INTERNATIONAL THE NEWS

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The IMF programme

On May 31, 2108, almost a year ago, when the PML-N government finished its term we left an economy that was growing at 5.8 percent and expected to grow faster in the next fiscal year. At that growth rate the economy was creating about 125,000 new jobs every month, just about enough to absorb all the new entrants into the labour market. Our inflation was a little less than four percent and the State Bank interest rate was 6.25 percent.

Just a few months before that we had ended power loadshedding as we were able to set up new power plants with the capacity of 10,000 megawatts. We had set up in the private sector two LNG regasification terminals and a gas pipeline capable of conveying 1.2 billion cubic feet of gas from Karachi to upcountry everyday. We were now able to supply gas to much of the industry on a regular basis.

The war on terror had paid great dividends in the tribal areas and the law and order drive in Karachi had also made Karachi a peaceful city after decades. On all fronts we were making progress and therefore things were looking bright for the Pakistani economy.

Of course no country, no matter how rich or how well managed, is without challenges and like all countries we too had economic issues. Since the passage of the seventh NFC award in 2010, our budget deficits were increasing, in spite of the impressive increase in revenues during the PML-N government. And more problematically our current account deficit was also growing. These were challenges that the new government was going to face, whether it was our government or that of the opposition parties.

It’s worth mentioning that a current account deficit or a trade deficit is not a bad thing necessarily. In fact, for developing countries it is desirable to run a trade deficit. Think of the need that Pakistan had of power plants and machinery for producing cars, textiles, chemicals, etc. It’s best to import those machines and produce those things locally rather than have your people suffer even if the trade deficit goes up for a year or two.

A current account deficit actually only means that foreigners are transferring their savings into the country. For a country like Pakistan, with a low savings rate and an appetite for growth, a current account deficit is indeed expected.

And of course Pakistan is not the only country to have a current account deficit. Indeed, according to latest data Turkey, Argentina and Jordan all had a bigger current account deficit than Pakistan in 2017, and England about the same as us (as a fraction of the size of the economy). But by 2018 our current account and fiscal deficits had grown even more and now that we had imported all the basic infrastructure projects as part of CPEC, it was important to methodically rein in both these deficits.

But when Imran Khan was made the prime minister and he further selected Asad Umar as his finance minister, our economy’s luck finally run out. A few days before taking oath in August, 2018, our prime minister told us he would not go to the IMF. Then as early as September our finance minister told us he was going to the Fund to negotiate a programme, as it was in the larger national interest. But then a few weeks later we were told that the larger national interest lay in not going to the Fund. That we had solved the problem of the current account deficit at least for this year. Unfortunatel,y however the larger national interest kept alternating every fortnight between going or not going to the Fund. Having promised us that they would emulate the prime minister of Denmark, who presumably goes to work on a bicycle, the PTI ended up playing Prince Hamlet of Denmark in their dithering and indecisiveness.

In between, of course, our new rulers kept badmouthing the Pakistani economy, both at home and abroad. This they presumably did to disparage the PML-N but in doing so they destroyed investor sentiment and consumer confidence. With the stock market tanking, foreign portfolio investors pulling out, foreign direct investment declining, and large-scale manufacturing seeing a decline, the growth rate halved. Of course, the fast increasing interest rates didn't help. And while the heavy depreciation didn't increase exports, it did compress imports and caused inflation.

In the last nine months our government borrowed, and spent, a few billion from our friends Saudi Arabia, UAE and China -- while our budget deficit, domestic borrowing and printing of money created new records. But for nine long months our finance minister couldn't decide what to do about the Fund. Moreover in those nine months, the PTI government tried its own remedy. But all it's homeopathic and Unani remedies just made matters worse.

Here are some eye-opening facts. In its quest to curtail our current account deficit, the PTI devalued our currency by 20 percent. It increased inflation. It raised interest rates. It slowed down growth. And indeed it made our economy in dollar terms go from $313 billion down to $280 billion (a loss of $33 billion). Yet for all this pain how much reduction was achieved in the current account deficit? Only four billion dollars. The current account deficit will only decrease from $19 billion to $15 billion.

One reason our current account deficit didn't improve is because it is closely linked to the budget deficit. While the PTI is Rs450 billion behind its own target in revenue collection, it has been quite profligate with money it doesn't have. Although it has cut to the bone all development spending, it has not seen fit to cut any money from current spending. So this year it will make the largest deficit in Pakistan's history.

Presumably frustrated at the rapidly worsening economy, the prime minister let go of his finance minister. In came Hafeez Sheikh and in three weeks he did what the previous incumbent couldn't or wouldn't do in nine months: he finalised a deal with the Fund. No IMF programme is pleasant and this won't be either. It will require considerable belt tightening, much more so than the last time around. However, I would take the new minister and his new tax czar at their word that the poor and middle classes will not be burdened as a result of this programme, that new taxes will be collected from current non-taxpayers, that reliance will be made on direct taxation, and that the poor will be protected from the effect of rising utility prices.

I am sure the current team tried to get the best deal under the circumstances. So, as easy as it is to do so, I won't criticise any specific aspect of the deal. However, I would only say that it is unfortunate that the IMF insisted on language relating to money laundering and terror-financing. This makes us more vulnerable in the FATF and I fear this is yet another stick in the West's arsenal to browbeat Pakistan.

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