Pakistan battered by inflation, anemic growth and power cuts

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The International Monetary Fund (IMF) has delayed disbursement of the fifth installment of its US$ 11.3 billion standby loan to Pakistan, after disagreements with Islamabad over Pakistan's burgeoning budget deficit and the introduction of new revenue-raising measures.

The IMF had been scheduled to approve the transfer of a $1.2 billion tranche at a meeting March 24. The decision was reportedly postponed to March 31, then put off again. Some Pakistani news reports have claimed that the money will only be made available to Islamabad in the early summer, but Pakistan's government insists that the matter will be resolved rapidly now that all four of the country's provincial assemblies have introduced legislation to establish a value-added tax or VAT.

An IMF spokesman, meanwhile, has said that the agency, which is dominated by the US and its European allies, will begin, within the next two weeks, its fourth review, under the current loan, of Pakistan's economic performance and that the fifth tranche will be approved once that review is complete.

Given the pivotal role Pakistan is playing in the US war in Afghanistan, it is unlikely the IMF will do anything that will seriously destabilize the country's economy. But it continues to work alongside Washington to force through pro-market policy changes aimed at resolving the state's fiscal crisis at the expense of working people and further opening the country to profitable foreign investment.

In November 2008, the Pakistani government was forced, due to the depletion of its foreign currency reserves, to seek emergency IMF assistance. Last July, the IMF increased the $7.6 billion emergency loan to $11.3 billion.

Eighteen months after the original emergency loan, Pakistan's foreign currency reserves have swelled to more than three times their November 2008 level. But the country remains mired in economic crisis as a result of rapid inflation, a depreciating rupee, increased debt-servicing costs, stagnant exports, a widening trade deficit, a dearth of foreign investment, and chronic power and water shortages.

According to Pakistan's central bank the country's GDP will grow only between 2.5 and 3.5 per cent during the current fiscal year (July 2009 to June 2010). When Pakistan's rapid population growth is taken into account, this amounts to virtually no growth and this in a country marked by extreme poverty and social inequality

In government circles there is already discussion that Pakistan will be forced to seek a further IMF loan, although it hopes to do so under the IMF's "Poverty Reduction & Growth Facility."

A deterioration in Pakistan's budget deficit to GDP ratio has led to renewed pressure from the IMF, Pakistan's state bank, and the Pakistani corporate media for the government to impose still further public spending cuts.

In a report issued at the end of last month, the State Bank of Pakistan said that the deficit to GDP ratio is certain to exceed the 4.9 percent target the government negotiated with the IMF for the current fiscal year and could reach as high as 5.5 percent. It attributed the deteriorating deficit-to-GDP ratio to anemic economic growth, higher-debt servicing costs as a result of the decline in the value of the rupee, and increased military spending, due to the counterinsurgency war the Pakistani military is waging, on Washington's behalf, in the country's Afghan border region.

The state bank called for aggressive measures to lower the deficit, including public spending cuts, tax increases, and the sell-off of government assets and companies. Fiscal reform, said the bank will require using the "entire range of options, from increasing efficiency of public expenditures and reducing the size of government to raising the tax-to-GDP ratio."

As a condition for the 2008 IMF loan, the Pakistan People's Party (PPP)-led coalition government slashed development spending and pledged to phase out fuel price subsidies. It also agreed to implement a value-added tax. The latter measure met has with considerable resistance from Pakistan's elite, in part because of fears it would dampen economic activity in the midst of a slump, but largely because till now they have been very successful in escaping taxation—the burden of which falls, even as compared with other lesser developed countries, more heavily on the working class and poor.

The PPP-led government of President Zardari and Prime Minister Syed Yusuf Raza Gilani has yet to say how it will deal with the rising deficit. But it has ruled out any cuts to the country's bloated military budget, for no less than the dictatorship of General Pervez Musharraf that preceded it, the current civilian government is committed to maintaining the strategic alliance with the US and the Pentagon-Pakistani military nexus. Addressing students at the National Defence University President Zardari insisted, “We cannot afford to cut down allocations for the armed forces.”

In a further demonstration of the continuity between the current government and that of Musharraf, Gilani recently appointed Musharraf’s privatization minister, Hafeez Shaikh, as his finance advisor and de facto finance minister.

