Luck running out

On September 4, 2013, the Government of Pakistan signed its 19th Agreement with the International Monetary Fund (IMF).

In 2011, it appeared that Pakistan had bid adieu to the IMF for good, but 2013 has shown that the legacy of borrowing continues. This September Pakistan was given an approval for a US$ 6.68 billion loan under the international lending agency's Extended Fund Facility.

The very first promise by the IMF in 1958, of 25 million SDR, was never fulfilled; which makes this the 18th loan granted to Pakistan since then. The stated purpose of these loans is to bring economic development and self-sufficiency to the country. As in the case with many other countries that have signed similar agreements with the fund, this goal has remained elusive in Pakistan's previous 17 attempts. Moreover, out of these 17 agreements, 11 ended on a bitter note.

Each time Pakistan failed to comply with the IMF's prescribed agenda, the IMF refused to release the remaining tranches and ended the program. The amount that was suspended, during programmes signed in the 80s and 90s, was more than 40% of the agreed amount.

Nevertheless, despite the government's failure to meet targets, leading to abrupt suspension of programs, the fund never abandoned its unruly child. Instead, it granted more loans with more strings attached.

The last Standby Agreement signed in 2008 ended rather terribly and was a public relations disaster. Non- compliance with the policy resulted in a failure to claim the last two installments of US$ 3.7 billion. Not surprisingly, the new government set in another arrangement with the fund. However, the government's fiscal track record has warranted more stringent scrutiny this time. Unlike the last arrangement which dispensed 40% of the then agreed total package immediately, the current agreement's first installment is only 8% of the total amount, despite the intense requirement of foreign reserves by the GoP.

Perhaps, for a moment if we all become adherents of the neoliberal agenda of the IMF, reflected in the reforms, it becomes quite easy and tempting to attribute the ineffectiveness of the reforms in delivering the desired outcomes to a lack of implementation by the recipient government. Well, this is not the case. A main reason mentioned in one of IMF's own publications, is the over ambitious and unrealistic estimation of the outcomes. It's reported that the optimistic projections led to the overestimation of growth rate by 1.5pp on average in the program agendas from 1993-2000.

The most recent experiences suffer from similar problems. The Memorandum on Economic and Fiscal Policies 2013/14-2015/16 by GoP shows an estimation of 4.5 to 5% growth rate at the end of the program. The elusive nature of reforms mentioned in the documents does not justify this

optimism. For instance, the document claims that the program aims at boosting private investment, while the monetary reforms mentioned fail to augur this. The document states that during the first year, a moderate monetary policy is followed. State Bank of Pakistan (SBP) accumulates more reserves, the rupee weakens and as a consequence inflation rises. However, growing inflation will be brought to 6-7% level by following a tightened monetary policy in the second and third year, which means an increase in interest rate in these years.

The expectation of an increase in interest rates indicates higher future cost for existing and new businesses. Furthermore, owing to the inclination of our banking sector to choose government over private investor, it is likely that an increase in interest rate will result in scheduled banks buying more government bonds instead of lending to private investors. Above all, the biggest source of discouragement to the private investor is the possible negative rate of return due to soaring inflation. One cannot put much faith in State Bank of Pakistan's (SBP) recent decision of increasing interest rate by 0.5pc (which actually offsets the previous reduction of 0.5pc) as an effective policy measure to mitigate such a risk. The link between a tight monetary policy and stable exchange rate regime is weak .This change in interest rate remains ineffective in stabilizing the exchange rate and the rupee value continues to fall and inflation risk rises.

The Memorandum enlists structural reforms which promise to foster an environment conducive to growth of private investments. However structural reforms cannot deliver benefit in the short run. A simple example which illustrates this is the condition of all indebted governments of free market economies which are struggling to generate revenue from domestic sales tax regimes to offset the loss incurred due to reduction in tariff duties. It is not the easiest task to shift the tax burden to domestic activity from international trade.

Above all, given the IMF's tendency to renew/extend loans, it would be naïve to attribute the extension in the loan to the suitability of the proposed reforms by the GoP. The structural adjustment loans by IMF have a documented repetitive element, i.e. one country is given loans multiple times, one after another. An overview of the Fund's relationship with the other recipients gives a similar or even worse picture at times. None of the programmes, initiated by the Fund in Peru, Egypt, Mongolia and Guyana during the decades of 80s and 90s, disbursed the full amount of the loan.

Is not it disturbing that a country which not only failed to achieve the desired economic goals, the primary reason of granting the loan, but also failed or at times refused to carry out the agreed reforms, is given yet another loan? This multiplicity in lending makes one skeptical of the IMF's role as a facilitator of enhanced growth.

Pakistan's sanguine current government, which is showing its full faith in the current agreement, should not forget Pakistan's earlier encounters with the Fund. We should understand that neither the carrot nor the stick is going to bring any change. If we want to put the economy on a long-run growth trajectory we need to undertake reforms which we have the political will and institutional

capacity to implement. Such reforms should necessarily be related to the fiscal state of the economy and not manipulated by adhoc monetary policy or troubleshooting initiatives by the FBR. The current uproars to revisit the promised tax reforms are indicative of the fact that before pledging to overly optimistic agendas it is important to realize the state we are in. Perhaps, this may save Pakistan from yet another embarrassment.

Naheed Memon is the CEO of Manzil Pakistan, a public policy think tank in Karachi. She is also a Visiting Faculty at IBA and a Director of a private conglomerate. She holds a MSc in Economics from Birkbeck College, London and an MBA from Imperial College London.