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ABSTRACT

Pakistan has been one of the countries worst affected by COVID-19, with the economic disruption caused by the pandemic exacerbating an already existing crisis. This paper discusses how the public health crisis has affected some of the most critical sectors of the Pakistani economy. While the government has implemented some mitigation measures, they are inadequate to counter the impact of the pandemic. The paper analyses the likely fallout of a near-meltdown of Pakistan's economy on the nation's hybrid political system that is dominated by the military. Finally, it examines the possible impact of Pakistan's economic crisis on its strategic environment and strategic alignments, especially its relations with India.

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I. INTRODUCTION

Before the COVID-19 outbreak, Pakistan's economy was struggling to stay afloat but was in no imminent danger of collapse.[1] However, the pandemic has severely impacted the nation's economy and virtually pushed it to the brink of bankruptcy. While almost all nations have been substantially affected by the global health emergency, Pakistan's economy does not have the capacity to absorb the massive disruption caused by the pandemic.

Months before the pandemic, in July 2019, Pakistan was forced to seek an Extended Fund Facility (EFF) programme with the International Monetary Fund (IMF) due to its twin deficit problem, i.e. fiscal and current account. With aggressive curbs on imports and massive devaluation, the country managed to reduce the current account deficit (CAD) by over 70 percent in the first seven months of Financial Year (FY) 2019-20. However, this came at the expense of economic growth, which fell from 5.6 percent in 2018 to 3.3 percent in 2019. In 2020, it was being projected to fall further to 2.4 percent, without accounting for the pandemic. Meanwhile, the fiscal deficit problem continued unchecked—partly because the revenue collections fell drastically short of the targets and because the government slashed developmental expenditure to demonstrate a positive primary balance, which was one of the conditionalities of the IMF programme.

Amidst the ongoing COVID-19 pandemic, both these deficits are likely to re-emerge, with a drastic decline in exports and foreign remittances. Pressure will also mount on the expenditure front. In 2019, Pakistan's military had voluntarily foregone any increase in the defence budget. Now, it is likely to demand a substantial increase. Further, the government will be forced to reverse the trend of cutting expenditure on health, education and other social service sectors.

These issues are compounded by Pakistan's growing public debt, the servicing of which constitutes a substantial part of the government expenditure.

The pandemic has forced most countries to break with the past and initiate deep reforms, not only in the economy but also in politics and foreign and security policy. However, being a national security state, Pakistan continues to adhere to its existing model, since changing its foreign and security policy will require upending the power dynamics between the dominant military and the civilian political establishment. Consequently, Pakistan is treating COVID-19 as an opportunity to obtain concessions, bailouts and debt relief,[2] to avoid undertaking the reforms it had accepted as part of the 2019 IMF bailout.[3] The country is also seeking bailouts from China and Saudi Arabia. While helpful, these measures cannot replace the underlying need for deep structural reform in Pakistan.

II. PAKISTAN'S ECONOMY BEFORE COVID-19

On 2 January 2020, PM Imran Khan claimed that the government had stabilised the economy, declaring this to be the year of growth, development and wealth creation.[4] A week later, the finance ministry issued a press release asserting that the economy was moving "progressively along the adjustment path and stabilization process and economic recovery is expected towards the end of FY2020." The statement noted several achievements in the first five months of FY 2020: the CAD dropped by nearly 73 percent; the fiscal deficit was at 1.6 percent of GDP; the "primary balance" was positive, at 0.3 percent of the GDP; the credit rating had improved from negative to stable; and the country's rank on the Ease of Doing Business Index had improved from 136 to 108.[5]

Foreign banks and ratings agencies, too, have endorsed Pakistan's management of the economy. In December 2019, Moody's upgraded Pakistan's credit outlook from negative to stable,[6] and Citibank's top management in Pakistan commended the Khan government's economic policies.[7] As late as the last week of February 2020, Credit Suisse released a report titled "Pakistan: On the Path to Recovery," noting that the "fundamentals" of the economy had improved significantly as a result of the IMF package, fiscal consolidation and the necessary reforms being undertaken by the government.[8] In its second-quarter report on the state of the country's economy, the State Bank of Pakistan (SBP) claimed that the "cumulative effect of stabilization and regulatory measures taken during the past one year" had led to "notable improvements" in the economy. Additionally, there was an increase in foreign investment, tax and non-tax revenues and exports; currency had stabilised; inflation had started to ease; and large-scale manufacturing showed "some positive signs." While the SBP tempered its optimism with several caveats, on the whole, it seemed to suggest that the economy was on the right track.[9]

However, a closer look at Pakistan's pre-COVID-19 economic landscape reveals a very different picture.[10] The 70 percent reduction in the CAD was a result of import compression and steep depreciation of the Pakistani Rupee, which came at the cost of economic growth.[11] From around 5.5 percent in FY18, Pakistan's GDP growth came down to 3.3 percent in FY19, and was further projected by the IMF to fall to 2.4 percent in FY20. The unofficial estimate by independent economists was bleaker, at 1.9 percent in FY19[12] and 1.2 percent in FY20. While most international organisations were projecting Pakistan's growth to be around 2.4 percent in FY20,[13] renowned Pakistani economist, Dr. Hafiz Pasha, estimated that the 3.3 percent growth claimed by the government and multilateral institutions in FY19 was actually 1.9

percent, set to fall further to 1.2 percent in FY20.[14] Moreover, Dr. Pasha predicted a fall in per capita income in light of the population growth rate of 2.4 percent.[15] Thus, Pakistan's economy was faltering on virtually every economic parameter.

