Budget Strategy Paper & Medium-Term Fiscal Framework

FY2023-24 to FY2025-26

Finance Department
Government of the Punjab

Contents

I. Medium-Term Macroeconomic Framework

Pakistan`s economy continued to face enormous challenges during FY2022-23. Major challenges included devastation caused by floods, commodity shock from Ukraine war, and the tightening of external and domestic financing conditions together with policy backsliding which aggravated economic conditions and halted the pace of post-pandemic recovery. But this phenomenon was not only Pakistan specific as the global economy also faced decline in growth from 3.5% in 2022 to 3% during 2023. The impact of slowdown in global economy is more pronounced in emerging and developing economies of the world, such as Pakistan. Due to various factors, the target of GDP growth of 5% for FY2023 could not be achieved and the country's economy contracted by 0.17% from 6% growth in FY2022.

Based on the prevailing economic conditions the medium-term macroeconomic framework is presented below:

Table-1	**Actual**	**MTFF Forecast**		
Macroeconomic Framework	**2022-23**	**2023-24**	**2024-25**	**2025-26**
Real GDP Growth (at Basic Prices) (%)[1]	-0.17%	2.80%	3.20%	3.60%
Inflation (Average) (%)	29.2%	25.8%	20.0%	17.0%
Nominal GDP Growth (%)	26.15%	28.6%	23.2%	20.6%

- Government budget projections for FY2023 indicated an uptick in economic activity based on optimistic projections and strong performance of key indicators by targeting the GDP growth at 5%. However, the devastating floods hit the economy hard with a loss of PKR 3.9 trillion (US$15.2 billion) to the national GDP and raised the rehabilitation requirements additionally worth PKR 4.2 trillion. This led to slowdown in growth causing contraction of the economy by 0.17% which is even higher than the negative growth during COVID-19 period i.e. FY2019-20. The negative growth of manufacturing and commodity production`s sectors coupled with marginal growth in the services sector compared to previous year, contributed mainly in dismal performance of economy during FY2022-23. For forward estimates of growth, World Bank report namely "Pakistan Development Update" has been used as a reference published in Apr`2023 which foresees economic recovery from FY2024 onwards.
- During FY 2023, Pakistan faced an inflationary hike that was unparalleled in the last forty years causing exorbitant increase in cost of living. This was exacerbated due to disruptions in the global supply chain resulting from the Ukraine conflict. As Pakistan relies heavily on imported energy and food items, it has been particularly susceptible to external price fluctuations. Import costs have risen, and inflation

[1] Estimates are provisional and extrapolated from the World Bank and the IMF forecast of country`s economic outlook.

persisted at double-digit levels throughout FY2022-23. Furthermore, floods inflicted significant damage on both major and minor crops, leading to disruptions in domestic food supplies and price hikes.

- The forecast of inflation by international development organizations and domestic economic analysts reveals that it is anticipated to remain in the double digits despite expected economic recovery from FY2023-24 onwards. This is primarily because of high monetary policy rate, high imports, and the upward revision of energy tariffs leading to impact not only the cost of production but also the basket price of consumer goods.

The state of the national economy surely has a bearing on the provincial economy. However, despite pressing economic challenges, the Government of Punjab remains committed to economic recovery and stability over the medium-term and the same has been considered while finalizing the estimates of revenues and expenditures for the Medium-Term Fiscal Framework (MTFF) for the period FY2024-FY2026.

II. Medium-Term Fiscal Framework (MTFF)

The primary objective of the Medium-Term Fiscal Framework is to facilitate policy formulation based on reliable projections of revenues and expenditures. It reflects upon various sources of revenue and heads of expenditure considering historical trends as well as emerging challenges and policy measures of the Government to deal with them. It also indicates specific requirements of the Government and its strategic priorities in the medium-term, with planned levels of revenue balance (Total Revenue less Current Expenditure) and the budget balance (Total Revenue less Total Expenditure) while considering the quantum of estimated provincial surplus committed by the Provincial Government under the IMF Program.

Under this MTFF, the Government has aimed to enhance revenues and rationalize expenditures to create fiscal space to spend sizable amount on the infrastructure development of the Province. Moreover, the reduction in non-essential spending coupled with increased focus on pro-poor initiatives has also been the key priority while finalizing the estimates of MTFF period.

