PAKISTAN'S BALANCE OF PAYMENTS *
Historical Perspective, Current Situation and Future Evolution

Historical Perspective

A. 1994-98 (Table I)

- Exports were stagnant. Structural problems persisted.
- Import growth led to widening of trade deficit
- Debt Servicing burden was rising
- Current account deficit hovered around $ 3-3.5 billion or 4-5% of GDP.
- Financing was unsustainable as Foreign Current Accounts and FE 45 swaps with banks were used.

B. May 1998 aftermath

- An exogenous shock exposed the weakness of the balance of payments situation and the non-viability of the trade and financing.

Presentation made at the Oil and Gas Conference 2000 held at Islamabad on October 10,2000.

- Freezing of FCAs, Hub Power Dispute and Political uncertainty eroded the confidence in the economy.
- Extraordinary restrictive measures had to be put in place which included administrative controls on foreign exchange and introduction of multiple exchange rates.
- Debt rescheduling and new inflows from IMF, World Bank and Asian Development Bank in January, 1999
- Helped build up the reserve situation to comfortable levels by end June, 1999.
- A unified exchange rate was re-introduced in May, 1999.
- Underlying structural problems were not attacked during the breathing period to enable the country to exit from rescheduling.

C. Current Situation (Table II) (October 1999 Onwards)

- Foreign exchange regime was liberalised and all restrictions on foreign investment outflows removed.
- Stable exchange rate maintained until June, 2000 and the premium over open market rate was stable – 4 to 5%.

- Current account deficit has been reduced from 3.8% to 1.6%. Export growth recovered to 10% in 1999-2000 after a long time.
- As inflows from international financial institutions almost dried up, purchases from open market enabled the country to meet its payment obligations. $ 1.3 billion of debt relief under Paris Club was eroded by increase in oil prices.
- Since June 2000, rupee has been put on free float and there has been depreciation of almost 12% with greater volatility and fluctuations.
- In 1999-2000 cash payments of $ 3.6 billion were paid on external debt servicing in addition to rescheduling of debt (Table III).
- External Cash outflows exceeded inflows during 1999-2000 despite purchases from the market and exceptional financing putting pressure on foreign reserves. There was a draw down of almost $ 400 million from the reserves by end – June 2000 (Table IV).

- The present government has initiated a number of key structural reforms which had been postponed for a long time. Introduction of agriculture income tax, extension of GST on Retail Trade and Services, aligning prices of gas, petroleum products to international prices, documentation and survey to widen tax base will reduce fiscal deficit and hence further narrow the current account deficit and external borrowing requirements in future.
- Current account deficit is likely to narrow further in 2000-2001 as exports are projected to rise by 14% and imports by 8%.

- Exceptional financing requirements are expected to be reduced from 4 billion annually in 1998-99 and 1999-2000 to $ 2.2 billion in 2000-2001. Reserve target for end June 2001 is $ 1.7 billion.
- Workers' remittances are down by $ 400 million, and Foreign Investment by $ 500 million -–compared to the pre-1998 trends. If these flows are reinstated, oil prices decline, and export growth is further accelerated the gap between inflows and outflows will narrow and the need for further rescheduling will be reduced.

Future Evolution

- Efficient import substitution of furnace oil by domestically produced natural gas in thermal power generation and enhanced refinery capacity will lower the import bill for petroleum products and improve the current account deficit. Thus new investment in gas exploration, transmission pipeline and distribution systems will have a large pay off both to the macro-economy as well as the investors. The government has therefore identified oil and gas as one of the four priority sectors for economical revival strategy.
- Foreign Direct Investment is preferred to debt creating flows as it not only brings capital but also technology and managerial skills. Multinational Corporations help promote competition in the sector by their improved corporate governance standards and practices which have to be emulated by the domestic companies to stay afloat.
- Profits, Dividends and Remittances account for only a small fraction of our external payments. In 1999-2000 the total payments on this account were only $ 430 million compared to $ 3.6 billion account of external debt servicing obligations.
- If FDI flows to Pakistan are doubled and payments on account of dividends, profits etc., rise in the same proportion we will have no difficulty in servicing them.

Under this scenario, the FDI inflows will lead to a diminution in external borrowing and hence our debt servicing would consequently decline. The investors will get a remunerative return on their investment which they can remit abroad without much difficulty while the country is able to reduce its dependence on foreign loans and the conditionalities associated with them. In fact, foreign investors will remit only if they are able to generate positive earnings for the economy unlike the external creditors who have to be paid fixed charges irrespective of the fact whether their loan has created positive cash flow or not.

