, both in terms of direct costs of the fight against extremism, as well as in terms of a knock-on effect on investment inflows and market confidence. A significant collateral impact has been borne by Pakistan in terms of the

squeezing of fiscal space for critical development and social sector expenditures.

The cumulative effect of these challenges has been a significant loss of growth momentum in the economy. Real GDP growth in the outgoing year is now estimated at 2 percent, compared to a revised 4.1 percent in the previous fiscal year, with the commodity producing sector recording a rise of only 0.2 percent – the lowest since 1992-93. Gross fixed investment declined substantially, from 20.4 percent of GDP in 2007-08 to 18.1 percent provisionally in 2008-09, with a significant fall in investment by the private sector.

In response to the challenges outlined above, the government of Pakistan strongly committed itself to restoring macroeconomic stability as well as the confidence of markets and investors after assumption of office in March 2008. To this effect, general subsidies on fuel and food were withdrawn through large increases in administered prices during 2008-09, among other measures in a wider home-grown stabilization programme that was implemented with support and endorsement of the IMF. A pivotal element of the stabilization program included putting in place direct income support measures to protect the poor and vulnerable sections of the population. The government is now expanding the social safety net to a broader platform of social development, the scale of which is unprecedented in Pakistan's history.

In addition, and equally fundamentally, a comprehensive and integrated medium term strategy has been evolved, which is embedded in the government's "9-point" program [see Box-1] to

increase productivity, efficiency, and high growth rates that are both sustainable as well as more equitable. competitiveness of the economy, and to ensure

Box-1 : The government's "9-point" Plan

An assessment conducted by the Planning Commission (PC) and the Prime Minister's Economic Advisory Council (EAC) over end-May to September 2008, broadly identified nine areas as priorities for deep, broad-ranging, and sustained policy intervention with a view to addressing deep-seated structural impediments to sustained and more equitable economic growth. The nine areas are:

1. Macroeconomic Stabilization
2. Social Development, including Social Protection
3. Agriculture
4. Industrial Competitiveness
5. Human Capital Development
6. Energy
7. Capital Markets
8. Public-Private Partnerships for Infrastructure
9. Institutional/Administrative Reform

These nine points form the pillars of the government's poverty reduction strategy as articulated in the Poverty Reduction Strategy Paper (PRSP) – II.

While the economic environment in Pakistan remained inhospitable for growth and investment during the first half of 2008-09, firm policy action to restore macroeconomic stability paid off dividends by December. The Rupee stabilized, after losing 19.3 percent in value against the US Dollar. This occurred on a build-up of foreign exchange reserves from November onwards, when Pakistan entered an IMF program, after the country's international liquidity had declined to an import cover of only several weeks. Confidence in the banking system and financial markets was largely restored from December, with the second half of 2008-09 exhibiting greater stability and positive trends in virtually all macroeconomic indicators barring inflation.

Despite the negative effects on the economy of a host of challenges during 2008-09, especially with regard to growth, viewed in a global context Pakistan's economic performance has not been out of sync with its peers, as highlighted in the following section.

Global developments

The global financial crisis which was ostensibly triggered by a deterioration of sub-prime mortgage loans in the US in mid-2007, has assumed unprecedented scale, magnitude and depth since. The International Monetary Fund (IMF) has revised downward its latest forecasts for world economic growth to a decline of 1.3 percent in

2009, the first global contraction in nearly sixty years. The predicted outturn by the IMF compares with an expansion in the global economy of 3.2 percent in 2008, and a recent peak of 5.2 percent in 2007. It now expects real GDP growth in *advanced economies* to fall 3.8 percent in 2009, from 0.9 percent in 2008, while the previously torrid pace of growth in *developing countries* is estimated by the IMF to decelerate to 1.6 percent from 6.1 percent a year earlier.

The economic and social costs of the severe shock to the global economy are massive. According to the World Trade Organisation (WTO), world trade is expected to shrink 3.5 percent in 2009, after a 6.2 percent expansion in 2008 – the first decline in international trade since 1982. The International Labour Organisation (ILO) recently predicted global job losses could touch 30 to 50 million by the end of 2009, while the Asian Development Bank (ADB) has projected that the ranks of the poor in Asia alone could rise by 230 million by 2010 – an increase of over 50 percent of the region's population.

The global financial crisis is impacting the real and social sectors of developing countries through multiple channels. As the process of globalization intensified over the past two decades, the linkages between developed and developing economies have deepened as well as broadened. Foremost amongst these linkages is international trade. The

collapse in global demand will drive exports down by roughly 9 percent in volume terms in 2009 — the biggest contraction since the 2nd World War. The contraction in developed countries will be particularly severe with exports falling by 10 percent this year. In developing countries exports will shrink by some 2-3 percent in 2009.

The social and economic development of a host of developing economies since the 1970s, beginning with the East Asian countries, followed by China, India, Vietnam and a few others, led to the globalisation of the international production chain. Better communication, cheaper and faster transportation, and wage-arbitrage all played an important role in the global dispersion of production facilities of the world's largest companies, and formed the basis for the export-led success of most rapidly developing emerging economies. Another equally important linkage that developed over the decade of the 1990s was via financial flows. According to World Bank/ Institute of International Finance (IIF), private capital flows to emerging economies rose from US\$ 74 billion in 1990 to US\$ 359 billion by 2007. For emerging Asia alone, the IIF estimates a drop in net private capital flows to US\$ 65 billion in 2009, from a peak of US\$ 315 billion in 2007. Credit flows to the region are expected to contract by US\$ 21 billion from the 2007 peak of US\$ 202 billion, while equity-related flows are expected to decline to nearly US\$ 86 billion in 2009 from US\$ 113 billion in 2007.

Yet another potential transmission channel of the global financial crisis is worker remittances. According to the IMF/World Bank's Global Monitoring Report, 2009 worker remittances to all developing countries totaled nearly US\$307 billion in 2008, making up a larger source of external capital for emerging economies than official assistance. Based on current estimates by the IMF/World Bank, inflows of international worker remittances are expected to decline nearly 5 percent in 2009, as dislocation in host country labour markets feeds through to either job losses in the expatriate workforce or lower wages and incomes. Such an outturn could lower the overall income of remittance-dependent households in countries of origin of the expatriate labour force.

Finally, an important transmission channel is international prices of commodities. The sharp decline in world prices of commodities following the eruption of the global financial crisis has hurt commodity net-exporting countries, while providing an extremely significant offset to the adverse effects of the crisis for commodity net-importing countries. The steep and unprecedented rise in world prices of commodities, especially oil, in the run up to the crisis impacted net-importing countries in a variety of ways including via high inflation, strained public finances and balance of payments, pressure on the exchange rate, and higher interest rates.

In Pakistan's case, the dominant effects of the global financial crisis are being transmitted through the external trade and capital flows channels, while prospects for worker remittances remain a wild card at this stage. After a period of healthy growth, Pakistan's export receipts have begun to plummet since November 2008, with year-on-year growth declining to contraction of 23.9 percent in April 2009. With over 60 percent of its exports routed to *advanced economies*, mainly the US and Europe, Pakistan is extremely vulnerable on this front. In terms of external financing, Pakistan's vulnerability is also quite acute. For the period July 2008 to April 2009, inflows into the financial account declined 44 percent, with a substantial contraction in all categories of capital inflows, including private as well as official capital.