The increase in foreign exchange reserves (after the IMF approved the EFF programme in 2019) was largely based on borrowed money, such as bailout loans from China, Saudi Arabia and the UAE.[16] Despite a nearly 30 percent depreciation in the value of the Pakistani Rupee, exports increased only marginally. In the first nine months of the current fiscal year, exports rose by only 2.2 percent in dollar terms.[17] Meanwhile, there was a steady rise in inflation. The data released by the Pakistan Bureau of Statistics shows that the year-on-year inflation in January 2019 was 5.6 percent, with food inflation at 2.6 percent and 1.8 percent in urban and rural areas, respectively.[18] However, by January 2020, the percentage had spiked to 14.6 percent, with food inflation at 19.5 percent in urban areas and 24 percent in rural areas. In March 2020, the inflation number did fall to 10.2 percent, with food inflation at 13 percent and 15.5 percent (urban and rural, respectively),[19] but this was largely due to the disruption and dislocation caused by the pandemic.

As part of the IMF agreement and to control inflation, the SBP had been steadily raising interest rates. From 6.5 percent at the time when the Pakistan Muslim League-Nawaz (PML-N) government demitted office in May 2018, the SBP's benchmark interest rate increased to 13.25 percent in July 2019.[20] The high interest rate was also meant to attract 'hot money' into Pakistan. Around US$ 3 billion flowed into Pakistan in the form of purchases of short-term treasury bonds, but it started to flow back as soon as the COVID-19 crisis started to unfold in the West.[21]

Ultimately, high taxation,[22] high interest rates, and the devaluation of the Pakistani Rupee (which raised the prices of imported inputs) lead

to a massive fall in industrial production.[23] According to Dr. Hafiz Pasha, "Many of the industries have registered double-digit declines in the first four months of 2019-20. The production is down by 43 percent of cars; 19 percent of motorcycles; petroleum products by 14 percent; cigarettes by 36 percent; steel products by 30 percent; chemicals by 20 percent and so on. In fact, out of the 112 product lines covered by the QIM, there has been a decline in output in 65 lines."[24]

Even as the industry was facing an unprecedented crisis, it was reported that the cotton output would be 20 percent lower than in the previous year.[25] Since textiles (mostly cotton) constitute nearly 60 percent of Pakistan's exports, this slump in cotton output would pose an additional foreign-exchange burden, because Pakistan's dependence on cotton imports would increase to keep the textile industry running.

The tax target of PKR 5.5 trillion set for the Federal Board of Revenue (FBR) became impossible to achieve after the sharp fall in growth. The Government of Pakistan and the IMF commended the 17 percent rise in revenue but failed to factor in the inflation of 12–14 percent, which meant that the actual increased in revenue was only three to four percent. In December 2019, at the time of the second review of the EFF programme, Pakistan requested the IMF for a lower tax target of PKR 5.23 trillion.[26] By February 2020, however, Pakistan was forced to demand a further reduction to PKR 4.8 trillion.[27] This steep fall in revenue targets came before the pandemic, even as the expenditures remained static, portending a fiscal deficit that would breach the target set in the 2019–20 budget.[28]

Since the Imran Khan government came into office in 2018, the fall in growth coupled with high food prices and rising unemployment had caused almost 10 percent of the population to slip below the poverty line. According to Dr. Pasha, around eight million people (four percent

of the population) fell below the poverty line in FY19, which is likely to increase by an additional 10 million people (five percent of the population) by the end of FY20. Thus, nearly 87 million people in Pakistan will be living below the poverty line by 2021.[29]

According to the Debt Policy Statement issued by the government earlier this year, Pakistan's debt has increased by almost 40 percent since Imran Khan assumed office. The total debt and liabilities increased from PKR 29.9 trillion in FY18 to PKR 41.5 trillion in September 2019. Additionally, public debt as a percentage of revenue went up from 447 percent to 667 percent in the span of one year, and debt servicing as a percentage of revenue increased from 37.3 percent to 62.5 percent between FY18 and FY19.[30] According to the IMF's estimates, Pakistan's external debt would reach US$ 113 billion by the end of FY20[31] and that the country would need over US$ 27 billion to finance its external requirements.[32]

III. AFTER COVID-19: DIRE PREDICTIONS

In Pakistan, the first confirmed cases of COVID-19 emerged only in the last week of February.[33] A month earlier, Pakistan's Ministry of National Health Services had alerted border posts and healthcare institutions to be vigilant about any suspected cases.[34] A week after this alert was issued, authorities in the Gilgit Baltistan region of Pakistan-occupied Kashmir announced that the land border with China, which was to open in the first week of February, would remain closed until April.[35] Beyond these measures, however, the nation's overall attitude towards the pandemic remained blasé. Additionally, it felt that China's misfortune, i.e. a fall in production, could be an opportunity for Pakistan to increase its exports, particularly textiles. Many analysts believed that Pakistan could benefit from industries relocating from China to prevent supply chains from being overly dependent on a single country.[36]

Towards the end of February, the possibility emerged of the pandemic leading to negative growth in Pakistan.[37] Disruption in raw material supplies from China prompted alternative sources to increase prices, and Pakistani manufacturers started to feel the pinch.[38] Textiles, which constitute almost 60 percent of Pakistan's total exports, depended on China for 70 percent of their input requirements. Overnight, the cost of importing from China surged by up to 100 percent. Since Pakistan had banned all trade with India, the only alternative sources left were South Korea and Taiwan, which too had spiked prices by 30–35 percent.[39] Pakistan's privatisation drive was at the risk of being delayed due to the withdrawal of Chinese companies that had expressed interest in picking up some of the power plants that were being put on the block.[40]

Despite these issues, the magnitude of the crisis continued to be either ignored or downplayed at the official level. On the day the first infected cases were discovered, the de facto Health Minister Dr. Zafar Mirza said, "With Allah's blessings, this [virus] will not take the form of an outbreak in Pakistan."[41] Khan, too, appeared nonchalant about the seriousness of the infection during his national first address on the pandemic. "*Ghabrana nahin* (don't panic)," he said, claiming that while the virus would spread, 97 percent of the people will survive it, and that it is just like any other flu.[42] However, it has now become increasingly clear that COVID-19 is catastrophic for Pakistan's already ailing economy. On virtually every single economic metric, Pakistan is staring at an abyss.

