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Analyzing the Impact of IMF Policies on the Economic Health of the Pakistan

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ABSTRACT

The International Monetary Fund is called a lender of a last resort for those countries who are in need of emergency bail outs. Countries faced bankruptcies as they exhausted all of their options hence the option left for them is to approach the IMF. The International Monetary Fund was originally founded on the idea of helping countries who were to finance their debts. This would have provided stability in the financial market, improve growth and reduce poverty. The objective of this study was to analyze the impact of IMF policies on the economic health of the Pakistan. The results suggest that IMF programs have increased external debt to GDP ratio, which in return increased debt burden on the economy. IMF policies led to increase in taxes, which induce inflation and lower growth. The results further concluded that structural adjustment programs affected negatively to the domestic economy. Due to IMF, economy has to achieve stabilization, which leads decline in growth. The decline in fiscal deficits through increase in taxes and reduction in development expenditure led to increase in unemployment and social decline. The devaluation of the currency increases inflation in the economy whereas reduction subsidies increase costs in the rural economy. As most of the agricultural inputs required subsidies so they are mostly effected by reduction in subsidies. The IMF program also increases pressure on external debt, which leads to acquiring of further debt in order to pay the previous debt. This accumulation of debt increases external debt to GDP ratio and increases the sovereign risk of a country. To come out of vicious cycle perpetuated by IMF prescription, Pakistan needs alternate solutions including overhaul of its export policy to boost export; aggressive privatization to curtail expenditure; floating of international bonds to build up foreign exchange reserves and invest agriculture, livestock and dairy sectors for inclusive growth.

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1. Introduction

Pakistan's economy has experienced boom and bust cycles, but it has kept afloat by clinching frequent bailouts from the IMF to boost ailing foreign exchange reserves. Currently, Pakistan is facing severe macroeconomic imbalances notably, cavernous current account and budget deficit, inflation and depleting foreign exchange reserves making the IMF bailout imminent. IMF bailouts always come with few strings i.e., conditionalities; therefore, it is taken as a political stigma for the governments to go out for IMF bailout. It is therefore, a careful decision to opt for which option? Although borrowing from IMF is portrayed in Pakistan as a political stigma by political parties and the media, yet, the conditionalities of broadening tax base, improving export competitiveness, restructuring Public Sector Enterprises (PSEs), plugging line losses etc. are the right prescription for ailing economy.

Every bail-out package from the IMF is assumed to be the last, and Pakistan will not require another bail-out package in the future. Unfortunately, Pakistan's desire was not realized. Because of the foregoing, the primary premise is that IMF programs failed to produce the desired results between 1988 and 2016. As a result, Pakistan's economic development rate remained a boom-bust narrative, and the country was unable to break free.

Pakistan has so far availed 21 IMF programs. In the last decade 2008-2018, Pakistan entered into three agreements with the Fund: Stand by Arrangement (2008-2010), Extended Fund Facility (2013-2016) and ongoing Extended Fund Facility (2019-onward). However, it successfully completed Extended Fund Facility (EFF) 2013-16 and got an amount of SDR 4.393 billion (about US$6.15 billion, or 216% of Pakistan's current quota at the IMF)[1]. Pakistan is currently undergoing 22nd IMF program by agreeing to access $6 billion loan spanning over 39 months. All the IMF programs were meant for meeting the balance of payment (BOP) needs as Pakistan has protracted macroeconomic illness. Our problems in external sector and real sectors are associated with each other and causality runs in both directions. Therefore, IMF conditionality coerces us for policy correction in both sectors simultaneously.

Pakistan has been afflicted with chronic balance of payment problems. The IMF approved $1 billion installment on February 22, 2022 out $6 billion bailout package signed in May, 2019 without realizing that majority of the past programs could not be graduated because of failure to meet the macroeconomic targets agreed with IMF. However, Pakistan's performance under Fund Program (2013-16) was noteworthy as it recoded real GDP growth of 5.6 % at the end of financial year 2017-18.