While the *advanced economies* appear to have borne the brunt of the economic impact of the crisis, at least in terms of reduction in headline economic growth and the costs of recapitalizing the banking system, *developing countries*, where the bulk of the world's poor and vulnerable reside, will inevitably have to suffer disproportionately greater social consequences of this crisis. With public finances coming under strain, the enormous challenge of up-scaling inadequate social safety nets is likely to overwhelm the capacity to manage for many developing countries, especially smaller economies that were well-integrated with the world economy at the start of the global financial crisis.

To mitigate the adverse effects of the various shocks to the economy stemming from both exogenous as well as endogenous developments, the government has launched a wide-ranging social safety net, which initially involves a cash transfer program (the Benazir Income Support Programme – BISP) that will target 7 million poorest households in the country. At the same time, the government is expanding the social protection plank to a much broader social development platform that will include skills development, health interventions, employment via small works programs, as well as a host of other policy measures. This is the largest and most ambitious social development intervention in Pakistan's history.

Notwithstanding the intensity of the multiple shocks Pakistan's economy has had to face over the past two years, in relative terms, its economy has exhibited a fair degree of resilience. Compared to other countries affected by the global financial crisis, it is remarkable that Pakistan is among a handful of countries with a positive rate of growth, and among a very few with the lowest decline in real GDP growth (see Table 1.1).

The worst ever global financial crisis has had serious repercussions for the developed and the developing markets. The fallout has spread through an extensively interlinked global financial market and resulted in a tightening of credit and general drying up of liquidity. The crisis is not limited to the meltdown of financial markets, the real economy at the national and international levels, its institutions; its productive structures are also in jeopardy. The financial meltdown inevitably backlashes on the process of investment in the production of goods and services.

The world economy is likely to contract by 1.3 percent in 2009 with almost all developed countries are to post negative growth. Despite numerous stimulus packages and government action of unprecedented scale and nature, advanced economies are expected to contract by 3.8 percent in 2009. The world's largest economy US is projected to contract by 2.9 percent in 2009, further down from positive growth of 1.1 percent in the previous year.

European economies were initially thought to be quasi-insulated against contagion of financial crisis and consequently policy response to the crisis was lacklustre. However, soon fallout of the financial crisis engulfed the Euro area and contraction in trade volumes crippled Euro area growth powerhouses like Germany. Resultantly, growth in the Euro area slowed to a meager 0.9 percent in 2008, and is projected to contract by 4.2 percent in 2009.

In emerging economies, the slowdown manifested itself through various channels like volatility in the financial markets led to a flight of capital. Furthermore, constricted access to external financing and widening spreads on sovereign bonds to record levels are apparent. Growth in world trade volumes fell to 3.3 percent in 2008, as compared to 7.2 percent in 2007, and is expected to contract substantially by 11 percent in 2009. Exports from developing economies are projected to contract by 6.4 percent during the same period and developing economies started experiencing substantial slowdown in growth in 2008, with real GDP growing at 6.1 percent as compared to robust growth of 8.3 percent in 2007. Growth in these economies is projected to slow down further to 1.6 percent in 2009.

Emerging economies have already seen the spreads on sovereign and corporate debt widening, and a retreat in equity prices as a result of the global crunch. East Asian tigers Malaysia, Thailand, Korea, Philippines and Singapore all are prospective candidate for posting negative growth. Pakistan, India, Indonesia, Bangladesh and Sri Lanka are the rare positive growth depictees around the globe. The effects of adverse developments at global level have been felt unevenly and countries with weaker macroeconomic fundamentals taking a bigger hit.

The fallout has been complicated further by ever increasing globalization and inter-weaving connectivity of financial markets. There might be no quick fix to the current situation, but all efforts must be made through monetary and fiscal responses with reforms in the financial sectors. Developing countries need to keep a close eye on

inflation, while guarding against any spill-over effects from the slowdown.

Macroeconomic imbalances continue to pose a risk to stimulus efforts. The payment imbalances are part of a wider problem of imbalances in the global

economy. The main risk posed by these global imbalances is a disorderly resolution of the problem for example, an abrupt adjustment of exchange rates and interest rates, with obvious implications for emerging market debt.

Table-1.1: Comparative Real GDP Growth Rates (%)

Region/Country	2005-06	2006-07	2007-08	2008-09	Diff (FY09-FY-08)
World GDP	5.1	5.2	3.2	-1.3	-4.5
Euro Area	2.9	2.7	0.9	-4.2	-5.1
United States	2.8	2.0	1.1	-2.8	-3.9
Japan	2.0	2.4	-0.6	-6.2	-5.6
Germany	3.0	2.5	1.3	-5.6	-6.9
Canada	2.9	2.7	0.5	-2.5	-3.0
Developing Countries	8.0	8.3	6.1	1.6	-4.5
China	10.4	10.7	10.4	10.7	0.3
Hong Kong SAR	7.0	6.4	2.5	-4.5	-7.0
Korea	5.2	5.1	2.2	-4.0	-6.2
Singapore	8.4	7.8	1.1	-10.0	-11.1
Vietnam	8.4	8.2	8.4	8.2	-0.2
ASEAN					
Indonesia	5.5	6.3	6.1	2.5	-3.6
Malaysia	5.8	6.3	4.6	-3.5	-8.1
Thailand	5.2	4.9	2.6	-3.0	-5.6
Philippines	5.4	7.2	4.6	0.0	-4.6
South Asia					
India	9.8	9.3	7.3	4.5	-2.8
Bangladesh	6.5	6.3	5.6	5.0	-0.6
Sri Lanka	7.7	6.8	6.0	2.2	-3.8
Pakistan	5.8	6.8	4.1	2.4	-1.7
Middle East					
Saudi Arabia	3.0	3.5	4.6	-0.9	-5.5
Kuwait	5.1	2.5	6.3	-1.1	-7.4
Iran	5.8	7.8	4.5	3.2	-1.3
Egypt	6.8	7.1	7.2	3.6	-3.6
Africa					
Algeria	2.0	3.0	3.0	2.1	-0.9
Morocco	7.8	2.7	5.4	4.4	-1.0
Tunisia	5.5	6.3	4.5	3.3	-1.2
Nigeria	6.2	6.4	5.3	2.9	-2.4
Kenya	6.4	7.0	2.0	3.0	1.0
South Africa	5.0	4.8	5.1	5.0	-0.1

Source: World Economic Outlook (IMF), April 2009.

Structural transformation-led growth

After several years of strong economic expansion, Pakistan experienced a full-blown macroeconomic crisis beginning early 2008. While the immediate trigger appeared to be the large terms of trade shock that buffeted Pakistan – and other commodity-importing developing countries – since

2007, in fact the crisis had more “classic” roots: economic growth powered by large capital inflows, a growing fiscal imbalance accompanied by large-scale monetisation of the deficit, a credit bubble in the economy, and an increasingly overvalued exchange rate.

