Pakistan braces for a 'tough' budget

by Ramtanu Maitra

A great deal of attention is now focused in Pakistan on Prime Minister Benazir Bhutto's first budget, for fiscal year 1989-90, to be unveiled before the National Assembly on June 1. Warning that the budget will be a "tough" one, the prime minister acknowledged that under the prevailing circumstances, Pakistan has no other choice but to bite the bullet.

When she assumed power last December, Bhutto was quite blunt about the fact that she had inherited a sick economy. She found Pakistan's Treasury empty, and the previous regime, after making its due contribution to bankrupting the economy, had already signed on the dotted line with the International Monetary Fund (IMF), handing the country's economic management to the Washington-based technocrats.

Looking at the fiscal part of Pakistan's economy, it is evident that foreign debt is on the rise and will continue to be so for the foreseeable future. Pakistan has a foreign debt of about $15 billion now, compared to $3.86 billion in June 1973, and debt service in 1987 was $1.23 billion. Internal debt, because of years of budget deficits, an inability to mobilize resources from investments, and high-cost domestic non-bank borrowing, has reached the point that 20% of current expenditure is siphoned off as interest payment.

The Pakistani rupee has been devalued severely during the last seven years. In 1982, 100 Pakistani rupees could buy $10, but it can fetch no more than half that amount now. A cheaper rupee had promised large exports. But has anything like that happened? No. More than 70% of Pakistan's exports are cotton and cotton-related merchandise, and thus immune to whether or not the rupee is cheap. Cheapening the rupee has resulted only in the increase of the cost of imports.

Looking at the physical side of the economy, the picture is even bleaker. The new aid committed to Pakistan by the Paris Club of $3.1 billion, which translates into Rs. 62 billion—more than Pakistan's entire Annual Development Plan (ADP) for the year 1988-89, which was Rs. 57.84 billion. But most of that aid will remain unused because of the lack of matching funds. In fact, Pakistan has consistently failed to utilize project-directed aid money, which calls for a matching amount in rupees. Right now, leaving aside this year's aid, about $4.8 billion (Rs. 96 billion) is sitting in the pipeline unutilized, and the government has to pay about $25 million annually as interest to keep it there. That $4.8 billion is about 50% of Pakistan's annual budget and almost twice the ADP. The inability to mobilize resources from within the economy is an indicator of Pakistan's real problems—an inherently weak physical economy, which shows the real problems Ms. Bhutto faces.

A weak physical economy

It is estimated that 35-45% of the population lives below the poverty line, which means they consume nothing more than the minimum calories of food. About 40% of Pakistan's population has no purchasing power; they come to market only to buy perishable consumer items such as vegetables, fruit, and milk. Unemployment runs as high as 15%.

Pakistan started off as a food-surplus nation, but it is now importing wheat regularly. Agriculture, because of a simultaneous lack of water and waterlogging of land, and rampant feudalism, remains highly unproductive, while absorbing more than 50% of the workforce. This year Pakistan faced a shortfall of 3 million tons of wheat, and Ms. Bhutto has arranged so far to procure 1.8 million tons abroad, at a net cost of $335 million.

At the time of independence in 1947, less than 30 million Pakistanis were illiterate. Today, 42 years later, 75 million out of 105 million Pakistanis cannot read or write. According to some, the number of illiterates is actually closer to 90 million. Pakistan can provide enrollment in primary educational institutions to only 61% of boys and 32% of girls. The figure drops sharply at the secondary level. Existing schoolhouses can accommodate only 24% of the boys and 9% of the girls. At the post-high school level, Pakistan's colleges can enroll only 5% of the applicants. While developing nations such as Thailand, South Korea, and the Philippines spend more than 15% of their revenue on education, and the People's Republic of China and India spend close to 10%, Pakistan's last 35 years' average was close to 3.5%.

The situation is similar in the public health sector. In 1986, federal expenditure on public health, in a nation where almost half the population does not have money to buy any medicine, was only 1% of the total government expenditure. This means that on an average, Pakistan spends $1 per person per year for the public health facilities. This neglect of public health shows up where it hurts most:
69 infants out of 1,000 below one year of age die on average in developing nations, in Pakistan 111 infants die. Due to lack of medical facilities, 600 out of 100,000 mothers, on average, died at childbirth in 1980 in the developing nations; in Pakistan the average was almost 1,200.

The lack of concern of the powers-that-be to provide safe drinking water and adequate sanitation is also glaring. It is estimated that in Pakistan, 70% of the population does not have access to safe drinking water. As a result, 30% of all reported cases of illness and 40% of all deaths are attributed to water-borne diseases.