The IMF given polices is not steering the economy out of vortex. IMF one-fit-solution based on 1980's Washington Consensus in the ongoing IMF program has deepened the crisis. The economic growth has lowered; per capita income dropped to US$1355 from US$ 1652 in just two years and budget deficit touched to 9.5 percent of GDP. The prevailing indicators coupled with slowdown in global trade due to COVID-19 pandemic present very bleak picture. To come out of vicious cycle perpetuated by IMF prescription, Pakistan needs alternate solutions including overhaul of its export policy to boost export; aggressive privatization to curtail expenditure; floating of international bonds to build up foreign exchange reserves and invest agriculture, livestock and dairy sectors for inclusive growth. The basic objective of this study is to critically evaluate the impact of the bailout packages of the IMF on the economy of Pakistan. The scope of the study is to critically evaluate the impact of the bailout packages of the IMF on the economy of Pakistan. This research paper is an attempt to explore the other avenues to get financial assistance to support the economy of the country. This research paper will also evaluate the reasons that why Pakistan go to IMF off and on. Issues and challenges of the IMF bailout package will be analyzed on the basis of analysis doable recommendations will also be suggested.

[1] https://www.imf.org/external/index.htm (Accessed on 26-02-2022)

2. Research Methodology

This paper will apply both quantitative techniques for comparative time-specific analysis of Pakistan's economy. Emphasis has been made on the packages secured during the last decade i.e. Standby Agreement (2208-2010), Extended Fund Facility (EFF) (2013-16) and on-going EFF (2019-2022) by establishing relationship between economy's two important indicators; Current Account (CA) and Fiscal Balance.

3. Literature Review

Khan (2016) has analyzed the debt issue and its implications for national security. The author finds out that over the period of last decade Pakistan has accumulated huge external debt and if the pace of borrowing remained unchecked, it will be disastrous and can have severe implications for macroeconomic stability and national security as well. Dawood (2018) in a research report identifies that Pakistan has so far availed 21 IMF programs and 12 of them were bailout packages. The report analyzed the reasons for current macroeconomic problems, which led to the current crisis and also highlighted the importance of structural reforms.

Farooq, Muhammad, (2019) discussed the sustainable solution to the debt problem and identified that borrowing either from IMF or friendly countries is not the solution to the problem, rather improving trade balance and revenue generation are sustainable solutions. Shabbir (2013) analyzed the long run relationship of external debt and economic growth for 70 developing countries and found that accumulation of external debts shrikes the fiscal space and thus stifles the economic growth. She identified FDI and openness as a way out for developing countries in such situations.

Two Fund officials of Pakistani origin have discussed Pakistan's engagement with IMF in (Ahmad & Mohammed, 2012) and identified it as a special case of "Dutch Disease". Dutch Disease is referred by economists to describe a situation where a country is used to easy money from a particular source — like income from oil exports. Pakistan and IMF relationship must be viewed in the broader context of Pak-US relationship. Ronald Reagen and subsequent US administrations kept on providing assistance to Pakistan for their strategic motives and also used Fund (i.e. IMF) for provision of easy money to Pakistan.

3.1 Performance of Pakistan's Economy under IMF Packages

3.1.1 Standby Agreement (2008-2010)

Pakistan performed fairly well during three periods of its history i.e. 1960-69, 1977-88 and 2002-2007. GDP grew by an average of 6.2 percent per year. Agriculture contributed nearly 62 percent to the GDP. The share of Manufacturing was less than 7 percent. But by 2008, share of agriculture declined to 22 percent while that of manufacturing increased to 18 percent. The service sector had also taken lead from other sectors with a share of one-half of the GDP. Despite the prominent signs of progress, the country was confronted with grim economic situation in 2008: a sharp reduction in economic growth rate, an unsettling rate of inflation, a decline in per capita income leading to enhanced incidence of poverty, a widening regional income disparities and huge fiscal and balance of payments deficits (approx. 9%) coupled with power shortages.

So, the economic managers approached IMF and entered into SBA amounting to US$ 11.3 B. The fiscal program sought to reduce the deficit from 7.4 percent of GDP in 2007-08 to 4.2 percent in 2008-09 and finally to 3.3 percent in 2009-10 while ensuring enhanced spending on the social safety net. The program also envisaged tight monetary policy. However, Pakistan was not able to continue the program and quit it in May 2010 after transfer of US$ 8.7 B only.