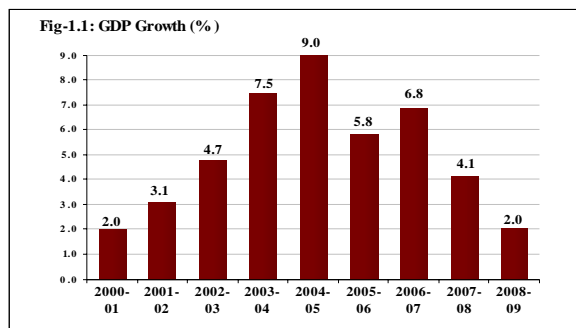
Hence, Pakistan's vulnerabilities were already quite pronounced well before the start of the global crisis. Both external as well as internal imbalances in the economy had risen sharply in the wake of the growth episode of fiscal 2003 to 2008. The external current account had swung from a surplus of 4.9 percent of GDP in 2002-03 to a deficit of 5.1 percent of GDP in 2006-07, before widening to a historic high of over 8.5 percent of GDP in fiscal 2007-08. The fiscal deficit had risen somewhat more moderately prior to the crisis, to 4.3 percent of GDP in 2006-07, before ballooning to 7.6 percent of GDP in 2007-08, largely on account of policy inaction in reducing energy and food subsidies.

In the case of the twin deficits, the imbalances were being financed via a heavy reliance on external financing. In 2007, portfolio capital inflows "financed" almost 50 percent of the external current account deficit – underscoring Pakistan's vulnerability to "sudden stops" – while 70 percent of the fiscal deficit in 2008 was budgeted to be financed by external inflows, i.e. official capital, proceeds from privatisation and divestment (mainly by issuance of Global Depository Receipts), and issuance of global sovereign bonds.

Ultimately, the virtual drying up of flows of confidence-sensitive capital to Pakistan led to a massive monetisation of the fiscal deficit in 2007 and 2008. Not surprisingly, public debt had begun to rise fairly significantly, especially with reference to revenues, thus reversing the favourable debt trajectory established post-2001. Finally, inflation had begun to crawl upwards due to the unfavourable combination of a growing output gap in the economy, and increasing monetisation of the fiscal deficit.

Despite marginal success in introducing incremental economic reform, Pakistan missed a unique opportunity over the past several years to fundamentally restructure the economy. The painful lack of fundamental structural reform in the past several years before the current government took over is manifested in the low, and declining,

tax to GDP ratio – amongst the lowest in the world. The combination of weak tax administration, an exemptions-ridden tax system, and a questionable introduction of the universal self-assessment scheme in terms of sequencing (in the absence of risk-based audits), has dealt a severe blow to Pakistan's efforts to broaden the tax base.



The continued strain imposed by public sector enterprises (PSEs) on fiscal resources is another important area of public finances where desired results could not be achieved, despite the large-scale losses imposed on the economy year after year. In aggregate, the charge on the budget on account of absorption of explicit as well as implicit contingent liabilities losses of the PSE's crossed Rs 217 billion in 2007-08, the equivalent of over 2.1 percent of GDP.

Cognizant of the limitations of the growth strategy followed in the past, which has invariably produced boom-bust cycles, and has invariably been followed at various intervals by a balance of payments crisis, the present government is embarking on a fundamental change of the development paradigm. The new growth strategy is embodied in the government's "nine-point" plan, and seeks to foster sustainable and more equitable growth by means of structural improvements in the productive sectors of Pakistan's economy.

After analyzing the overall growth, investment and consumption, it is imperative to look into the growth performance of the various components of Gross National Product for the year 2008-09 in the historical context. The performance of the various components of national income over the last two and a half decades is summarized in Table 1.2.

Table 1.2: Growth Performance of Components of Gross National Product

(% Growth At Constant Factor Cost)									
	1980's	1990's	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Commodity Producing Sector	6.5	4.6	4.2	9.3	9.5	5.1	6.6	1.4	0.2
1. Agriculture	5.4	4.4	4.1	2.4	6.5	6.3	4.1	1.1	4.7
- Major Crops	3.4	3.5	6.8	1.7	17.7	-3.9	7.7	-6.4	7.7
- Minor Crops	4.1	4.6	1.9	3.9	1.5	0.4	-1.0	10.9	3.6
- Livestock	5.3	6.4	2.6	2.9	2.3	15.8	2.8	4.2	3.7
- Fishing	7.3	3.6	3.4	2.0	0.6	20.8	15.4	9.2	2.3
- Forestry	6.4	-5.2	11.1	-3.2	-32.4	-1.1	-5.1	-11.5	-15.7
2. Mining & Quarrying	9.5	2.7	6.6	15.6	10.0	4.6	3.1	4.4	1.3
3. Manufacturing	8.2	4.8	6.9	14.0	15.5	8.7	8.3	4.8	-3.3
- Large Scale	8.2	3.6	7.2	18.1	19.9	8.3	8.7	4.0	-7.7
- Small Scale *	8.4	7.8	6.3	-20.0	7.5	8.7	8.1	7.5	7.5
4. Construction	4.7	2.6	4.0	-10.7	18.6	10.2	24.3	-3.9	-10.8
5. Electricity & Gas Distribution	10.1	7.4	-11.7	56.8	-5.7	-26.6	4.7	-22.0	-3.7
Services Sector	6.6	4.6	5.2	5.8	8.5	6.5	7.0	6.6	3.6
6. Transport, Storage and Comm.	6.2	5.1	4.3	3.5	3.4	4.0	4.7	5.7	2.9
7. Wholesale & Retail Trade	7.2	3.7	6.0	8.3	12.0	-2.4	5.8	5.3	3.1
8. Finance & Insurance	6.0	5.8	-1.3	9.0	30.8	42.9	14.9	12.9	-1.2
9. Ownership of Dwellings	7.9	5.3	3.3	3.5	3.5	3.5	3.5	3.5	3.5
10. Public Administration & Defence	5.4	2.8	7.7	3.2	0.6	10.1	7.1	1.2	5.0
11. Services	6.5	6.5	6.2	5.4	6.6	9.9	7.9	10.0	7.3
12. GDP (FC)	6.1	4.6	4.7	7.5	9.0	5.8	6.8	4.1	2.0
13. GNP (FC)	5.5	4.0	7.5	6.4	8.7	5.6	6.7	4.1	2.6

* Slaughtering is included in small scale sector

Source: FBS

II. Commodity Producing Sector (CPS)

The Commodity Producing Sector (CPS) has been severely ignored during the last eight years. It is comprised of production sectors like agriculture and industry. It accounts for 46.2 percent of the GDP. Notwithstanding stellar growth performance by the agriculture sector, CPS was mainly responsible for modest GDP growth at 2 percent. Barring agriculture, the growth performance of its main components remained lackluster at best. In the industrial sector the only positive growth came from a relatively smaller subsector mining & quarrying and thus it witnessed a negative growth of 3.6 percent which was neutralized by a positive growth of 4.7 percent by the agriculture sector which helped in depicting overall marginal positive growth of 0.2 percent by the CPS. This is the worst performance of the CPS in more than a decade [See Table 1.2].