Baseline year (FY2022-23) is critical to project forward estimates of MTFF period i.e. FY2024-2026; therefore, its alignment with economic situation, macro variables, FBR targets and Government's priorities remained in focus in order to ensure proper estimation for next three financial years. Moreover, the projections are also guided by the Government's priorities, challenges, and fiscal risks of the Province.

Keeping foregoing in view, the estimates of revenues, current expenditure, revenue balance and development expenditure are summarized below:

(Rs. in billion)

Table-2	Actual	MTFF Forecast		
Medium-Term Fiscal Framework	**2022-23**	**2023-24**	**2024-25**	**2025-26**
A - General Revenue Receipts	2,491	3,200	3,794	4,379
B - Current Expenditure	1,667	2,074	2,244	2,564
C = (A-B) Revenue Balance	**824**	**1,126**	**1,550**	**1,815**
D - Net Capital Receipts	(226)	(337)	(64)	(55)
E = (C+D) Available Resource for Development	**598**	**789**	**1,486**	**1,760**
F - Development Expenditure	589	655	760	877
G = (E-F) Budget Surplus/ (deficit)	**9**	**134**	**726**	**883**

a) General Revenue Receipts

General Revenue Receipts (GRR) of the Government represent revenue collection which includes three streams namely; share of Punjab in Federal Divisible Pool, Provincial Tax Revenue and Non-Tax Revenue. The macroeconomic outlook of the country and the potential impact of policy measures are the primary sources of revenue projection. A snapshot of revenue projection, based on performance of FY2022-23, for the next three financial years FY2024-2026 is given below:

(Rs. in billion)

Table-3	Actual	MTFF Forecast		
General Revenue Receipts	**2022-23**	**2023-24**	**2024-25**	**2025-26**
FBR Collection	7,169	9,308	11,036	12,741
A- Punjab`s Share in FDP	**2065**	**2,675**	**3,172**	**3,662**
YoY Growth- FBR	17%	30%	19%	15%
Total Tax Receipts	310	363	441	520
Non-Tax Receipts	116	162	181	198
B- Total Own Source Revenue (OSR)	**426**	**525**	**622**	**717**
YoY Growth- OSR	-1%	23%	18%	15%
(A+B) General Revenue Receipts	**2,491**	**3,200**	**3,794**	**4,379**
YoY Growth-GRR	14%	28%	19%	15%

The General Revenue Receipts (GRR) of the Government for FY2022-23 was budgeted at Rs. 2,521 billion. This has, however, been realized to the tune of Rs. 2,491 billion which is slightly (i.e. -1%) low from the budget estimates of FY2022-23 mainly due to less than budgeted receipt of own source revenue collection of the Province. For MTFF period, an average growth of 21% is forecasted in GRR against the historical average growth of 12% for the last five fiscal years (FY18-FY22) primarily due to growth in FBR revenues led by high inflation and impact of policy measures of the Provincial Government to increase own source revenue collection.

Table-4	Actual	MTFF Forecast		
Revenue Components as % of GRR	**2022-23**	**2023-24**	**2024-25**	**2025-26**
FDP as % of GRR	82.9%	83.6%	83.6%	83.6%
Own Source Tax Revenue as % of GRR	12.4%	11.3%	11.6%	11.9%
Own Source Non-Tax Revenue as % of GRR	4.7%	5.1%	4.8%	4.5%

It is pertinent to mention that historically (based on last five financial years) 80% of the GRR has been contributed from the Federal Divisible Pool (FDP) share of Punjab under the 7th NFC Award, whereas around 14% has been collected from provincial tax receipts and around 6% comes from non-tax receipts including federal grants. For projected period (Table-4) percentages are aligned with the historical averages with slight decline in the share of own source tax collection but increase in the FDP share of Punjab during next three financial years. The primary reason behind this is upward revision of FBR collection targets under the IMF program and impact of measures taken by the Federal Government to tax the real estate sector under Sections 236C and 236K of the Income Tax Ordinance 2001, which on the other hand has negative impact on the collection of Provincial own source revenue from Stamp Duty.