Housing conditions are equally revolting. About 52% of the houses consist of one room only, and are occupied on average by six people. Fewer than 30% of the houses have electricity; the bulk of those with electricity are in major cities like Karachi, Lahore, Islamabad, and Hyderabad. It is likely that four out of every five houses in rural Pakistan have no electricity. Sanitation is available to a limited degree in the cities and major towns. Two-thirds of the houses in Pakistan are built of unbaked mud, and are without electricity, piped water, a bathroom, or even a room in which to cook.

The 'People's Program'

It is not that Prime Minister Bhutto is unaware of these facts and figures. On the contrary, in a recent interview with the Islamabad-based English daily *The Muslim,* Ms. Bhutto showed her exasperation when she said, "We have such a large number of talented people. We have no physical infrastructure."

The prime minister's awareness of these realities helped motivate the government's recently launched "People's Program." The program caused an uproar among the opposition, and was promptly consigned to the wilderness by the vested interest politicians in two of the four provinces, Baluchistan and Punjab, on the complaint that it is designed to secure the ruling Pakistan People's Party (PPP) a greater "vote bank" through payment of "largess" to the poor. But, as Minister for Local Government Syed Faisal Seleh Hayat said recently in a speech, the People's Program is aimed at "creating infrastructure in the society necessary to prepare the nation for stepping into the 21st century with confidence and courage."

There is no reason to second-guess the government's motives in launching the People's Program. In truth, however, it is not clear what a mere $100 million—the People's Program budget—can really accomplish. It seems almost absurb even to suggest that $100 million, which would shrink significantly by the time it reaches the poor, could make a dent in Pakistan's poverty or the infrastructure backlog.

Yet it is imperative for Ms. Bhutto and her colleagues to work out a comprehensive plan which *will* provide adequate electricity, safe drinking water, minimally livable housing, and a tolerant transport and communication system, and mobilize the population to achieve such a program using internal resources. No task before the prime minister is more important. But to do this will require fighting and winning some battles. The most immediate is with the IMF and the bankers who are circling overhead like vultures, ready to swoop down and devour what is left. The current IMF diktat directs the coming budget to reduce the budgetary deficit. The Fund wants the deficit, which is now 8.6% of Gross Domestic Product, to be reduced to about 6.5% of GDP. In monetary terms, it means slashing about $350 million from a $10 billion budget, already geared to do nothing more than maintain the status quo.

Few choices

Given the constraints under which she is forced to operate—including Pakistan's formidable defense requirements and the economic burden of nearly 4 million Afghani refugees—Ms. Bhutto is left with very little choice. She will have to either cut the expenditure or impose fresh taxes to enhance revenues, or both. However, it is quite certain that she will have to follow the three-year fiscal plan given by the IMF—which is fully backed by the U.S. government—under the agreement to advance $813 million in aid money.

On the expenditure side, as Maleeha Lodhi, editor of *The Muslim,* pointed out in a recent column, "two-thirds of all current spending goes into defense and debt-servicing. The latter, the government can do little or nothing about. On defense, the largest single item in the budget, the government's room to maneuver is obviously limited by the political and security conditions." This has also been echoed by the prime minister herself in a recent speech, when she vowed to strengthen the country's defense.

This leaves Ms. Bhutto between the Scylla and Charybdis of cutting food subsidies or slashing the development plans. Cutting food subsidies may have dangerous fall-out. Recent incidents in Venezuela and Jordan should be eye-openers to those who are pushing that particular IMF recipe. In the case of Jordan, King Hussein replaced Prime Minister Rifai as a token of punishment for the food riots. It is not inconceivable that Ms. Bhutto could face a similar "punishment" at the hands of President Ghulam Ishaq Khan, in the event she orders a cut in food subsidies.

Given the nature of the choices, and her own political acumen, Prime Minister Bhutto will most likely keep the development plan as it is, and instead agree to widen the sales tax net, a measure that the World Bank-IMF has also been pushing. Officials are considering imposition of sales taxes between 6-7% on an aditional 150-odd items, a move which may yield about $50 million. Additional tax reforms may fetch about $200 million more from income taxes.

The IMF has also suggested trade liberalization, whereby restricted items will be allowed to be
customs duty to generate revenue in the process.

In any event, the government will have to take some painful measures which could be politically risky and, in all likelihood, will do little to improve the basic structure of Pakistan's economy. Unless the prime minister treads warily, the IMF-directed austerity budget may prove to be a perfect political weapon in the hands of those politicians who have made no secret of their desire to oust Ms. Bhutto on any available pretext as soon as possible.