

TOPIC 1 BUDGET DEFICIT OF PAKISTAN

CURRENT AFFAIRS

General, Specific, Summary → Attempt of Question

What is deficit?

- 1- Less collection and more expenditure (Source Lecture)
- 2- A deficit is an amount by which one resource, especially money, falls short of what is required. If expenditure exceed income, Imports exceed exports, or liabilities exceed assets, a deficit exists. (Source Cleartax.in)
- 3- The total amount by which money spent is more than money received (Source Cambridge Uni Press [Google])
[Synonym of deficit is SHORTFALL]

- 1- **BUDGET DEFICIT:** are negative balance between a government's spending and revenues. When a government spends more than it collects in tax revenues, there is a deficit. Conversely, if there is more collected than spend, there is a surplus (Source Investopedia)
- 2- A Budget Deficit occurs when government expenses exceed revenue. Many people use it as an indicator of the financial health of a country. It is a term more commonly used to refer to government spending and receipts rather than business or individuals. Budget deficit effect the national debt, the sum of annual budget deficits, and the cumulative

total a country owes to creditors.

- 3- A Budget deficit occurs when a government's spending on public services, infrastructure, and other projects surpasses the revenue it generates (from taxes, fees etc)

Ask if or add or not [Although this financial imbalance may require borrowing or reducing saving, it can help governments invest in initiatives that provide long term benefits to their citizens. (Source Study master .co.uk)

Example:

Envision a country, where the government plans to improve its transportation system and what healthcare facilities. The government collects currently 15 Billion \$ in taxes, but the project costs you will 18 Billion \$. In this case the country experience give a budget deficit of \$3 Billion. However, having examples a deficit isn't always negative; investing in essential projects like these can lead to a more prosperous society and improved quality of life for its citizens.

INFO POINT

Budget Surpluses occurs when the government's tax revenues are greater than its spending for a particular year."

MAJOR ISSUES OF ECONOMY:

1. BALANCE OF PAYMENT CRISES
2. BUDGET DEFICIT.

Pakistan also faces same issues. Both of these problems are collectively known as Twin problems.

UNDERSTANDING BUDGET DEFICIT

When a budget deficit is identified, current expenses exceed the income received through standard operations. To correct its nation's budget deficit often refer to as **FISCAL DEFICIT**, a government may cut back on certain expenditures or increased revenue-generating activities. (After the fiscal year, any deficit the government has will be added to the national debt.)

What is FISCAL YEAR?

A fiscal year is a period of 12 months, used by organizations in order to calculate their budgets, profits, and losses, at the end of which a firm's accounts are closed. In Pakistan, the government's fiscal year is 1 July of the previous calendar year and concludes on 30 June.

The state fiscal year runs from 1 July through June 30 of the following year, and is named for the calendar in which it ends (e.g. July 1, 2021 through June 30 2022 is state fiscal year 2022.) This means the academic calendar year 2021-22 falls within state fiscal year 2022.

Source
investopedia

A budget deficit can lead to higher levels of borrowing, higher interest payments, and low reinvestments, which will result in lower revenue during the following year.

As Pakistan also faces budget deficit i.e. the collection of tax, fees is less and expenditure is more.

e.g. In Fiscal Year 2021-22, the total amount left with the center is 4.1 Trillion PKR while total expenditure was 8.4 Trillion PKR creating a shortfall of 4.3 Trillion PKR

This issue remains the same in every fiscal year due to multiple reasons and massive negative implementations while major steps should have to be taken to convert the budget deficit to budget surplus.

In Fiscal Year 2021-22 The BD was 4.3 Trillion PKR

" " " 2020-21 " " 4.1 " "

Source
Lecture

In Fiscal Year 2019-20, The BD was 4 Trillion PKR
 In the last 10 years, the average deficit was,
 8.5 trillion PKR.

In the last 20 years, the average deficit was well
 above 2.3 Trillion PKR.

Source: Economic Survey of Pakistan
 Finance division of Pakistan

IMF (International Monetary Fund) works to achieve
 sustainable growth and prosperity of all of its
190 countries

WTO	World Trade Organization
UN	United Nations
WHO	World Health Organization

CAUSES / REASONS OF BUDGET DEFICIT:

- Source
Lectures
- 1- Flawed taxation system results in lesser collection.
 - 2- Debt Servicing
 - 3- Subsidies
 - 4- Economic downturn and rising unemployment
 - 5- Decreased consumer spending
 - 6- Increased government spending and fiscal stimulus
 - 7- High Interest Payments
 - 8- Demographic Factors.
 - 9- Unplanned emergencies (Natural disaster)

1. FLAWED TAXATION SYSTEM RESULTS IN LESSER COLLECTION:

In the fiscal year 2021-22, 6.1 Trillion PKR was collection while expenditure was 8.4 Trillion PKR.

