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Budget 2020-21: Cutting expenses in pandemic

Non-development expenses should be reduced instead of development expenditure

DR MANZOOR AHMAD | June 22, 2020

Representational image. PHOTO: REUTERS

ISLAMABAD: The recently released Economic Survey and the budget document present a rather worrying picture.

Unfortunately, with a few exceptions, legislators and opinion-makers are not dealing with the matter constructively and the usual point-scoring game is being played. The elite is using the chaotic conditions to benefit themselves to the extent they can.

For the first time in the past 68 years, Pakistan's gross domestic product (GDP) growth has fallen to negative 0.38%. Not only it missed almost all the growth targets, whether it was industrial, services or agriculture, in most cases, the growth was negative.

Pakistan's public debt has risen by almost 40% in the past two years – from Rs30 trillion to Rs41 trillion. As a percentage of revenue, debt servicing has gone up from 37% to 62% within one year and per capita income has further shrunk to $1,271 from $1,363.

Of course, the pandemic has a role in such a worsening situation, but the nine-month data before Covid-19 was also not very promising.

In this scenario, the best way forward would have been to look at the data and plan the budget accordingly.

We are deceiving ourselves by showing highly exaggerated expected revenues. Last year, when the revenue target was fixed at Rs5.5 trillion, an increase of 45%, it was patently obvious that to achieve this in a slowing economy would be impossible.

The same folly is being repeated now by counting on a rise of 27% in income while the economy continues to shrink. The revenues have been stagnant since 2018, or even before the outbreak of coronavirus.

If the revenues are not rising and the country has reached the limit of high taxation and borrowing, what else can be done?

The only way seems to be to cut the non-development expenditure until such time that we can afford otherwise. Currently, almost 60% of expenses is on interest payments and defence.

Without controlling these big-ticket items, we should not expect to be able to control expenditure. Temporary debt relief could provide some breathing space but is not a real solution.

Instead of cutting down on non-development expenditure, it is the development expenditure that has been reduced further – to Rs650 billion. Public investment is the only tool which the federal government has for coping with unprecedented unemployment and for providing fiscal support for a contracting economy. If there is one area which needs a boost, it is the public sector expenditure.

It could at least have been restored to the level of 2017-18 when the allocation was Rs1,001 billion.

According to the World Bank, "Pakistan's share of public investment in its GDP is one of the lowest in the world... This results in inadequate infrastructure, lack of access to sufficient levels of energy and water, poor quality of schools and hospitals. The problem is further exacerbated by low private investment, the share of which in GDP is also a dismal 10%. With such low investment, it is not likely that the employment situation or any other social indicator can improve."

Positive signs

While there is so much doom and gloom, the budget does have some positive points. It is relatively tax-free. It seems that the newly set-up National Tariff Policy Board, headed by the adviser to prime minister on commerce, has become functional.

The budget includes several recommendations for rationalisation of customs duties, particularly on industrial raw material and smuggling-prone items.

Unfortunately, several of these changes have been made specifically for selected industries through Statutory Regulatory Orders (SROs). Also, overprotection to some industries, which makes them uncompetitive, has not been addressed.

It was expected that the tariff board would simplify tariffs and level the playing field, but that objective seems to have been delayed to a future date. There is a need to set up or empower similar policy boards for other taxes so that the reforms process can be separated from the revenue collection function.

Trade across borders

The decision to introduce the system of advance ruling and authorised economic operators by the Customs Department would greatly facilitate trade and reduce the cost of trade across borders where Pakistan fares poorly compared to its competitors. This step may also improve Pakistan's position in the World Bank's Doing Business rankings.

Another positive step of the budget is to reform the withholding income tax regime, including the change in collection of advance tax on imports from person-specific to goods-specific. This will reduce rent-seeking as many industrial concerns have been benefitting from this differential at the expense of small and medium enterprises.

Exempting income of charitable trusts, including some deserving hospitals and educational institutions, from income tax is another welcome step.

This measure would somewhat compensate the low spending on social sectors and perhaps encourage more donations to these entities and enable them to expand their social network.

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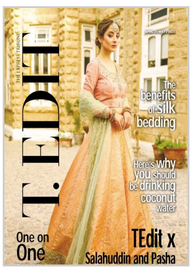

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