PAKISTAN AND THE IMF

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There are not many countries in the world with a track record of being on an IMF program as long and protracted as Pakistan's. The first program was a Standby Arrangement signed in 1958, and in the 65 years since then Pakistan has spent 34 of them inside an IMF program. This has to be a record.

This article will not go into why the causes behind this prolonged use of Fund resources. It merely looks at the course Pakistan's economy has charted through these years and how its protracted engagement with the Fund has shaped its evolution.

Pakistan has used the multilateral lenders like ATM machines over the decades. Successive governments were keen to sign whatever documents were placed before them in order to secure the loan. Once the funds were disbursed, the program was left to languish. This became especially true from the 1980s onwards. The facilities signed in the decades prior were basically short term Standby Arrangements, some of which were not even drawn down fully. Their objectives did not go much beyond short term macroeconomic adjustment, driven mostly by a need to raise revenues and build foreign exchange reserves.

This began to change with accession to a three year Extended Fund Facility (EFF) in 1980. That program was the first to introduce structural conditionality, especially in the exchange rate and energy pricing. Pakistan abandoned the dollar peg in January 1982 as part of the EFF and moved towards a managed float instead, although the dollar remained the intervention currency. Within months the rupee lost close to 10 percent of its value against the dollar, although this devaluation was far too slow for program purposes. "The ultimate adjustment should not be too long delayed," the staff wrote in a mid term review of that facility in April 1982, "especially if evidence were to arise of adverse leads and lags induced by speculative considerations."

No less important was the EFFs emphasis on energy pricing reform, especially fuel. New wellhead prices for domestically produced oil were to be more than doubled, and most importantly, an agreement was reached to increase gas wellhead prices at Sui by more than a factor of 4. These were sweeping changes that carried steep ramifications for inflation, and necessitated a far reaching review of the administered pricing regime that dominated the economy. The formation of the Price Reform Committee a few years later was to move towards market based pricing of foreign exchange and energy, and let a larger process of liberalisation follow in the wake of these changes.

The reforms proved abortive, however. Oil prices at the pump were not pegged to international market prices until the 2008 Standby Arrangement was signed, and gas prices have still not been fully adjusted to global market terms to this day, despite the depletion of domestic gas fields and the rapidly growing induction of imported LNG into the system. The Weighted Average Cost of Gas (WACOG) reform was not legislated until 2022, and to this day has not been notified into practice.

In 1988 Pakistan signed onto a Structural Adjustment Facility (SAF) of three years combined with an SBA of one year, and this package carried the most far reaching set of structural conditionality that the country had seen until that point. The 1988 SAF became the template for all subsequent programs the country signed. It was the first program to advance the idea of shifting the base of taxation away from foreign trade towards domestic consumption. It called for deeper market based reforms not only in foreign exchange management but also in public debt issuance. It was the first facility to use Net International Reserves as performance benchmarks. And it was under this facility that the privatisation program took institutional shape in 1989. In short, it was the facility through which a comprehensively liberalised economy was envisioned for Pakistan.

The Value Added Tax came to be called the General Sales Tax, and the country struggled with trying to administer it in value added mode. Every IMF program since 1988 (save perhaps for the 2000 SBA) had it as a central structural reform measure till it died a spectacular death on the floor of parliament in 2010. The effort was abandoned altogether after that. The GST proved difficult to implement due to the pervasive informality that permeated Pakistan's services sector, which was the fastest growing component of the country's GDP from the 1980s onwards. Far too many entrenched interests stood in the way of the documentation requirements of this tax.

Debt management reforms also showed a stop and go pattern. In the closing years of the 1988 EFF the government finally inaugurated a system of auctioning treasury bills in order to raise domestic debt. The idea was to move away from borrowing by dictate from state owned banks towards borrowing from the market. Initially that meant market pricing for government debt, with auctions as the mechanism to generate the price. This was no less important a reform than the market pricing of the exchange rate.

For a decade it worked, in patches. Through the 1990s the banks bid for government paper, and the State Bank set the cut off yields. But the bureaucrats at the finance ministry chaffed at the rates they were now being charged for liquidity that they otherwise believed was their own property. The reform was undone in the early 2000s, when the State Bank surrendered the prerogative to set the cut off yields in government debt auctions to the Finance Ministry, where it has rested ever since. Then in 2008, the IMF tried once again to bring some discipline to government borrowing by asking for an auction calender to be published at the beginning of the fiscal year. This limited the discretionary space for the government to access banking sector liquidity. But government regained this space by resorting to direct borrowing from the State Bank instead, which reached levels it had never seen in the 2010s.

A journey that began in the early 1980s under IMF auspices and aided along with policy support from the World Bank, and inscribed into the seventh and eighth five year plans, chalked out a meandering path over the decades that left Pakistan's economy with neither market driven dynamism nor state controlled protections. In all spheres – management and divestment of state owned enterprises, pricing reform in energy, documentation of the economy and tax reform for base broadening and improving revenue elasticity, management of government debt to cite just a few examples – the path the country chalked out was patchy, piecemeal implementation with some progress followed by regression. The result is an economy stuck in a halfway house between state and market, unable to benefit from the advantages of either.

The main reason for this shallow commitment to reform is weak ownership at the country level. The existing model of import substituting industrialisation had hit is limits by the early 1980s. Around the world countries were searching for a way forward outside of the old paradigms. But in Pakistan, the search for a path forward in the face of a globalizing world became entangled in the ruler's efforts to procure legitimacy for himself, an effort that subordinated economic policy to the requirements of military rule. The most significant requirement for the dictatorship was foreign exchange – dollars. And out of this thirst for dollars, his regime built a relationship with multilateral lenders that wanted them for nothing more than their money.

Below the top levels of the state, the bureaucrats sought to preserve and safeguard the prerogatives they had grown accustomed to in the days of big government. And big business sought to either protect its rents, or build rent seeking opportunities for itself, as the state withdrew from large areas of the economy, starting with upstream energy supplies and working down to power generation and eventually financial services and manufacturing.

These are the compulsions under which Pakistan's economy evolved in the globalizing world. Little wonder it was unable to build the competitive bases required to compete in the new world dawning all around it, and instead developed an addiction to foreign supplied liquidity injections via geopolitical rents that its leadership called 'aid'. To put it simply, with a reform story that went stop and go, we had a growth story that went boom and bust.

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