

Institute for Policy Reforms

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Balance of Payment is a critical challenge

“Without an overall strategy, the new budget will again tweak at the edges.” This is stated in a report by the Institute for Policy Reforms released today. The report gives comprehensive proposals for the coming budget. It says that a meaningful budget should be guided by a medium-term economic strategy. So far, it seems that this is being done in name alone. Clarity of goals and coherence in government plans are important for economic management. It is therefore no surprise that there has been no improvement in the economy’s fundamentals. The report called upon the government to respond especially to the balance of payments challenge. Depending on Chinese largesse is not a plan.

There are concerns with the way government makes the budget. Both its stated goals and estimates often turn out to be misplaced. In most years, the budget sets out to realize the aims of growth and poverty alleviation. However, few measures in the budget support these goals. Similarly, GoP forecasts a lower than justified target for the fiscal deficit. It usually gives higher revenue and lower expense amounts than circumstances merit. It also uses high provincial surplus estimate to bridge the gap. Why must we resort to artifice, the report asks. Because successive governments have made no fundamental shift in policy.

To earn more revenue, GoP must make hard choices that affect the political economy of tax avoidance and evasion. To make spending more effective, it must revisit subsidies for PSEs and power supply. It must also think through development priorities and debt management. These are top level decisions. Government has done well at fiscal consolidation recently. In fact, 2015-16 was the first time in years that FBR achieved its target. Yet, for many reasons we are far from having a stable macroeconomy that can underpin growth.

The economy faces enduring challenges. These include the twin fiscal and current account deficits, insufficient funds for services and investment, and ineffective public spending. There are indications that energy prices may increase again. That means further pressure on the Balance of Payment and on inflation. The latter has been in control recently. Manufacturing growth is well below target and agriculture has only modestly recovered from last year’s radical decline. Exports are stagnant.

The budget cannot meet all the above challenges, but it must begin to move the economy in the right direction. That is possible only if it is part of a strategy, because most important shifts must take place before preparation of the budget.

The report calls on GoP to strengthen the macro framework. This is possible by increasing government revenue through broadening the tax base, reducing exemptions, and strengthening

compliance. There is need also for structural tax reforms through simplified procedures, rationalized systems, and removal of distortions.

On the other hand, GoP must rationalize expenditure and to the extent possible increase the share of development spending. It must reduce subsidies by reforming or privatizing PSEs. There is urgent need also to review the power sector policy structure. The present power policy will take us back to a dead end after initial improvement. The report especially raises the issue of governance. No economic policy will work without governance improvement. Pakistan performs poorly in all governance indicators with the result that in most areas government is a hindrance rather than a support to economic activity.

The PSDP has too many projects with an average throw forward of eight years. To be effective it must keep just those projects that directly support growth in priority sectors.

The above proposals will help with competitiveness of the economy. There is need also to focus on urban infrastructure so that cities support economic growth and serve as service clusters. Skills development and R&D too are key for the economy, especially for priority sectors. Such support must go with setting up of industrial parks under CPEC.

We must offer opportunity to the young and those outside the economic mainstream. This is important for economic progress and social stability. GoP can stimulate private sector investment through access to credit and make an earnest review of regulations that reduce barriers to investment. It should make major investment in training of youth. Training centres may collaborate with international providers of mass open online courses to train millions of young people each year. At the same time, GoP must link unemployed youth with an existing social security system e.g. BISP. It must promote export of workforce by providing skills training with international certification.