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In June 2024, Pakistan's Finance Minister presented the budget for the fiscal year 2024-25, sparking significant controversy and debate. Basic necessities such as bread, butter, and tetra-pack milk have been reclassified as luxuries, subjecting them to higher taxes. Additionally, the petroleum levy was raised from 60 to 80 rupees per liter, significantly increasing fuel costs and impacting the prices of essential goods. Critics argue that the budget aligns too closely with IMF directives, emphasizing austerity measures at the expense of local economic needs.

The recent budget has faced significant backlash, with various associations and individuals voicing their concerns. Critics argue that the budget places an undue burden on consumers and hampers economic recovery efforts. Additionally, there is widespread criticism of the heavy reliance on direct taxes, which primarily affect a limited taxpayer base and risk undermining business confidence.

These fiscal measures come at a time when limited fiscal buffers and vulnerabilities pointed out by the World Bank’s latest Crisis Preparedness Gap Analysis pose significant risks. Political instability could derail economic recovery with potential protests and disruptions. However, BMI forecasts a 3.2% GDP growth for FY2024-25, presenting an optimistic view following a staff-level agreement with the IMF. Recent figures show the economy expanded in FY2023-24, surpassing the 1.8% consensus forecast. This analysis delves into Pakistan's economic performance in FY2024, examining GDP growth, sectoral developments, trade dynamics, and the impacts of recent budgetary measures on various industries.

Economic Performance

Pakistan’s GDP growth accelerated to 2.4% in FY2024. This growth was broad-based, with the agriculture sector expanding by 6.3%, while industry and services grew by 1.2%. The markets have rallied due to improvements in economic conditions. The PSX has surged by 79.5% since July 2023, with the KSE 100 index rising to 78,810 points by June 21, 2024. The government has initiated discussions with the IMF for a new three-year program to further support the external sector and encourage investment flows to steer the economy toward its potential growth.

CPI inflation reached its lowest level in 30 months, with YoY inflation recorded at 11.8 percent in May 2024, a significant decrease from 38.0 percent in May 2023. This decline can be attributed to monetary tightening, fiscal consolidation, smooth supplies of food items, favorable global commodity prices, and exchange rate stability. The government's efforts have played a significant role in containing inflation, demonstrating its commitment to price stability.

The fiscal accounts have improved during Jul-Apr FY2024, led by various revenue-enhancing and expenditure-control measures. As a result, the fiscal deficit has reduced to 4.5% of GDP from 4.7% of GDP last year. Effective management of non-interest spending has improved the primary balance to a surplus of 1.5% of GDP, keeping it well on track to meet the full-year target of 0.4% of GDP.

A sustained improvement was observed in the current account balance. The current account posted a deficit of $0.5 billion for Jul-May FY2024, compared to a deficit of $3.9 billion last year, largely reflecting improvements in the trade balance and remittances. YoY, exports increased by 17.3% to $3.0 billion.

Sectoral Analysis

Agriculture Sector

- The agriculture sector demonstrated robust growth in FY2024, backed by strong quarterly growth rates of 8.6% in Q1, 5.8% in Q2, and 3.9% in Q3. This recovery is attributed to government initiatives, improved input supply, and increased credit disbursement to farmers.
- Important crops, including cotton, rice, and wheat, showed healthy growth, while sugarcane and maize experienced slight declines. During Jul-May FY2024, farm tractor production increased by 44.5% and sales by 48.0%. Agricultural credit disbursement also increased by 34.5% during this period.
- Despite these gains, the budget introduces new taxes on crucial inputs such as machinery and pesticides, threatening to increase production costs for farmers, particularly smallholders who already face barriers in accessing subsidies and support. The budget's failure to address critical issues like land reforms and crop diversification further jeopardizes the sector's long-term sustainability.

Manufacturing Sector

- The large-scale manufacturing (LSM) sector experienced moderate growth of 0.45% during Jul-Apr FY2024, marking a notable improvement compared to the 8.8% contraction during the same period last year. After consecutive negative growth in Q1 and Q2, the LSM sector is now showing a recovery in Q3 of FY2024. Nearly 50% of sub-sectors have recovered and posted positive growth.
- Factors such as high inflation, prolonged tight monetary policy, and the slow recovery process in major trading partners contributed to the initial contraction of the LSM sector. Additionally, the industrial sector grapples with high energy costs, outdated machinery, and regulatory hurdles that hinder growth. New taxes on industrial inputs and energy further strain profitability, exacerbating the sector's competitive disadvantages. Despite some incentives in the budget, a lack of strategic infrastructure investments and clear diversification strategies restricts the industry's potential to contribute significantly to economic recovery.

Trade Sector

- The 2024 budget introduces measures aimed at boosting exports by reducing export duties and providing subsidies. However, these efforts are overshadowed by new taxes on imported raw materials and intermediate goods. The overall impact has raised production costs for exporters, undermining Pakistan's competitive edge in global markets.
- Persistent bureaucratic inefficiencies and inadequate infrastructure further hinder the sector's growth potential, preventing exporters from fully capitalizing on global opportunities.

Pakistan's Trade Overview July FY'24 vs. July FY'23

	July FY'24	July FY'23	% Change
Import Value ('000 US$)	3,705,022	4,981,491	-25.62
Export Value ('000 US$)	2,067,926	2,250,259	-8.10
Trade Balance ('000 US$)	-1,637,096	-2,731,232	40.06

Source: Pakistan Bureau of Statistics

- In July FY'24, Pakistan's import value was recorded at 3,705,022 thousand US dollars, which represents a significant decrease of 25.62% compared to the import value of 4,981,491 thousand US dollars in July FY'23.
- The export value in July FY'24 stood at 2,067,926 thousand US dollars, showing a decrease of 8.10% from the 2,250,259 thousand US dollars recorded in July FY'23.
- Despite the 2024 budget's efforts to boost exports by reducing export duties and providing subsidies, the increased production costs due to higher taxes on imports have undermined Pakistan's competitive edge in global markets.

Pharmaceutical Sector

- The recent taxation changes in Pakistan have severely impacted the pharmaceutical sector, potentially crippling its economic viability. Industry experts highlight that introducing multiple taxes, including a 10% surcharge on salaries above Rs10 million, has already burdened the sector, making treatments increasingly unaffordable. The imposition of a sales tax on all diagnostic kits is projected to raise the cost of medical tests and kits by 20-25%, further straining the healthcare system.
- The export industry faces significant setbacks, with the previous 1% tax on exports now replaced by a 29% income tax and a 10% super tax, which could halve the current $300 million in pharmaceutical exports. Experts argue that this approach discourages investment and could lead to a larger undocumented economy and increased smuggling. Despite the positive impact of deregulating non-essential medicine prices, which improved access and reduced spurious drugs, the new export taxes threaten to undermine these gains and stifle the industry's growth.

While the 2024 budget introduces several measures aimed at fiscal consolidation and economic recovery, it falls short of addressing critical structural challenges across various sectors. The heavy reliance on direct taxes and new taxation policies has sparked widespread discontent among stakeholders, undermining confidence in Pakistan's economic prospects. Comprehensive reforms, targeted investments, and strategic policy adjustments are essential to overcoming these challenges and fostering sustainable economic growth.