Growth

The economy has been unravelling at such a bewildering speed that even seasoned institutions and individuals cannot accurately estimate the extent to which the pandemic will impact growth. In the first week of

March, the Asian Development Bank (ADB) came up with a number that seemed incongruous with the dire predictions being made around the world. According to the ADB, Pakistan's economy would lose around US$ 16 million in the best-case scenario and around US$ 61 million in the worst-case scenario. In the event of a significant outbreak of COVID-19, the loss would amount to approximately US$ 5 billion, the GDP would contract by 1.57 percent, and nearly a million people would lose their jobs.[43] By the third week of March, the ADB had drastically revised its estimates to a US$ 415 million loss in the best-case scenario, and a US $6.6–17 billion loss in case of significant outbreak, with the loss of employment ranging from 1.2 million to 3.2 million jobs and the GDP growth contracting by two to five percent.[44]

Moody's, too, has been constantly revising its growth projections for Pakistan. In December 2019, just before the pandemic hit the world, it projected a GDP growth of around 2.9 percent in FY20.[45] By mid-March, this was reduced to 2.5 percent because of the higher debt burden and weaker fiscal balances of the government,[46] and by end-March, the number was down to two percent.[47] Both ADB and Moody's projections—2.6 percent and two percent, respectively—were in line with Pakistan's growth estimations. In the third week of March, Pakistani authorities projected a GDP loss of PKR 1.3 trillion due to supply shocks, disruption in foreign trade, suspension of operations of service and manufacturing industries;[48] two weeks later, the estimate was increased to PKR 2.5 trillion, with nearly 20 percent of the workforce projected to lose their jobs.[49] The Pakistan Planning Commission declared that the virus would lead to a 0.8–1.3 percent loss in the GDP, which would bring the growth down from 3.3 percent to around 2.5 percent.[50] However, multilateral institutions, such as the World Bank and IMF, and independent economists in Pakistan did not share this optimistic assessment.

In a video conference held on 2 April 2020, the World Bank office in Pakistan noted that the nation's GDP growth would reduce from 2.4 percent (the earlier projection for FY20) to 1.1 percent. The fiscal deficit would be close to 10 percent.[51] On 12 April 2020, however, the World Bank's "South Asia Economic Focus" report forecasted a GDP growth of negative 1.3 percent in FY20 and 0.9 percent in FY21. If the pandemic worsened, the GDP could contract by 2.2 percent in FY20, being only barely positive (0.3 percent) in FY21. The World Bank Report lists Pakistan's population growth rate to be 1.8 percent, noting the prospect of a "painful decline in per capita income."[52] According to the 2017 Census, however, the growth rate is 2.4 percent, which only exacerbates the situation further.[53] While IMF, too, has projected a negative 1.5 percent growth in GDP in FY20, it is more optimistic than the World Bank about growth prospects of the Pakistani economy in FY21, estimating a two percent GDP growth.[54]

The magnitude of the crisis confronting Pakistan is evident in the negative growth being projected, this being the first time in history that its economy will contract. Independent Pakistani economists Dr. Hafiz Pasha and Dr. Shahid Kardar initially presented two scenarios of different severity. In the best case, the economy would contract by 4.6 percent in the fourth quarter of FY20, and in the worst case, by 9.5 percent.[55] Eventually, Pasha and Kardar simulated a third scenario, taking into account new information. According to this, Pakistan's GDP would contract by 13.6 percent in the fourth quarter of FY20, and as many as 11.5 million people could face temporary job loss due to the lockdown. Their projection for long-term job loss is approximately 6.5 million, an unemployment rate of 16 percent. Nearly 15–20 million people could slip into poverty, and the total number of poor is likely to cross the 100 million mark, i.e. almost 50 percent of the population.[56]

Unemployment and Poverty

The poverty and unemployment estimates by the Pakistan Institute of Development Economics (PIDE) are even more dire than those of Pasha and Kardar. In a series of bulletins published on the likely impact of COVID-19, the PIDE presented four possibilities. The worst-case scenario is "high impact," and entails a 0–1.5 percent GDP growth. PIDE estimates that poverty rate will increase from around 23.4 percent to nearly 59 percent (an additional 75 million people), bringing the total population living below poverty line to 125 million people.[57] However, in light of the looming recession and likely negative GDP growth, this scenario could be a conservative estimate.

