

### **Imports, wider current account deficit: Unwise economic policies cause surge**

Pakistan's imprudent economic policies have contributed to a surge in imports and a wider current account deficit, says the International Monetary Fund (IMF). The Fund in its latest report titled, "Regional Economic Outlook- Middle East and Central Asia", states lingering policy uncertainty and persistent macroeconomic imbalances in some countries (Lebanon, Pakistan, Sudan, Tunisia), along with tightening global financing conditions, underscore risks to private investment, and thus prospects for achieving a more balanced and broad-based mix of growth.

The report has projected an increase in inflation rate for Pakistan from 3.9 percent in 2018 to 7.5 percent in 2019 and revised downward the GDP growth rate from 5.8 percent in 2018 to 4 percent in 2019. The report has projected government overall fiscal balance at negative 6.9 percent of GDP for 2019 compared to negative 6.5 for 2018, while current account balance is forecast at negative 5.3 percent for 2019 compared to negative 5.9 percent 2018.

Bilateral and multilateral official financing has supported reserve buffers in several countries (Egypt, Jordan, Pakistan, Somalia, and Tunisia). Despite improvements in current account balances, reserves have continued to decline in some countries since the start of 2018.

Further appreciation of the US dollar and higher interest rates in the United States could reinforce capital outflow pressures, which, coupled with higher oil import bills, would put additional strains on reserve buffers in some countries, particularly those with significant external financing needs (Pakistan, Sudan).

Tighter global financial conditions could worsen external and fiscal burdens (Lebanon, Pakistan, and Tunisia), while putting strains on the balance sheets of banks and private firms, the report states.

Even if consolidation efforts go as planned in 2018, debt will remain very high in a number of countries. In particular, debt in Bahrain, Egypt, Jordan, Lebanon, Mauritania, Morocco, Pakistan, Sudan, and Tunisia will remain above the 60 percent vulnerability threshold for emerging market economies. The importance of addressing the debt burden is also illustrated by the significant gains from fiscal adjustment being lost through rising interest payments. Accordingly, going forward, a significant fiscal adjustment is still needed.

The weaker outlook for the Euro area could pose challenges for some countries in the Middle East, Afghanistan, North Africa, and Pakistan (MENAP) and the Caucasus and Central Asia (CCA) regions, particularly for oil importers with strong trade ties. The regions may also face headwinds from the projected moderation in activity in China.

As in other regions in the world, countries in the MENAP and CCA regions are exposed to tightening in global financing conditions and ongoing global trade tensions. The former has already begun to impact several emerging market economies in MENAP and could have more severe implications should financial market sentiment suddenly deteriorate, the report further maintains.

Escalating global trade tensions will have a limited direct and immediate impact on these regions but could impart significant strains over time through negative effects on trading partners and through market confidence effects, the report states.

Supported by higher oil prices, oil exporters in the MENAP region will experience visible improvements in external and fiscal balances in 2018-19.

Non-oil activity is expected to continue its recovery, supported by a slower pace of fiscal consolidation, while oil production picks up where spare capacity is readily available.

Risks remain skewed to the downside over the medium term. These include a faster-than-anticipated tightening of global financial conditions, escalating trade tensions that could affect global growth and put downward pressure on oil prices, geopolitical strains, and spillovers from regional conflicts.

Growth among oil-importing countries in the MENAP region is expected to continue at a modest pace in 2018 and to strengthen slightly over the medium term. However, growth is uneven and likely to remain low relative to previous trends, while unemployment remains elevated. Furthermore, higher oil prices are weighing on already weak external and fiscal balances.

A recent pickup in public consumption in some countries (Afghanistan, Pakistan) and relatively stable private consumption across the region have provided a moderate boost to growth. Credit expansion (Pakistan, Tunisia) and improved security (Pakistan) have also lifted growth by spurring private investment. Together, these developments have helped offset the negative effects of low agricultural output (Mauritania, Morocco), policy uncertainty (Lebanon, Pakistan, Tunisia), security risks (Afghanistan, Somalia, Tunisia), and spillovers from regional conflicts (Jordan, Lebanon).

Growth projections for 2018-19 have been revised downward in nearly half of the countries from the May 2018 Regional Economic Outlook Update: Middle East and Central Asia due to low agricultural output resulting from drought (Mauritania), policy slippages and external imbalances (Lebanon, Morocco, Pakistan, Sudan), and weak extractive sector output (Mauritania).

In some countries (Lebanon, Pakistan, Sudan) further fiscal consolidation will also be required to rein in central bank financing and limit any inflationary pass-through. Monetary policy space is also limited by the need to remain alert to potential shifts in emerging market sentiment that would trigger capital outflows or exchange rate volatility.

Macroeconomic and structural reforms to improve competitiveness through exchange rate adjustments (Tunisia), easing access to credit (Egypt, Morocco, Pakistan) and industrial land (Egypt), and diversifying the economy (Mauritania), among other measures, would help the private sector compete more effectively, better enabling it to take advantage of external demand.

Countries where the agricultural sector makes a sizable contribution to growth (Afghanistan, Mauritania, Morocco, Pakistan, and Somalia) remain vulnerable to weather developments.

To enhance the equity of reform and support growth, some countries (Egypt, Jordan, Pakistan, Oman, and Saudi Arabia) have coupled subsidy reforms with strengthening targeted social safety nets. The level of social spending is relatively low across the MENAP region.

Most MENAP oil importers have exhibited a decline in their private-investment-to-GDP ratio since 2008, particularly in Egypt. This trend can also be seen in Afghanistan and Pakistan since 2004. This indicates that political instability has not been conducive to attracting private investment. Iraq and Pakistan suffer from particularly low levels of business creation, with one business per 5,000 and 1,000 residents, respectively.

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