- Pakistan has suffered in the past due to perception of poor governance and reneging of contracts. This government has taken actions to introduce transparency, predictability, rule of law and accountability in the system. Even the worst critics of this government do recognise that the overall governance has improved although a lot of reforms are either underway or planned to strengthen judiciary, police, civil service and other institutions.
- In Oil and Gas Sector, the government has moved out of running commercial operations and decided to privatise all publicly owned assets in this sector. Foreign Investors have a great opportunity to own these assets, make them operationally and financially efficient and earn profits.

- Pakistan is open for foreign investors and as you can see the measures being taken by the government will further strengthen the balance of payments situation in the future. This should provide comfort to the potential investors about the security, return and transferability of their investment.

PAKISTAN : BALANCE OF PAYMENTS

TABLE 1 : HISTORICAL PRESPECTIVE

$ Billion

	1994-95	1995-96	1996-97	1997-98	1998-99
• Trade Balance	-2.5	-3.7	-3.1	-1.8	-1.8
• Services (net)	-2.3	-3.2	-3.6	-3.2	-2.5
O.W.Interest	(-0.9	-1.0	-0.9	-0.9	-1.0)
• Current Transfers (Net)	2.7	2.6	3.2	3.4	2.7
Workers Remittance	1.8	1.4	1.4	1.5	1.0
FCAs – Residents	0.4	0.7	1.3	1.5	0.5
Officials	0.3	0.2	0.3	0.2	0.2
• **Current Account Balance**	-2.1	-4.3	-3.5	-1.7	-1.6
• Long Term Capital (Net)	2.5	2.4	2.2	1.3	1.4
a) Official	0.7	0.7	0.7	0.6	1.1
b) Private	1.8	1.7	1.5	0.7	0.3
(FDI	1.5	1.3	1.0	0.8	0.3)
• Official Assistance (Medium ST Loans)	-0.1	4.3	-0.3	0.6	-1.4
• Foreign Currency Deposits Non Residents	0.3	1.0	0.2	-0.7	-2.3
• **Overall Balance**	0.2	-0.4	-1.0	-0.3	-3.3
Financing					
• Net International Reserves	-0.3	0.4	1.2	0.1	-1.2
• Use of Fund Credit	0.1	-	-0.2	0.2	0.4
• Exceptional Financing	0	0	0	0	4.1

PAKISTAN : BALANCE OF PAYMENTS

TABLE II : CURRENT SITUATION

(US$ Million)

	1999-2000	2000-2001 Projection
• Trade Balance	-1435	-1214
• Services (net)	-2766	-2987
O.W.Interest	-1715	-1787
• Current Transfers (Net)	3197	3195
Workers Remittance	983	
FCAs – Residents	322	
Officials	136	
Purchases	1634	
• **Current Account Balance**	-1004	-966
• **Capital Account Balance**	-2890	-84
• Long Term Capital (Net)	-212	-124
c) Official	-492	-231
d) Private	280	107
FDI	546	
• Official Assistance (Medium & ST Loans)	-426	223
• Foreign Currency Deposits Non Residents	-2381	-183
• **Overall Balance**	-3894	-1050
Financing		
• Net International Reserves	209	-977
• Use of Fund Credit	-289	-239
• Exceptional Financing	3965	2266

TABLE III

Pakistan's External Debt Servicing

(1999-2000)

(US$ Million)

		Actual Paid	Rescheduled	Total Accrual
A	**Interest Payments**	**1365**	**381**	**1746**
	1) LT Public	556	381	937
	2) ST Public	120	-	120
	3) Private	238	-	238
	4) SBP Deposits, FCBC, FC Bonds	402	-	402
	5) IMF Charges	49	-	49
B	**Principal Repayments**	**1965**	**3134**	**5098**
	1) LT Public	858	984	1842
	2) ST Public	191	152	343
	3) Private	623	-	623
	4) Euro Bonds	-	610	610
	5) FE-45 Deposits	246	1087	1333
	6) SBP Deposits	-	300	300
	7) NBP Deposits	-	500	500
	8) FCBC/FEBC	47	-	47
	9) IMF Repurchases	265	-	265
	GRAND TOTAL:	**3595**	**4015**	**7610**

TABLE IV

Pakistan's External Cash Flow Position

(1999-2000)

(US$ Million)

A	**Reserves at the begning of the year**		**1740**
B	**Inflows**		**20873**
	of which	Exports	8158
		Services	1505
		Remittances	983
		Purchases	1634
		Foreign Investment	546
		Exceptional Financing	4025
C	**Outflows**		**21255**
	of which	Imports	9731
		Services	4285
		(Interest Payments)	(1776)
		Amortization	3231
		Eurobonds	610
		Foreign Currency Deposits	2382
D	**Reserves at the end of the year**		**1358**