The PIDE has estimated that 56 percent of the workforce falls under "vulnerable employment." This includes 80 percent of the people employed in agriculture, 75 percent in wholesale and retail trade, 50 percent in hotels and restaurants, 60 percent in real estate and business, and 40 percent in transport and communication sectors.[58] The World Bank expects the brunt of the recession to be borne by the informal sector (which accounts for 72 percent of employment) and daily-wage workers employed in the formal sector (who constitute five percent of the total workforce).[59] According to a PIDE study, in the event of a complete shutdown, around 18.5 million people (30 percent of the employed labour force) who were part of vulnerable employment would be laid off. This scenario is now unlikely, given the relaxation in lockdown. However, even with moderate restrictions, over 12 million people (20 percent of the employed labour force) could lose their jobs. Within the vulnerable employment, the bulk of the layoffs would comprise daily-wage workers and those who work on a piece-rate basis.[60] Formal-sector workers are also at risk. According to one report, one of Pakistan's largest hotel chains has already laid off 20 percent of its

workforce.[61] There is a growing sense of insecurity about employment in the country. In a survey by IPSOS, 51 percent of the surveyed people (from both urban and rural areas) were concerned about losing their jobs over the next six months.[62] The situation is further exacerbated by the looming prospect of tens of thousands of Pakistanis working in the Middle East, losing their jobs and returning home,[63] which will also impact the remittances that are so critical for Pakistan's balance of payments.

Punjab, the most populous province in Pakistan, will suffer the majority of job losses. PIDE estimates that 10–12 million people in Punjab could get laid off. Compared to other provinces, Sindh has the least number of vulnerably employed, but the estimates are alarming nonetheless, with three to four million people at risk of job loss. For the other two provinces, PIDE data suggests that two million in Khyber Pakhtunkhwa and one million in Balochistan are likely to be rendered unemployed.[64] According to the calculations of Pasha and Kardar, the unemployment rates by province will be 16 percent for Punjab, 15 percent for Sindh, 14.5 percent for Khyber Pakhtunkhwa, and nine percent for Balochistan.[65]

Foreign Trade and Balance of Payments

A PIDE study into the trade disruptions caused by COVID-19 and its impact on Pakistan's GDP had worked out a worst-case scenario in which there would be a 20 percent decline in exports and imports. Almost 70 percent of Pakistan's imports constitute raw materials, intermediate goods, and capital goods; around 60 percent of exports are textiles, which depend heavily on imported raw materials. Therefore, a decline in imports will, in turn, affect both exports and growth. By the PIDE's calculations, a trade disruption of 20 percent would lead to a GDP contraction of 4.6 percent in the last quarter of FY20.[66]

The latest data released by the Pakistan Bureau of Statistics validates the PIDE's worst-case scenario. In March 2020, imports fell month-on-month by over 20 percent and exports by over 15 percent.[67] Textile exports fell by 18 percent,[68] machinery imports by 15 percent, petroleum imports by 40 percent, and imports of raw material for textiles by 20 percent.[69] In its latest country report on Pakistan, the IMF found a sharp decline in container traffic, which is "consistent with cancellation of export orders or requests to delay the shipments."[70] This was corroborated by the Pakistani media, which reported containers piling up at the ports. According to one report, between 22 March and 3 April, there was a 31 percent fall in shipments of export containers at the Karachi port, with nearly 7,000 containers not being shipped. Further, there was a 50 percent decline in the number of containers reaching the port, due to order cancellations.[71] According to Pakistani textile exporters, nearly 50 percent of the "ready for shipment" export orders were delayed by importers because of lockdowns in Europe, which they anticipate will result in order cancellations.[72] Meanwhile, the hosiery manufacturers claim that for 90 percent of their exports to the US and Europe, clients have either cancelled orders or refused to accept shipments.[73] Pakistan's commerce ministry has estimated an export loss of US$ 2 billion, in addition to delayed payments of shipments already sent. This will create huge cash-flow problems for the textile industry.[74] According to the de facto Commerce Minister Abdul Razzak Dawood, the export loss could go up to US$ 4 billion.[75]

The prospect of reduced remittances by overseas Pakistanis further adds to the crisis. Remittances account for approximately eight percent of the country's GDP, being equal to (and sometimes more than) exports. COVID-19 is expected to have a severe impact on the remittances, especially from the Middle East. The IMF has estimated a

drop of over US$ 5 billion in FY20 and FY21. Together with the fall in exports, this will significantly impact Pakistan's external finances.

Given the decline in imports, the IMF has projected a manageable CAD of around 1.7 percent in FY20 and 2.4 percent in FY21.[76] However, these CAD calculations will be rendered inaccurate if the remittances fall below current projections. According to the worst-case scenario presented in a PIDE paper, remittances in FY20 could decline by 14 percent, i.e. US$ 3.5 billion. The PIDE's projections for FY21 are even more concerning, showing a 47 percent fall in remittances in the worst-case scenario, reducing the baseline projection of US$ 26.5 billion to just over US$ 14 billion. Even in the best-case scenario, remittances are likely to fall by around 15 percent, bringing in only US$ 22.5 billion.[77] The World Bank estimates are bleaker than the PIDE's, at 23 percent or over US$ 5 billion in FY20 alone.[78] If the World Bank or PIDE projections come true, then Pakistan's balance-of-payments difficulties are likely to increase, especially given its external financing requirements. Speaking in a webinar, the chief macroeconomist of Pakistan's Planning Commission revealed that the country will need to return US$ 19 billion in principal and interest to international creditors. With the fiscal space getting further constricted, exports and remittances declining, and international financial markets tightening, Pakistan could face serious problems in servicing its debt.[79]

Fiscal Balance and Revenue

Even before COVID-19, economic activity in Pakistan had slowed down to a point that the government was simply unable to collect its tax target of PKR 5.5 trillion. The target was scaled down to PKR 5.2 trillion in December 2019, and to PKR 4.8 trillion by February 2020. Post COVID-19, the IMF has conceded that Pakistan will only be able to collect PKR 3.9 trillion in FY20, a shortfall of PKR 1.6 trillion. Moreover, the latest

tax target of PKR 3.9 trillion means that in the last three fiscal years, i.e. FY18, FY19 and FY20, the revenue collected by Pakistan's FBR has remained almost identical, even as expenditure has increased by PKR 2.6 trillion. For FY21, the IMF has projected a tax revenue of PKR 5.1 trillion, which is PKR 1.2 trillion more than what the FBR is expected to collect in FY20. However, this target is unachievable in an economy expected to grow by only two percent, by IMF's own calculation.