In the F.Y 2020-21, 4.7 Trillion PKR was collected with an expenditure of 7.7 Trillion PKR.

In the F.Y 2019-20, Collection was 4.1 Trillion PKR with 7.2 Trillion PKR expenditure.

The Reasons of less Collection and more expenditure is that Economy of Company/Businesses is not properly documented.

According to a research by IMF (International Monetary Fund) Min 35% of the economy in Pakistan is not documented / partially documented.

When the business unit is too big to hide, they get documented but partially. By doing ~~this~~ ^{this}, they start a pattern of tax evasion.

The biggest Tax ~~evader~~ ^{evader} in Pakistan is REAL ESTATE BUSINESS.

Majority of societies deals in files. The total land in societies is usually less and files that are issued or sold are always way more.

The society owner will never show all the files / total no. of files to FBR, till the society is fully developed in next 10-20 years. This will save the owner alot of money that will otheewise go to tax collection, which is state's right

Builders, Property Dealers, ~~and~~ Industries, Retailors are biggest tax evadors in the Economy of Pakistan. Hotels and Restaurants, Private Hospitals, Private Educational Institutions. All these businesses are partially registered and are biggest evador of tax.

TAX AVOIDANCE: Majority of small businesses are not registered as they are small enough to hide, and avoid tax by ~~with~~ becoming invisible to the system and FBR.

Wood Industry, Private Clinics, Small Laborotaries, Radiological Labs, Small Hotels and Restaurants and Local Shop Keeper are all unregistered businesses doing tax avoidance.

ADMINISTRATION PROBLEM WITH THE TAXATION SYSTEM OF PAKISTAN

1. Problem of documentation

The business units are not properly documented or not documented at all

2- The business is not automated:
 Many of the businesses are not computerized or automated. Major businesses are human dependent. Inspection is done by inspector through paper documented data which opens many doors to errors.

Another reason of failed taxation system is that state has not properly invested in the capacity building of FBR, according to the standards set by IMF, world bank, ECB, ADB etc. i.e. at least 2% of the collected amount must be spent on tax collecting bodies. While Pakistan only spends 0.6% on FBR. Shortfall of funding by the government is the main reason. FBR is not able to document and automate businesses. Furthermore, Salaries are quite less of IRS and Custom officers, results in the involvement in Corrupt Practices.

Until unless proper documentation, automation and proper spending on FBR, sizable increase in collection would remain an exclusive dream.

In the recent past, 2 major steps were taken toward documentation and automation

1. Track and Trace System introduced in the industries.

2. Point of Sale introduced in retailers and other big businesses.

By introducing these measures in the tax collection, a sizable increase has been noticed:

From 2000-2008 ^{We jump from} ~~increase~~ 300 billion to 14 Trillion PKR.

From 2008-13 we reached 2.4 Trillion PKR

From 2013-18 " " 3.8 Trillion PKR

In FY 2020-21, we reached 4.7 Trillion PKR

Real change occurs in 2021-22, when collection was 6.1 Trillion PKR.

Pakistan in last 25 years, crossed the target given by IMF which is 300 Billion dollars.

2. DEBT SERVICING:

Another issue with the budget of Pakistan is debt servicing along with interest.

The minimum 35-40% of the expenditure portion in budget is allocated to Debt Servicing.

In the year 2021-22, total expenditure was

8.4 Trillion PKR, while 3.4 Trillion was allocated to debt servicing.

In FY, 2020-21, 3 trillion PKR was allocated

for debt servicing out of 7.7 trillion PKR expenditure.

In FY 2019-20, total expenditure was 7.2 Trillion PKR and allocation of debt servicing was 3.2 Trillion PKR.

Under NFC, 57.5% of total tax collection goes to the provinces, 42.5% goes to the center.

In FY 2021-22, total collection was 6.1 Trillion PKR out of which 3.8 trillion was given to provinces and center was left with 2.3 trillion PKR only.

Other sources of collection for the center were federal excise duty (FED), issuance of bonds, issuance of license, privatization etc.

