DAWN

Cautious optimism

Page NO.01 Col NO.01

Some good news, first. Pakistan's foreign exchange reserves have increased, the rupee has recovered some lost ground, a foreign bank is making a foreign exchange loan to the government for liquefied natural gas (LNG) imports, a $100 million loan of International Islamic Trade Finance Corporation has been rolled over, a fresh $2 billion official lending from China has reduced our external financing gap from $10-$11bn to $8-$9bn and Islamic Development Bank (IDB) has reportedly activated a three-year credit line of $4.5bn for oil import financing.

Most of these developments have taken place after the July 25 elections. One can also add to this list the reported inflow of $366m through that part of the tax amnesty scheme that dealt with the declaration of undisclosed foreign assets of Pakistanis. But it's up to readers to decide whether it's really good news in the backdrop of speculations that Pakistanis hold up to $150bn of undisclosed foreign assets abroad.

Foreign exchange reserves held by our central bank plunged on July 26 to $9bn, sufficient to cover the import bill of just one and a half months. But on August 2, reserves grew to $10.35bn, or equal to the imports of two months, after $1bn financing from China came into our coffers.

Unless exports and remittances take a great leap, temporary gains in the value of the rupee cannot be sustained over time

The rupee had closed at 128.32 per dollar in the interbank market one day before the elections. On August 3, it closed at 124.05 a dollar, showing a smart recovery of 3.3 per cent within 10 days following a continuous slide since December last year due to four consecutive depreciations by the State Bank of Pakistan (SBP).

Between Dec 1 and July 24, the rupee lost 21.6pc value to the greenback in the interbank market due to the largest-ever current account deficit of $18bn and highest-ever $37.6bn trade deficit in 2017-18.

And now, some bad news.

Securing the much-needed balance-of-payment bailout from the International Monetary Fund (IMF) has become all the more challenging after the US warning to the Fund against it. Moreover, the United States has slashed Pakistan's defence aid to just $150m this year from $700m last year. The much-trumpeted tax amnesty scheme ended on July 31 could not bring back home undeclared foreign assets of even half a billion dollars. According to a report in a local daily, Switzerland has never offered our government to return even a single dollar of Pakistanis deposited in Swiss banks.

Meanwhile, a review mission of the Asia-Pacific Joint Group of the Paris-based Financial Action Task Force (FATF) is due next week to review progress with regard to overcoming weaknesses in our anti-money laundering and combating financial terrorism regime. Satisfying the mission is a must to prepare the ground for attracting foreign investment and skipping harsh disciplinary action from the FATF itself.

Keep in mind the good and bad news listed above and imagine what the future possibly holds for the economy. To make your imagination work better, also remind yourself that the decisions to overcome external financing challenges need to be taken “in weeks, not months,” according to Asad Umar of the Pakistan Tehreek-i-Insaf (PTI), expectedly our next finance minister.

Crucial decision-making on the external financing front by the upcoming government will become somewhat easier if it strikes a fine balance in dealing with key global powers, notably the United States and China.

For the time being, financial markets are confident that the rupee will remain where it is or fluctuate in a narrow band at least during this quarter. Caretaker Finance Minister Shamshad Akhtar has also hinted that the situation will remain OK during this quarter. “We hope the upcoming quarterly repayment won’t bring the rupee under pressure. Beyond that, we are expecting that the new government will either be able to secure an IMF programme or find alternatives for filling in external financing gaps,” says the treasurer of a large local bank.

Markets are also abuzz with guesstimates about how much foreign exchange Beijing can pump in and speculations on whether Saudi Arabia can once again give us $1-2bn in the form of either one-off “official support” or an oil import credit facility.

Mr Umar is on record saying that in addition to seeking another IMF loan, the new government may launch dollar bonds for the Pakistani diaspora.

The launch of a new batch of sovereign bonds can be considered once the FATF concerns are removed and global credit rating agencies, such as Moody’s and Fitch, upgrade our sovereign credit ratings that they have recently downgraded, sources in the Ministry of Finance say. But that prospect can be explored sometime next year.

Bankers say the recent build-up in the central bank’s foreign exchange reserves has renewed the SBP’s confidence in its ability to keep the rupee from falling beyond a certain level on a particular day of trading in the interbank market. “Now if the exchange rate comes under pressure due to a large outward payment on any account, shortage of dollars in the market should hopefully not create a panic-like situation,” says the treasurer of one of the top five banks. “The SBP can pump in dollars in the market at a desirable rate to keep interbank rates stable.”

With the $4.5bn IDB oil credit window now operational, our state-run oil companies will be footing petroleum import bills out of the IDB credit line. That means relief for their bankers as they will not have to arrange dollars from their own inventories of foreign exchange.

Despite that, exchange rates may remain under pressure in the near future. Excessive external borrowing by the government has remained under discussion in the media. But a recent SBP report revealed that corporate external borrowing has also been growing fast. The report says the stock of such borrowing increased 42pc to $7.4bn in 2017 from $5.2bn in 2016. Obviously, just like governmental foreign loans, corporate external loans also weigh on the exchange rate movement as their servicing becomes due.

Unless our exports and remittances take a great leap and growth in imports slows down further, temporary gains in the rupee value cannot be sustained over time. To make that happen, the new government will have to quickly fix structural problems facing our exports and incentivise overseas Pakistanis to send more foreign exchange back home. Mr Umar has said the new government will seek input in economic policymaking through an economic advisory council and a business advisory council.

That sounds good. Bankers and businessmen reminisce how timely input from top businessmen and bankers during the days of finance minister Shaukat Aziz would help the government revisit its policies and fine-tune them to boost exports and attract big foreign investment.

“Remember we’d then retired an IMF loan ahead of schedule?” said a former central banker.

Published in Dawn, The Business and Finance Weekly, August 6th, 2018