While analyzing the reasons of this failure, it has been observed that two years prior to this agreement Pakistan was one of the fastest growing economies in the region. However, the then government could not capitalize the gains of the previous Government because of extraordinary exogenous price shocks in oil products and food. The then Government was also ill-prepared to tackle the challenges on these fronts. Consequently, Pakistan swayed from one crisis to another as it mainly relied on short term fixes as followed rather than introducing structural changes in the economy.

It is generally said that during the period 2002-07 the country witnessed growth and reduced deficit from 7.7 percent of GDP in 1999 to 5 percent of GDP in 2007. Was this achievement a result of some home-grown solutions relating to structural changes in the economy? The answer is not in affirmative. The then government also sought IMF assistance. The economic indicators improved as the government had ceased expenditures and banned government employment over a three-year period. Reductions in non-development expenditures became possible after significant reduction of country's outstanding debt by USA and other donors in the wake of participation in 'War on Terror'. This lowered the interest payments. The concessions in debt payments and transfer of a large sum of USS12 B as military and economic package helped Pakistan to perform fairly well which the government during 2008-2010 was not blessed besides being incompetent to look beyond IMF assistance.

3.1.2 Extended Fund Facility 2013-2016

In 2013, Pakistan was again facing slow growth, falling foreign exchange reserve and widening fiscal deficit. Again, the government approached IMF for EFF for preserving economic stability and boost economic growth besides ensuring social safety net. Pakistan was successful to get 36-month US$ 6.6 B EFF from IMF in September, 2013. By entering this agreement, economic growth gradually increased and fiscal balance remarkably improved due to (i) cut in expenditures by phasing out of energy subsidies, (ii) increase in Tax-to- GDP ratio by approximately 2½ percentage of GDP by eliminating tax concessions and exemptions, raising withholding taxes slabs for non-filers of income tax returns, broadening of tax base by registering new tax payers and imposing regulatory duties on luxury goods. However, Public debt jumped up and it touched at about 66 % of GDP. The elevation in public debt in Fiscal Year 2015-16 was over and above the projected one mostly due to accrual of government payments accompanied with exchange rate swings. The target budget deficit was also not met.

The State Bank of Pakistan (SBP) data showed that current account deficit hovered around 0.9 percent of GDP in FY 2015-16 as against 1.0 percent of GDP in FY 2014-15. Total exports of goods and services were recorded at US$27.469 billion in FY 2015-16 as compared to $29.969 billion in FY 2014-15. Imports of goods and services were amounting to $48.343 billion as compared to that of US$50.123 billion in the corresponding period. Remittances increased from US$19.915 billion in FY 2015-16 as against US$18.721 billion in FY 2014-15. The country also fetched US$1.282 billion in foreign direct investment during FY 2015-16, the major part of it was from CPEC. The analyst viewed that the current account deficit improved marginally due to low oil prices and the country would be facing balance of payment stress after completion of IMF program.

Conditions of External and Real Sector after Phasing out IMF Program 2016-2018: Real GDP grew by 5.6 % in financial year 2017-18 due to enhanced power supply, investment flows to the China-Pakistan Economic Corridor, and resilient consumption growth along with on-going improvement in agriculture. As for widening of fiscal deficit is concerned, we have to take into account that the government again resorted to expansionary fiscal policy, thereby undertaking larger development expenditures; increase in tax exemptions and release of funds to unrelenting loss-incurring public sector enterprises (PSEs), All resulted into huge fiscal deficit. Provinces surplus scored more than 0.7 % of GDP, tax revenue fell short of 0.3 % of GDP and accumulation of circular debt again emerged within one year of completion of the IMF Program.

