

## Balance of payments and foreign policy

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A balance of payments crisis is brewing in Pakistan as data suggests that the current account deficit is over USD 12 billion. This is not being helped by the trends in merchandise exports and imports.

During the last fiscal year, the annual change in exports of goods and services was

**Pakistan's weak trade diplomacy has pushed the current account deficit to over \$12 billion**

negative 0.7 per cent while the change in imports was a whopping 18 per cent. During the same period, the year-on-year rise in Pakistan's total debt and liabilities was 11 per cent (standing at almost 79 per cent of GDP).

This was contributed by a 13 per cent increase in external debt; 9 per cent increase in government's domestic debt, and 45 per cent increase in debt of public sector enterprises.

The overall current and future burden of debt is of course estimated by the government authorities, based on an exchange rate which many have termed overvalued. Any downward slide in the value of Pakistani rupee is bound to increase this burden.

Several experts have come up with various options to save the balance of payments and prevent another resort to International Monetary Fund (IMF) and other lending institutions. The range of suggested measures is long.

For example, gradually correcting the exchange rate, in turn, is making imports expensive. There is, however, no clear evidence if the correction in the exchange rate will result in medium to long term revival of exports.

Second, imports may be curtailed through tariffs, regulatory duties and related instruments. Higher tariffs, particularly on luxury items, e.g., luxury vehicles, mobile phones, packaged food items, cosmetics, etc., could result in some savings on the import side.

Just by way of giving numbers, Pakistan imports food worth USD 5.4 billion (not all of it can be termed essential); mobile phones, apparatus and accessories worth USD 1 billion. Imported cars (including luxury German and Japanese cars and bullet proof vehicles) and related equipment are worth almost another USD 1 billion.

A regulatory duty on non-essential imports may be considered. Import policy can also be corrected. For example, for a long time the age limit of three years is maintained in the case of import of cars, and five years in case of SUVs (sport utility vehicles), including 4x4; the latter type of cars being given an advantage as per current rules. Such conspicuous consumption may be curtailed through appropriate amendment in import policy.

Several statutory regulatory orders (SROs) by various federal authorities allow for preferential (lower) rates of trade taxes while importing. Some exemptions are now also

being allowed in the name of special economic zones, with no past evidence from already existing zones and industrial estates whether or not such preferences actually deliver.

These exemptions and preferences, if not essential, may be done away with to curtail imports and stop domestic production decisions to get distorted. Likewise, cash margin for imported items can be altered to control the inflow of non-essential imports.

Many are also looking in to how remittances can help save the day for balance of payments. Suggestions under this heading include: early launch of diaspora bonds, increased privileges for remittance senders, and reducing costs of remitting to Pakistan.

This, however, will require removal of several restrictions currently in place on movement of financial flows in and out of the country, revival of confidence of expatriates in Pakistan's macroeconomic performance and sustained increase in quantity and quality of labour which is exported from Pakistan.

Most of the above-mentioned steps are not enough and will not take us beyond the next couple of months. The real issue is lack of growth, productivity and exportable surplus in the economy. This requires a more coherent response from both public and private sector.

In a recent meeting of some major exporters in the country, convened by the Sustainable Development Policy Institute, it was highlighted that exporters are facing several structural issues. Possible remedial measures were suggested to help boost exports.

The top five key constraints highlighted by exporters include: complex domestic and trade taxes regime, including refunds issues



faced by exporters; overvalued exchange rate; regulatory complexities (including dealing with quotas, licenses and permits) while importing raw material and machinery, expanding operations, and claiming adjustment for inputs; higher unit costs of electricity, fuel and gas in comparison to competitor economies; and weak trade facilitation i.e. rules, regulations and controls on the movement of goods.

A longer term and bipartisan vision for achieving export competitiveness is necessary. The Ministry of Commerce and Federal Board of Revenue will have to ensure through correct signaling that small and medium exporters will not face frequent shifts in import, tax and energy policies in the country; not have to spend over 500 hours every year, facing federal and provincial tax authorities and audit officers; have access to export development fund (EDF) for their value addition needs (in line with the ambition in Export Development Fund Act 1999); be helped towards achieving product compliance required for entering new markets; be facilitated towards reduction in their customs, transportation and related logistic costs through appropriate trade facilitation measures; see expanded availability of refinance under the Export Finance Scheme (EFS).

