Drop in C/A deficit

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February 26, 2020

The news on the external sector of the economy continues to be encouraging. According to the latest data released by the State Bank of Pakistan, current account (C/A) deficit of the country has nosedived to dollar 2.654 billion during July-January of the current fiscal year from dollar 9.479 billion in the corresponding period of last year, showing a massive decline of dollar 6.825 billion or 72 percent. Such a huge fall was possible due to a steep fall of 20 percent to dollar 32.489 billion in import of goods while our exports depicted only a small increase of only 2 percent to dollar 14.442 billion during July-January, 2020. With a massive contraction in imports and only a slight increase in exports, merchandise deficit of the country fell by 35 percent to dollar 11.644 billion in the first seven months of FY20 compared to dollar 18.353 billion in the same period of last year. With dollar 3.237 billion of exports and dollar 5.211 billion of imports, services sector registered a deficit of dollar 1.974 billion while income sector inflows were dollar 374 million against an outflow of dollar 3.952 billion, resulting in a large deficit of dollar 3.578 billion during July-January, 2020. The aggregate deficit of merchandise account, services and income sectors in the first seven months of FY20 stood at dollar 17.196 billion as against dollar 23.867 billion in the corresponding period of FY19. The C/A deficit in the month of January, 2020 at dollar 555 million was lower by 35.84 percent over dollar 865 million in the same month of the previous year but higher by 77.32 percent over dollar 313 million in December, 2019.

Such a significant improvement in C/A balance of the country in a period of less than two years is of course extraordinary and shows that improvement in important sectors could be achieved if a right set of policies is adopted by the government. The PTI government was faced with a mammoth C/A deficit of dollar 20 billion in FY18 when it assumed office with prospects of default looming large due to a continuous decline in foreign exchange reserves that could have disastrous impact on various sectors of the economy due to obvious reasons. Realising the gravity of the situation, the present government opted to take harsh but warranted measures such as a massive depreciation in the value of the rupee and restriction on imports by adjustment in tariffs that yielded the desired compression. As a consequence, not only has the C/A deficit gone down significantly, the exchange rate has also been stabilised and foreign exchange reserves held with the SBP have also risen to a reasonable level of about dollar 12.5 billion to remove the threat of insolvency. It needs to be highlighted, nonetheless, that while imports have declined significantly to improve the C/A balance, exports have not lived up to the level of incentives and expectations to make a difference. Other areas that need attention are the continuous high deficits in both services and income sectors of the C/A. Hopefully, the government will examine the situation in totality and take some imaginative measures to boost exports and narrow deficits in other components of the C/A to ensure that the present improvement is sustainable and on a longer lasting basis so that the country has not to rely on outside sources of finance and could follow independent economic policies without dictation from foreign agencies or governments.

It is of course a matter of great satisfaction that C/A deficit has gone down to 1.6 percent of GDP during the first seven months of FY20 as compared to 5.5 percent in the same period of last year. As per the SBP estimates, the C/A deficit was likely to stay in the range of 1.5-2.5 percent of GDP during 2019-20. Another improvement has been the inflows of over dollar 3.1 billion of foreign investment in domestic debt papers including T-bills and PIBs which has boosted foreign exchange reserves of the country and created a cushion for the government. The SBP does seem to realise that this kind of investment in government papers could suddenly flee the country if monetary policy is eased or some other unfavourable factors come into play. As such, the SBP is not oblivious to the need to build up buffers to cushion the impact of such occurrence.

Anyhow, the healthy outcome in the external sector, besides building forex reserves and stabilising the rupee rate, would also facilitate uninterrupted flow of raw materials and investment goods in the country, promote growth, create employment and contain inflationary pressures in the economy. A combination of befitting policies at home and certain favourable exogenous factors like the continuation of GSP plus status to Pakistan, stability in international prices of oil, removal of Pakistan from FATF's grey list and a positive nod from the IMF could support the external account of the country further in order to enable it to pay back the heavy baggage of foreign loans in time and improve the standard of living of ordinary households.