Table 1
Economic Performance of Pakistan from 2013 to 2016

Economic Performance of Pakistan from 2013 to 2016[2]			
Indicators	**2012-13**	**2015-16**	**Performance**
Real GDP growth	3.7	4.7	↑
Fiscal Balance % GDP	-8.5	-4.6	↑
Public Debt (% GDP)	62.4	64.81	↓
Tax-to-GDP Ratio	10.1	12.42	↑
Exports (growth annual)	0.46	-08.4	↓
GIR ($ billions)	6.01	18.2	↑
NIR (U.S billions)	-2.5	7.52	↑
Real Effective Exchange Rate (2000=100)	100.71	118.32	↓

Source: Daniela Gressani and Kristina Kostial, "12th and final review IMF",IMF Country Report No. 16/325, (Sep16, 2016):6-24,

The current account deficit is alarmingly widened which shows solid domestic import demand amidst a hyped exchange rate. Fiscal deficit also ballooned along with a lax monetary policy stance. The situation resulted into foreign exchange reserves depletion only covering 70 days of imports and Govt. was unable to service its debt payments. In 2019, exports took off to recover after three years of tenacious decline, assisted by gain of cotton prices in international markets, and duty drawbacks sanctioned under the umbrella of export funding package introduced in 2018. Remittances steadied in 2019 following last year's (2018) waning. But the overall scenario was gloomy.

Table 2
Balance of Payment of Account

Balance of Payment of Account			Million (US$)
ITEMS	**FY 2016- 17**	**FY 2017- 18**	**FY 18-19/ (Change)**
Current Account Balance	-12,621	-18,130	(-5,509)
Trade Balance	-31,019	-36,385	(-4,055)
Direct Investment	-2,663	-2,760	(-127)
SBP Reserves	16,144	9,789	(6,355)
Export(Growth)	0.1	12.6	(10.3)
Import(Growth)	18.0	14.7	19.9
Current Account (%age of GDP)	-4.1	-5.8	-8.6
GDP Growth	4.5	5.3	5.6
Fiscal Balance	-5.5	-5.8	-5.5

Source: State Bank of Pakistan," *Quarterly Report*", (July, 2018): Accessed on 18th March, 2022, http:www.sbp.org.pk/reports/quarterly/.htm

3.1.3 Extended Fund Facility 2019-2022

After taking over of powers in 2018, the new government found itself mired in a dire macroeconomic crisis: current account deficit increased from $2.7 billion in 2015 to $18.2 billion in 2018 due to rising imports under new China-Pakistan Economic Corridor (CPEC) projects and low exports in general; the gross public debt touched USD $179.8 billion ; 25 percent depreciated Pakistani rupee against the U.S. dollar with stagnant exports; inflation touching 9.4 percent ; rising energy prices ;tax collection was mere equivalent to 13 percent of GDP, unpaid government bills amounting to Rs 2.5 trillion ,slower economic growth @ 3.8 percent per annum, unattended power sector issues (Rs 664 B in 2018-2019) and NFC lay out creating serious

[2] https://tradingeconomics.com/pakistan/ (Accessed on 11th March 2022)

budgetary challenges . Under this back drop, the Pakistani authorities and the IMF reached an agreement for a 39-month Extended Fund Arrangement (EFF) for about US$6 billion. The program aims to reduce domestic and external imbalances, improve the business environment, strengthen institutions, increase transparency, and protect social spending.

As Pakistan has chequered history of relationship with IMF owing to frequent untimely quitting of previous programs, it has to undergo harsher terms at the time of 22nd bailout package. The situation worsened on account of hostile relationship between American administration and Pakistan on CPEC and role in War on Terror. The 22nd IMF program is the toughest IMF program ever given to Pakistan. Adjustments on currency, interest rate, gas prices, electricity prices along with unrealistic revenue target – all in one go were expected to put tremendous pressures on Pakistan's economy and people.

After twelve months of the EFF, there are no signs of any improve in economic indicators. Devaluation of rupee since July 2018 and until the end of March 2020 added Rs 4666 billion into Public Debt. Interest payment on these debts, increased by Rs 131 billion. Discount Rate increased from 6.5% in June 2018 to 12.5% till March 2020. High discount rate has alone added Rs. 1687 billion to interest payment. Thus, total interest payment increased approximately Rs. 1818 billion. The combined cost of devaluation and increase in discount rate to the economy amounts to Rs 6484 billion or $ 39 billion. Gas prices have been increased on average by 176 percent and electricity prices have gone up by 26 percent. The unemployment surged to 8.5% from 5.8% in 2018. The inflation also touched the double figure. The FBR recorded growth of 18% in its revenue collection which was quite below the target of 27% growth in revenue collection as projected in Finance Act 2019. The per capita income declined US$ 300 resulting an increase in incidence of poverty. Some marginal improvement observed in foreign exchange reserves from US$ 7.6 B in May 2019 to US$ 10.10B and in current account deficit from 13.4 percent to 4.5 percent largely owing to the restrictions on import of finished consumer goods in terms of regulatory duties and low oil prices.

