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PROJECT INFORMATION DOCUMENT (PID)
IDENTIFICATION/CONCEPT STAGE

Report No.: PIDC87282

Project Name	Pakista Debt Management Reform Program - Ministry of Finance (RETF)
Region	SOUTH ASIA
Country	Pakistan
Lending Instrument	IPF
Project ID	P161451
Borrower Name	Islamic Republic of Pakistan
Implementing Agency	Debt Policy Co-ordination Office, Ministry of Finance, Islamabad, Pakistan
Environment Category	C - Not Required
Date PID Prepared	20-Oct-2016
Estimated Date of Approval	30-Jan-2017
Initiation Note Review Decision	The review did authorize the preparation to continue

I. Introduction and Context

Country Context

1. The Government of Pakistan has made significant progress in the design and early implementation of its economic reform program in its first three years in office. Upon taking office, the Governments first priority was to re-establish macroeconomic stability and strengthen macroeconomic fundamentals, addressing significant internal and external imbalances. In doing so, it also initiated a number of crucial structural reforms. Upon taking office, it cleared pending power arrears; successfully completed the first equity and strategic sales of its privatization agenda; removed most discriminatory tax exemptions and concessions previously established through statutory regulatory orders (SROs) and transferred the authority to issue SROs to parliament. To improve the business environment, it created the One Stop Shop for business registration and strengthened the regulatory environment for the financial sector. It has also initiated a number of measures to improve tax policy and administration to address the chronically low tax revenue levels. Over the past few years the Government has also strengthened the pro-poor orientation and governance structures of the Benazir Income Support Program (BISP) and expanded the Conditional Cash Transfers (CCT) for primary education. Taken as a whole, the Government has been implementing a comprehensive and challenging set of reforms. More importantly, reform momentum has been maintained and Government of Pakistan (GoP) is deepening reforms and accelerating implementation, despite a challenging political environment.

2. The Government needs to step up the reform efforts and for this, filling-in key gaps is a must. Despite early gains in stabilizing the economy and implementing initial actions on the structural reforms agenda, knowledge gaps, weak capacity of the government to complete the design and implementation of the program, and difficulty in securing the buy-in of all interested stakeholders poses downside risks to the economic reform program. The DFID-fund Trust Fund for

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Accelerating Growth and Reforms main development objective is to support the governments economic reform program by filling knowledge gaps, strengthening the capacity of key institutions federal and provincial--to complete the design and implementation of the reform agenda, and strengthening dialogue and building consensus. More specifically, it will provide assistance for key federal and provincial ministries and agencies, to expand and sustain the fiscal space and revenue collection; liberalize trade and economic activities; facilitate private investment; improve the quality of expenditures and debt management and tackle other binding constraints facing the economy.

3. Fiscal management appears central to the support being provided by development partners. More specifically, one of the two development objectives and reform pillars under the WBG Competitiveness and Growth Development Policy Credit (DPC) was structured around enhancing fiscal management. The reforms supported under this pillar sought to enhance the effectiveness of public investments by creating the necessary fiscal space for higher public investment and more pro-poor spending. Furthermore, one of the four main reform areas of Pakistans program under the recently concluded International Monetary Fund (IMF) Extended Fund Facility (EFF) focused on sustaining fiscal consolidation by broadening the tax base and strengthening the medium-term fiscal framework.

4. Debt management was one of the agreed areas under these interventions. Moreover, a USAID recent project aimed at improving domestic financial markets in Pakistan attempts to complement the support under the broader area of debt management. The focus of the program, however, is different - on regulators such as SECP, SBP (central bank) and the stock exchanges.

Sectoral and Institutional Context

5. Pakistan, like many other oil importing countries, is benefiting from low oil prices, which has reduced the trade deficit (in spite of a notable decline in exports) and increased consumption. Fast-growing remittances and rising investments under the China Pakistan Economic Corridor (CPEC) have also supported growth. The risk of a balance of payments crisis which appeared eminent in 2012/13 has receded, with a significant increase in international reserves resulting from strong remittances, foreign capital and financial inflows and the windfall gain from lower oil prices. With prudent monetary and fiscal management, the current account deficit remains moderate and the foreign exchange market has been stable. However, contractionary fiscal stance and mild recovery of GDP in recent years has been insufficient to reverse debt dynamics of Pakistan as Pakistans debt to GDP ratio has increased to 67.4 percent in 2015/16 compared to 64.1 percent in 2012/13, above the 60 percent limit stipulated in the Fiscal Responsibility and Debt Limitation Act (FRDLA) of 2005. Moreover, interest payments on public debt continue to absorb a large share of governments revenue.

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6. Over the last five years there have been some significant changes in the federalism landscape of Pakistan. The 7th NFC Award sharply increased the share of provinces in federally collected revenue, while the 18th Constitutional Amendment has introduced some profound changes in multi-order governance in Pakistan, including devolution of significant number of additional functions from the federal to the provincial governments. Further to this enactment and particularly with regards to the provinces right to borrow, after an impasse of almost five years, the National Economic Council on July, 1, 2015 took a decision to allow the provinces to borrow in the domestic markets. This change has heightened the need to look into borrowing framework with a federation perspective and subsequently strengthen provincial debt management in parallel with the strengthening at the federal level.

