



## PAKISTAN'S BALANCE OF PAYMENT CRISES OF 2022 AND THE EXTENDED FUND FACILITY FROM IMF

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### Abstract

*A balance of payments deficit is one of the predominant raison d'être (basis) for the decelerated financial status of Pakistan. Deferred policy action in the face of rising international prices led to a rapid loss of foreign reserves. Pakistan generally has been a low-inflation economy developing at a rather gentle pace. At the moment it has turned into a low-development and high-inflation economy. The year 2022 is marked by a lack of economic progress. The troubled areas are the balance of payments, lack of foreign investment, and a falling Rupee against other international currencies. This paper focuses on the causes of the balance of payment issues, and structural hindrances to the economic growth of Pakistan. The paper also evaluates a staff-level understanding with the IMF team on policies to conclude the 7th and 8th reviews of Pakistan's Extended Fund Facility (EFF). Data is collected through primary (interviews) and secondary (books, surveys, governmental records journals, newspapers, and websites) sources. The work aims to examine the response of the government to the worsening situation and recommends some policy measures.*

**Keywords:** Balance of Payments, high inflation, macroeconomic management, foreign investment, structural issues, Extended Fund Facility, International Monetary Fund<sup>1</sup>

### INTRODUCTION

Since its birth in 1947, Pakistan's economy has become diversified with time, to be known as semi-industrialized. In recent years food production, agriculture, and textiles have established a drive in the direction of technological expansion. Pakistan made significant improvements in terms of security and energy in 2012. Since then, GDP growth has made progress. Nevertheless, years of exploitation and internal political conflict resulted in reduced levels of foreign investment coupled with slow progress.

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According to Parvez Hassan:

*“The economic growth has meant an increase in an average income of about 150 percent from 1950 to 1996, but Pakistan like many other developing countries has not been able to narrow the gap between itself and rich industrial nations, which have grown faster on a per head basis. Per capita, the GNP growth rate from 1985 to 1995 was only 1.2 percent per annum.”<sup>2</sup>*

1957 - 2015, the average rate of Pakistan's inflation was 7.99 percent.

### The purpose of disquisition

This paper aims to highlight the crisis of balance of payment, identifying challenges that led to financial distress over the years. For this purpose, data is collected via interviews.

→ Develop an in-depth understanding of Pakistan's financial crisis.

### The Paper is based on three sections-

- I. The first section is a short historical review of Pakistan's economy.
- II. The second section is terminated or suspending foreign assistance under the Foreign Assistance Act
- III. Policy measures are suggested.

#### 1. Section One

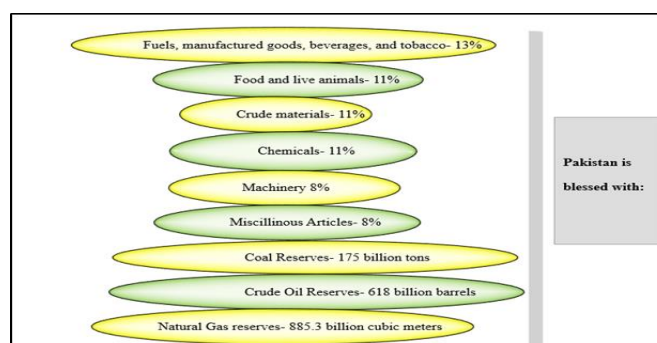
The section is based on:

- ❖ The historical rundown of Pakistan's economy.
- ❖ Rise and setbacks to the economy/missed opportunities.
- ❖ Balance of payment crisis, and
- ❖ Structural hindrances to financial growth.

#### 1.1 Historical Vista

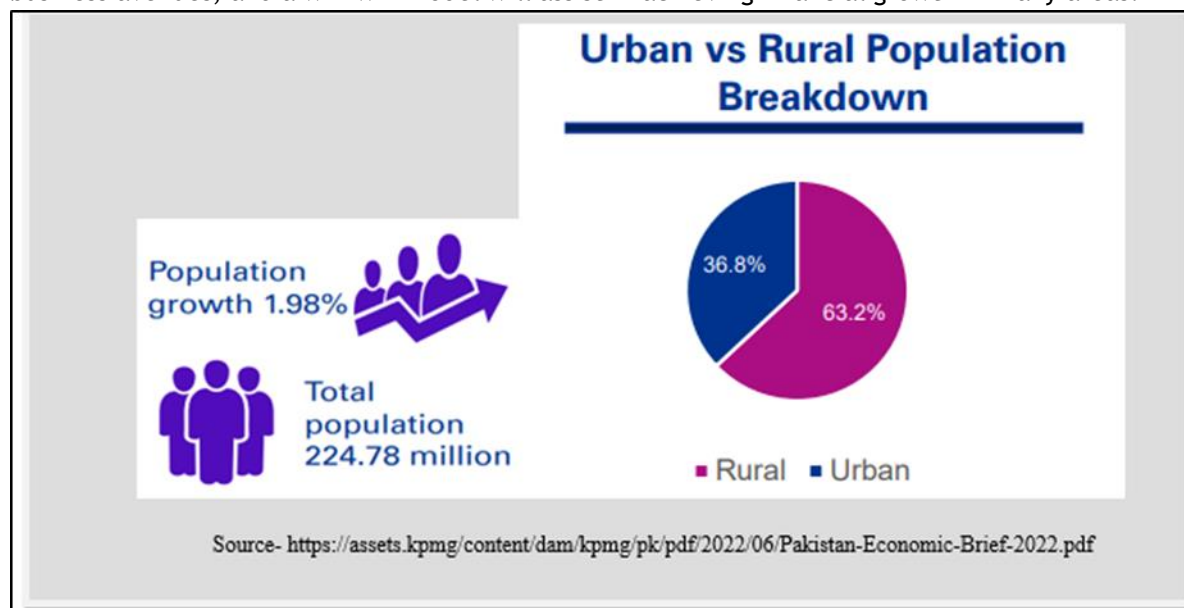
Pakistan is strategically situated at the intersection of Asia. China is its neighbor in the north, India in the east, and Afghanistan and Iran in the west. Therefore, its strategic position allocates Pakistan to develop into significant energy, transport, and trade corridor. Notably, Pakistan is a doorway to the wealthier States of Central Asia, the Gulf States, and far Eastern countries. This distinguished attribute of Pakistan alone makes it a position of vast potential outcomes. Pakistan positions 23rd in the world as the major economy in purchasing power parity (PPP), whereas it occupies 40th rank as the largest economy regarding nominal GDP. According to the evaluations made by the World Bank, Pakistan ranks 8th among the top 10 recipients of remittances. Significant areas of Pakistan's economy are Agribusiness/agriculture, Industrial, and Services spheres which add 19%, 20%, and 61%, distinctly to the Gross domestic product.

Pakistan is an energy-rich country. It has mineral resources and a massive belt of agricultural land. 27% is cultivated out of the total geographical area. The Indus Basin Irrigation System of Pakistan is the most developed in the world. Pakistan is blessed with rivers and the sea. There are harbors to import and export goods. Pakistan is enriched with four seasons and tropical weather beneficial for agriculture and farming.