Federal Divisible Pool: Punjab`s finances are heavily reliant on the federal transfers which is based on collection of taxes by the FBR. For base year FY2022-23, FBR growth was budgeted at 14% which turned 17% mainly due to increased collection of taxes following upward revision of the FBR target by the IMF and the levy of new taxes on the real estate sector. This impacted the federal divisible pool share of Punjab positively and resultantly the actual inflow of FDP increased the budget estimates of FY2022-23. The base year FDP share growth remains 17% compared to previous fiscal year receipt, reasonably higher than the average FDP growth of 13% based on performance of last five financial years (FY2018-2022). For projections of FDP during MTFF period, 21% growth is targeted which is aligned with the historical average growth of 21% during last three financial years but higher than the average growth of last five financial years (FY2018-FY2022) i.e. 13%. The possible reasons of growth in FBR collection being translated into FDP share of Punjab include economic recovery, high inflation, application of new taxes e.g. 236C & 236K of the Income Tax Ordinance 2001 and policy measures of the Federal Government to raise the tax.

Own Source - Tax Revenue of the Province: The second important component of GRR is the own source tax collection of the Province which has outperformed average collection of last 3 financial years by achieving 20% growth mainly due to post pandemic recovery of the economy especially the services sector of the country. This growth was far ahead of the last five FYs` average growth of 9%, but the momentum could not continue due to economic slowdown starting from FY2023. For FY2022-23, an year-on-year growth of 18% was initially budgeted, but it was realized to be 8% compared to the actual collection of the previous financial year. This growth rate was lower than the average growth rate of the last three financial years i.e 20%, but closely aligned with the average growth rate of the last five financial years (FY2018-FY2022) i.e 8.7%. The factors contributing to the sluggish growth in tax revenue include alterations in provincial Stamp Duty rates and increased taxation under Sections 236c and 236k of the Income Tax Ordinance 2001. These changes have resulted in a decrease in transactions involving the transfer of immovable property within the Province. For tax revenue estimates during MTFF period, a growth of 17% is set following the assumption of economic recovery, implementation of revenue mobilization strategy, and anticipation of new taxation measures like:

- Implementation of long-awaited revaluation of rental tables of property in Punjab and shift to DC valuation
- Expected increase in the rate of Stamp Duty in urban areas
- Implementation of lease-based Agriculture Income Tax rates
- Efficiency measures for tax base enhancement by Punjab Revenue Authority

Tax agency-wise projection of own source tax collection estimates is at **Annex-A.**

Own Source - Non Tax Revenue of the Province: Non-tax receipts mainly include Net Hydel Profit (NHP), sales/lease of Government owned assets, royalties from mines extraction, water rate charges, traffic challans, universal health insurance proceeds and some other user fees. In provincial non-tax receipts expected growth for the projected period is 20% against the actual growth of 5% for the last five financial years (FY2018-2022) and 18% for the last three financial years (FY2020-FY2022). For baseline year, the actual collection was 29% less than the budgetary target mainly due to non-realization of proceeds from disposal of Government assets and NHP arrears from the Federal Government. For projected period of MTFF, the reason of expected growth in non-tax revenue include:

- Release of NHP arrears by the Federal Government.
- Increased reimbursements from provincial health insurance scheme which is a new initiative.
- Expected inflow of PSDP grants in the range of 10-20 billion during projected period of MTFF.

The details of department-wise non-tax collection estimates is at **Annex-B.**

b) Current Expenditure

The Government's current expenditure for FY2022-23 was initially budgeted at Rs. 1,712 billion. However, it was realized to be Rs. 1,667 billion, marking a 21% increase from the actual current expenditure of FY2021-22 and a 3% decrease from the budgeted amount. The reported growth during FY2022-23 surpasses the average growth rates of the last three and five financial years, which stand at 7% and 10%, respectively. This heightened growth can be attributed to several factors, including a significant rise in salary and pension rates compared to historical averages, impact of inflation leading to increase in operating expenses and utilities costs, and substantial depreciation of the Rupee against foreign currencies throughout the year.

