Institute for Policy Reforms

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Economic revival nowhere in sight

“That the economy this year missed all its targets is no surprise”, states the Institute for Policy Reforms in its review of the Pakistan Economic Survey released today. This was expected, as since completion of the IMF programme in September 2016, most economic fundamentals had weakened. Last year’s high growth rate was built on a weak base.

Yet, news about the economy is anything but sanguine. Fiscal 2019’s GDP growth estimate of 3.3% is well short of the year’s target of 6.2%. Large Scale Manufacturing growth was negative 2% and construction by 7.6%. Agriculture saw a tepid growth of 0.85% against a target of 3.8%. Production of major crops dropped by 6.6%. Ginned cotton, a key input for Pakistan’s exports fell by almost 13%. Combined, commodity production of agriculture and industry grew by a meager 1.1%. Growth in services was 4.7% against a target of 6.5%.

Government revenue collection was especially dismal. It will likely miss GoP’s revised target by Rs. 400 to 500 Billion. For July-March 2019, total revenue increased by a paltry 1.8%. Meanwhile, there was rapid increase of almost 20% in current expenditure. Debt servicing and defence grew by 24% each, while PSDP spending declined. PSE losses continued unabated, while citizens are being cajoled to pay more taxes and higher utility tariffs. The fiscal deficit for nine months was 5% of GDP compared to last year’s 4.3%. IPR forecasts a full year fiscal deficit of 6.5 to 7% of GDP.

Resultantly, debt has increased. Total debt is almost 85% of GDP. Including liabilities, it is 91% of GDP. External debt alone is 35% of GDP.

The one area of promise was reduction in the current account deficit. Last fiscal Pakistan’s current account deficit was an unprecedented USD 19.9 Billion or 6.4% of GDP. July-March FY 19 current account was USD 11.6 Billion which suggests a final deficit of about 14 Billion for the year. However, reduction in the current balance was because of reduced imports and not from export growth, despite substantial devaluation of the Rupee. Also, decrease in imports included those products that induce growth such as machinery. FDI for the ten-month period until April 2019 declined by 55%.

Pakistan’s abysmally low rate of savings and investment is a fundamental and enduring concern for the economy. In FY 19, investment was 15.4 % of GDP against a target of 17.2 %. Historically, Pakistan’s Investment/GDP ratio has been 20%. Pakistan needs to increase its investment ratio to generate 5% or more of GDP growth.

Also, national savings has continued to decline. It was 10.7% of GDP against a target of 13.1%. The gap of about 5% of GDP between savings and investment is the economy's dependence on external sources. Any increase in investment or overall expenditure brings us close to default. Improved savings rate will be key for any meaningful growth of the economy.

All of these developments have put a pressure on growth. With continued price adjustments and a tight monetary policy as agreed with the IMF, economic revival would likely not take place before a year or two. Delay in finalizing agreement with the IMF may have multiplied our troubles.

IPR recalled that for decades now, Pakistan policy makers have focused on firefighting to make ends meet rather than plan strategically to build competitiveness.

In the last two decades there were two occasions when Pakistan had large fiscal space to build its production base for sustained GDP and export growth. On both occasions, we missed the opportunity. The first was after 9/11, when Pakistan received massive aid funds. Along with rescheduling of debt for fifteen years, a total of USD 60 Billion was available to Pakistan.

The second was during 2015-2018 when along with IMF's Extended Fund Facility, Pakistan received massive Chinese assistance for CPEC. On the second occasion we at least built infrastructure, albeit on a lavish scale. During 2001-2007, when most flows were either grant or Coalition Support Fund and concessional multilateral funds, we did not even do that. The energy shortage and the circular debt are products of that decade.

Over many governments, we have repeated the same mistakes, avoiding structural reforms consistently. During these periods we should have contained current spending, targeted infrastructure development to boost exports, and invested in our technical capacity. Reforms of revenue and spending policy to correct inequities in the society were necessary. We neither stabilized nor built competitiveness. There could have been much better use of the space provided by foreign assistance.