Although Pakistan is expected to incur the highest-ever fiscal deficit in FY20, at around 9.2 percent of the GDP, the IMF is convinced that the country will be able to bring this down to 6.5 percent by FY21.[80] This conviction seems unfounded, especially since experts are questioning Pakistan's ability to meet even the drastically cut-down target of PKR 3.9 trillion in FY20.[81] Moreover, factoring in the PKR 1.2 trillion stimulus package to combat the COVID-19 crisis would push the fiscal deficit to double digits in FY20. However, the IMF has agreed to exclude the expenditure incurred in combating the virus while calculating Pakistan's fiscal deficit in the current fiscal year.[82] Thus, Pakistan has been failing to meet the targets formulated by the IMF, and data suggests that the situation will remain the same in future. For now, the IMF continues to make accommodations for the country's shortcomings. One example of this is the drastic cut in the development programme to meet the IMF targets, despite the IMF insisting against such cutbacks in development expenditure. The Federal government had budgeted PKR 701 billion for the Public Sector Development Programme (PSDP) in the annual budget for 2019–20.[83] However, shortly before the pandemic, Pakistan cut the PSDP to PKR 588 billion to meet its obligations on primary balance. Post COVID-19, it was further reduced to PKR 488 billion. Thus, the PSDP was cut down by almost 30 percent of the original budgeted amount. The provinces development programme, too, has been reduced from the budgeted

PKR 912 billion to PKR 461 billion in the aftermath of the pandemic, i.e. a reduction of almost 50 percent.[84]

Trade, Industry and Business

As established in the previous sections, Pakistan already had very little fiscal space to absorb any major shock. Unlike most other countries, Pakistan does not have the financial bandwidth to provide meaningful succour to businesses on the verge of failure due to the pandemic. According to calculations made by Pasha and Kardar, in the fourth quarter of FY20, the industrial sector is estimated to contract by 14–22 percent, while the services sector by 11–15 percent. Agriculture is expected to grow by a marginal one percent.[85] The World Bank expects industrial growth to contract by 2.1 percent and services sector by 1.7 percent in this entire FY20. In FY21, the industrial and services sectors are expected to remain anaemic, at 0.7 and 0.8 percent, respectively.[86]

The latest data by the Pakistan Bureau of Statistics reveals that large scale manufacturing (LSM), which accounts for nearly 80 percent of total manufacturing and around 11 percent of the GDP, has shown a negative three percent growth in the first seven months of FY20. The petroleum sector has witnessed the steepest decline of around 14 percent. The data shows a worsening trend year-on-year, with the output decreasing by 36 percent and 1.15 percent for petroleum companies and LSM companies, respectively.[87] The disaggregated data reveals an even bleaker situation, with the automobile sector, pharmaceuticals, agricultural machinery, white goods (e.g. air-conditioners and refrigerators) and power looms taking a substantial hit.[88] The data for March 2020 is even worse. According to the Pakistan Bureau of Statistics, LSM output in March 2020 declined by nearly 23 percent year-on-year and 22 percent as compared to February 2020.[89]

Reports from the ground reveal that businesses and industries are in deep distress. Pakistan's flagship carrier, Pakistan International Airlines (PIA), which was already incurring losses, has been listed as the airline most at risk of bankruptcy in the next two years because of the COVID-19 crisis.[90] Pakistan's Ministry of Aviation ministry has estimated that the sector could lose up to PKR 25 billion in just two weeks of lockdown.[91] The Pakistan Railways was losing PKR 1 billion per week due to the lockdown.[92] Amongst the worst hit is the automobile sector, with sales down by nearly 50 percent.[93] The pharmaceutical sector, which was already reeling under the impact of PM Khan's decision to ban all trade with India,[94] has seen a drop in sales by 50 percent and an increase in the cost of raw material (mostly imported from China) by 300 percent.[95] In the telecom sector, too, revenues have fallen by 10–15 percent due to a decline decrease in voice traffic amidst the lockdown. Much of the telecom revenue came from pre-paid cards, which are not being recharged as frequently, given the restrictions on movement.[96]

Small and medium businesses are also suffering, particularly the small traders. In 2014, it was estimated that a one-day nationwide shutdown costs the economy over PKR 60 billion.[97] Extrapolating from this and adjusting for 2020, the economy would bleed at least PKR 100 billion a day, which is corroborated by the estimates made in early April, i.e. a loss of PKR 2.5 trillion. According to a recent report, in the main commercial centres in Rawalpindi, small businesses are losing over PKR 600 million daily.[98] In a petition to Khan, the association of large, tax-paying organised retailers has claimed a loss of PKR 900 billion in 45 days of lockdown.[99]

Energy

Amidst the largely negative impact of COVID-19 on Pakistan's economy, the crash in the prices of oil comes as a relief. Petroleum

products constitute around 30 percent of Pakistan's total imports. Thus, a fall in Petroleum, Oil & Lubricants (POL) prices is a windfall for the country, since it not only eases the pressure on the balance of payments, but also helps moderate inflationary pressures if the government reduces prices. Further, if the government does not reduce taxes on petroleum products, it can garner additional taxes for the exchequer. During the current crisis, Pakistan has tried to balance the fiscal needs with the need to provide relief to people. With regard to petroleum, despite reducing prices by PKR 15 per litre, the government expects to gain an additional PKR 60 billion in the next fiscal.[100]

However, the reduction in international oil prices is at best a mixed bag. While Pakistan could save approximately US$ 5–8 billion on its oil import bill if the prices remain at the current levels, this is likely to be compensated by the fall in remittances because of lay-offs of Pakistani expatriate workers in the Middle East. Moreover, due to the steep fall in oil revenues, these countries will now be hard-pressed to provide any financial bailouts to Pakistan.