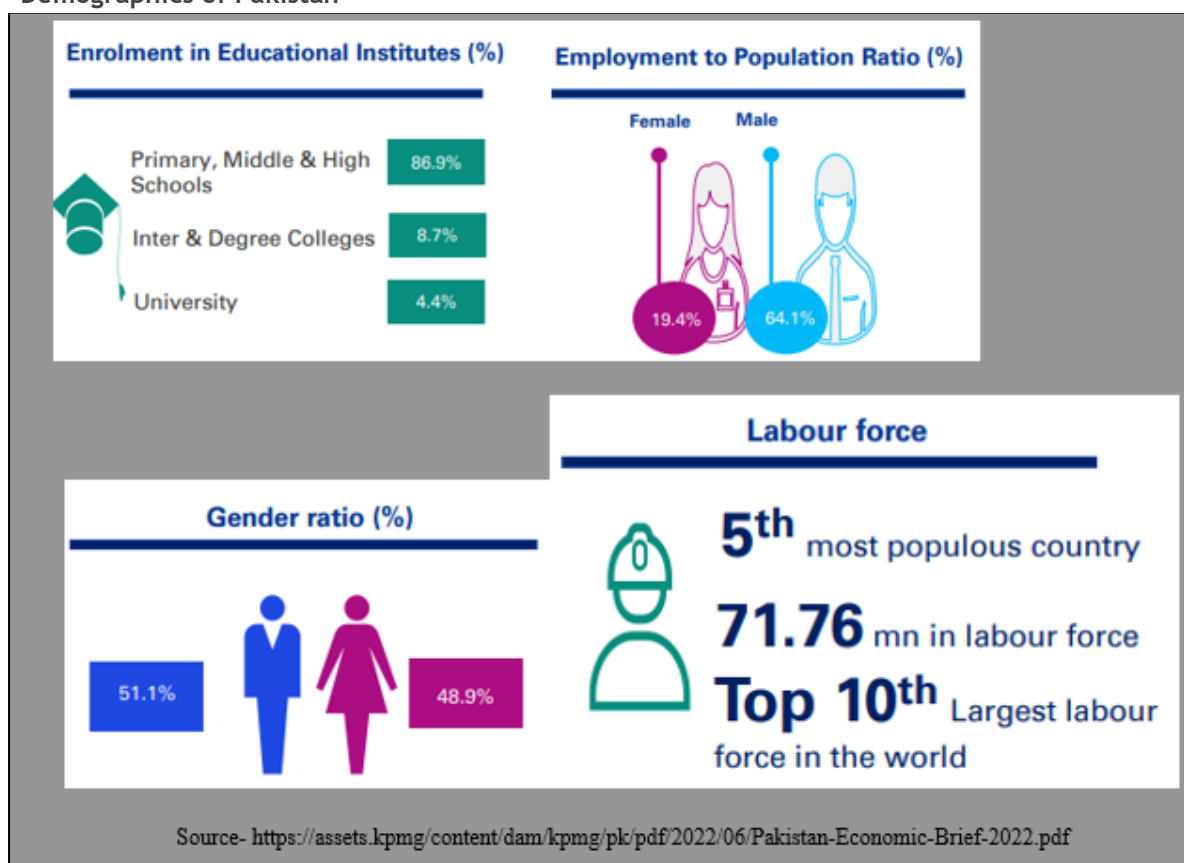


<sup>2</sup> <https://tribune.com.pk/story/501111/is-pakistans-economy-in-recession>

One of the reasons that Pakistan and China have started the CPEC project. The aim is to derive benefits through regional connectivity. Other goals are to further improve relations with its neighboring states such as Iran, Afghanistan, and Central Asian Republics. The enhancement of the geographical connections, regional knowledge, trade, transportation system, infrastructure, business avenues, and a win-win model will assist in achieving financial growth in many areas.



### <sup>3</sup>Demographics of Pakistan



#### • Type of Economy

An economy is a composite structure of interdependent producers and consumers that function lucratively. Servitude of individual and societal freedom is the result of a flawed/weak economy.

<sup>3</sup> \*Figure 2 and 3 source- [Pakistan Economic Brief 2022 \(assets.kpmg\)](https://assets.kpmg/content/dam/kpmg/pk/pdf/2022/06/Pakistan-Economic-Brief-2022.pdf)

Globally, various kinds of economies exist with their benefits and weaknesses. Disorders and recessions leave every kind of economy imperfect. Literature exhibits different kinds of economies such as;

- a. Free Market Economy
- b. Command Economy
- c. Free and Command Economy (Mixed Economy)

#### **Free-Market Economies:**

These economies are largely capitalist, companies and individuals make better decisions regarding their economic interests. A competitive environment provides better opportunities to exchange goods and services. Individuals and businesses make their own fiscal decisions mostly visible in democratic states. These economies yield more economic growth. as is the case with the countries of Europe, North America, and the Tigris.

#### **Command Economies:**

These economies are regulated by the government, thus they are centrally planned, controlled, and administered. Production and consumption activities are managed to secure certain economic and security goals, sometimes to save incipient industries and at times to perpetuate a monopoly within or outside the borders of the state. Central government takes all major decisions in these types of economies.

These economies are found in communist or authoritarian states. For instance, Russia and China. Many economists evaluate that the USSR's disintegration was due to unjust distribution and ill planning. China has also felt the need to move from a command economy to a distinct and relatively unconventional structure. The need is discerned due to its cardinal economic laws and drives.

#### **Free and Command Economy:**

This kind of economy still retains the characteristics of both types. It combines components of both, therefore, dealing with rising socio-economic issues in a better way. Today, the state plays a limited role in regulating economic issues even in free-market economies, namely fiscal and monetary policy. Other interventions are price fixing, subsidies, and tariff policy. Due to these factors, most economies today are mixed economies. Today, agriculture contributes nearly 21% of GDP, which is more than 50% when the state was founded in 1947. While the industrial and service sectors accounted for 20.9% and 57.7% respectively of GDP, compared with 8.03% and 39.3% in 1947. The trade account deficit still lingers on, and Pakistan's foreign exchange reserves are also disrupted due to over-dependence on imports and shortages in the energy sector. The persistent depreciation of the Pakistani rupee is also a result of these monetary issues. Public debt, to manage the economy, is increasing sharply and reached 60% of GDP. this shows that Pakistan's economy has many problems. Thus, a robust and coherent socio-economic model and stable political framework are needed to get Pakistan out of this sinking state. Here is a brief introduction to the economic structure of Pakistan.

Pakistan exhibits a mixed economy; Government takes major decisions in both areas which are state-owned and privately-owned enterprises. The economy of Pakistan is further dependent on other sectors such as; industrial, agriculture, and textile. Since its creation in 1947, Pakistan's growth rate remained higher for five decades as compared to other world economies at that time. During the 1960s Pakistan was regarded as a model of progression in the world due to its economic growth. The average growth rate per year was 6.8 %. Karachi in the 1960s was regarded as an economic role model around the world, with Seoul, South Korea, adopting the city's second " Five-Year Plan ". Pakistan's economy showed slow economic growth during 1970-1990 due to mishandling of fiscal policy. Nevertheless, it recovered through the policy of deregulation. At the beginning of the 1970s, significant sectors of Pakistan's economy were nationalized; manufacturing, transportation, and financial services. More modifications were brought by the military regime of Zia ul-Haq during the 1980s. Pointedly, an Islamic Economy was established., which made all practices illegal that are not allowed by Shariah (Muslim law).



The salient features of Pakistan's economic history are:

- Self-sufficient in most food production.
- From time to time the per capita incomes showed fine results in terms of expansion.
- Pakistan is resourceful in the production of cotton and cotton textiles.
- Pakistan has also shown improvement regarding the furnished goods domestically and internationally (access to the markets of CARs and Africa)
- Expansion of physical infrastructure network (highways, Motorways, power, energy, ports, and telecommunication facilities).

Despite acute structural impediments, Pakistan can accomplish certain goals in different areas such as income, agriculture, industrial production, and consumption. It has lost significance due to setbacks and missed opportunities.

### 1.2 Rise and setbacks to the economy/missed opportunities

*The economy is the start and end of everything. You can't have successful education reform or any other reform if you don't have a strong economy.*

David Cameron <sup>4</sup>

Throughout Pakistan's economic history, the biggest obstacle has been that human development is overlooked even in times of a flourishing economy. If investments in population education and improving the training, skills, and health of the workforce are in line with those of East Asian countries, the policy of opening up to world markets can be maintained without being jeopardized, Pakistan's exports might reach at least \$100 billion instead of \$13 to \$14 billion. Reducing the population growth rate from 3% to 2% shall avoid problems of overcrowding and lack of infrastructure and social services, and the poor will also have better access to education and health. Moreover, poverty will decrease, as compared to what prevails currently.

