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Pakistan Economic Crisis: An Analysis

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The economy of the South Asian country has plunged into a grim state with enormously high inflation, depreciation of the currency value against the dollar combined with the shoot up of fuel prices. The sorry state of affairs in Pakistan brings back the recent memories of Sri Lankan instability of the last year. The deep economic crisis was not a sudden development and several events have built up which resulted in the recent growth of the economic crisis.

Background

Despite the support from the International Monetary Fund, Pakistan is struggling with what is termed the worst economic crisis since its formation in 1947. With multiple crises at hand, the country has been questioned about its continuous instability in the political sphere which contributed to the current economic crisis. The journey has been a process that evidently started in the last three years and naturally affected the lower-income groups the most. The inflation rate rose to 41% and the debt-to-GDP ratio was dangerously risky in the zone of 70% (Banerjee 2023). The forex reserves of the nation have dwindled to a point where the government has declared that it will last only three weeks before the country goes bankrupt.

The country has also witnessed continuous clashes with its neighbours, contributing to its decline in economic conditions. The impact of these clashes including the recent clash in the Durand line affects the production cycle which further fuels the economic depreciation. Thousands of people belonging to the lower strata of society have been in protests in recent times due to a shortage of food and an increase in fuel prices. The country has also experienced severe power outages which were one of the means that was initiated by the present government of Pakistan to save energy (Deuskar 2023).

Causes

The economic crisis of Pakistan was not built in a day and multiple factors over the years contributed to the position that it is in today. Following are some of the major causes discussed below:

Political Instability

Since its formation, the political condition of Pakistan has been unstable. The situation can be predicted from the point that no government has completed a full five-year term until now since its formation in 1947. The current government of Shahbaz Sharif lost their esteem and reliability within months of coming to power, the setback of which was further pushed by the last ruling government led by Imran Khan demanding an internal military enquiry and fresh elections. Moreover, the policies of the country have to be always supported and backed by the military which puts constant pressure on the ruling government of Pakistan. Additionally, the imbalance between the general Pakistani budget and the defence budget concerning the persistent border dispute with India has further contributed to the ongoing economic crisis of Pakistan (Khilji and Mahmood 1997).

Economic Liberalisation

After struggling with irregularities in external deficits and financial imbalances, Pakistan adopted the structural adjustment program under World Bank and reforms resulting in economic liberalisation in the year 1988. However, the implementation of the policies could not attain the goals and Pakistan was hit with an economic crisis at the end of 1988. The country was trapped in a vicious cycle of low returns, poverty, low investment, and low growth. To curtail this, Pakistan privatised the state-owned enterprises so that the role of the state can be reduced in economic activities (Khan n.d.). However, the country has faced economic constraints repeatedly over the years and the financial sector has continued to be frail with the export-import imbalance and no retrieval from bad loans. All these factors combined with the country's constant struggle with economic instability and no chance to recover have contributed to the current economic crisis.

External debt from China and other countries

Pakistan is struggling with a huge external debt of around $100 billion from different countries, the highest of which is from China and Saudi Arabia. With the huge gap in the current account deficit after Pakistan has been trying to attract several countries for additional loans, the debt pile has just increased over time. Pakistan has failed to repay the loans from time to time because of which countries like Saudi Arabia has refused to provide any loan further. China has been accused of using "Debt-Trap Diplomacy" against several developing countries which includes Pakistan (Shaikh and Kai Chen 2021). The "China-Pakistan Economic Corridor" (CPEC) project that connects Kashgar province of China to the Pakistani port of Gwadar has raised major concerns about the debt trap and has forecasted the economic loom long back among experts but the project is still positively supported by many actors in the domestic front. All these factors have contributed to economic dependency of Pakistan on the international community and have resulted in the ongoing economic crisis.

Natural Calamities

Fourthly, natural calamities have also played a major role in causing the recent economic crisis. Pakistan has suffered the wrath of rain Gods in the form of floods that have resulted in the loss of 1730 lives and affected around 33 million people out of which 8 million people got displaced. The expenditure required for reconstruction and rehabilitation as a result of the flood has intensified the already difficulties of the economy (Altaf 2022).

Current Crisis

A gap in the Balance of Trade

Pakistan has always experienced a deficit in its export and a surplus in its import. This naturally has created a negative balance in the trade which means that exports are not getting enough currency to pay for the imports. The enormous piling up of the deficit over the years has created a burden on the Pakistani economy. Moreover, internal clashes, as well as instability, have further widened the trade gap which is compounded by high unemployment and unskilled youth. The imbalance in trade has gathered every month until it reached its present position (Baloch n.d., 151).

Devaluation of Currency

As the alarm bells started ringing for the Pakistani economy, the government sought refuge from the international community once again. However, due to multiple refusals from several fronts, Pakistan had no other option other than the International Monetary Fund (IMF) for external sourcing of money. One of the major conditions from the IMF was to remove the cap resulting in the artificial distortion in the economy. The removal of the cap resulted in the devaluation of the currency to a very low point of 275.58 PKR per dollar (Shahid and Shahzad 2023). The Pakistan Stock Exchange however is positive that the devaluation of currency will lead to the road to recovery.

Strict Conditions by IMF

The IMF had agreed to help out Pakistan with the crisis by adding $1 billion to the 2019 bailout of $6.5 billion but with multiple conditions. These include devaluation of the currency, hike in electricity and fuel prices, imposition of taxes on luxury goods and richer sections of the society apart from other restrictions on the government personnel. Although the conditions have been described by Prime Minister Sharif as “beyond imagination”, Pakistan has to bow down with no other options open against bankruptcy. In a recent development, China has approved $700 million for Pakistan, which will help the country come out of its cash crunch (Jain 2023).

Implications for India

As a neighbouring country, India would naturally have certain consequences. Two kinds of speculations can be observed among the experts regarding the implications for India of the economic crisis of Pakistan. One observation is that while Pakistan’s crisis would affect India’s exports to a certain extent, India should look at this as an opportunity to consider formal talks with Pakistan regarding every issue between them. India has helped other neighbouring countries before and sees this as an opportunity (Deccan Herald 2023). On the other hand, another observation is in contrast to this which observes that Pakistan’s downfall would negatively affect India as it would invite the further influence of China in the region. However, the trouble in the

Pakistani economy does not directly suggest an alliance that would be against India (Dhyeyaias 2023).

Is there any Remedy?

Although it would take time for Pakistan to bounce back, some steps can be taken in this regard. Firstly, Pakistan should focus on building industries on the domestic front which would help in reducing the dependency on exports. Secondly, the focus must be put on widening the taxes of the higher-income individuals of the nation (Nazar 2022). Thirdly, steps can be taken for initiating a privatisation programme that would invite external investments to the country and lastly, the huge chunk of the Pakistani budget that is dedicated to the defence sector should be reduced to half of its present level.

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