7. The Pakistan Debt Management Support Program (PDMSP) of the TAGR is aimed at

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strengthening debt management at the national and sub-national levels. The Federal pillar aims at improving debt management practice in the Federal Government of Pakistan by assisting the authorities strengthen three key functions: (i) formulation of a debt management strategy and risk management in the Debt Policy Coordination Office; (ii) external debt recording and reporting in the Economic Affairs Division; and (iii) funding in the external markets in the External Finance Wing, Ministry of Finance. Nonetheless, building staff capacity remains at the cornerstone of this program. The Subnational component (currently operational in Punjab and Sindh with the potential to expand to KP/Balochistan) entails building the capacity of the sub-national governments to undertake the existing and additional debt management role in the most efficient and effective manner. As such, the overall program will largely be run through the Bank-executed Trust Fund arrangement. In addition, PDMSP includes two stand-alone Recipient Executed Trust Funds for (i) MoF -- DPCO and EF Wing, and (ii) Economic Affairs Division to enable the client agencies to undertake activities designed for their specific focus areas. This project is essentially one of the envisaged RETFs.

8. Debt management at the federal level in Pakistan is scattered among various institutions and entities, most of them within the Ministry of Finance (MoF), with little coordination among them. Federal debt management operation includes the Budget wing (MoF), External Finance wing (MoF), State Bank of Pakistan (SBP), Central Directorate of National Savings (CDNS), Economic Affairs Division (EAD), and Debt Policy Co-ordination Office (DPCO). Of the six units involved, no single entity has overall responsibility and necessary authority to achieve the debt management objectives and the strategic goals. Although SBP is just a fiscal agent and all other debt entities are located within the MoF, the coordination amongst those remains weak and there is limited planning on how the different sources should contribute to the total funding in a manner that addresses the risks of the current portfolio, while promoting the development of the market for government securities. Also, no single unit has developed a critical mass of expertise in designing and implementing an overall funding program aligned to the government objectives.

9. DPCO remains central to debt management in Pakistan as it is mandated by Pakistan Fiscal Responsibility and Debt Limitation Act (FRDLA) to undertake co-ordination within all designated entities. More specifically, DPCO is responsible for preparing a debt reduction path, providing policy advice on domestic and external borrowing, monitoring and evaluating the debt reduction path and preparing a debt management strategy, providing consistent and authenticated information of government debt and guarantees and maintaining a centralized and updated record of government debt and guarantees. In addition to fiscal policy responsibilities, the DPCO has the functions of a middle office (market, credit and operational risk m anagement functions) within a typical debt management unit. However, since inception, DPCO has had significant capacity constraints to be able to perform its functions which has been a major challenge towards improving debt management in Pakistan.

10. After a gap of almost a decade, Pakistan once more entered the international capital market with the issuance of US$2.0 billion Eurobonds in April 2014. Subsequently, it maintained its presence in the market in the succeeding year through regular issuance of Sukuks and Eurobonds. The structures and capacities at EF wing in MoF, are geared towards managing official financing, less so for managing market funding transactions that require agility in determining the timing, structure and other parameters in the transaction. Currently EF wing execution functions are partly outsourced and the unit's functions revolve exclusively around supporting the transaction. Given Pakistans increasing reliance on Eurobonds and international Sukuks, there is a need to develop institutional capacity to lead these operations backed by strong technical underpinnings by EF wing.

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Relationship to CAS/CPS/CPF

11. The World Bank Group (WBG) Pakistan Country Partnership Strategy 2015-19 is structured around four strategic themes, or result areas: energy, private sector development, inclusion, and service delivery. The proposed grant project is aligned with the fourth result area of Service Delivery (Outcome 4.1: Improved Public Resource Management).

II. Project Development Objective(s)

Proposed Development Objective(s)

12. The objective of the proposed grant project is to assist the GoP to formulate and implement a debt management strategy that contributes to fiscal sustainability while minimizing the funding costs and keeping the debt exposure under control. Achieving the end objective would require building capacity in the entities responsible for different debt management functions. Accordingly, this grant is designed to improve debt management practice in Pakistan by assisting the authorities strengthen two key functions: (i) formulation of a debt management strategy and risk management in the Debt Policy Coordination Office (DPCO); and (ii) raising funding in external markets by the External Finance Wing (MoF).

Key Results

13. DPCO: (i) Extension of the Medium-term debt strategy analysis to 5 years; (ii) potential narrowing of the bands for the currency and refinancing risk indicators as defined per MTDS 2016-19, i.e., (a) share of external debt in total public debt and (b) domestic debt maturing in 1 year (as percent of total); and for EF: (iii) quarterly market monitoring reports.

III. Preliminary Description

Concept Description

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IV. Safeguard Policies that Might Apply

Safeguard Policies Triggered by the Project	Yes	No	TBD
Environmental Assessment OP/BP 4.01			
Natural Habitats OP/BP 4.04			
Forests OP/BP 4.36			
Pest Management OP 4.09			
Physical Cultural Resources OP/BP 4.11			
Indigenous Peoples OP/BP 4.10			
Involuntary Resettlement OP/BP 4.12			
Safety of Dams OP/BP 4.37			
Projects on International Waterways OP/BP 7.50			
Projects in Disputed Areas OP/BP 7.60			

V. Financing *(in USD Million)*

Total Project Cost:	1.53	Total Bank Financing:	0.00
Financing Gap:	0.00		
Financing Source			**Amount**

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Pakistan - Accelerating Growth and Reforms MDTF	1.53
Total	1.53

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