But as if the dereliction of human development was not adequate, the country sagged in the 1990s. It started to lose growth, exports, income, and development spending and was stuck in external and domestic debt. This is due to underlying structural and institutional issues, disappointing governance, and continuing shifts in the political regime. Short-lived, successive governments were reluctant, if not extremely disinclined, to make difficult and unpopular economic decisions to turn the economy around. Furthermore, two to three years of rule was not enough to produce significant political or institutional changes. Post-May 1998 events, the external environment also became inapt, as Pakistan had to conduct its first nuclear test in response to India's nuclear tests. The repercussions of this ordeal have resulted in the economic isolation of Pakistan. Western governments-imposed sanctions on Pakistan. Under the Foreign Assistance Act, the US ceased or suspended foreign assistance to Pakistan. By the late 1990s, Pakistan had fallen into near recession in its economy, especially in the external zone. Remittances of workers dropped significantly, exports grew negative, IMF and World Bank aid programs were suspended, donors stopped assistance, and debt payments exceeded. Pakistan was about to default on its external payments. Economic growth was sluggish, debt was precariously high, and poverty rates had risen to 32% again.

This epoch of structural adjustment was identified by the absence of regular macroeconomic policies. Lacking a cohesive economic and political framework left the state dependent on an increasing number of international actors. Constant dealings with international financial institutions have thrown Pakistan into the debt cavity and wrested economic sovereignty from it. Every consecutive government has borrowed from domestic and international sources regardless of the extent of the economic damage and hardship.

**Reform Era- Economic Liberalization:** *Political and Economic Trends from 1999 to 2007* General Pervaiz Musharraf took over the reins of the government by suspending the 1973 constitution and overthrowing the government of Nawaz Sharif on 12 October 1999 and became the state's chief executive. The main causes for this power struggle were political instability, economic bankruptcy, international constraints, state failure, and public resentment due to inflation. The institutional

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<sup>4</sup> \*Brainy Quotes.com



building process could not flourish as expected due to the negative role of the opposition. Mixed results appeared regarding the economy of Pakistan during Musharraf's time. The success was visible because of the increased flow of foreign aid. This coup d'état was welcomed by most of the country as the Pakistani people were not satisfied with the role of political parties. This era was also marked by the independence of the media and the political socialization of the public. Some analysts appreciate his liberal policies and for some, his policies were short-sighted and flawed. Economic growth in the Musharraf era was as strong as that of the previous autocratic rulers. During his time, the average GDP growth rate was recorded at 5.3%. Many international investors were attracted to invest in Pakistan due to Musharraf's liberal economic policies. It was possible due to his policies to restore investors' confidence, thus FDI increased remarkably. Consistent growth occurred in different sectors due to these investments.

On the other hand, his import-led policy generated an economic bubble (it is a time when prices of current assets largely bypass intrinsic valuation) in Pakistan's economic policy. The huge inflow of imports in the sectors of auto and telecommunication put pressure on the economy's supply side. The worst form of energy crisis created as the power supply did not increase with the rate of change in energy demand, is affecting the economy even now. The supply of electricity to far-flung regions also exacerbated the distress because of the fixed supply and increase in the number of consumers. Inflation was recorded as high due to the energy stress in the country. This inflation, therefore, gobbled economic development and purchasing power of people. As a result of ill-advised economic policies, economic bubbles ruptured soon after their implementation.

Aside from these setbacks, there are many of Musharraf's policies have hitherto been highly acclaimed in economic and political circles. The first of these was the reforms of education to form build human resources. More autonomous public and private sector universities were founded with an efficient Higher Education Commission.

**Privatization period: 2008 to 2013 Political and Fiscal Environment-** the revival of democratic government under Asif Ali Zardari was crucial because a military ruler had just left the office of chief executive. The process of democratization was challenging as it was multidimensional, political (to complete the tenure uninterruptedly), and also to bring economic stability to the country. Completed five years of democratic rule for the first time in the history of Pakistan despite challenges.

Amendments were also made to the constitution to reinforce the political system of Pakistan. Pakistan's economy went through phases of negative and positive fluctuations. The country faced serious economic issues. Difficult decisions were required at both micro and macroeconomic levels. Due to such decisions, the stock market showed favorable results.

After consultation with the IMF, a macroeconomic stabilization program was also launched. A restrictive fiscal plan was made in the Zardari period to solve the issue of inflation and also steps were taken to lessen the problem of budget deficit in Pakistan. Due to efforts, inflation was reduced in 2009, the budget to 24.3 % of GDP, and the current account balance was recorded at 5.3 %. Foreign exchange and GDP reserves surpassed 13 billion USD. Due to reduced oil subsidies and development spending, the budget deficit decreased.

During the Zardari era, revenue earnings were low. The delay in taxing measures led to revised RBF targets every year, as capital was needed to execute a better budget discipline. The sudden drop in GDP growth in the following years made the situation worse.

The lowest tax to Gross Domestic Product ratio in the region also posed an alarming situation for future growth. The increase in public debt weighed on revenue, as interest payments increased at a quick rate. The energy crisis severely affected our production capacity, causing our exports and foreign income to decrease. In short, any economic activity threatened our very existence. As a result, some economic reforms were implemented and were successful to some extent. Policies included stabilization measures, optimizing the use of reserves, managing public sector companies, and businesses, and reforming the electricity sector.

The government followed procedures through Presidential Order,

*Short-term tax policy procedures to add 53 billion rupees fund in the 2010-11 fiscal year.* Here are the actions are taken:

- ❖ Removed Sales tax exemption for agricultural inputs like pesticides, tractors, and fertilizers. Previously, these were subject to 17% GST.
- ❖ The excise tax rate increased from 1% to 2.5% for non-essential items.
- ❖ Total and net accumulation of direct rights increased by 31.3% and 22.6% individually in the first ten months of 2011-12.
- ❖ This increase in revenue was largely due to deductions from the source, voluntary money transfers, and interest collection.
- ❖ For the July-April 2011-12 period, gross and net cumulative of diverted rights grew by 23.1% and 24.9% respectively.
- ❖ 62.9% of total RBF royalty revenue.

It was the same period that the share of the agricultural sector in GDP fluctuated at 21.3% in 2008, 21.8% in 2009, and 21.4% in 2012. Pakistan's national savings in the period 2010-2011, were 13.2 and subsequent years exhibited a reduction in its magnitude to 10.7%.

### **2013 and onward: Privatization and liberalization**

In 2013, Nawaz Sharif made his government and inherited a crumbling economy due to a lack of energy, increased inflation, high debt, low fiscal growth, and inflated budget deficits. Pakistan *"launched the \$6.3 billion IMF Expansion Fund, focused on alleviating energy shortages, stabilizing public finances, increasing revenue and improving the balance of payments position"*.

- The 2014-2015 fiscal year experienced a reduction in oil prices, increased remittances, and better security, spending by consumers fueled growth to 4.3%, and exchange rate reserves enhanced to US\$10 billion.
- The IMF in May 2014, established inflation had decreased to 13% in 2014 from 25% in 2008, encouraged Standard & Poor's and Moody's Corporation to declare Pakistan stable in a long-term position.
- The IMF lending program of September 2016. However, Pakistan was not able to attain many structural reform benchmarks, yet it could restore macroeconomic strength and thus improve its credit rating.
- Pak-Rupee 2015, remained stable against the US dollar, yet depreciated by 10% between November 2017 and March 2018.
- BOP also appeared due to an increase in imports and a decrease in exports and remittances.

South Asian Growth Report, the World Bank said:

*"In Pakistan, a gradual recovery to around 4.5% growth in 2016 was supported by low inflation and fiscal consolidation. Increased remittances and stable agricultural activity contributed to this result. required to address widespread power outages, a heavy business environment, and poor access to finance. The outlook for 2020 is "very good", predicting that Pakistan will transition from a "low-income country to a middle-income country within the next 5 years".<sup>5</sup>*

In 2016, Forbes and Reuters articles noted that Pakistan's economy was a rising market in Asia and that its expanding middle class was decisive to its economic outlook. On November 7, 2016, Bloomberg News also stated that

*"Pakistan is on the verge of an investment-led growth cycle."*

On 10 January 2017, The Economist prediction was that Pakistan's GDP would increase by 5.3% during 2017, the fifth fastest-growing economy in the world and the rapid expansion in the Muslim World.

