Lurking dangers

It is hard to find a parallel in the past on differing perceptions about the state of the economy as we see today. Analysts and generalists are equally confused whether the economy is heading in the right direction or going south.

In our last article, we had indicated that green shoots of stability are visible in some key economic indicators such foreign reserves, exchange rate and improved balance of payments. However, the indicators relating to production, growth and employment is worsening. If the government is highlighting the former, others are showing deep concerns on the latter.

The government is emphasizing four key achievements, which have also led to successful completion of the first IMF Review. These are: contained fiscal deficit (whose details have yet to be published), rising reserves, stable exchange rate and contained domestic credit. Without tempering this point of view, what is somewhat puzzling is the relative indifference shown by economic managers toward the rest of the economy. In their enthusiasm to promote a narrative of stability and turnaround, fundamental economic principles are overlooked. Hyping surplus in current account deficit as a strength of an economy, like that of Pakistan, or generally celebrating massive decline in imports, is to relegate growth and employment as undesirable objectives of economic policy. The more common response to these developments is silence. Policymakers would be well advised to address these perils lest the lurking dangers undermine the nascent stability.

Let us examine the state of the neglected part of the economy. Of utmost concern is the production in both industrial and agriculture sectors. For the last 15 months, production of the large-scale manufacturing sector is declining.

In the last fiscal year, LSM growth was negative 3.64 percent. In the new fiscal year, three months data has shown a negative growth of 5.9 percent. The sub-sectors prominently hit by this production decline include petroleum products (14.48 percent), chemicals (8.93 percent), cement (1.46 percent), iron and steels (33.21 percent), pharmaceuticals (11.95 percent), automobiles (34.13) and food and beverages (8 percent). The only notable positive growth was recorded in fertilizer (15.94 percent) and electronics (5.51 percent). Textiles production was stagnant while some minor sectors also showed small growth.

This decline in production is the mirror image of major decline in imports. Barring a small positive growth of 3.17 percent every group of import has seen double digit declines. The current account deficit (CDA) declined by $4 billion compared to a decrease in imports of $4.4 billion. The increase in exports was $267 million and that too basically from the obscure group of ‘other exports’. Thus all the economic policy has done is compress imports with consequent compression of domestic production.
With such large production decline businesses are resorting to holidays or outright closure. Layoffs are an inevitable outcome. It is estimated by some economists that 800,000 jobs have been lost and much greater loss is in the pipeline. The agriculture sector had a bad start with even the modest target of 11 million bales, taken in the national accounts, is likely to be missed. Until 15 October, cotton arrivals were down by 1.6 million bales compared to the same time last year. Sugarcane was already billed to be negative, from 67 million tons to 64 million tons. Rice is likely to be on track. Wheat is too early to be predicted as sowing is continuing. So it is most likely that even if all the remaining crops do well, cotton would have significant adverse impact on the final agriculture outcome. Thus the growth prospects are not very promising.

The price situation has been most alarming for the common person. Since the beginning of 2019, food inflation has risen from 0.6 percent to 15 percent in September and declined to 13.7 percent in October. Non-food inflation, particularly core inflation, is in the single digit and declining. The prices of items like tomatoes, onions, potatoes, pulses, wheat etc have increased, pinching low-income groups the hardest. Taxation measures and devaluation have led to cost increases which also contributed to higher prices. Even the middle class has felt the pinch as their real and disposable incomes have declined.

The monetary policy stance remains tight as the monetary policy committee (MPC) believes that the economy is still overheated. In its last meeting, the MPC left the policy rate unchanged at 13.25 percent, undeterred by the reservations expressed by many economists. The broad-money supply (M2) has showed no growth. Credit to the private sector has been negative since the start of the fiscal year and was negative Rs4 billion until 1-11-2019 compared to Rs223 billion for the same period last year. High interest rates have reportedly led to debtors asking banks to give them more time to payback. Non-performing loans have shown a small reduction in September relative to June, but with high interest rates this may see some spike.

The prime minister has been expressing great joy and satisfaction on the economic turnaround, and performance of his team. One would hate to spoil his reading of the picture. The least we would like to say is that things have indeed improved in some critical areas, as we noted above, but the larger battle of price stability, investment, growth, employment and poverty reduction is raging. There is no sequential path to fight this battle. The Fund programme would give an average growth of 3 percent during the programme period. That would leave only one year in the government’s term. Would that be sufficient to lead into new elections? The answer is no. Accordingly, the time to act is now.

Without a rebound in production and investment one stands no chance of giving jobs or housing to people. Food distribution and small loans under the Ehsaas Programme are good initiatives but the much-needed economic growth comes when investors believe that there are opportunities that would enrich them and the people alike.

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