II.i. Agriculture

The share of agriculture in GDP has been falling persistently. It accounted for 25.9 percent of GDP in 1999-2000; however, gradually its share shrank to 21.3 percent in 2007-08 but improved slightly to 21.8 percent of GDP in 2008-09. Notwithstanding its declining share it remains the single largest sector of Pakistan's economy and an overwhelming majority of the population depends directly or indirectly on income streams generated by the agriculture sector. The agriculture sector remained the dominant sector with its job absorption ability and it still absorbs 44 percent of the country's labour force. It gives a kick-start to aggregate demand for industrial goods and services as well.

The agriculture sector consists of crops, livestock, fishing and forestry sub-sectors. The crop sub-sector is further divided into major crops

(primarily wheat, cotton, rice, sugarcane, maize and gram) and minor crops (such as pulses, potatoes, onions, chilies and garlic). Historically, the crops sub-sector has had the largest share of the agriculture sector, but with changing patterns of income and expenditure, the crop sector accounts for 45 percent of agriculture. The crop sector has the potential to influence the overall performance of the agriculture sector and it has spearheaded the growth in the agriculture sector. Recent trends point towards a reduction in the share of the crops sub-sector. The share of crops in agriculture has declined from 65.1 percent in 1990-91 to 45.4 percent in 2008-09. Global integration, rising incomes and living standards as well as changing dietary patterns across regions have caused a paradigm structural shift. The share of livestock in agriculture has increased from 29.8 percent to 51.8 percent in the same period.

Agriculture sector has depicted a stellar growth of 4.7 percent as compared to 1.1 percent witnessed last year and a target of 3.5 percent for the year. The improved performance is mainly attributed to a sharp pick-up in the major crops sub-sector on the back of exceptionally good performance of wheat, cotton, rice, maize and gram. The only major crop which performed below par was sugarcane. As a result of this impressive performance this sub-sector grew by 7.7 percent in 2008-09. **Minor crops** registered a growth rate of 3.6 percent compared to the target of 2.0 percent and an impressive growth of 10.9 percent last year. Smaller sub-sector fishing posted a modest growth of 2 percent while forestry continued its historical negative growth by declining by 15.7 percent. A detailed analysis of the performance of each of the sub-sectors of agriculture is given below:

II.i.a. Major crops accounting for 33.4 percent of agricultural value added registered an impressive growth of 7.7 percent compared to a negative growth of 6.4 percent last year and a target of 4.5 percent. Almost all major crops recorded double digit growth except sugarcane where production is down by 21.7 percent. The wheat which accounts for 12.1 percent of the agriculture and 37.1 percent of major crops has witnessed a record crop at 23.4 million tons — higher by 11.7 percent over last year's crop size. The other two major crops rice

and gram also broke all previous records of production. Rice accounts for 5.4 percent of overall agriculture and 16.6 percent of the major crops. It witnessed an increase of 25 percent in production whereas relatively smaller stakeholder gram grew by 60 percent. The important crop cotton, with 7.4 percent stake in agriculture and 22.7 percent in value addition of major crops, grew modestly by 1.4 percent and its production at 11.8 million bales is below par. Other major crops jawar, tobacco, barley, oil seeds and maize depicted mixed trends but their stake is small.

II.i.b. Minor crops, accounting for 12 percent of value added in overall agriculture, grew by 3.6 percent which is far below the 10.9 percent growth last year. Production of pulses has declined by 8.9 percent which has added to the supply side shock to the food inflation. Vegetables recorded marginal growth of 0.9 percent. The production of all fruits grew by 3.1 percent, out of which production of citrus fruits grew marginally by 0.1 percent whereas production of other fruits including dry fruits grew by 4.1 percent.

II.i.c. Livestock. With rising incomes, globalization and changing dietary patterns, the consumption of livestock products has increased significantly. The price of livestock items has remained a major contributor to inflationary pressures in Pakistan's economy. The demand for livestock has grown at a phenomenal pace. The upsurge in prices has provided incentives for greater production and thus prospects for growth. The government has also placed great focus on this important sector which accounts for 52.3 percent of value addition in the agriculture sector. The importance of this sector can be gauged by the fact that the livelihoods of about 36 million people in the rural areas depend directly or indirectly on the livestock and dairy sector. It is a highly labour-intensive and job creating sector. Its share in agriculture is much more than the combined shares of major and minor crops. It accounts for 11.3 percent of GDP. Accordingly, it has emerged as a major alternative source of income, particularly for the landless rural poor. Livestock includes: cattle, buffalos, sheep, goats, camels, horses, asses and mules. The livestock sector grew by 3.7 percent in 2008-09 compared to 4.2 percent last year. Poultry

& products grew by 11.2 percent while milk production grew by 3.2 percent only.

II.i.d. Fisheries: The fisheries sector accounts for only 0.4 percent of GDP and witnessed a growth of 2.3 percent against the target of 3.4 percent and actual outcome of 9.2 percent for last year. Components of fisheries such as marine fishing and inland fishing, contributed to an overall increase in value addition in the *fisheries* sub-sector. Marine fisheries registered a growth of 3.9 percent compared to 4.9 percent last year. Inland fish segment also registered a growth of 1.6 percent compared to 11.1 percent last year.

II.i.e. Forestry: Forestry accounts for 0.2 percent of GDP and value addition contracted by 15.7 percent compared to a contraction of 11.5 percent last year. The forestry sector is depicting negative growth for the sixth year in a row. Forests are a key component of our environment, degradation of which can pose severe socio-economic challenges for the generations to come.

II.ii. Manufacturing

The manufacturing sector has been hard hit by international and domestic factors. Political instability and frequent eruptions of incidents detrimental to law and order have created an uncertain environment resulting in loss of working hours. This sector has also fallen victim to the acute energy shortages. Continuous power breakdowns are preventing industries from operating at far less than their optimal level. In unison with the increasing cost of doing business, all these factors have caused a slowdown in output.

The *manufacturing sector* is witnessing erosion of share in the GDP to 18.2 percent which is the lowest ever share of it in the last five years. The process of deceleration in growth that started in the fiscal year 2004-05 continued unabated partly because of acute energy shortages but more importantly owing to structural problems. Output in the manufacturing sector has contracted by 3.3 percent in 2008-09 as compared to expansion of 4.8 percent last year and an over-ambitious target of 6.1 percent. *Small and medium manufacturing sector* maintained its healthy growth of last year at 7.5 percent.

Large scale manufacturing which accounts for 12.1 percent stake in GDP faced the most difficult period of its recent history and depicted a negative growth of 7.67 percent during July-March 2008-09 compared to 4.0 percent positive growth in the same period last year. Main items showing positive growth included; fertilizer (21.5 percent), non-metallic mineral products (4.8 percent), chemicals (3.8 percent), leather products (2.9 percent), paper & paper board (2.9 percent) and engineering products (0.8 percent). Major items showing decline in production included automobiles (-39.0 percent), electronics (-31.3 percent), petroleum products (-9.2 percent), food & beverages (-10.5 percent), rubber products (-4.0 percent), and iron & steel products (-5.6 percent). There was negative growth all around in all major groups with one or two exceptions. This implies that the large-scale manufacturing sector is exhibiting signs of moderation since 2004 on the one hand and acute power shortages along with several other factors like the rising cost of doing business, demand compression in the export sector, and deteriorating law and order situation in the country. The negative growth of 20.7 percent in the month of March 2009 may have been caused due to the massive disruption in economic activity because of the long-march for almost two weeks. The LSM growth is adversely impacted by a sharp reduction in demand from both domestic and international factors.