The fall in the oil prices is not a panacea for all of Pakistan's economic woes. According to an energy-sector expert, it will present a challenge for the local oil industry, in turn depriving the government of up to PKR 250 billion in taxes and other revenue.[101] In theory, Pakistan's cost of power generation should decrease with the fall in POL prices, since 66 percent of it is based on oil and gas.[102] However, this is unlikely to happen due to the kind of contracts that the country has signed with the independent power producers, which mandate that they must be paid capacity charges regardless of the consumption of electricity generated. In March alone, electricity consumption was down by 30 percent, gas consumption by 40-50 percent, and petrol and diesel by around 60-75 percent.[103] This is compounded by the fact that Pakistan does not have

the storage capacity to buy and stock up oil at cheap prices to hedge against the future rise in prices.[104]

Despite the oil price windfall, the COVID-19 crisis is going to exacerbate the financial crisis in Pakistan's energy sector. Already, the "circular debt" has touched an astronomical PKR 2 trillion mark.[105] Relief measures for power consumers will cost over PKR 380 billion, according to calculations made by the power division of the government.[106] The crisis is exacerbated by the fall in the collection of bills during the lockdown, in part due to the instruction to not collect bills from consumers using less than 300 units for the next three months,[107] as well as the government's decision to raise power tariffs under pressure from Chinese power producers demanding compensation for the exchange-rate losses incurred because of the fall in the value of the Pakistani Rupee by around 10 percent.[108]

Debt

Pakistan's public finances were already in a parlous state. The COVID-19 crisis has made it even more difficult for Pakistan to service its mountain of debt. In FY19, the net revenue of the Federal government was less than the debt servicing incurred by the government,[109] i.e. much of the government's expenditure was incurred through debt. In the 18 months since the previous PMLN government demitted office, Pakistan's total debt and liabilities have gone from PKR 30 trillion to PKR 41 trillion.[110] The Central government's debt increased by over five percent in the first eight months of FY20, and by 21 percent year-on-year in February 2020.[111] According to the IMF's estimates, the federal government's debt has surged from 80.4 percent of the GDP pre-COVID1-9 to 85.4 percent post-COVID-19.[112]

The pandemic gave Pakistan an opportunity to obtain debt relief, particularly for its external debt, at US$ 107 billion or 38 percent of the GDP. It viewed the crisis as a way out of the economic straitjacket imposed by the IMF. In the words of one of Pakistan's top economic journalists, "Covid-19 has affected most of the global economies which should provide a room for the International Monetary Fund (IMF) to relax stance on critical programme benchmarks. In fact, the situation also provides an opportunity to access emergency funds allocated by leading international lending agencies to fight coronavirus."[113] This is reminiscent of Pakistan's strategy after the 9/11 tragedy. Under the guise of "unstinted support" to the US-led coalition forces against the Taliban and Al Qaeda terrorists, Pakistan sought to be rewarded monetarily. In an interview on national TV, Gen. Pervez Musharraf, the then military dictator of Pakistan, noted, "Our strategy is to go for debt write-off, as the country has US$ 38 billion debt, including US$ 12 billion bilateral and the remaining multi-lateral debt."[114] Despite such efforts, however, Pakistan only managed to obtain a new IMF programme and a rescheduling of around US$ 12 billion worth of debts to the Paris Club.[115,116]

Currently, Pakistan is obligated to return around US$ 28 billion to creditors in the next three years.[117] Once again, the country is seeking to obtain loan write-offs; short of that, it hopes to get around 50 percent (US$ 14 billion) of loans rolled over. Already, Pakistan has received US$ 9 billion in bailouts in 2019, from countries such as China, Saudi Arabia, UAE and Qatar. The IMF insists that the money being given to Pakistan cannot be used to pay back its loans from 'friendly countries' and expects China to lend an additional US$ 6 billion to Pakistan over the next 12 months.[118]

Pakistani Foreign Minister Shah Mehmood Qureshi has lobbied over a dozen countries for debt relief in some form—as moratorium,

restructuring or even debt write-off. Additionally, the Pakistan foreign office launched an intense diplomatic push for debt relief,[119] hoping to get a waiver on not only bilateral loans but also multilateral loans.[120] According to the de facto Finance Minister Abdul Hafeez Shaikh, Pakistan would be approaching the IMF, World Bank and ADB to seek US$ 4 billion in fresh loans to combat the COVID-19 crisis.[121]

So far, Pakistan has managed to obtain a Rapid Financing Initiative loan worth US$ 1.4 billion from the IMF to meet its balance-of-payments needs to tide over the pandemic.[122] The World Bank and the ADB have also pledged around US$ 2.5 billion in assistance. Much of this comes from funds that had been allocated for projects already under execution but were either moving slowly or were stalled, and are now being diverted for COVID-19 assistance.[123]

