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Founded by M.A. Zuberi

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EDITORIAL

External debt servicing

The State Bank of Pakistan (SBP) report has revealed that the government paid 11.55 billion dollars in debt servicing and repayment of principal due last fiscal year, a rise of 54 percent when compared to the comparable figure of the year before. This rise is unprecedented given that the rise between fiscal year 2017 and 2018 was 23.6 percent. The question is whether the Pakistan Tehreek-i-Insaaf (PTI) government procured more loans to meet the increase in government expenditure during 2019, a claim made repeatedly by members of the opposition particularly the PML-N legislators, or whether it was paying for loans procured during 2018 - the last year in the tenure of the PML-N?

There is little doubt that the PTI government inherited a historically high and economically unsustainable current account deficit of 19 billion dollars necessitating significant funding from external sources. The IMF report uploaded on its website reveals that the government, in its Memorandum on Economic and Financial Policies, acknowledged the need for 38.6 billion dollars for the next 39 months (the duration of the programme commencing July 2019) and stated that “to close the gap for the first 12 months of the arrangement we have secured financing commitments from bilateral and multilateral partners as follows: China $ 6.3 billion, Saudi Arabia $ 6.2 billion, the UAE $1 billion, the World Bank $ 1.3 billion, the Asian Development Bank $1.6 billion and the Islamic Development Bank $ 1.1 billion.”

Around 13.5 billion dollars was procured by the government before the country went on an IMF programme though the loans acquired from China, Saudi Arabia and the UAE, with a maximum of one-year amortization period, was extended and the Fund’s Board of Directors assured of the extension before the loan was formally approved. Multilateral support including from the IMF is projected at around 5 billion dollars in the current year and as per the Memorandum, Pakistan authorities claimed they are “further working on the modalities to ensure the new financing will be consistent with the programme debt sustainability objectives.”

Interest and repayment of debt also significantly rose due to the currency depreciation that began on 16 May 2019 - four days after the Pakistani authorities reached a staff-level agreement with the Fund to adopt a market-based exchange rate. On 21 May, the State Bank delivered on the other ‘prior’ condition to the Fund and raised the discount rate to 12.25 percent and yet again on 16 July to 13.25 percent. The IMF staff-level report maintains that “the debt ratio exceeds 70 percent of GDP under all stress-test scenarios, and it is the most sensitive to the interest rate and exchange rate shock, under which debt reaches 73 and 72 percent of GDP in 2024, respectively. Contingent liabilities from loss-making state-owned entities to the extent not covered by government guarantees represent additional fiscal risks (about 2 percent of GDP).”

What should be a major source of concern for the Khan administration is the Fund’s claim that “the resulting higher inflation and interest rate will initially prompt a surge in interest expenditure. The expected drop in growth rate will negatively affect the fiscal position in the short run but the expected pick-up in growth in the medium-term together with significant fiscal adjustments will help put public debt on a firm downward sloping trajectory.” The short run for low growth is at least one year, and fiscal adjustments so far have not met targets because depreciation lowered imports, though the Saudi oil deferred facility played a major role, thereby reducing tax collections from imports which may have to be met through some other revenue measures during the first quarterly mandatory review with the Fund.

And finally, “bound and stress tests suggest that external debt-to-GDP ratio would be adversely affected by shocks,” and one would assume external and internal shocks. To conclude, one would hope that the government takes appropriate mitigating measures and not only reduces its own expenditure under all heads but also begins to deal with the loss-making state-owned entities, especially those that have been non-operational for years; for example, the Pakistan Steel Mills.