The projections for the Medium-Term Fiscal Framework (MTFF) period anticipate an average growth rate of 15% for current expenditures. This contrasts with the historical average growth rate of 10% over the last five financial years (FY2018-2022). Regarding current expenditure, it is pertinent to mention that almost 75% of the current expenditure includes salary, retirement benefits and transfers to local governments which is quite inflexible, therefore, the probability of higher variance in current expenditure remains low during routine years which are without any unusual event. The driving forces of variation in current expenditure include inflation, salary raise, and pension expenditure in addition to social protection measures of the Government, and the same has been the case for projections of forward years wherein these factors have contributed towards the current expenditure growth higher than the average growth of last five financial years i.e 10%.

Moreover, while finalizing these estimates, due consideration has been given to improved service delivery by prioritizing health, education and social protection related requirements of the Province. A snapshot of current expenditure projections for MTFF period is given below:

(Rs. in billion)

Table-5	**Actual**	**MTFF Forecast**		
Current Expenditure Heads	**2022-23**	**2023-24**	**2024-25**	**2025-26**
A- Employee Related Expenses	**414**	**514**	**562**	**646**
B- Employees Retirement Benefits	**324**	**392**	**431**	**482**
C- PFC	**517**	**628**	**679**	**781**
D- Interest Payments	**43**	**68**	**61**	**59**
E- Service Delivery Expenditure	**368**	**473**	**511**	**596**
Repair and Maintenance	46	55	76	106
Purchase of Drugs and Medicines	44	44	58	69
Electricity / Utilities	19	20	26	29
Acquisition of Physical Assets	17	20	24	31
Subsidies	27	62	28	30
POL	18	23	35	40
Other Service Delivery Expenditure	198	248	264	290
F= (A+B+C+D+E) Total Current Expenditure	**1,667**	**2,074**	**2,244**	**2,564**
YoY Growth - Current Expenditure	21%	24%	8%	14%

c) Net Capital Receipts

Net Capital Receipts is the difference of current capital receipts and current capital expenditure. The baseline year i.e. FY2022-23 represents a negative flow of funds amounting to Rs. 211 billion which is likely to continue during the MTFF period i.e. FY2024-FY2026 in the range of negative Rs. 55-337 billion. The table below shows high volumes of negative net capital receipts during the base year (FY2022-23) and the first year of MTFF period (FY2023-24) which is mainly due to retirement of commodity debt in these two years which has evolved as a circular debt having severe financial implications for the Government. The other reasons for negative capital account include massive Rupee depreciation resulting in higher debt servicing expenditure and the lower-than-expected receipt of financing from multilateral donors. However, the gap between capital expenditure and capital receipt is expected to squeeze in years ahead mainly due to improved pace of foreign aided development projects and stabilization of PKR-USD exchange rate.

The projected estimates of net capital receipts are summarized below:

(Rs. in billion)

Table-6	**Actual**	**MTFF Forecast**		
Net Capital Receipts	**2022-23**	**2023-24**	**2024-25**	**2025-26**
A- Capital Receipts	121	145	98	114
B- Capital Expenditure	347	482	162	169
C= (A-B) Net Capital Receipts	**(226)**	**(337)**	**(64)**	**(55)**

d) Development Expenditure

Expenditure by the Government that enhances its capability of service delivery to citizens is classified as development expenditure. Reference Table 7 below, the development expenditure stands at Rs. 589 billion during the base year (FY2022-23) which is 14% less than the budgeted spending for the year but close to the development spending during the same period of the preceding financial year amounting to Rs. 586 billion. Over the past five years, historically, the Government has allocated an average of 23% of total expenditure towards development. However, for FY2022-23, this allocation increased to 26%, and it is projected to remain at 25% during the envisaged period of the Medium-Term Fiscal Framework (MTFF). Likewise, the proportion of development expenditure relative to General Revenue Receipts (GRR) stands at 24% for FY2022-23, compared to an average of around 20% over the last five years, a trend expected to continue into the projected period as well.