IV. WEIGHING THE MITIGATION MEASURES

Government Rescue Package

In light of the massive economic disruption, Pakistan's government announced a rescue package worth PKR 1.2 trillion on 24 March 2020. Of this, PKR 150 billion was allocated for direct benefit transfer to the most vulnerable families, with each family receiving PKR 3,000/month for four months, disbursed upfront as a single payment of PKR 12,000. PKR 100 billion was allocated to SMEs and agricultural loans towards deferred payments; PKR 280 to wheat procurement; PKR 200 billion to the labour force; PKR 75 billion to reduce the prices of petroleum products; and PKR 100 billion for the export sector, in lieu of the refunds due to them.[124]

While this package seems impressive, many of the items included under it were already part of the government budget. For example, the

government is obligated to provide refunds to exporters but had been postponing it. Similarly, wheat procurement is supposed to be done annually as part of a government undertaking and taking loans from banks under "commodity operations" is par for the course.[125] Furthermore, the income support programme for the most vulnerable sections had already been included in the FY20 Budget, but the bulk of it remained unutilised, which was now being presented as a separate allocation. By the Pakistani cabinet's own admission, the additional burden on the exchequer is less than half of the total package, i.e. PKR 550 billion.[126] The IMF, while lauding the "comprehensive fiscal support package aimed at accommodating the spending needed to mitigate the impact of the Covid-19 shock," pegged it at 1.2 percent of the GDP (~ PKR 500 billion),[127] compared to Khan's claim of two percent.

State Bank of Pakistan

The SBP has formulated a slew of measures in response to the pandemic,[128] of which the most significant one was to reduce the benchmark policy rate from 13.25 percent to nine percent. Pakistani businesses had long been demanding a cut in the interest rate, since the high rate of interest was an impediment to doing business. The SBP governor had previously been opposed to the move[129] because of high inflation, but the outbreak of COVID-19 on 16 March 2020 forced the SBP to cut the interest rate by 75 basis points. The rate was reduced by another 150 basis points a week later, and by 200 basis points more three weeks after that.[130] Businesses have demanded the rate to be further reduced by four to five percent. While this move will provide temporary relief, it is unclear whether it will stimulate economic activity despite the pandemic, and if old stimulus tools will work in such an unusual situation. For example, top economists have already questioned the efficacy of the Pakistani government's package for the

construction industry in kickstarting economic activity.[131,132] Members of the construction industry, too, remain sceptical.[133]

External Debt

On the external debt front, Pakistan is set to receive US$ 4 billion from the IMF, WB and ADB,[134] and there is some talk of the Islamic Development Bank offering a package of US$ 650 million.[135] However, debt write-offs are unlikely to be offered. Much of Pakistan's hopes have been pinned on the G20 summit—in particular, on the Paris Club countries. On the eve of the G20 meeting, PM Khan and Foreign Minister Qureshi lobbied other G20 countries for debt relief.[136] However, as some Pakistani journalists pointed out, the Paris Club component had already rescheduled Pakistan's debt in 2001,[137] and Saudi Arabia, China and UAE had previously undertaken to "roll-over" their debts as part of the conditions imposed by the IMF for granting the EFF facility in 2019.[138]

In April 2020, the G20 and the Paris Club had only provided debt relief to the "highly indebted poor countries." Since this did not include Pakistan, the country was left with no relief in terms of rescheduling or moratorium. On 15 April 2020, the G20 and the Paris Club announced a one-year debt relief to the poorest countries,[139] including Pakistan. The country expected to receive US$ 10–15 billion in relief,[140] and some analysts postulated a US$12 billion debt repayment obligation under the plan.[141] Khan welcomed the move,[142] and Qureshi credited it to the PM's diplomatic standing, calling it a "great" and "very timely decision."[143] Qureshi further noted that while Pakistani officials were doing a detailed study of the impact of the G20 debt relief, it would likely be "substantial."[144] However, the G20 statement offered a maximum debt relief of approximately US$ 1.5 billion, which they had to service to

the Paris Club over the next two years.[145] On 20 April 2020, the IMF's Resident Representative for Pakistan revealed that the country had not yet made an official request for debt relief.[146] According to Pakistan's finance ministry, the maximum relief they expected to get was only around US$ 1.7 billion.[147]

V. THE POLITICAL AND STRATEGIC FALLOUT

The economic fallout of COVID-19 will be severe on Pakistan. This, in turn, will impact its domestic politics as well as foreign, security and strategic relations with other countries. To meet the challenge of the economic downturn, the country must initiate sweeping economic, political and security reforms, which will require significant bailouts from international donors and friendly countries. However, Pakistan is neither inclined to making reforms nor likely to receive any major bailout programme, since most donor countries have to provide huge stimulus packages to kickstart their own economies, leaving little fiscal space to assist other countries. The IMF's EFF programme, too, has been suspended for now, and pressure is growing on the Imran Khan government to re-negotiate it.[148]

In the absence of traditional donor countries and institutions, Pakistan must turn to 'friendly countries' such as China and Saudi Arabia. The Saudis have already given Pakistan US$ 3 billion as deposits to improve its national balance sheet and have extended a deferred oil-payment facility worth an additional US$ 3 billion. Thus, Pakistan's hopes are currently pinned squarely on the "Iron Brother," i.e. China. However, Chinese businesses and officials are concerned about the viability and profitability of Chinese investments. Already, Pakistan has requested China to relax the payment obligations due to them for the power plants set up under the aegis of the China–Pakistan Economic Corridor (CPEC).[149] Further, the inquiry commission set up to

investigate the Independent Power Projects in Pakistan has reported that a "$1.7 billion power transmission line project of the China-Pakistan Economic Corridor (CPEC) was 234% more expensive than a similar project in India with better technology."[150]

In the fast-changing geostrategic scenario after COVID-19, however, China could put aside some of its commercial and financial concerns regarding Pakistan to strengthen their strategic relationship. Pakistan's dependence on China for economic, military and political support is likely to increase in future, placing it firmly in the latter's ambit. Many Pakistani analysts and thinkers feel that the nation's future lies with China, not with the West. COVID-19 has only cemented this conviction further. The Sino-Pak relationship will not obviate Pakistan's need to engage with the West, but it will allow room for manoeuvre in its dealings.

