South Asian Nuclear Power in a debt trap

It sounds ludicrous that Pakistan, a South Asian nuclear power, is caught in a debt trap and is beating every nerve to be bailed out. Amusingly, the debt trap is laid out by none other than the home managers and allegedly also by a country which it proudly calls it *"all-weather friend"*. It is not the first time that Pakistan is faced with a financial crunch. It has braved many such critical situations in the past and found a temporary solution of borrowing loans to pay loan instalments. However, the situation today is that economic growth has slowed down and sharply increasing fiscal imbalance is hindering the government to fulfil its developmental commitments to a burgeoning population.

According to a recent Bloomberg study, the Pakistani rupee has been on the downslide since June 2017, losing more than 3.7% value by the end of 2017. In December, the value of the Pakistani rupee against the US dollar was 105 but downslide did not halt there, reaching 119.84 in June 2018. As of the third week of November 2018, the US dollar is valued at 132.81 Pakistani rupees. Foreign debt has reached nearly $95 billion. Debt servicing costs are crippling and foreign exchange reserves are at almost the lowest level in the financial history of the country while exports have dropped, and so has the quantum of foreign remittances. Devaluation of the Pakistani rupee is the most dismal picture.

Why is Pakistan faced with economic crisis intermittently? Is it because of fiscal expertise deficit in the country? Is it because of not prioritizing production and export? Is it the wide-scale loot of public exchequer by the invisible but privileged actors in and outside the government, or is it because of what is axiomatically called *"a State within a State"*, which is consuming the largest chunk of the country's annual budget.

Commentators come out with numerous theories, practical and theoretical, but strangely they avoid unravelling Pakistan's political-religious-military conundrum. Very few analysts are willing to dispassionately debate the financial impact of the Pakistani Army intermittently throwing out elected governments and jumping into the seat of power under the oft-repeated pretext of setting right the derailed administrative machinery owing to large scale corruption by people holding public office. At the end of the day when military rule is withdrawn and power is restored to the civil society, we find more corruption and more irregularities committed during the martial law regimes. It is a different matter that the media cannot summon courage to spill the beans.

However, notwithstanding a political angle to the debate, let us come to the brass-tacks while examining the technicalities of the economic and financial crisis. It has to be remembered that developing countries have been taking loans from various international lending agencies and Pakistan is not an exception. The problem with which Pakistan has got stuck up now is of debt servicing, which has been accentuated by inflation and sharp decline in the value of the rupee against the dollar.

China

Writing in the *Economic Leader* of 4 August 2018, Gareth Heather argues that at the background to mounting and seriously increasing economic crisis, is the ambitious and big infrastructure raising programme with Chinese collaboration. Sandwiched between the world's two giant financial powers, Pakistan has borrowed heavily from China and also from the Western world. It has taken out billions in Chinese loans and run up a huge Chinese-funded master plan to revamp its ports, roads, bridges and railways. A $62 billion plan called the China Pakistan Economic Corridor (CPEC), running through the disputed region of Gilgit Baltistan (part of Jammu & Kashmir), has been celebrated by both countries as a long term investment that will increase trade, whereas in essence Beijing considers these projects as ways to demonstrate its power besides securing allies.

Certainly, the Pakistani economy needs to grow beyond rice and textile, which means building new infrastructures, but the question is that in pursuing ambitious projects, China is pushing Pakistan's deficits to unsustainable levels. Debts are rising rapidly while the country's hard currency is running out to pay its bills and as a consequence, Pakistan is left with no choice but to beg for monetary fund for a multi-billion dollar bailout which would be one of more than a dozen that Pakistan has received since the 1980s. China is seeking new markets for its construction companies and new pathways to ship its goods and that is why it is financing ambitious infrastructure projects across Central and South Asia. Obviously, China views it as a way to project its power and secure allies.

China claims that its loans do not have the same strings attached as the loans from various international lending agencies, which is not wholly true, and Pakistan is an example. Much of the profit from new power plants and roads goes straight back to Chinese companies. Another glaring example in this context is that of Sri Lanka; When that country could not pay back the money it had borrowed from China, it handed over Hambantota seaport to China. Sien Fenner, the Lead Asia economist for Oxford Economics, a global research firm, made the cryptic remark that *"Pakistan is clearly falling to the Chinese side"*.

The CPEC is based on a $46 billion loan (now $62 billion) that Pakistan has taken from China under *Sovereign Guarantee*. From the original allocation, the $11 billion amount for infrastructure purposes is a Chinese loan whereas the $35 billion is an investment for the power sector. Infrastructure investment offered by China for CPEC is to be paid back as equity which is guaranteed at either 17% or 20%.

A close examination reveals the actual malpractice in CPEC projects. A substantial portion of the Chinese investments is focused on power projects and the viability of these projects is based on interest rates charged by the China Development Bank and the China EXIM Bank.

Loaners

In comparison, global funding sources fundamentally focus on stabilizing the distressed economies and help countries avoid unsustainable financial imbalances; Loans are sanctioned with strict conditions to increase the chances that the country will clean up its finances and be able to pay back its loans.

Soon after Imran Khan took the reins of the new government in his hands, he was informed of the critical financial situation into which the country had landed. The rhetoric of bringing accusations to the preceding regime resounded furiously for some days but recalling the tall promises made by the Pakistan Tehreek-i-Insaf (PTI) under the leadership of Imran Khan, the new government had no choice but to consider possible sources of raising loans running into billions. Three sources were identified: (a) International Monetary Fund (IMF), (b) friendly countries, and (c) Pakistani diaspora.