II.iii. Mining and Quarrying

Extraction of minerals and ores through efficient mining and quarrying provides convenient and economical access to raw materials and provides a competitive edge to developing countries. The mining and quarrying sector witnessed the lowest ever growth in almost one decade and grew by 1.3 percent in 2008-09 as compared to 4.4 percent growth last year and a target of 5.0 percent. The contribution of this sector towards GDP has remained low at around 2.5 percent. Within the sector, the output of crude oil and coal has decreased by 3.0 percent and 2.0 percent, respectively. The production of natural gas has increased by 1.3 percent. Because much of the country's mining reserves exist in remote areas, infrastructure improvements are necessary to

attract higher investment in this sector and as investment in mining is coming from abroad, improvement in the security situation is crucial in boosting this sector.

II.iv. Services Sector

In recent times the importance of the services sector has increased all around the world and it emerged as the main driver of economic growth around the world. Pakistan has also seen a major transformation in the economic structure and the share of the services sector has risen to 53.8 percent in 2008-09. The services sector grew by 3.6 percent against the target of 6.1 percent and actual outcome of 6.6 percent. This implies a major correction from last year's growth as well as the target for the year.

The services sector has made a contribution of 96 percent to the GDP growth. The services sector has been an important contributor to Pakistan's economic growth over the past five years by growing at an average of 6.6 percent annually since 2003-04. The continuing buoyant trend, even while growth in the industrial sectors has been slowing, implies that the services sector in Pakistan has been relatively insulated from the challenges faced by the rest of the economy and has been better able to cope with them.

The sector consists of the following sub-sectors: Transport, storage and communication; Wholesale & Retail Trade; Finance and Insurance; Ownership of Dwellings; Public Administration and Defence; and Social Services. **Finance and insurance sector** displayed a stellar growth performance by posting double digit growth for the last few years. However, on the eve of the global financial meltdown the contagion is well observed in Pakistan's banking and financial sector. The growth in the financial sector slowed down to 12.9 percent in 2007-08 but registered a negative growth of 1.2 percent in 2008-09. The performance of this sector shows that Pakistan's financial sector is integrated in the world economy and feeling the heat of the financial crisis plaguing international financial markets. The **Transport, Storage and Communication** sub-sector depicted a sharp deceleration in growth to 2.9 percent in 2008-09 as

compared to 5.7 percent of last year. Value added in this **sector** is based primarily on the profits and losses of Pakistan Railways, Pakistan International Airlines and other airlines, Pakistan Posts & Courier Services, Pak Telecom and motor vehicles of different kinds on the road. Mechanized road transport has depicted a growth of 2.9 percent, followed by road transport (6.4 percent), communication sector (3.6 percent) and storage (2.7 percent). The value addition of Pakistan Railways has declined by 6.4 percent. Other sectors that showed a decline are; air transport (2.1 percent) and pipeline transport (8.0 percent). Value added in the **wholesale and retail trade sector** is based on the margins taken by traders on the transaction of commodities traded in the wholesale and retail market. In 2008-09, this sector grew at 3.1 percent as compared to 5.3 percent last year and the target for the year of 5.4 percent.

Public administration and defense posted a stellar growth of 5.0 percent as compared to 1.2 percent in 2007-08. The estimates of this sector are based on budgeted figures of federal, provincial, district and local governments. The performance of this sector far outstripped the target of 4.0 percent mainly due to a positive change in the wage component of public sector employees, and an increase in defense and security related expenditures. Growth in the **Ownership of Dwellings** has remained constant at 3.5 percent for the past 5 years. **Social Services Sector** grew by 7.3 percent which is slightly higher than the target of 7.0 percent but lower than last year's actual growth of 10 percent.

III. Contribution to Real GDP Growth (Production Approach)

The contribution to economic growth is spearheaded by the services sector with 96.1 percent stake while only 3.9 percent contribution came from the Commodity Producing Sector (CPS). One of the important components of CPS, agriculture alone contributed 50.1 percent to real GDP growth; however, this is more than neutralized by 50.4 percent negative contribution from large-scale manufacturing. Thanks to 16.7 percent positive contribution from small-scale

manufacturing, the overall negative contribution of the manufacturing sector stood at 31.9 percent.

The Commodity Producing Sector has been overshadowed by another year of exceptional growth in the Services sector. The modest growth of just 2.0 percent is shared between CPS (0.08) and services sector (1.92). Within the CPS, agriculture contributed 1.0 percentage points or 50.1 percent to overall GDP growth (a significant increase from its contribution of only 5.0 percent last year) while industry dragged 0.92 percentage

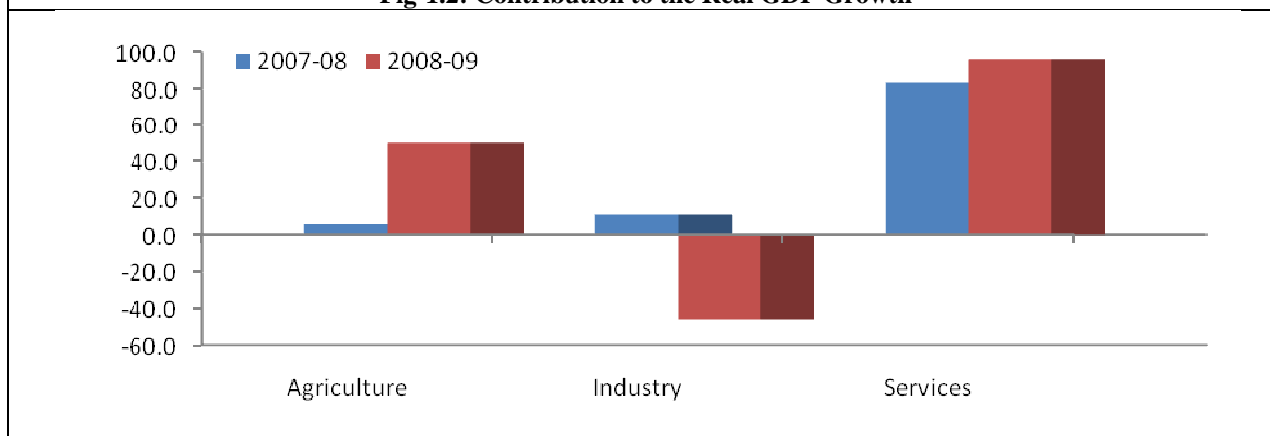
points or 46.1 percent to neutralize positive contribution of the agriculture sector [See table 1.3 and fig. 2 for details]. In the services sector major contributions to GDP growth came from transport, storage & communication (0.3 percentage points or 14.6 percent), wholesale & retail trade (0.7 percentage points or 27.1 percent) and social services (0.8 percentage points or 38.6 percent). Going forward diversification in favour of more positive contribution from commodity producing sector is required for inclusive growth with human face.