3.2 Pakistan's Experience with the IMF

Managing Director of IMF in her statement of September, 2016 emphasized that the demand depressing policies could destroy the economy by decreasing the growth rate and increasing unemployment. Consequently, countries could face depressed trade, low production, increase in fiscal and current account deficit and depleting foreign exchange reserves as outcome of IMF Policies. She also advocated that developing countries are in need of demand boost policies, increase in public and private investment, and reduction in cost of trade and in doing business. They should devise complete plan for inclusive growth to spread the prosperity to all sectors of economy. Unfortunately, the practical policies of IMF do not match to its Managing Director's views/vision. Pakistan after following 10 years' stabilization policy of IMF is still facing high unemployment and low growth rate. Despite decreasing interest rate, it is facing low investments and growing public debt and current account deficit.

When we critically examine the Pakistan's performance in the past 21 IMF programs encompassing assistance US$ 26.924 B, we arrive at the conclusions that out of these 21 programs, o5 programs pertained to Stand by Agreement (SBA) encompassing financial assistance to the tune of US$13.347 B. However, in the agreed amount, only US$ 10.11B was dispersed as the three programs were put off due to non-realization of harsh conditionality in the wake of public pressure. Similarly, in 04 programs of Extended Fund Facility (EFF) envisaging US$ 8.411 B, only US$7.011B was transformed to Pakistan. Only one EFF (2015-2018) was accomplished and that too with 15 waivers. So, in most of the IMF programs Pakistan to had quit before their graduation leading to further deepening of economic crisis.

3.3 Growth and Employment

Pakistan is following the IMF's anti-growth policies since past decade so the economy is severely damaged and growth is limited to only 3-4 percent per year. During this decade, the growth of LSM showed a decline from (6.0) in 2008-09 to (0.7) in 2018-19. The agriculture sector also recorded downward growth from 3.5% to 0.5% and services sector from 3.2% to 3.8% after touching height of 6.5% in 2016-17 in the period under review. Agriculture, services and industrial growth declined due to demand contracting policies of IMF. Now there is no charm for the investors to invest in this deficient demand environment. Overall productivity has been decreased on the account the macroeconomic policies adopted by the Pakistan. In fact, the last decade has made the economy permanently on life support and persistence decrease in economic growth has increased the unemployment, as there is no capacity of new job creation. Not only the overall unemployment rate has risen up to 10 % during the past decade but also there is a huge decline in annual entrants of labor market from 1.9 to 1.3 million. Labor force participation rate has also declined from 1-2% for both youth and prime aged workers. The unemployment rate for the graduates and postgraduates has risen up to 10% as 2.4 million peoples are facing deteriorated job prospects. Pakistan is in dire need to switch from IMF based stabilization to job-rich growth in order to get out of this vicious circle. Further, despite following the IMF policies for the past decade, budget deficit is still alarmingly high.

Table 3
Growth and Employment (Percent)

Item	2004-05 to 2007-08	2008-09 to 2017-18
Real GDP growth	6.3	3.8
Agriculture growth	4.5	2.3
Large Scale Manufacturing	10.2	3.0
Services	7.0	3.2

Source: Pakistan Economic Survey: Statistical Supplement 2017-18 and Pakistan Economic Survey 2010-11.

3.4 Public and External Debt

Pakistan's external debt showed a drastic increase due to decrease in non-debt inflows on one side and fiscal profligacy on other side. Public debt rose from 58.6 % to 74.4 % of GDP during the past decade. However, during FY 2013-14 and 2017-18 a relatively low growth in public debt 12.3 % was observed that was mainly due to fixed exchange rate policy, which resulted into overvalued exchange rate.