3 SUBSIDIES:

Source (Google) { A subsidy is an incentive given by the government to individuals or businesses in the form of cash, grants, or tax breaks that improve the supply of certain goods and services } and generate revenue for the country.

There are 32 state owned enterprises/businesses with more than 400 Billion PKR subsidies and bail out packages are given to these enterprises i.e. PIA, Pakistan Railways, Pakistan Post, National Steel Mills Karachi etc

In 2021-22 budget, 2 Trillion PKR subsidies were spent, from which more than 200 billion PKR on electricity, more than 200 B PKR on gas, petrol, diesel collectively, and more than 200 B PKR on Social Welfare Programs.

PIA has a loan of 400 B PKR and Government of Pakistan provided subsidies of 50 Billion PKR.

Similarly National Steel Mills Karachi was given 23 Billion PKR subsidy by Government of Pakistan.

As for Industries, electricity, gas and social welfare programs, subsidies are required. But the state owned enterprises are burden on the budget of Pakistan.

4 PENSIONS:

Another problem to the budget of Pakistan. In the federal budget 2022-23 pensions were nearly 761 B PKR from which pension of retired defense employees was 550 B PKR.

5 DEFENSE SPENDING:

Pakistan face multiple security threats both internal and external. Internal threats are TTP (Tehreek e Taliban Pakistan), BLA while

external sources include India, security situation of Afghanistan and the maritime security threats in the Arabian sea.

Spending on defence is an almost need unfortunately. Economy of Pakistan is very weak and can not afford huge spending which is above 2 trillion PKR.

~~Spending~~ War on terror and retired military spending is not included in it.

Source
Study
Master
co. UK
Google.

[Some other reasons that effect budget deficit are Demographic factors and unplanned emergencies like natural disasters, floods, earthquakes etc., public health crises like Corona in 2019 or military conflicts.]

BUDGET DEFICIT FORMULA:

$$\text{Deficit} = \text{Government Spending} - \text{Tax Revenue.}$$

The greater the Government spending and lower the tax collection results in greater deficit. In contrast, lower the Government spending and greater the tax revenue, lower the deficit or potentially even a surplus.

~~STRATEGIES TO REDUCE BUDGET DEFICIT:~~ IMPLICATIONS:

- 1 Increase in the Public debt.

{ When a government's expenditure on goods, services, or transfer payments exceed their tax revenue, the government has run a budget deficit, Governments borrow money to pay for budget deficit and whenever a government borrows money, this add this to national debt. } (Khan Academy source)

In FY 2008-09 The total volume of loan on Pakistan was 6 Trillion PKR.

In FY 2012-13 it reached 12 Trillion PKR.

" " 2017-18 " " 29 Trillion PKR

" " 2021-22 it reached 38 Trillion PKR

" " 2022-23 " " 51 Trillion PKR. (Lecture)

Government then increase taxes on businesses to collect tax money and pay off national debt.

2 LESSER ALLOCATION FOR DEVELOPMENTAL PROJECTS:

Less budget is allocated for Industries, dams, canals, roads and other infrastructure development due to frequent budget deficit and country's changes are boom are likely to become less and less.

3 LESS ALLOCATIONS FOR SOCIAL WELFARE ACTIVITIES:

Budget deficit in every year reduce the chances of better health education and security services in the country as less ^{money is} allocated for these departments.

SOLUTIONS / STRATEGIES TO REDUCE BUDGET DEFICIT:

1. By proper documentation and automation of economy
2. By reducing government spending and increasing taxes
3. Increasing Investment to GDP ratio

(Gross domestic product) Pakistan's GDP is below 14%.

GDP is the total monetary or market value of all the finished goods and services provided within a country's borders in a specific time period. Increasing GDP is a sign of economic strength and -ve GDP indicates economic weakness.

Investopedia
Source.

4. Privatization of Government owned enterprises

The Job of government is not to run businesses but to play role of a regulator. Business is the Job of private individuals. therefore state owned enterprises must be privatized to decrease the burden.

on the budget
CONCLUSION:

~~Many people assume that deficits are "bad" but an economist would remind that we tend to stick~~

Sticking to the positive side of deficits rather than doing a ~~material~~ normative analysis. A deficit might be a result of ~~an~~ an event such as a recession which gets paid off the next time an economy experiences a boom (and a budget surplus as a result of that boom. However running many deficits leads to debt, and debt must be repaid. That means eventually paying a debt will limit what a government can spend in the future.