Table 1.3: Sectoral Contribution to the GDP growth (% Points)

Sector	2004-05	2005-06	2006-07	2007-08	2008-09
Agriculture	1.5	1.4	0.9	0.24	1.00
Industry	3.1	1.1	2.3	0.45	-0.92
- Manufacturing	2.7	1.6	1.6	0.91	-0.64
Services	4.4	3.3	3.6	3.41	1.92
Real GDP (Fc)	9.0	5.8	6.8	4.10	2.00

Source: Federal Bureau of Statistics.

Fig-1.2: Contribution to the Real GDP Growth



IV. Contribution to Economic Growth (Aggregate Demand Side Analysis)

Consumption, investment, net exports are figuratively described as the 'three horses of Troika' that drives economic growth. In all economies the expansion of output is the sum of consumption (both private and government) plus investment (public and private) plus net exports of goods and services (exports minus imports). Pakistan's economic growth is historically characterized as consumption-led growth; however, massive demand compression measures and stabilization efforts bring consumption under control in 2008-09. The GDP market price grew by

3.7 percent contrary to 2.0 percent growth in the GDP factor cost. The contribution of the consumption sharply decelerated from 142.6 percent in 2007-08 to just 47.8 percent in 2008-09. Within consumption the private consumption remained strong but government consumption dragged the contribution down by a huge margin. The share of investment in real GDP (mp) growth decelerated from 37.3 percent to negative contribution of 32.3 percent as investment to GDP ratio adjusted downward.

The terms of trade in real terms has improved as the exports real growth outpaced the import growth. The net exports contributed the highest

ever share in real GDP at market price growth. The contribution of net exports has traditionally been negative for most part of our history and it was only during the short-lived brief interval (2000-04) of external sector buoyancy that the net exports

contributed positively. The balance between investment and consumption which had improved during 2004-05 and 2006-07, disturbed significantly in the last two years (2007-08 and 2008-09) [See Table 1.4 and Fig. 1.3].

Table-1.4: Composition of GDP Growth

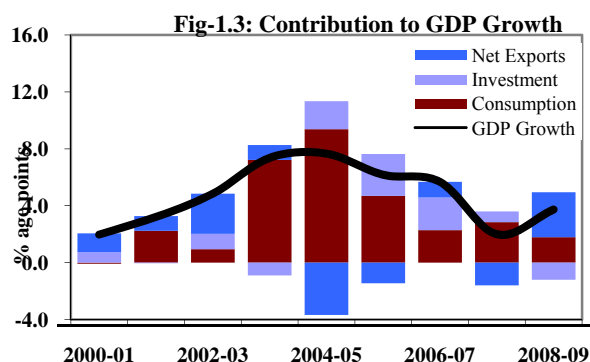
Flows	Point Contribution						
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Private Consumption	0.3	7.1	8.7	0.8	3.4	-0.9	3.6
Public Consumption	0.6	0.1	0.1	3.9	-1.1	3.8	-1.8
Total Consumption [C]	0.9	7.2	9.4	4.7	2.3	2.9	1.8
Gross Fixed Investment	0.6	-1.0	1.8	2.9	2.2	0.7	-1.2
Change in Stocks	0.4	0.1	0.1	0.1	0.1	0.1	-0.1
Total Investment [I]	1.1	-0.9	2.0	2.9	2.3	0.7	-1.2
Exports (Goods & Serv.) [X]	4.5	-0.3	1.7	1.8	0.4	-1.0	1.5
Imports (Goods & Serv.) [M]	1.6	-1.3	5.4	3.2	-0.7	0.6	-1.6
Net Exports [X-M]	2.8	1.0	-3.7	-1.5	1.1	-1.6	3.2
Aggregate Demand (C+I+X)	6.5	6.0	13.0	9.4	5.0	2.6	2.1
Domestic Demand (C+I)	2.0	6.3	11.3	7.6	4.6	3.6	0.6
GDP MP	4.8	7.4	7.7	6.2	5.7	2.0	3.7

Source: Federal Bureau of Statistics.

Given its lion's share in GDP, consumption mainly supported the on-going growth momentum has contributed in the range of 80 – 83 percent to overall economic growth over the last 7 years. In 2007-08 consumption accounted for 142.0 percent or 2.9 percentage points to real GDP (mp) growth of 2.0 percent and while in the current fiscal year private consumption contributed almost 97 percent of the size of the economy only to be neutralized by a massive fall in public consumption and investment. The huge current account deficit of the last fiscal year reinforced a huge negative contribution of the net export sector. The investment rate was rising since 2004-05, and reached its peak of 22.5 percent of GDP in 2006-07, however, amidst extraordinary headwinds the investment to GDP ratio declined since then persistently to 19.7 percent of GDP in 2008-09. National savings have shown their inadequacy for financing even the lower level of investment in the country. The national savings rate has nose-dived to 14.4 percent of GDP in 2008-09 compared to 13.5 percent of GDP last year.

The current year's relatively faster real growth is in sheer contrast to the falling dollar value of nominal exports. Going forward Pakistan needs real effort to reinvigorate exports to make total demand less sensitive to rising domestic real interest rates and

indebtedness, secure productivity gains as a result of competition in the international markets, and relax the foreign exchange constraints for imports which are crucial for giving a kick-start to economic growth.



V. Composition of the GDP

The patterns of economic growth are inimical to structural transformation. Some sectors of the economy may outpace others in the historical process. An analysis into shifts in sectoral patterns of growth provides further insight into a country's growth dynamics. This process of transformation has accelerated in Pakistan in recent years. The structure of the GDP has undergone substantial change during the last three and a half decades (see Table 1.5 for details). There has been a marked

shift away from the commodity producing sector (CPS) which accounted for almost 62 percent of the GDP in 1969-70, its share has declined to 46.2 percent in 2008-09 — a decline of 15.0 percentage points. The decline in the share of CPS is fully accounted for by the equal rise in the share of services sector. A further breakdown of the CPS shows that the share of the agriculture sector has been falling with time. In 1969-70, agriculture accounted for 38.9 percent of GDP, but steadily decreased in the share over the years and has seen it fall to 21.8 percent in 2008-09. The share of the agriculture has declined from almost 39 percent in 1969-70 to 21.8 percent in 2008-09. The share of agriculture in GDP has declined by 4.1 percentage points in the last 9 years alone and the share of the manufacturing sector has increased by the same proportion of percentage points in the same period. It implies that the space created by the agriculture sector is occupied by the manufacturing sector which signals a move away from an agriculture based economy to an increasing reliance on industry and manufacturing- a pre-requisite for the

first phase of structural transformation.

Beside compulsions imposed by the theory of economic development that with higher level of economic development the share of agriculture has to shrink, the other determining factor is the exclusive preoccupation of the successive governments in the past to four major crops, namely, wheat, cotton, sugarcane and rice in policy making and little or no efforts to increase yield per acre or no policy support to diversification of the agriculture sector. Livestock, which accounts for more than one-half of the agricultural value added, has been the major victim of the total neglect of the governments all along until few years ago that this sector started receiving some attention. A continued emphasis on four major crops and negligence as to the other sub-sectors of agriculture and stagnant yields, the contribution of agriculture to overall GDP is bound to shrink further in the coming years as rapid growth in industry and services sector outpaces the growth in agriculture.