Shaikh’s record underscores that the PPP government intends to ruthlessly pursue market reforms, including privatization, to attract foreign investments. As Pakistan’s minister for privatization during 2003-06, Shaikh oversaw the selling off of 34 state companies worth over US$ 5 billion. In gratitude, Pakistan’s business community named him “Man of the Year” for 2004. His direct connection to international capital is highlighted by the fact that he left his ministerial post in 2006 to become a general partner at an international investment company based in New York.

By virtually every measure, the Pakistani economy is in grave crisis—a crisis that preceded but has been enormously exacerbated by the world economic crisis.

Inflation remains high, well in excess of government forecasts, and is ravaging the living standards of Pakistan’s impoverished workers and toilers.

According to the Federal Board of Statistics (FBS), the Consumer Price Index was 13.02 percent higher in February 2010 than a year before, mainly due to hikes in electricity, energy and food prices. A key condition of the IMF loan is that the Pakistan People’s Party-led coalition government must reduce and ultimately eliminate gasoline and electricity price subsidies.

Since President Asif Ali Zardari came to office in 2008, prices have increased by a massive 36.3 percent. The rise in food prices has been far steeper, with the price of two critical staples, wheat flour and sugar prices, rising by 83 and 163 percent respectively.

According to the FBS, the trade deficit for the period from July 2009 to February this year narrowed to US$ 9.42 billion from US$ 11.7 billion a year earlier, as the result of the combined effect of a decline in imports (largely due to low oil prices) and a marginal increase in exports.

Despite a significant decline in the value of the rupee, textiles, the country’s main export and biggest manufacturing employer, lost ground to foreign competitors. Textiles, and many other industries, have been hard hit by electricity cuts or load-shedding.

It is very unlikely that the government’s export target of US $20 billion for the current fiscal year (July 2009-June 2010) will be met. In the first eight months of the fiscal year, total exports amounted to just $12.4 billion.

According to Pakistan’s central bank, Foreign Direct Investment (FDI) has declined sharply, falling by 53 percent to US$ 1.48 billion during the first eight months of the current fiscal year. Net Foreign Investment—FDI and portfolio investment combined—fell to US$ 1.02 billion, as foreign investors continued to pull their money out of Pakistan.

During the same period, remittances from overseas Pakistani workers declined by 8.2 percent to US $ 588.8 million.

By the end of last year, Pakistan’s external debt and liabilities reached an unprecedented US$ 55.67 billion, i.e. about one-third of Gross Domestic Product (GDP), and are expected to rise to US $ 60 billion by next June.

The PPP-led government of President Zardari and Prime Minister Syed Yusuf Raza Gilani had been banking on a surge in foreign investment and aid to buoy Pakistan’s economy, especially to help fund the tens of billions in investments needed for energy and water infrastructure projects. But thus far, the so-called Friends of Pakistan group of aid-donor nations has come up with little real money. And the $1.5 billion in annual economic assistance that the US has proffered is tied to Washington’s demands that Pakistan suppress the Taliban-aligned groups that have arisen in its predominantly Pashtun-speaking Afghan borderlands. The Pakistan military’s counter-insurgency war has already resulted in massive human suffering and economic dislocation that dwarfs the new US economic assistance.

The deteriorating socio-economic situation is fueling popular protests and unrest.

In the aftermath of one such protest—against bus fare hikes in the twin cities of Islamabad and Rawalpindi—Pakistan’s leading English daily sought to alert the ruling class to the danger of a social explosion. “If the government is so out of sync with the problems of people living in the twin cities,” declared the *Dawn* in its lead editorial for March 21, “their ignorance of the conditions prevailing in more remote parts of the country must beggar belief. We’ve said it before and we say it again because no one in authority seems to get the message: the real problems facing the country must be addressed. The ranks of the newly poor are swelling and the poorest are finding it difficult to find one square meal a day. Prolonged power outages are infuriating most citizens and the sick are dying from curable diseases in the absence of adequate healthcare. Access to justice, meanwhile, remains a dream. Resentment is brewing with people becoming convinced that no one in government cares for their welfare. We are sitting on a powder keg and the spark could come from anywhere.”