However, our discourse on the balance of payments situation is limited to macroeconomic fundamentals. The foreign

policy outcomes have added to the balance of payment woes. Our ongoing discourse ignores the fact that long term exports dwindled as Pakistan's relations with its neighbours and friends elsewhere worsened.

Islamabad has remained unable to host the SAARC Summit where several regional trade, investment, transport and energy agreements were to be signed. The lack of urgency in the already due revision of Afghanistan Pakistan Transit Trade Agreement has halted progress on bilateral trade and transit cooperation with Afghanistan and key Central Asian economies, including Tajikistan which has been demanding more expanded land route trade with Pakistan.

Weak response to Iran on bilateral trade and energy cooperation has led to changing interest of our neighbour and weak expectations from Economic Cooperation Organisation (ECO). There is almost no leverage which could persuade China, Thailand and Turkey to expediently finalise the under-negotiation free trade agreements — currently a source of concern for the local business community.

A review of European Union's Generalised System of Preferences (GSP) plus facility allowed to Pakistani exporters is around the corner and there are fears regarding its outcome. A similar GSP facility provided by the United States remained underutilised.

Let's look at the result of weak trade diplomacy which should have been a key pillar of Pakistan's foreign policy. Between 2011 and 2017, Pakistan faced declining exports in case of China (-1.4 per cent), United States (-10 per cent), Afghanistan (-40 per cent), Iran (-77 per cent), Bangladesh (-31 per cent) and Sri Lanka (-22 per cent).

Despite the GSP plus facility by the European Union (EU) the exports to EU could only increase (for the same time period) by 11 per cent — not compensating for the decline faced in other countries and regions. Here is another interesting fact: During the same time period, and despite of all political frictions Pakistan's exports to India have increased by 42 percent — indicating a large untapped potential if only trade is kept delinked from regional politics.

The very near future may not see Pakistan competitive vis-à-vis ASEAN countries, however, the markets in ECO, SAARC and African regions can still be regained. For this to happen, Pakistan's external and foreign security policies need to be aligned with growth and trade priorities.

Today, foreign investors, manufacturers and

traders find it hard to travel to Pakistan and see for themselves the talents, skills and comparative advantage of local business community. Anyone trying to arrange a business trip to

Pakistan realises rather quickly how difficult it is to get Pakistan's visa.

This is an important issue as Pakistan's peer economies, including several South Asian countries have liberalised their visa regime and allow visa-on-arrival facility to businessmen. It is increased people-to-people engagement that precedes stronger business-to-business relationships.

Going forward, engagement with United States should be a priority in the interest of uncertain level of current and future foreign exchange reserves in Pakistan. This engagement is required to: a) start crafting a positive image of Pakistan as the world

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believes CNN more than PTV, b) insure against any future embargos on trade, investment and defense cooperation with Pakistan, c) keep dialogue with Afghanistan on-track in the interest of Pakistan's own internal and external security, and trade and transit cooperation with the western and Central Asia region, d) help demand greater business-to-business interaction and deeper GSP facility inside United States for Pakistani exporters, and e) support in social and economic spheres particularly technology and knowledge transfer for improved productivity in agriculture and manufacturing sectors, education and health — not always provided by all-weather friends.

Perhaps sustained engagement with the US will also be critical for the sustainability of China Pakistan Economic Corridor (CPEC), peace in Balochistan and overall inclusive growth prospects in Pakistan. As the early harvest projects under CPEC come to a completion, Islamabad will need to seriously think how benefits of CPEC can be extended to neighbours for creating robust interdependencies in the region.

With time and as the relationship heals, United States and Pakistan can work together

in closing expectations gap which currently keeps Afghanistan, India and Pakistan to interact more closely. A democratic, economically stronger and regionally relevant Pakistan will be better able to deliver towards restoring regional stability and sustaining dialogue processes, e.g., Quadrilateral Coordination Group for Afghanistan.

There is a two-way gain here for Pakistan and friends, if only the former can demonstrate this through timely homework. Pakistan, now the fifth largest population can be a significant market for the United States, European Union and others — only if it is economically vibrant. Already, we can note an increase in the number of US and EU companies in Pakistan gaining important commercial, government and CPEC related contracts.

A key question going forward will also be how China wishes to see the Pakistan of future. After all, they are putting their money in the most expensive arm of Belt and Road Initiative, i.e., CPEC. China has the leverage to bring US and Pakistan closer; however, this will only happen if China and the US have a shared vision for the region and, more importantly, for Pakistan.

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