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Readying for the new IMF programme

Page No.02 Col No.01

Pakistan is no stranger to bust-boom-bust cycles; nor to the IMF. Having been caught in the trough of that cycle for the nth time, spadework for the IMF programme has reportedly begun. Although the decision to go or not to go with the IMF rests with the incoming government, the lender has, according to sources, begun engaging Q-block as well as non-government economists to fish for ideas that could feature in the bailout programme.

Of course, the IMF would have its own ideas. Box standard conditionalities focusing on macro-economic stability would obviously feature in the programme, albeit two of the likely recommended steps have already been taken: gradual depreciation of the rupee, and the interest rate hike.

Another set of conditions that the IMF would likely push would revolve around its preferred version of fiscal federalism. The IMF cannot dictate the provinces, nor can it push for rolling back the fiscal aspects of the 18th Amendment, and the 7th NFC Award. But it would very much like the centre to roll out legislations that can check combined federal and provincial budget deficits, possibly by strengthening the role of the Council of Common Interests and adding a fiscal body of technocrats to the CCI that can make fiscally binding decisions.

Since that might be a hard sell, VAT may also be on the table. Pakistan has been trying to roll out VAT under IMF's aegis for nearly two decades. But political exigencies lop off economic reasoning, because the most dreadful thing VAT can do is to help document the economy, and only two and half Pakistanis want that.

Even in the recent PPP-era IMF programme, VAT was proposed but later replaced with the alternate plan of removing major exemptions from the GST without passing a new comprehensive law. That plan too lasted less than a month. Such is the shutter power! VAT's history in Pakistan raises serious doubts over the ability to incoming government (regardless of whoever forms it) to roll out VAT in today's politically hostile environment.

Consider also that VAT will not be easy to implement now that the provinces have set up separate revenue bodies to collect the GST on services. VAT will require strong coordination between the federal and provincial tax bodies to iron out the complicated process of tax adjutments between manufacturing and service sectors. And coordination isn't what national and sub-national governments can boast about in Pakistan.

Still if IMF ensures that VAT is made a conditionality, and if the incoming government can blame the current crisis to PML-N (or to aliens in case PML-N wins again), then VAT may have a chance. In addition to VAT, the IMF might want strong action on PSE reforms and privatisation, a long-pending agenda that the PML-N could not finish in its just ended tenure due to strong political opposition, and as such there is no or little hope for privatisation.

Tax reforms, not by way of WHT-isation but serious tax reforms, may therefore be the hottest item on IMF agenda. The blueprint for that already exists in the shape of Tax Reform Commission's report that lays out plans for the expansion of tax net, improving tax audit, ondemand collection, refund mechanism, FBR's administrative and human resource reforms, and separating tax policy from tax collection amongst a host of other things.

The one thing that the IMF may be able to get going is push the government to put remittances growth on top agenda. That can be done by tightening the noose around informal channels, further subsidizing formal channels and the launch of investment bonds targeting Pakistani savers abroad.

But the most important thing that the IMF should and can do is to push for civil service reforms at least in areas of economic governance in the first year of the programme. The IMF has previously included civil service reforms in its list of structural conditions on Pakistani loans. But these were mostly planned for third year of the programme when IMF's money isn't critically needed anyway, and the IMF too tends to go easy on the conditions.

The IMF is a temporary provider of loans. Its lending facility ends much earlier than the time it takes to implement complex institutional or bureaucratic reforms and the economic dividends it bears. Demanding civil service reforms in third year therefore is tantamount to lip service and surface level changes. IMF's policy wonks should know that.

Need one emphasize that however important macroeconomic stabilization may be, it is the cogs of governance that needs to be fixed in Pakistan. Failing that, the bust-boom-bust cycle will keep frequenting Pakistan at much faster pace than it normally does global economies. If indeed Pakistan goes to the IMF this year, then let civil service reforms be first-year conditionality.