### **1.3 Achilles heel of Pakistan's economy is the stumbling block of the Balance of Payments**

Every time the economy is about to lift off, our heels are hurt by the arrow of increased imports and our journey abruptly stops. Resultantly, fiscal growth is hampered by the balance of payments problems, thus creating an inflationary spiral. There are several main reasons for this recurring

<sup>5</sup> \*South Asian Growth Report, the World Bank

problem- worsening trade conditions, unadaptable imports as well as exports of the underlying fundamental sector exports. Pakistan can sustain growth up to 4%, in addition, the import bill is starting to rise to unsustainable <sup>6</sup>levels.

This ultimately led to a balance of payments crisis and therefore Pakistan needs International Monetary Fund (IMF) assistance or other international lending institutions. The stagnation of exports is a big problem in this respect. Pakistan's exports remain concentrated in basic commodities (rice) and salient textiles (gray fabrics). This is a vital part of the economic crisis. The swelling perforation of imported goods into the public's day-to-day lives has impacted the balance of payments. Moreover, import prices are rigid, i.e., the depreciation of the rupee has only a restricted influence on the volume of imports. Thus, a balance of payments issue becomes mandatory as soon as development resumes in Pakistan. Similarly, the terms of trade over the years have evolved against Pakistan. The terms of the trade index decreased from more than 80 (2004) to 58 (2021). The US Central Intelligence Agency reported that in 2001, the purchasing power parity of Pakistan's exports was \$8.8 billion while imports reached \$9.2 billion, resulting in a trade deficit. \$399.9 million.

According to the International Monetary Fund (IMF) report in 2001, Pakistan's total merchandise exports were \$9.13 billion and imports \$9.74 billion. Service credits amount to \$1.46 billion and debits \$2.33 billion.

#### **1.4 Long-term structural challenges pose risks to Pakistan's sustainable growth: World Bank Pakistan Development Report**

*Pakistan's economy recovered strongly and could grow by 5.6% in FY21 subsequent government measures to mitigate the negative socio-economic impacts of the COVID-19 pandemic.*<sup>7</sup>

According to the World Bank's Pakistan Development Update, fiscal activity-maintained thrust from July to December 2021, strong demand pressures, and increasing global commodity prices caused two-digit inflation and an acute increase in import bills within this time. These developments adversely impacted the rupee. In addition, long-term structural weaknesses in the economy, including weak investment, weak exports, and weak productivity growth, cause risks to recovering from economic shocks.

According to the report, poverty—defined as living below the \$3.20 Purchasing Power Parity 2011 daily poverty line—declined from 37% in FY20 to 34% in FY21 as a result of economic growth and better labor market conditions. However, it is anticipated that rising food and energy costs will reduce households' actual purchasing power, disproportionately impacting poor and vulnerable households that spend a bigger amount of their income on these products.

The report underlines the;

- ❖ Financial recovery,
- ❖ Enhanced labor market conditions,
- ❖ The poverty rate- as calculated at the income of middle-class poverty level
- ❖ - is lower than US\$3.20 in 2011 in Purchasing Power Parity. equivalent per day- fell from 37% in FY20 to 34% in FY21.
- ❖ Nonetheless, an increase in energy and food prices may reduce the households' real purchasing power, and inordinately affect poor and weak households, who spend their budget on most of these articles.

*"Pakistan's economic recovery after the COVID-19 crisis indicates that the country has enormous potential to overcome challenging economic situations," said*

**Najy Benhassine, World Bank Country Director for Pakistan.**

*"However, sustaining the economic recovery requires addressing long-standing structural weaknesses of the economy and boosting private sector investment, exports, and productivity."*<sup>8</sup>

<sup>7</sup>\* <https://tribune.com.pk/story/2324182/recurring-balance-of-payments-problem>

<sup>7</sup> Pakistan's economic survey report

<sup>8</sup><https://www.worldbank.org/en/news/press-release/2022/10/06/world-bank-pakistan-s-economy-slows-down-while-inflation-rises-amid-catastrophic-floods>



Structural problems include low productivity in industry and agriculture and industry, lack of economic documentation, poor fiscal management, poor management of external sector problems, the indifference of banks to the credit requirements of the private sector, and complete incapability of self-organization and receptivity of the private sector. Innovation is the key to survival and growth. What stems from all these problems is political instability. The economy faces structural problems

Attempts to solve some structural problems complicate problems in other areas.

Outline of Pakistan's structural problems:

- 1) higher participation of government disproportionately in economics schemes,
- 2) huge informal economy,
- 3) agriculture has remained a vital employer of manpower,
- 4) focus on production activities cotton-related,
- 5) biased policies regarding import-trade activities,
- 6) services economy is neglected in public policies,
- 7) sparse investment in human development and infrastructure due to the low rate of savings
- 8) lack of ability of the government to gather ample tax revenues,
- 9) small and medium enterprises are neglected,
- 10) weak institutional structures and governance,
- 11) lack of accountability,
- 12) lack of deep-rooted reforms and their execution by the subsequent governments.

## 2. Section Two

This section is composed of:

- ❖ Brief prologue of International Monetary Fund and its Extended Fund Facility
- ❖ Pakistan's current (2022) financial status and IMF's EFF 7th and 8th Reviews
- ❖ Data collected via interview questions

### 2.1 International Monetary Fund and EFF Program

The IMF is an international organization that supports global fiscal development as well as economic stability, enhances international economic growth, and helps in reducing poverty. It was originally founded in 1945 as a result of the Bretton Woods Agreement and started to boost international financial cooperation by establishing a system of currency convertible with a fixed exchange rate. It gathers information related to national economies, worldwide economies, and international trade and thus shares economic forecasts. One of the IMF's most crucial roles of IMF is to give financial assistance to the struggling economies of the world to come out of the acute fiscal crisis.

The IMF also provides training and technical assistance, and policy advice to member states to build their capacities. These programs are comprised of training in data collection and its analysis, preparing reports, and conducting economic surveys. The IMF collects its funds via subscriptions and quotas from member states. Contributions are made according to the size of the state's economic position for example the US is the largest contributor due to its largest economy.<sup>9</sup>

#### Pakistan and IMF

*Pakistan: Transactions with the Fund from 2010 to September 30, 2022*

A look<sup>10</sup>

<sup>9</sup> \*IMF.org

<sup>10</sup> *Pakistan: Transactions with the Fund from 2010 to September 30, 2022*

(in SDRs)

Year	General Resources Account		Poverty Reduction and Growth Trust 1/2/				Total		
	Purchases		Charges Paid	Loans		Interest Paid	Purchases and Loans		Charges and Interest Paid
	Disbursements	Repurchases		Disbursements	Repayments		Disbursements	Repayments	
2022	1,644,000,000	522,166,666	86,676,243	0	0	0	1,644,000,000	522,166,666	86,676,243
2021	350,000,000	732,166,666	98,929,348	0	0	0	350,000,000	732,166,666	98,929,348
2020	1,015,500,000	690,000,000	101,645,558	0	0	0	1,015,500,000	690,000,000	101,645,558
2019	1,044,000,000	420,000,000	99,997,649	0	0	0	1,044,000,000	420,000,000	99,997,649
2018	0	150,000,000	92,728,234	0	0	0	0	150,000,000	92,728,234
2017	0	0	75,164,939	0	0	0	0	0	75,164,939
2016	793,000,000	0	47,077,743	0	0	0	793,000,000	0	47,077,743
2015	1,440,000,000	303,043,255	27,593,285	0	0	0	1,440,000,000	303,043,255	27,593,285
2014	1,440,000,000	1,273,770,379	24,003,733	0	34,456,000	0	1,440,000,000	1,308,226,379	24,003,733
2013	720,000,000	2,313,465,251	41,363,130	0	86,140,000	0	720,000,000	2,399,605,251	41,363,130
2012	0	1,342,738,125	86,533,909	0	146,438,000	0	0	1,489,176,125	86,533,909
2011	0	0	111,675,655	0	172,284,000	0	0	172,284,000	111,675,655
2010	1,063,682,010	0	82,726,174	0	172,284,000	67,025	1,063,682,010	172,284,000	82,793,199

### Pakistan's Debt and Liabilities-Summary June 2020-June 2022

<sup>11</sup>Provisional, Revised.