Table 1.5: Sectoral Share in Gross Domestic Product(GDP)

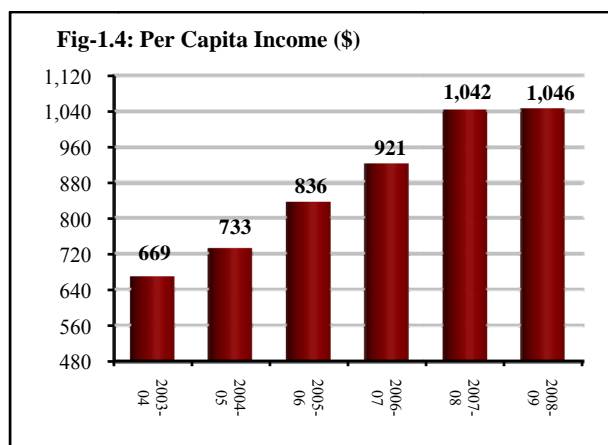
	(At Constant Factor Cost) (In %)					
	1969-70	2004-05	2005-06	2006-07	2007-08	2008-09 P
Commodity Producing Sector	61.6	48.7	48.3	48.2	47.0	46.2
1. Agriculture	38.9	22.4	22.5	21.9	21.3	21.8
- Major Crops	23.4	8.4	7.6	7.7	6.9	7.3
- Minor Crops	4.2	2.7	2.6	2.4	2.6	2.6
- Livestock	10.6	10.6	11.6	11.1	11.1	11.3
- Fishing	0.5	0.3	0.3	0.4	0.4	0.4
- Forestry	0.1	0.4	0.4	0.3	0.3	0.2
2. Mining & Quarrying	0.5	2.7	2.6	2.5	2.6	2.5
3. Manufacturing	16.0	18.3	18.8	19.0	19.2	18.2
- Large Scale	12.5	12.9	13.2	13.4	13.4	12.1
- Small Scale	3.5	4.1	4.3	4.3	4.4	4.7
4. Construction	4.2	2.1	2.2	2.6	2.4	2.1
5. Electricity & Gas Distribution	2.0	3.2	2.2	2.2	1.6	1.5
Services Sector	38.4	51.3	51.7	51.8	53.0	53.8
6. Transport, Storage & Communication	6.3	10.4	10.2	10.0	10.2	10.3
7. Wholesale and Retail Trade	13.8	18.7	17.2	17.1	17.3	17.5
8. Finance and Insurance	1.8	4.0	5.5	5.9	6.4	6.2
9. Ownership of Dwellings	3.4	2.9	2.8	2.7	2.7	2.7
10. Public Admn. & Defence	6.4	5.9	6.1	6.1	5.9	6.1
11. Other Services	6.7	9.5	9.9	10.0	10.6	11.1
12. GDP (Constant Factor Cost)	100.0	100.0	100.0	100.0	100.0	100.0
P Provisional						

Source: Economic Adviser's Wing, Finance Division

During the last seven years, the major impetus to growth has come from the services sector which has emerged as the main engine of the economic growth. The share of manufacturing in GDP has remained stagnant at around 16 percent for 33 years until 2002-03. Its contribution to GDP has increased only during the last five years - rising from 16.3 percent in 2002-03 to 18.2 percent in 2008-09. Within the services sector, almost all the components have raised their contribution over the last three and a half decades.

VI. Per Capita Income

Per capita income is not the proper measurement of the welfare in any economy because it imbeds a wide range of fluctuations behind the number. However, still it is treated as one of the foremost indicators of the depth of growth and general well-being of an economy. The recent and more sophisticated tools to assess effectiveness of economic growth, development, and economic advancement, not a single one has over-ruled the historical importance and simplicity of per capita income as a measure of the average level of prosperity in an economy. Per capita income, defined as Gross National Product at market price in dollar term divided by the country's population, grew by a meager 0.3 percent mainly because of slower economic growth and depreciation of Pak rupee.



The last few years have been in complete contrast, with per capita income growing at a much stronger pace. The per capita income in dollar terms has

increased from \$ 586 in 2002-03 to \$ 1046 in 2008-09 [See Fig-1.4]. The main factors responsible for the sharp rise in per capita income include acceleration in real GDP growth, and a four fold increase in the inflows of workers' remittances. Per capita income in dollar terms rose from \$ 1042 last year to \$ 1046 in 2008-09, thereby showing marginal increase of 0.3 percent. Fig. 1.4 shows the improvement in per capita income during the last seven years. Real per capita income in rupee terms has also increased by 2.5 percent as compared to 0.3 percent growth last year.

VII. Investment and Savings

Investment is a key determinant of growth and its fluctuation reflects the intensification of economic activity. The total investment has declined from 22.5 percent of GDP in 2006-07 to 19.7 percent of GDP in 2008-09. Fixed investment has decreased to 18.1 percent of GDP from 20.4 percent last year. Gross fixed capital formation in real terms has contracted by 6.5 percent compared to an expansion of 3.8 percent last year. However, in nominal terms gross fixed capital formation increased by 13.1 percent against 15.5 percent last year. Private sector investment also witnessed a contraction of 7 percent in real terms and expansion of 12.0 percent in nominal terms compared to a growth of 3.6 percent in real and 15.1 percent in nominal terms in last year. The composition of investment between the private and public sector has changed considerably during the last three years. Private sector investment was decelerating persistently since 2004-05 and its ratio to GDP has declined from 15.7 percent in 2004-05 to 13.2 percent in 2008-09. Public sector investment to GDP ratio was rising persistently from 4.0 percent in 2002-03 to 5.6 percent in 2006-07, however, declined to 4.9 percent in 2008-09.

Public sector investment is crucial for catalyzing economic development and it has created spillover effects for private sector investment through massive increase in development spending particularly on infrastructure in the past [See Table-1.6]. However, squeeze on development expenditures made it decelerate at a brisk pace.

Table 1.6: Structure of Savings and Investment (As Percent of GDP)

Description	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09P
Total Investment	17.2	16.8	16.9	16.6	19.1	22.1	22.5	22.0	19.7
Changes in Stock	1.4	1.3	1.7	1.6	1.6	1.6	1.6	1.6	1.6
Gross Fixed Investment	15.8	15.5	15.3	15.0	17.5	20.5	20.9	20.4	18.1
- Public Investment	5.7	4.2	4.0	4.0	4.3	4.8	5.6	5.4	4.9
- Private Investment	10.2	11.3	11.3	10.9	13.1	15.7	15.4	15.0	13.2
Foreign Savings	0.7	-1.9	-3.8	-1.3	1.6	3.9	5.1	8.5	5.3
National Savings	16.5	18.6	20.8	17.9	17.5	18.2	17.4	13.5	14.3
Domestic Savings	17.8	18.1	17.6	15.7	15.4	16.3	15.6	11.5	11.2

P: Provisional

Source: EA Wing Calculations

The contribution of national savings to the domestic investment is indirectly the mirror image of foreign savings required to meet investment demand. The requirement for foreign savings needed to finance the saving-investment gap simply reflects the current account deficit in the balance of payments. National Savings at 13.5 percent of GDP in 2007-08 is the lowest ever level since 1999-2000 and has financed 61.5 percent of fixed investment in 2007-08. The current fiscal year has improved upon this performance and national savings as percentage of GDP stood at 14.3 percent. Domestic savings has also declined substantially from 16.3 percent of GDP in 2005-06 to 11.2 percent of GDP in 2008-09. In the current scenario, net foreign resource inflows are coming in a huge quantum and financing savings-

investment gap. In the current fiscal year too we are expecting inflows of up to 5.3 percent of GDP.