The forecast of development expenditure during MTFF period is guided by the macro variables, fiscal commitments under IMF program and the strategic priorities of the Government. A snapshot of projected development estimates for the MTFF period is given below:

(Rs. in billion)

Table-7	Actual	MTFF Forecast		
Development Expenditure	**2022-23**	**2023-24**	**2024-25**	**2025-26**
Development Expenditure	589	655	760	877

The Government intends to invest more on development projects to generate economic activity and improve service delivery in the Province. The anticipated average growth in development expenditure over the MTFF period is 14%, as compared to actual average growth of 4.5% observed over the past five financial years (FY2018-FY2022). The size of development spending during the MTFF period could have been much better if the Government had not faced challenges like retirement of ballooning commodity debt, and commitments of estimated provincial surplus.

III. Fiscal Risks Analysis

Fiscal Risks Analysis involves identifying and quantifying risks, classifying them, reporting them through disclosure statements, analyzing their potential fiscal impact wherever applicable, and implementing appropriate risk mitigation measures to minimize the impact. Governments are exposed to various risks and uncertainties that could impact their fiscal outlook. Timely recognition of such risks and adoption of measures to reduce their impact need to be made part of financial planning because capital outflow is contingent upon realization of such risks. Pakistan being the developing country is passing through hard times following pandemic, floods, and inflationary surge which make it more vulnerable to such risks. Provinces are part of the Federation, therefore, the risks especially macro risks like stagnant economic growth, high inflation, Rupee depreciation, high policy rate etc. being faced by the Federal Government may also have repercussions for the Provinces

The Government of Punjab assesses its fiscal risks and presents these risks annually as "Fiscal Risks Statement". Referring that document, the possible sources of fiscal risks which may impact the estimates of MTFF are as under:

- **Macroeconomic risks**: fiscal position vulnerability to key macroeconomic variables, including GDP growth, interest rate, inflation, and exchange rate.
- **Fiscal structure**: The fiscal structure and the distribution formula have implications for Provincial Governments due to their reliance on Federal tax collections. Any shortfall in Federal tax collections will ultimately affect the receipts of Provinces through NFC share.
- **Own source revenue**: The variance between the projected and realized collections of own-source revenue compounds the fiscal challenges faced by the Government of Punjab. To address this issue, the Government is actively pursuing sustainable

growth through a Revenue Mobilization Strategy approved by the Provincial Cabinet.

- **Environmental risks**: Punjab is facing high risks from natural disasters and climate-related threats. Floods have been a frequent occurrence in the Province, causing significant damage to infrastructure and the economy. Punjab is also experiencing severe air pollution, particularly during the fall and winter months, which has both direct and indirect costs. In addition to floods and air pollution, Punjab is also facing other climate-related threats such as droughts and heatwaves. To address all such risks, the Government has taken steps like establishment of an Environment Endowment Fund, Climate Budget Tagging and block allocations for environment related initiatives.
- **Pension expenditure**: Rising annual pension expenses have restricted the fiscal space available to the Government to allocate funds for public investments and essential services. The previous pension scheme quickly evolved into an unsustainable financial liability for the Government, presenting a challenging situation. To mitigate this risk, the Government has recently approved a Pension Reform Plan. This plan incorporates measures aimed at managing pension expenditure in the near future and transitioning towards a contributory pension scheme in the long term.
- **Public debt**: The majority of Punjab's debt portfolio is denominated in foreign currency, exposing it to exchange rate fluctuations and primarily refinancing risks. Presently, Punjab maintains relatively low debt levels when assessed as a percentage of its GSDP (Gross Sub-national Domestic Product), standing at 2.9% at the end of FY2022-23. To mitigate this risk, the Government should decrease its dependency on foreign loans and focus on generating adequate own source revenues to meet both its current obligations and development requirements.
- **Provincial Guarantees**: Guarantee support has been granted by the Government of Punjab to GoPb-owned entities and initiatives. At the end of FY 2022-23, GoPb issued Guarantees totaling Rs. 48.9 billion. To manage the risks emanating from the issuance and management of Guarantees, a framework for issuance, valuation, and monitoring of Government Guarantees is being prepared under Punjab Public Financial Management Act, 2022 which will help the Government to manage such risks more efficiently in the future.

IV. Medium-Term Budget Priorities FY 2024-2026

Punjab is confronted with economic challenges that necessitate a shift towards a more sustainable and inclusive growth trajectory by prioritizing strategic initiatives. Government of Punjab is dedicated to pursuing a comprehensive recovery aligned with its established priorities. The Government remains steadfast in its commitment to enhancing security and access to justice, delivering high-quality public services, investing in enhancing capabilities and skills within the public sector, broadening of special safety nets, addressing climate impacts and ensuring the inclusive involvement of the most vulnerable and marginalized segments of society.