(In Billion Rupees)				
	R			
	Jun-20	Jun-21	Mar-22	Jun-22
I. Government Domestic Debt	23,282.5	26,265.4	28,076.3	31,036.2
II. Government External Debt	11,824.5	12,439.0	14,936.2	16,746.5
III. Debt from IMF	1,291.5	1,161.5	1,371.0	1,409.6
IV. External Liabilities <sup>1</sup>	1,663.3	1,378.4	2,116.3	2,275.6
V. Private Sector External Debt	2,628.2	2,543.5	3,135.3	3,596.0
VI. PSEs External Debt	869.5	1,064.6	1,341.0	1,675.7
VII. PSEs Domestic Debt	1,490.5	1,436.7	1,439.4	1,393.4
VIII. Commodity Operations <sup>2</sup>	813.4	904.0	844.8	1,133.7
IX. Intercompany External Debt from Direct Investor abroad	727.9	650.7	776.3	905.1
<b>A. Total Debt and Liabilities (sum I to IX)<sup>6</sup></b>	<b>44,591.5</b>	<b>47,844.0</b>	<b>53,561.5</b>	<b>59,696.8</b>
<b>B. Gross Public Debt (sum I to III)</b>	<b>36,398.6</b>	<b>39,866.0</b>	<b>44,383.4</b>	<b>49,192.3</b>
<b>C. Total Debt of the Government - FRDLA Definition<sup>3</sup></b>	<b>33,235.3</b>	<b>35,668.5</b>	<b>39,912.1</b>	<b>44,330.8</b>
<b>D. Total External Debt &amp; Liabilities (sum II to VI+IX)</b>	<b>19,005.0</b>	<b>19,237.8</b>	<b>23,676.0</b>	<b>26,608.5</b>
<b>E. Commodity Operation and PSEs Debt (sum VI to VIII)</b>	<b>3,173.5</b>	<b>3,405.4</b>	<b>3,625.2</b>	<b>4,202.8</b>
<b>As percent of GDP</b>				
Total Debt and Liabilities	93.8	85.7	-	89.2
Gross Public Debt	76.6	71.5	-	73.5
Total Debt of the Government - FRDLA Definition	69.9	63.9	-	66.2
Total External Debt & Liabilities	40.0	34.5	-	39.7
Commodity Operation and PSEs Debt	6.7	6.1	-	6.3
<b>Government Domestic Debt</b>	<b>49.0</b>	<b>47.1</b>	<b>-</b>	<b>46.4</b>
<b>Memorandum Items</b>				
	<b>FY20<sup>R</sup></b>	<b>FY21<sup>R</sup></b>	<b>FY22<sup>P</sup></b>	
GDP (current market price) <sup>4</sup>	47,540.4	55,795.5	66,949.9	
Government Deposits with the banking system <sup>5</sup>	3,163.3	4,197.5	4,471.4	4,861.5
SBP's on-lending to GOP against SDRs allocation <sup>6</sup>	-	-	474.9	474.9
US Dollar, last day average exchange rates	168.1662	157.3105	183.5146	204.3784

★ Annually revised data IIP 2020, data Dec 31, 2020, to Dec 31, 2021, by including the private sector loans provide through permissible offshore accounts.

<sup>11</sup>\* Figure 6 source-<https://www.sbp.org.pk/ecodata/Summary.pdf>

The EFF was established to assist countries experiencing severe imbalances due to structural constraints or slow growth and an already weak balance of payments position. The EFF supports comprehensive programs that include the necessary policies to correct structural imbalances over the long term.

#### ***Repayment Period-***

Extended agreements are typically approved for a period of three years, but can be approved for a period of up to four years to implement profound and lasting structural reforms. FEP withdrawals must be repaid within 4.5 to 10 years in 12 equal semiannual installments.

#### ***Structural adjustments***

A country in need of IMF's assistance commits to implementing the policy to solve the financial and structural issues. According to the EFF, these commitments, require particular circumstances. A strong focus is to uplift the weak economic position through macro management and structural reforms. The IMF's Executive Board regularly evaluates the policy execution and can alter the program to achieve the target of economic stability and growth.

### **2.2 Pakistan's current (2022) financial status and IMF's EFF 7th and 8th Reviews**

#### **Pakistan's economic outlook 2022**

##### **1. GDP Growth-**

For the second consecutive period in the fiscal Year 2022, Pakistan's economy reached a V-shaped recovery. Real GDP growth was recorded as 5.97% which is soaring as compared to the last year's growth that is, 5.74%.

##### **2. Current Account Deficit-**

The current account deficit in 10m22 is recorded as USD 13.8bn while last year it was USD 0.5bn. Due to high global commodity prices, upward pressure on import payments was noted.

##### **3. Remittances**

Remittances have always assisted to ease out the pressure of BOP (Balance of Payments) observed at USD 26.1bn in 10m22 thus, achieved a growth of 7.6%.

##### **4. Higher Inflation-**

Average CPI= 11m21(11.3%) whereas in last year, same time- Average inflation=8.8%<sup>12</sup>

##### **5. Fiscal Deficit-**

Pakistan's economy showed a fiscal deficit = of 6.3% relative to the Gross Domestic Product in FY22, whereas last year= 6.1%. During 9m22, the total tax was collected (collection increased)-28.1%, whereas non-tax revenues fell-14.3% 9m22. Therefore, the revenues collected by FBR (Federal Board of Revenue) outdid the revenue target by collecting net-tax revenue of PKR 4.86tn in 10m22.

##### **6. Downgrade in rating**

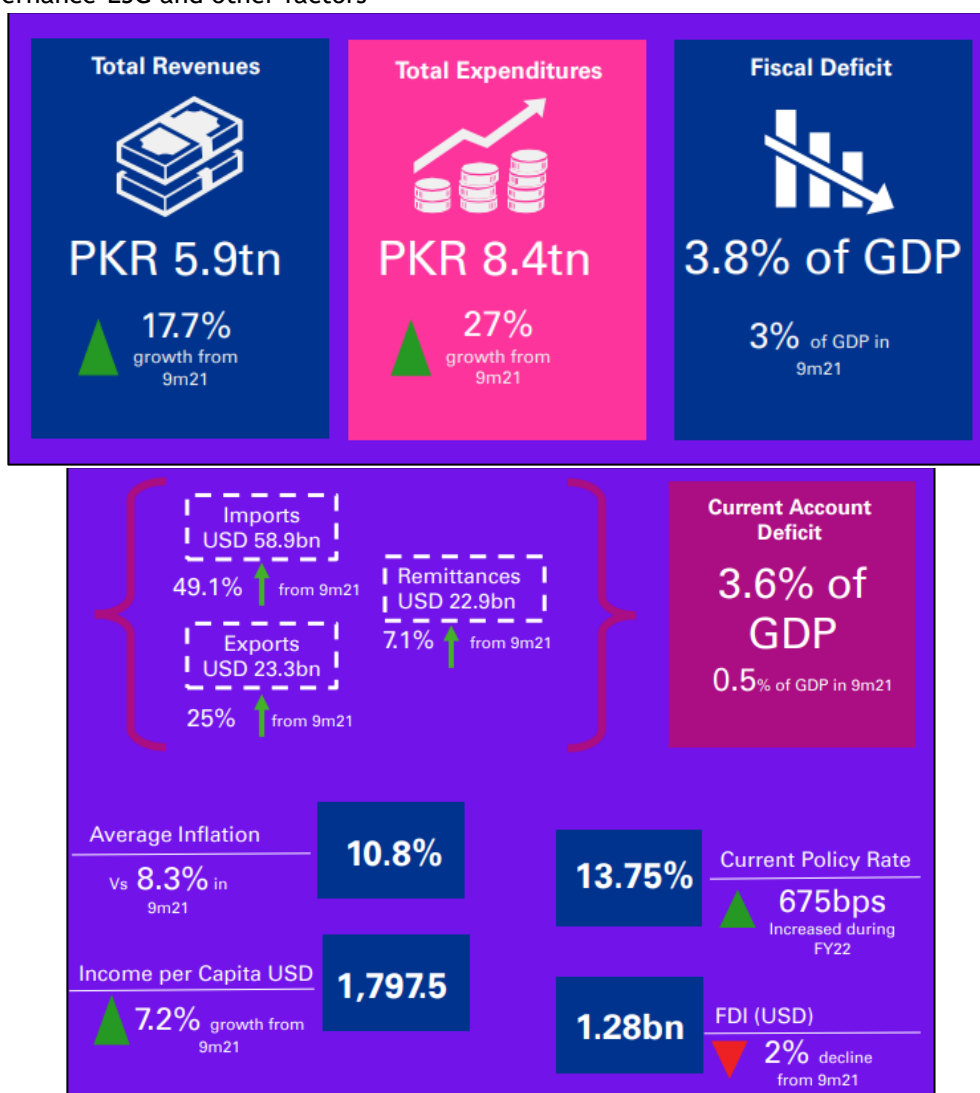
The current financial distress has affected Pakistan's credit rating outlook by Moody's, which is downgraded from stable to negative.