Table 4
Trends in Public and External Debt

Year	Public Debt (Billion Rs.)	External Debt and Liabilities (Billion $)
2007-08	6040	46.2
2008-09	7631	52.3
2009-10	8890	61.6
2010-11	10680	66.4
2011-12	12652	65.5
2012-13	14321	60.9
2013-14	16389	65.4
2014-15	17819	65.2
2015-16	20054	73.1
2016-17	21783	83.4
2017-18	25574	95.3

Source: State Bank of Pakistan; and Debt Policy and Coordination Office, Ministry of Finance.

Pakistan also witnessed a drastic rise in external debt from 46.2 to 95.3 %, approximately USD 49.1 billion during past 10 years. Since Pakistan was in agreement with IMF during the decade of 1990's and added USD 17.4 billion during that time, the overall rise in external debt was up to USD 66.5 Billion in these two decades. So, many economists called these two decades i.e., 1990s and 2010s as "LOST DECADES of Pakistan".

4. Conclusion

Scrutiny of all the programs so far, reveals that Pakistan failed to extract benefit from the policies suggested by IMF in last three decades. The policies involving these programs, applied in a way that Pakistan remained incapable to stop the IMF treatment. We still remained uncertain, having weak macro-economic stability, improbability and poor economic forecasting and ultimately Pakistan has undergone another agreement with IMF i.e. the 22nd Program. However, it is once again expected that Pakistan shall come out of conditions of uncertainty and achieve macro-economic stability goals resulting in economic growth. It is concluded from the study conducted above that pursuance of IMF Stabilization policies since the last thirty years has caused unsustainable economic growth rate, poor jobs creation with rising unemployment which is a bitter recipe of social unrest. IMF policies have raised fiscal deficit, and most importantly, the exports have declined significantly due to counter-productive policies.

Pakistan has been borrowing loans especially from external sources now to repay the previous loans and the debt has reached at unsustainable level. In this scenario, social or infrastructural development projects do not come in the top priority list. This situation also suggests sudden depletion of foreign exchange reserves may lead the country to default. Currently, the biggest share is spent on debt servicing, nearly 41% this year. Out of total PKR 8.5 trillion budget, approximately 3 trillion goes for debt servicing. Nearly, PKR 1.4 trillion is spent in defense services and further 1.2 trillion is transferred to provinces. Furthermore, approximately PKR 1.6 trillion goes in salaries, pension, and subsidies. After deducting only these few figures the government is left with PKR 2.5 trillion approximately. This remaining amount is spent for all the remaining sectors of the country.

After repayment to IMF a very meagre amount left in the pocket for spending in all the sectors, let alone the social development sectors. The research shows that the govt spent only 2.46% on average within last 14 years on education sector. Similarly, on average 0.46% of total budget was spent on Health sector in last 14 years. Almost, 0.13% within last 14 years was spent on Housing sector and meagre 0.13% was expended for Poverty Alleviation Fund by the government of Pakistan.

Pakistan is constantly in a jam and hazarded a guess about avoiding IMF help in the first place, but more often than not, it ends up using other programs. The Fund is fast to recognize our economy's profound structural problems. The country's economic status worsened worse as a result of two IMF programs implemented between 2008 and 2018. Despite bad economic indications, the country's economic manager signed the 22nd rescue package with the IMF, telling the people that there was no other alternative which is further deteriorating the economic conditions of the country. Hence, it can be concluded that the hypothesis is accepted that Pakistan do not have any option for financial assistance and borrowing other than the IMF until Pakistan cut down its expenditures and economy of Pakistan stabilized but borrowing from IMF has negative impact on the economy.

Authors Contribution
Imran Khan Bozdar: conceived the present idea, developed the theory, discussed the results
Nazar Hussain: conceived the present idea, verified facts and finalized first draft, discussion
Irfan Ali Lashari: conceived the present idea, prepared first draft, discussed the results
Ali Raza Lashari: conceived the present idea, developed the theory, discussed the results
Abdullah Shah: conceived the present idea, collected data, discussed the results

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