An appeal to the people and government functionaries to observe austerity in national interest or imploring Pakistani diaspora to accentuate foreign remittances can only have marginal response. The reason is the trust deficit, which Pakistani Governments have generated among the diaspora and also in a large section of citizenry at home. We may call it a gift of widespread corruption in the administrative structure as well as in the defence sector. Since in Pakistan, power rests with the triumvirate of feudal lords, entrenched bureaucrats and generals, it is very difficult for any government, to call the powerful to book. Even parliamentarians seldom muster courage to table any motion aimed at probing the accumulation of enormous wealth by anyone of the triumvirate. Imran Khan did not touch on the subject of enormous monies stashed by the Pakistani elite and highly affluent segment of society in foreign banks, especially in the United Kingdom and Switzerland.

Saudi Arabia

Saudi Arabia is a close friend and benefactor of Pakistan. Imran Khan made two jaunts to Riyadh breaking his commitment made during his election campaigns, that for six months after taking into his hands the reins of the Government, he would not go on any foreign trip as a symbol of the new government's austerity measures. However, Imran Khan's first visit to Riyadh did not bring any tangible result as the Saudis made no commitment whatsoever.

Notably, more than ever before, the Saudi monarchy was careful not to antagonize the United States (US) at a point of time when it was faced with simmering discontent among a large section of its own people. Imran Khan's second visit to Riyadh took place when Riyadh was in deep anguish about the murder of Khashoggi, the columnist of *Washington Post*. Trump administration had mounted pressure on Saudi Arabia to identify the culprits and bring them to book after Egypt held King Salman of Saudi Arabia responsible for the murder.

Eventually, Saudi Arabia agreed to sanction a loan of $6 billion to Pakistan to bridge over the difficult financial position. One has to take into account that no donor country gives loans without strings attached to it and although, we are not aware of the conditions of the deal between Pakistan and Saudi Arabia on a loan of $6 billion, it has trickled down from Pakistani sources that King Salman has asked Imran Khan to set his house in order and also to mediate in the dispute between the Saudi and the Houthi of Yemen. On his so-called triumphant return to Islamabad, Imran Khan announced that Pakistan would work for hammering out a deal to bring an end to the Gulf war.

There are two clear reasons why Pakistan agreed to make a mediation effort, though a similar effort made earlier had ended in a fiasco. Firstly, Pakistan wants to get money immediately to restore the financial well-being of the country. Secondly, Pakistan had declined to join the Gulf Islamic Force that would have launched an attack on Yemen even when Pakistan permitted the services of its retired Army Chief, Raheel Sharif, to be utilised to lead this force. This initial decline of Pakistan to join forces had soured its relations with Saudi Arabia, but it seems that Pakistan has decided to restore traditional relations with the Saudi ruling house by agreeing to undertake the mediation mission despite knowing that the differences between the Saudis and Yemenis are so deep as to leave no scope for an amicable solution.

The US and IMF

Ever since the creation of Pakistan, the US took it under its wings considering Pakistan a bulwark against the southward expansion of the communist ideology. The contours of this relationship began to show a change after the rise of the Taliban in Afghanistan and Pakistan's clandestine support to the Taliban. Since the US is directly involved in NATO+US engagement against the Taliban in Afghanistan, Washington and other capitals have evidence showing that Pakistan is providing safe havens to the Taliban leadership, especially the Haqqani network, on its soil and indirectly supporting their fight against the US in Afghanistan. The US demanded that Pakistan stops providing safe haven to the Taliban, the failure of which could lead to US undertaking punitive measures. Instead of obliging the old ally and playing a responsible role, Islamabad took recourse to its *"denial"* policy to the deep displeasure of President Trump. The result is the cancellation of $300 million aid to Pakistan to meet the expenses for fighting the Taliban and their terrorist activities in Pakistan. Pakistan stubbornly opposed the American move and when Pakistan began approaching the IMF for the sanction of about $11 billion, Washington stepped in and warned the IMF not to sanction the loan in favour of Pakistan. As the US is the largest donor of the IMF, it naturally has a say.

Pakistan's frantic attempt to motivate IMF and prepare its mindset for considering its request continues to be a burning issue. The IMF chief has now hinted that Pakistan needs to put its house in order before approaching the IMF. Washington's argument is that Pakistan will divert the loan money to pay the interest instalments to China which has stakes in Pakistan.

Conclusion

It needs to be noted that even China, too, told Pakistan to put its house in order and Pakistani financial authorities have conceded that there remains much to be done to provide crutches to its economy. Pakistan has nearly (in 2017) $72 billion debt all together. Even currently, Pakistan has raised loans at 8.75% interest rate from the IMF by mortgaging Motor Ways, Air Ports, and Radio & TV stations. To pay interest, Pakistan is taking other loans to cover it and will reach alarming levels of bankruptcy. In Pakistan only 1% of the population is registered in the Tax System, and the Government collects just 9% of country's wealth in taxes, which is the lowest in the world. This is one of the major causes of the Pakistani Government being depended on loans.

It may be said that low tax realization, endemic corruption and tax evasion, slide down of industrial growth owing to expensive energy resources, feeding the white elephant called the Pakistani Army and spending around $9 billion a year for purchase of arms with India-centric defence policy and patronizing terror - the Frankenstein of its own creation, all put together have dragged Pakistan to the brink of bankruptcy.

To crown all this, the CPEC, which has been trumpeted as the game changer, is actually proving a canker eating into the vitals of the country. Experts say that even if the IMF sanctions a loan of $5-$6 billion, it is not going to cure the ills of Pakistan as it needs anything to the tune of $20 billion to overcome the crisis.

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