More alarming is that FITCH has also downgraded Pakistan's rank to CCC+. Indicating a downgrading in Long-Term Foreign Currency Issuer Default Rating (IDR) to CCC+ from B- Key drivers were

- Worsening liquidity- policy risks
- Reserves falling risk
- Foreign deficits
- Large funding needed
- New Fundings
- IMF Programme risks
- Political instability
- Financial worsening consolidation
- High Inflation

<sup>12</sup> <https://www.fitchratings.com/research/sovereigns/fitch-downgrades-pakistan-to-ccc-21-10-2022>

- Slowing process of growth
- Governance-ESG and other factors <sup>13</sup>

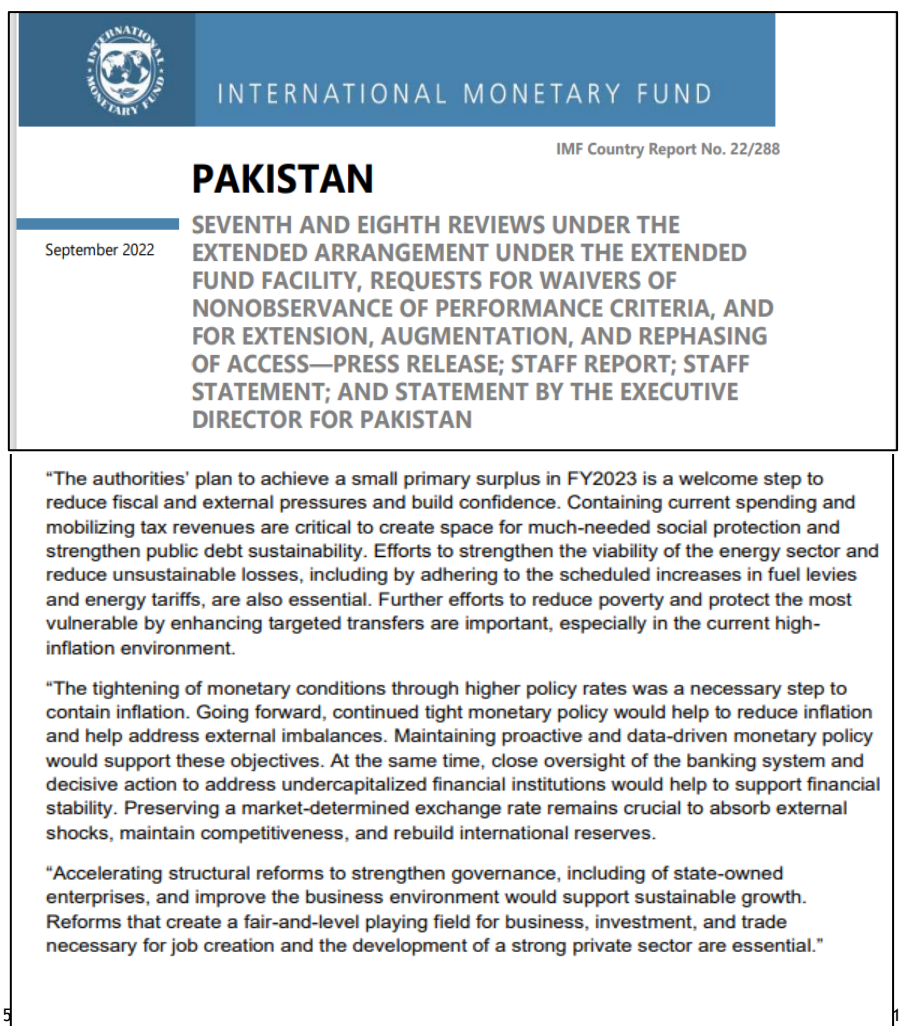


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Adverse external conditions have lashed Pakistan's economy, badly influenced by the Ukraine war. Domestically, several challenges and accommodative policies had given rise to unbalanced and uneven growth. To restore macroeconomic stability, it has become crucial to enact remedial policies and unrelenting reforms. Such efforts will solve the primary issues with imbalances, and will also provide a basis to achieve all-encompassing and sustainable growth.

<sup>13</sup> [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

<sup>14</sup> \*Figure 7&8 source-Pakistan Economic Brief 2022 (assets.kpmg)



<sup>16</sup> Source- IMF Country Report No. 22/288. September 2022

#### Response of the government of Pakistan:

Statement by Mr. Hosseini and Mr. Ahmed On behalf of Pakistani authorities,

*"We thank the mission team, led by Mr. Porter, for extensive consultations during the EFF 7th and 8th review discussions. The authorities appreciate the staff's policy advice and are keen to strengthen Pakistan's macroeconomic resilience and accelerate inclusive and sustainable growth. The authorities also express their gratitude to the Management and Executive Board for their continued support during these challenging times. They are also thankful to the country's bilateral and multilateral development partners for their support in facilitating the implementation of broad-based structural reforms."* <sup>17</sup>

#### ➤ Policy Dialogue:


As a result, the focus of the policy dialogue was on short-term measures to backpedal the policy slippages and to lessen the foreign and domestic imbalances. Medium-term measures are to be adopted to nurture long-term sustainable growth. To achieve the desired results broad-based action is required:

1. strengthen the fiscal area by revenue mobilization and management; Continued spending to reinforce debt sustainability by creating room for spheres of heed such as infrastructure and social issues;

<sup>16</sup>\*Figure 9- Source- IMF Country Report No. 22/288. September 2022, Figure 10. Source- 1PAKEA2022002.pdf

<sup>17</sup> \*IMF Country Report No. 22/288.



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2. contain inflation via relevant fiscal policy stance;
  3. support the market-regulated exchange rates as well as reconstruct the external shield
  4. restoration of economic feasibility of the energy sector;
  5. advancing structural reforms, resolving problem banks, and improving monetary policy transference.

➤ **Sharp spending Cuts**

FY23 budget consolidation by the government is established on exquisite spending cuts. June 29 (PA) budget approved which aims at an essential surplus of 0.4 percent of GDP, consolidating over 2% of GDP. Revenues collected by the FBR are much smaller than originally expected as the slowdown in the import-led revenue fallout is reflected in 19 different revenue indicators (several new taxes and accommodating subsisting taxes). PIT reforms will be implemented. The increase in PDL revenues (now reaching 50 PRs/liter, as opposed to 30 PRs/liter previously) was offset by a decrease in non-tax revenue (generated by lower SBP dividends), and spending cuts equivalent to 2 percent of GDP establish the huge support.