VII. Foreign Investment

Foreign direct investment (FDI) has emerged as a major source of private external flows for developing countries around the world. The developing countries like Pakistan are able to bridge their widening savings-investment gap through this important non-debt creating inflow. During the last two decades countries have liberalized their FDI regimes and pursued investment-friendly economic policies to attract investment to maximize the benefits of foreign presence in the host economy. In many developing countries,

Table 1.7: Inflow of Net Foreign Private Investment (FPI)

(Million US \$)

Country	2007-08			July-April					
	Direct	Portfolio	Total	2007-08			2008-09		
				Direct	Portfolio	Total	Direct	Portfolio	Total
USA	1309.2	439.2	1748.3	1161.4	520.6	1682.0	745.2	-278.5	466.7
UK	460.4	-125.1	335.2	304.8	-137.6	167.1	220.2	-74.7	145.5
UAE	588.6	4.3	592.9	535.3	17.9	553.2	170.2	9.3	179.5
Germany	69.6	-0.5	69.1	61.7	-0.5	61.2	60.4	-0.2	60.1
Kuwait	36.0	28.3	64.3	31.7	27.9	59.6	10.6	9.9	20.5
Hong Kong	339.8	-245.5	94.3	121.3	-227.5	-106.1	124.4	-35.5	88.9
Norway	274.9	0.0	274.9	154.8	0.0	154.8	91.9	0.0	91.9
Japan	131.2	9.9	141.1	100.3	10.9	111.2	65.2	-4.0	61.3
Saudi Arabia	46.2	-1.6	44.7	37.0	-1.6	35.4	-55.6	0.1	-55.6
Canada	13.3	0.4	13.7	13.0	0.3	13.3	2.1	0.2	2.3
Netherlands	121.6	24.5	146.1	77.4	39.7	117.1	63.8	8.9	72.7
Mauritius	99.6	5.9	105.6	338.7	5.3	344.0	320.7	2.7	323.4
Singapore	24.8	19.6	44.4	23.5	-19.5	4.0	246.2	-35.0	211.2
China	13.7	0.0	13.7	13.2	0.0	13.2	-69.7	0.0	-69.7
Australia	69.6	-73.2	-3.7	56.9	-64.8	-7.9	78.6	-11.6	67.0
Switzerland	169.3	-97.8	71.5	141.4	-79.3	62.1	210.4	-39.6	170.8
Others	1384.9	51.8	1436.7	546.5	7.1	553.7	920.8	-3.5	917.4
Total	5152.8	40.1	5192.9	3719.1	98.9	3818.0	3205.4	-451.5	2753.9

Source: State Bank of Pakistan

FDI has triggered technology spillovers, assisted human capital formation, contributed to international trade integration, helped in creating a more competitive business environment and promoted enterprise development. FDI has prevented developing countries from the ill-effects of exploding debt accumulation to finance their development needs and thus enabled exchange rate stability. Given the contagion of the global financial crisis developing countries are facing severe cutbacks in their private capital inflows like FDI. Pakistan has also witnessed a substantial fall in FDI inflows in 2008-09 in line with all other developing countries. However, the case of Pakistan is exacerbated by the deteriorating security environment.

The overall foreign investment during the first ten months (July-April) of the current fiscal year has declined by 42.7 percent and stood at \$ 2.2 billion compared to \$3.9 billion in the same period of last year. The overall foreign investment has two components – foreign direct investment (FDI) and portfolio investment i.e., investment in the equity market. Foreign direct investment (private) showed more resilience and stood at \$3205.4 million during the first ten months (July-April) of the current fiscal year as compared to \$3719.1 million in the same period last year thereby showing a decline of 13.8 percent (See Table 1.8). Private portfolio investment on the other hand showed an outflow of \$451.5 million as against an inflow of \$98.9 million during the comparable period of last year.

S.No.	ECONOMIC GROUP	2004-05	2005-06	2006-07	2007-08	July-April	
						2007-08	2008-09
1	Food, Beverages & Tobacco	22.8	61.9	515.8	57.1	35.3	146.5
2	Textiles	39.3	47.0	59.4	30.1	25.1	28.4
3	Sugar, Paper & Pulp	4.3	5.1	17.4	10.5	10.1	14.3
4	Leather & Rubber Products	6.5	8.2	7.3	5.5	4.8	4.0
5	Chemicals & Petro Chemicals	52.1	72.4	52.5	106.2	93.3	82.0
6	Petroleum Refining	23.7	31.2	155.2	74.5	62.9	103.7
7	Minning & Quarrying	0.5	7.1	23.7	42.3	24.1	12.8
8	Oil & Gas Explorations	193.8	312.7	545.1	635.0	509.4	612.1
9	Pharmaceuticals & OTC Products	38.0	34.5	38.4	45.6	41.0	26.2
10	Cement	13.1	39.0	33.7	102.5	95.5	31.7
11	Electronics & Other Machinery	16.5	21.0	22.0	51.9	45.5	39.9
12	Transport Equipment(Automobiles)	33.1	33.1	50.4	111.5	81.0	70.2
13	Power	73.3	320.6	204.6	70.3	52.2	80.2
14	Construction	42.7	89.5	157.1	89.0	77.2	76.8
15	Trade	52.1	118.0	173.4	175.9	139.6	147.7
16	Communications	517.6	1937.7	1898.7	1626.8	1164.9	828.5
	1) Telecommunications	494.4	1905.1	1824.3	1440.1	1032.6	767.1
17	Financial Business	269.4	329.2	930.1	1607.9	997.1	680.9
18	Social & Other Services	24.7	64.7	88.4	107.4	94.6	81.2
19	Others	78.9	65.5	166.1	202.9	165.5	-28.3
TOTAL		1,524.0	3,521.0	5,139.6	5,152.8	3,719.1	3,038.8

Source: SBP

US kept its distinction of being the largest investor with 23.2 percent stake in the FDI. Other big investors originated from Mauritius (10.0 percent), Singapore (7.7 percent), UK (6.9 percent), Switzerland (6.6 percent), UAE (5.3 percent) and Hong Kong (3.9 percent) [See Table 1.7].

The communication sector (including Telecom)

spearheaded the FDI inflows by accounting for 27.3 percent stake during July-April 2008-09 followed by financial business (22.4 percent), energy including oil & gas and power (22.7 percent), and trade (4.9 percent) [See Table 1.8]. The current wave of uncertainty in the global demand and economic activity in the country has a major backlash on FDI inflows.