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- ARTICLES

Misguiding people on debt

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- Pakistan's external and p
- ublic debts have grown at a pace seldom seen in the past that we have witnessed over the last one decade (2008-18). To be more specific, the overall public debt grew at an average rate of 15.4 percent per annum while external debt and liabilities grew by an average rate of 7.5 percent per annum during the period. External debts have, however, grown at a threatening pace of 9.3 percent per annum during the last five years (2013-14 - 2017-18). This speaks volumes about the way the previous regime recklessly borrowed, of course, with pride and pleasure, and brought the country to a very difficult situation.

What were the country's independent/professional economists doing? Why didn't they raise a hue and cry to stop the government from becoming reckless of the highest order? These are the relevant questions. The answer to these questions is that the independent economists have done their job; they tried to educate the people of Pakistan, political parties and all those who mattered in this country regarding the emerging trend in debts and its consequences for the economy. Through their writings, they warned the regime about the impending disaster that they would bring to the country if they continue to borrow remorselessly/shamelessly.

True to our belief, the government, its finance minister and his henchmen continued to damage the economy willfully. Some henchmen wrote articles under the name of the then finance minister Ishaq Dar, accusing independent economists including myself of being selective in presenting information, misinterpreting the facts, predicting doomsday scenario for Pakistan's debt situation, venting bias through writings and most importantly, committing disservice to the nation. These henchmen branded few of us as 'pseudo intellectuals' and 'spin doctors'.

These henchmen who partnered with Dar advised him to change the definition of debt to hide his reckless borrowing. They defended the minister's act of changing definition, wrote articles in justifying the new definition, and today one of them is blaming the same minister for ruining the country's economy (Badalta hai rung asmaan kaise kaise).

The developments of the last one decade in general, and last five years, in particular, have proved us right. Those who damaged the economy have run away. The fact is that the previous regime and its henchmen have drowned the country into debt, created serious balance of payment crisis and attempted to close all alternative avenues of external finance while leaving the only door of seeking support from the IMF open. This has indeed been a deliberate attempt to weaken Pakistan's economy and take it back to the IMF once again. Whether the regime and their henchmen succeed in taking Pakistan's economy back to the IMF once again will be known sometime late August or early September 2018.

While Dar and his group of supporters with shared characteristics accused me and my fellow independent economists committing disservice to the nation, there cannot be more disservice to the nation by drowning the country in debt and yet misguiding the people of Pakistan on the issue of country's debt burden. This takes me to the second part of my article.

It is a fact that debt in absolute terms is a meaningless concept. It is not the debt but the burden of debt that matters. Burden of debt is defined in many ways but it all boils down to the country's debt payment capacity. The country can sustain large debt burden provided it has the capacity to repay the debt in an orderly manner. When Dar and his henchmen were trying to change the definition of debt to misguide the people of Pakistan about the rising debt burden, they, at the same time were also trying to hoodwink (particularly the then Principal Accounting Officer of the Ministry of Finance) the people of Pakistan as to not to worry about the debt because Pakistan's debt burden is much lower than Japan's, Brazil's, Canada's, India's, Italy's, Singapore's, and the US'. Nobody talks about the debt crisis in these countries; it is only in Pakistan that we have created unnecessary alarm and that Pakistan's debt is fully under control. What is surprising is that the current caretaker finance minister also consoled the people of Pakistan as they should not worry about the debt as these are far less in terms of percentage of GDP compared with other countries. (This is reported in a section of press on July 15, 2018).

Let me dispute such arguments through some facts. The readers are asked to concentrate on the table below. Pakistan's public debt to GDP ratio is the lowest (74%) among the listed countries and yet it is most vulnerable among them. Its foreign exchange reserves (that too is borrowed) at $9.5 billion is the lowest; it has the poorest debt repayment capacity and accordingly it is rated at the bottom by the two international ratings agencies (S&P and Moody's). Such ratings reflect the vulnerabilities of the country in terms of its debt repayment capacity.

On the other hand, Japan with 236 percent public debt to GDP ratio appears to be far worse than Pakistan in terms of debt burden. On the contrary, Japan is rated as A+ by S&P and A1 by Moody's because it has $1.3 trillion foreign exchange reserves which are sufficient to finance Japan's two years of imports. Its debt repayment capacity has never been in doubt. It is a top rated country despite a very high debt to GDP ratio.

Similarly, Brazil's public debt is 89 percent of the GDP but it is better rated than Pakistan because its foreign exchange reserves are sufficient to finance two and half years of imports. Take the example of Singapore, its public debt is 111 percent of GDP, far worse than Pakistan's and yet it is rated by S&P and Moody's A- and Aaa, respectively. Singapore's reserves are sufficient to provide a 10-month import cover, hence, its debt repayment capacity is beyond question. Thus, like debt in absolute number, public debt as percentage of GDP has become meaningless too. What matters is the country's capacity to repay debt as well as the sufficient foreign exchange reserves of a country to provide at least three months of import cover.

In the case of Pakistan, despite relatively low public debt to GDP ratio, its foreign exchange reserves are not only pathetically low but these are also distorted. In $ 9.5 billion foreign exchange reserves as on July 6, 2018, $6.7 billion is short positions. In other words, the State Bank of Pakistan has borrowed $ 6.7 billion from Commercial Banks in forward market (for up to one month and more than 1 month up to 3 months) to boost its reserves. Therefore Pakistan's foreign exchange reserves are sufficient to finance only two weeks of imports. Hence, there is no comparison of Pakistan with the sample countries as reported in the table. Despite relatively low public debt to GDP ratio, Pakistan is extremely vulnerable to external shocks.

They must have the courage to call a spade a spade or they should do something else. Today, the SBP is talking about market, that is, the exchange rate is being determined in the market on the basis of the demand and supply of foreign exchange. For four years when Ishaq Dar was at the helm of affairs, the SBP kept its eyes and ears shut and never talked about the market. They maintained a fixed exchange rate regime and forgot the lessons of the market, naturally, in fear of Dar. In so doing, did the SBP serve Dar or the State of Pakistan? Let the SBP respond to this query.

(The writer is Principal & Dean at NUST School of Social Sciences and Humanities, Islamabad. Email:)

Table: Comparison of Debt-to-GDP Ratio

Countries	Public Debt % to GDP	Foreign Exch Reserves (Billion $)	Credit Ratings S&P	Credit Ratings Moody's	Import Cover
Pakistan	74%	$9.5	B	B3	7-8 weeks
Brazil	84%	$380	BB-	Ba2	28 months
Canada	90%	$87.0	AAA	Aaa	2.2 months
India	70.2%	$426	BBB-	Baa2	11.4 months
Italy	131.4%	$143.2	A+	Baa2	4 months
Japan	236.4%	$1300	A+	A1	24 months
Singapore	110.9%	$283	A-	Aaa	10 months
US	107.8%	$123	AA	Aaa	-