➤ **Fiscal reforms-**

Despite the testing milieu, fiscal reforms were continued by authorities. With the help of the World Bank, work is still in progress to coordinate the services sales tax throughout provincial administration. To improve public fiscal management, the officials aim to operationalize the single treasury account effectively by the end of December 2022, therefore created a Treasury and Cash Management Unit and a Cash Forecasting Unit have been created by the Ministry of Finance in the Federal Treasury Office in Islamabad. Cash prognosticating activity launched quarterly and monthly since January 2022 with the help of ADB. The national assembly has passed an amendment act called, 'amendments to the Fiscal Responsibility and Debt Limitations Act'. The main purpose is to enhance debt management, with the assistance of the World Bank and IMF TA, becoming law in June 2022. This will institutionalize the formation of a central Debt Management Office to devise the agreed-upon Medium-term Debt Management Strategy. With the support of the monetary adjustment plan, vigorous growth, and reforms, the national debt is expected to drop by 7% – 72.1% points of GDP by the end of FY23. Public debt is trending downward towards 60% of GDP by FY27, while foreign debt is projected to fall to<sup>18</sup> 25% of GDP.

**2.3 Qualitative Method- Open-ended Interview Questions:**

To gather an in-depth understanding of Pakistan's economy, and current fiscal crisis primary data was gathered via open-ended interview questions. Whereas secondary data was collected through books, online reports, articles, documents, and websites.

Interviews focus more on conceptual understanding and experiences as compared to numerical values. It also allows the interviewee to expand their views by giving references. It enhances the natural conversation and remains focused on the topic. Validity also increases as it allows the interviewer to explore more in-depth understanding, can ask for clarification, and also the interviewee can add further details. Interviews were conducted with retired and in-service bankers, experts having economic backgrounds, and academia.

**Data gathered through interviews:**

**A. Troubled areas of Pakistan's economy-**

The data gathered via interviews exhibits the sources of instability generally-

○ **Two major sources of financial setbacks:**

*Exogenous Shocks* (terms of trade shocks, natural disasters, capital flight)

Developing states possess a narrow export foundation. That is why when there is a price hike in commodities at the international level it also impacts the states' export payment. So, if the country's export foundation is manifold, then the shocks whether small scale or large, do not adversely affect the economy adversely or destabilize it.

*Self-Induced Shocks by poor macroeconomic management*

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<sup>18</sup>\*Dr. Romana Khan, (Associate Professor) IM Sciences Peshawar. October (2022), shared details during an interview with the reference of- [www.economicshelp.com](http://www.economicshelp.com).

Aggregate demand may increase with the exclusive loose financial policy  $\Rightarrow$  creating stress on the state's balance of payments, also inflation and exchange rate  $\Rightarrow$  increasing public debt  $\Rightarrow$  interest payments increase  $\Rightarrow$  eroding financial space  $\Rightarrow$  declining investment in health, education, and infrastructure.

**Financial stability-** Aggregate Demand improves when firms are willing to invest in a country. It happens when there is fiscal stability and banks are ready to lend. Pakistan faced both external and domestic (self-induced) blows- in 2008 and 2013, respectively. Pakistan is still pursuing the IMF stabilization policy since the 1980s till this day.<sup>19</sup> Pakistan's economy suffered due to a prolonged period of anti-growth or stabilization/austerity policy. Resultantly short to medium-term progress potential also could not grow due to the rise in socioeconomic challenges for Pakistan.

**Pakistan's economy is currently suffering in the following broad categories;**

- High inflation
- Declining investment
- Budget deficits
- Slow growth in overseas yield
- A month of foreign exchange reserves are left to cover the costs of imports

All these areas depict that Pakistan's governments were unable to address the structural problems effectively and that the lack of achieving inclusive development has disrupted social stability as well.

**The main troubled areas are**

- Balance of payment issue
- Lack of investment
- Falling Rupee against other foreign currencies

To solve the above-mentioned issues, it is crucial,

$\rightarrow$  *To make an expert team in the finance ministry composed of researchers, experienced administrators, and specialists in the economic field.*<sup>20</sup>

★ To improve competitiveness, stimulate entrepreneurial activities, and increase efficiency and technological advancements.

★ Improve saving rate, one of the reasons why Pakistan has relied on foreign capital. And when not available the investment graph goes down creating an adverse environment for fiscal growth and employment.

★ Tax culture has to be nurtured.

★ Public Awareness.

★ Corruption and all sorts of malpractices have to be discouraged.

★ Political stability and economic growth are interlinked, political chaos often ends up in economic instability as it affects the ongoing security and economic measures badly.<sup>21</sup>

○ **Significant steps by the government of Pakistan-Government Initiatives**

➤ *FY22, the State Bank of Pakistan established a regularity and licensing model for commencing digital banks in Pakistan- a distinct discrete and distinct section in the banking business.*

➤ *The predominant goals of the arrangement encompass*

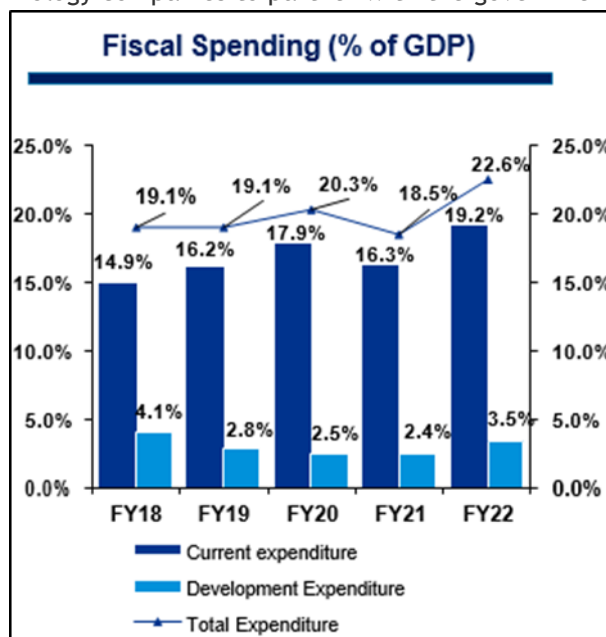
- ★ Fiscal inclusion
- ★ Issuing remunerative digital fiscal services,

<sup>19</sup> \*Interviews: from ex-Vice President of Hbl- Vice president of HBFC, CFA, ACCA accountant, CA accountant, Associate professor at IMS Peshawar, Ph.D. Economics Malaysia, Businessmen, Analysts on economic issues.

<sup>20</sup> Haider Khan, (October-2022). Regional Head North Mobil Power Solutions Pvt Limited. (Business man)

<sup>21</sup>\* Shehzad Ahmed, (October 2022) Senior Chief Manager. Credit Head KP.

- ★ Extending credit facilities to the underserved and unserved.
  - *FY22, Special Technology Zones Authority (STZA) is created by the Federal government*
  - *The fundamental purpose:*
- ★ Promoting surrealistic entrepreneurship and modern advanced solutions.
- ★ Generating awareness about the economy and technologically-run ecosystem.
- ★ Extending special Providing favorable impulse to attract builders, investors, technology enterprises, and technology companies to partner with the government.<sup>22</sup>



- ★ SBP also initiated Raast during FY22 for the first time in Pakistan for instant payment. This will assist in digital rapid, end-to-end payments among businesses, government organizations, institutions, financial setups, and individuals.
- ★ FY22, SBP started:
  - Banking Equality policy*- it aims to lessen the Gender Gap in economic zones via significant strategy, which would give women a cordial and trustworthy business environment.<sup>23</sup>
- ★ Helpful to reach the National Financial Inclusion Strategy (NFIS) goal - active women bank accounts (20mn) by 2023.
- ★ During interviews, for the steps initiated by the government a reference was established to the Economic Survey of Pakistan which shows the fiscal spending of years 2018-2022 concerning present spending and development.