Current & Capital Expenditure Priorities

Current and capital expenditure priorities of the Government include:

- Improving resource base of the Province
- Curtailing current expenditure
- Management of increasing pension liabilities
- Improved service delivery in health, education, water & sanitation
- Targeted social protection measures
- Support to local government(s)
- Climate proofing the government investments
- Overhaul of commodity operations regime

Development Expenditure Priorities

Public sector development spending plays an integral role in the mobilization of indigenous resources to uplift the socio-economic condition of the people. The Government's priority in development spending revolves around fostering inclusive economic growth which encompasses sectors such as health, education, energy, small and medium enterprises (SMEs), water and sanitation, agriculture, environment, and human capital development mainly.

The guiding principles of development agenda of the Government include:

- Inclusive economic development
- Making Punjab climate resilient
- Developing vibrant institutions
- Improved governance, transparency, and rule of law
- Citizen-centric policy approach
- Focus on international commitments (SDGs)

The newly elected Government has an extensive array of sectoral initiatives, with a few highlighted below to underscore its emphasis on people-centric areas of provincial development, such as:

- Establishment of five IT cities in Punjab
- Expansion of Danish Schools network
- Establishment of low cost housing units (Apni Chat, Apna Ghar Program)
- Expansion of metro bus network
- Establishment of E-Libraries in Punjab
- Smog and pollution control measures
- Establishment of economic zones
- Inter & intra city road programs

- Expansion of safe city network
- Establishment of nursing school
- Small business loan scheme
- Establishment of working women hostels
- Youth programs (interest free loans, scholarships, technical training etc.)
- Electric motor bikes for females
- Provision of free wifi in major cities

V. Conclusion

Budget Strategy Paper & Medium-Term Fiscal Framework FY2023-24 to FY2025-26 presented under Section 4 of the Punjab Public Financial Management Act, 2022 reaffirms the commitment of the Government to uphold the principles of transparency, responsiveness, inclusiveness, and improved financial management over the medium-term. The Government is committed to support the economy and move towards sustainable and inclusive growth in the medium-term by spending on strategic development projects, working on revenue mobilization and rationalization of current expenditure while maintaining strict fiscal discipline.

Annex-A

(Rs. in billion)

	Actual	MTFF		
Punjab's Tax Revenue	**2022-23**	**2023-24**	**2024-25**	**2025-26**
Board of Revenue	68.3	71.9	81.1	98.0
Excise & Narcotics Control	38.8	44.7	63.8	67.7
Punjab Rev. Authority	201.1	244.7	294.2	352.6
Energy	0.2	0.2	0.2	0.2
Transport	1.3	1.2	1.2	1.2
Total	**310**	**363**	**441**	**520**

Annex-B

(Rs. in billion)

Punjab's Non-Tax Revenue	**Actual**	**MTFF Forecast**		
Departments Wise	**2022-23**	**2023-24**	**2024-25**	**2025-26**
BOR	2.2	3.2	3.8	5.2
Health	7.9	11.6	11.8	14.4
Mines & Minerals	14.2	17.7	20.4	23.4
Irrigation	4.5	10.8	24.8	26.5
Finance	41.5	75.0	76.9	83.0
Police	5.2	6.5	6.8	7.2
Agriculture	2.6	1.6	1.7	1.8
C&W	3.0	4.2	4.4	4.6
Cooperatives	0.0	0.0	0.0	0.0
Education	1.9	2.2	2.3	2.4
FW and Fisheries	1.1	1.9	2.0	2.1
Home	1.9	1.2	1.4	1.5
HUD&PHED	0.7	0.9	0.9	0.9
Industries	4.8	1.6	0.5	0.5
Law & Parliamentary	1.0	1.1	1.2	1.2
L&DD	1.6	1.8	1.9	2.1
Miscellaneous (others, unclaimed deposits, Misc. Recoveries etc)	21.9	20.6	20.5	21.0
Total	**116**	**162**	**181**	**198**