

## Inflation paradox

We expect that overall Inflation for CY16 will increase as government has invested huge amount in Energy, Transportation and Connectivity. The inflation y-o-y could increase by 4% as per our model (Jan 3.3%).

We believe inflation could keep on increasing until

~ Improvement in tax collection i.e. inclusion of informal sector.

In Pakistan 70% of labour force is associated with informal sectors. As a result it is very difficult for government to collect direct tax. Thus the only option government utilize is indirect taxation. Therefore beside reduction in crude oil prices of petroleum products are not reduced at the same rate. Similarly withholding tax of 0.6% on transactions above amount of Rs50,000 is also one step of government indirect taxation. In order to boost incidence of direct taxation in the tax collection mix, government announced voluntary tax scheme in which 1 % of tax will be charged and source of income will not be required. So far the response has been lukewarm in the month of February wherein only few hundreds have opted for the voluntary scheme.

Last month in Jan 2016 IMF approved loan USD 495 mn for Pakistan which is part of bailout plan given to Pakistan three years ago. Total amount of bailout plan is USD 6.7 bn out of which USD 5.6 bn has been given. Pakistan's precarious balance of payment crisis given weakening real sector is forcing government to go to IMF for bail outs.

Given the removal of subsidies on energy sector and no reduction in electricity price (as significant amount of electricity is generated through oil) - inflation we believe would likely to increase. Since government is working on this issue and developing new power plants which require LNG for electricity production, a comparatively cheaper source of energy. While government is also converting conventional furnace oil power plants into LNG.

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## REK-66

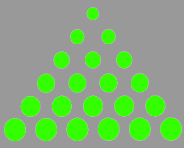
Government should develop mechanism for inclusion of informal sector in taxation. Thus protection of small and medium enterprises should be encouraged and must encourage by interest free loans. Thus development of specialized banks is very important. Since banks branches are not enough as compare to population therefore people take loans from illegal market. On other hand they are also unable to show collateral for getting loans which deprived them from getting loan. Currently there are 9.4 bank branches per 100,000 populations which are not enough.

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