#### B. Improvement of Structural hindrances to the economic growth of Pakistan-

The introduction of structural reforms is very crucial for Pakistan in the following areas-

- ↑ Trade, Imports, and Exports
- ↑ State-owned enterprises, and business climate to encourage higher investment.
- ↑ Restoration of financial stabilization by boosting the opportunities.
- ↑ Boosting the investors' confidence in Pakistan.
- ↑ Improvement of international competitiveness by diversifying the market via CPEC Projects.
- ↑ Accessing the markets of Central Asian Republics and African states.
- ↑ Improving relations with neighboring states to improve trade relations.

<sup>22</sup> \* Abdul Basit Ghani. Branch Manager, Bank Al Habib Islamic- KP.

<sup>23</sup> \*Figure 12. Source- Pakistan Economic Brief 2022 (assets.kpmg)



↑ This will also enlarge Pakistan's export share globally and regionally.

Some measures taken by the government have helped to contain new arrears, especially in the energy sector. The IF-backed circular debt supervision purpose is to enact the National Electric Power Regulatory Authority Act. Through these changes, the aim of restoring fiscal viability shall be managed along with cost cutting, tariff adjustments, and quality choosing of subsidies.

**Removing structural hindrances will reinforce confidence, investment in the private sector, and economic productivity.**

It will improve-

- ❖ transparency, efficiency, and governance of state-owned enterprises
- ❖ business environment and job opportunities
- ❖ accountability measures to control corrupt practices
- ❖ implementation of laws effectively (rigid actions are required)
- ❖ The completion of a much-advanced plan of action on AML/CFT which is essential

#### **C. Advantages of undertaking an IMF-backed program!**

*The main objective of the IMF is to enhance the revenue collection of the borrowing states.*

Unfortunately, in the case of Pakistan, the IMF has not been able to do much previously. The main issue lies with the IMF is that it needs to differentiate the primary causes of the debt required by the states. It comes with the same placard for all states. Therefore, it accelerates the economic issues and the general masses suffer eventually due to restrictions and suggested measures such as price hikes. It also adversely affects the business environment, especially in the sector of imports required in the country. Public response to such policies also poses questions about the credibility of the government. To prevent the country's economic structure from collapsing, the government was left with no choice but to take a loan from the IMF. currently. Pakistan's financial status and government's future economic condition of Pakistan and the future program of the g show that Pakistan is once again trapped by the debt. So much so, "Pakistan's debt and liabilities have risen steeply:"<sup>24</sup>

In the case of Pakistan, IMF-backed programs play a crucial role in economic decision-making. Currently, Pakistan is facing high international prices. Due to delayed policy actions fiscal and trade positions are getting worse. A few advantages are listed below

#### **Advantages:**

1. Providing loans (which has current benefits, but in the future, it may create hurdles of high taxation)
2. Covering fiscal and current account gaps (this is also for the short-run period, gaps can be filled with loans, but in the long term, we can face instability in the international trade market and domestic market as well)
3. Policy improvement (when Pakistan is in crisis, policy think tanks made poor decisions knowing that IMF aid will be serving us)<sup>25</sup>

#### **D. Pakistan's balance of payment difficulties-Improvement in the balance of payments-**

To meet the financial challenges and to monitor the balance of payments, the government had to restore to the IMF to get loans to stabilize its deteriorating economy.

- Promote exports and reduce imports<sup>26</sup>
- Import taxes and quotas
- By making the domestic industry more competitive
- Stable interest rate


#### **Section three-**

#### **Policy measures to be adopted-**

<sup>24</sup>\* Haider Khan, (October-2022). Regional Head North Mobil Power Solutions Pvt Limited. (Business man)

<sup>25</sup>\*Dr. Hanana Khan, Economist (October 2022). Ph.D. from -University Technology, Petronas Malaysia (UTP).

<sup>26</sup> Samina Ali Asghar, (October 2022). Teaching Research Associate, Department of Technology and Project Management. Faculty Management Sciences-IIUI

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- In Pakistan, fiscal efforts must be on the revenue side. (Tax evasion
  - High taxation makes the public more aggressive (avoid high taxes)
  - In Pakistan the utilization of resources must be efficient.
  - Expenditures should be spent on productive projects which can generate more income.
  - Fiscal consolidation is very important to avoid any financial crisis in the future.<sup>27</sup>
  - State-Owned Enterprises are devouring huge sums of budgetary capital, affecting public finances and economic growth negatively.
  - Misspend SOEs- due to inefficiencies, overstaffing, (often they are incompetent due to nepotism or bribery) corruption, the government needs to take stern action to ensure merit.
  - Regulatory system should be improved.
  - Institutional capacity needs to be improved.<sup>28</sup>
  - Business environment should be made friendlier by simplifying start-up procedures, internationalization of companies, educating entrepreneurs, reducing administrative burden, and introducing rewards of excellence for promoting entrepreneurship.<sup>29</sup>
  - We should increase our focus on improving our exports such as textiles, sports goods, surgical instruments, IT industry, also to encourage small and medium enterprises, policy adoption to support the digital trade among different countries be relaxed.
  - Monitoring of the quality of the exported goods.
  - On top of all of it, loyalty to the resources of Pakistan is a must.<sup>30</sup>

Urgent policy actions are needed to place Pakistan on a higher and inclusive growth path including-

#### Structurally-

- revenue mobilization
- strengthening the public sector
- restricting low-priority expenditure
- reinforcing the fiscal decentralization model
- improving energy area to get rid of a larger extent of power deficit
- lessen the involvement of government in the economy
- introduce fiscal policies to control inflation,
- secure the financial sector stability
- Remove deficiency in the market by reinforcing competition law
- Resource reallocation in a favorable direction
- adopt policies to remove biases against private, non-agriculture and non-textile-sectors
- bring political stability to the country
- structural changes can bring the economy on its footing to be less dependent on foreign aid to sustain growth. would make the economy less dependent on foreign assistance for sustaining growth.
- introduce more fiscal saving strategies<sup>31</sup>

**The private sector-** acts as an engine in the development of any economy. This sector needs attention. One of the reasons why this sector could not contribute much to the economic uplift. A functioning regulatory domain is needed. Providing physical and social infrastructures will also protect the underprivileged class of society.

In exchange for a loan from the CPEC opened the channels for growth and business ventures. The IMF loan is also anticipated to enable Pakistan to encourage its dollar reserve, to get dollars to pay its import bills and return maturing loans.

<sup>27</sup> \*Dr. Hanana Khan, Economist (October 2022). PhD Scholar-University Technology, Petronas Malaysia (UTP).

<sup>28</sup> \*Ikramullah Jan (October- 2022) Retired Assistant Vice President. Habib Bank Limited

<sup>29</sup> \*Qaiser Jamal (October-2022) CEO of AQURAS. (Lahore-based businessman)

<sup>30</sup>\* Dr. Samreen Fahim Babar (October-2022). Senior Associate Professor, managing studies Department. Bahria University Islamabad.

<sup>31</sup> \*Mohammad Atif Ikram, (October-2022). Head of SME and Private Banking, Saudi British Banks. A subsidiary of HSBC



### Concluding Remarks-

The EFF aims at protecting macroeconomic stability, smooth financial recovery, and support inclusive growth. Decisive actions taken by the authorities in Pakistan and commitments to achieve future targets, reinforce the 7th and 8th reviews under EFF. It is linked with waivers as well as extensions for rephrasing access. This will improve the balance of payment and fiscal growth. This will help ensure that the pressing balance of payments and fiscal financing needs are fully met. The authorities view Fund support as an important catalyst in mobilizing donor support.


The real challenge to Pakistan's economy is to bring an immediate robust economic plan by the experts of the economy in line with the IMF EFF program. Despite certain steps, Pakistan still needs to launch measures to upgrade its economic position from negative to positive shortly in the credit ratings of Moody's and Fitch. Focus is required in key areas such as ESG governance, improving CADs (Current account Deficits), to avoid further deteriorating external liquidity, and declining foreign exchange reserves (FX). A milestone of the expected forecast to achieve;

Amid policy tightening, tackling fiscal and external imbalances to slow to 3.5% in fiscal year (FY) 2023 (ending 30 June 2023). The FY2022 is also expected to reach 6.0%, according to the Asian Development Bank.<sup>32</sup>

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