For the US and its Western allies, the pandemic offers an opportunity to effectively pressure Pakistan, provided they do not allow altruism to guide their policy. Pakistan is currently far more vulnerable than it has been since the War on Terror started in 2001 and can be forced to deliver on issues it has reneged on in the past, especially in the context of Afghanistan and terrorist safe havens in Pakistan. However, it appears for now that these economic vulnerabilities will not impact Pakistan's strategic game-plan in Afghanistan. The US has evidently lost interest in Afghanistan and seems inclined to engage with the Taliban on their terms. Even the FATF has eased the pressure on Pakistan. In this very limited sense, the COVID-19 outbreak has worked in favour of Pakistan.

Internally, the pandemic will result in dislocation and economic distress. Poverty and unemployment are bound to increase, as discussed in Section 3. There are serious concerns of law-and-order disturbances

and rise in crime. While the Opposition will try to capitalise on the problems of the government, so far, there is no sign of the current dispensation being destabilised or deposed. The Opposition parties are not strong enough to not confront the ruling government and would prefer that PM Khan to bear responsibility for all the tough decisions that will need to be taken to keep the economy from derailing.

In the 20 months since he has assumed office, Khan's lack of administrative and governance skills has become evident. However, destabilisation is unlikely, since he continues to enjoy the support of the military, which paved his way to power. Despite occasional reports of rifts between Khan and the military, there have been no significant long-term fallouts. According to a member of the cabinet, this is because "Imran Khan agrees to whatever the military says."[151] Moreover, Khan's government has responded to the pandemic in complete adherence to the military vision,[152] which further cements his position. There are three primary reasons that Imran Khan still enjoys unequivocal military support:

1. The military has no viable political alternative.
2. Khan serves as the military's interface with the rest of the world, actively seeking loans and bailout packages from friendly countries.
3. His anti-India stance endears him to the Pakistani deep state.[153]

Unless the situation on the ground changes drastically, such that the military no longer finds it tenable to keep Imran Khan in office, he is likely to remain the face of the government for the foreseeable future.

However, problems can arise between the military and the civilian government due to the economy. While there is growing pressure from the military to increase defence budget allocations, the precarious fiscal

situation leaves no room for this. The army is now trying is to influence a change in the formula for dividing the revenue between the Federal government and provincial governments, demanding that its budget be deducted directly from the divisible pool of revenue.[154] It is unlikely that Khan or the Opposition will resist the military's demand for more resources; historically, such moves have proven to be politically unwise.[155] Unfortunately, if Khan does accede to the military's demands, he will further reduce the financial space to initiate development schemes, thus damaging his political standing.

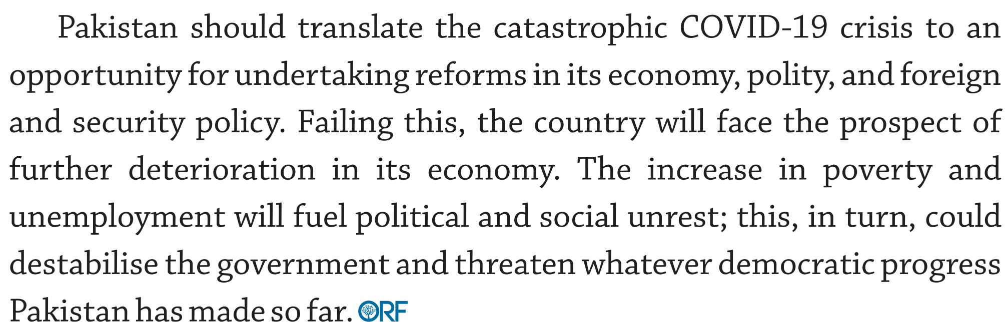
CONCLUSION

Over the last few years, the Pakistani military has come to see the economy as an essential component of national security. Further, the top brass views the current problems as not being structural but managerial. Both the de facto finance minister and governor of the SBP are reportedly the Pakistan Army's choice. With the induction of the army chief into the newly formed National Development Council, the military can now participate in economic decision-making.[156] As the economic crunch worsens, the military's focus on national security will heighten, leading it to be more aggressive on its efforts to control the economy. Thus, the military's dominance over the political system will only increase in future.

With the military embedding itself deeper into the state structure of Pakistan, there is little hope for any initiative from Pakistan to reduce tensions with India. However, the country's economic vulnerabilities present India with an excellent opportunity to develop new levers to mount pressure. To seize this, India must first recover from the economic setback caused by the pandemic. Pakistan will be hard-pressed to rationalise its defence expenditure, which consumed nearly 70 percent (including defence pensions) of the net revenue of the

federal government in FY19.[157] Given Imran Khan's stance against his Indian counterpart, it is evident that Pakistan has no intention of tempering its aggression in the region. If tensions continue to run high, the Pakistan Army is likely to extract whatever resources it can to sustain its confrontationist approach and maintain strategic parity with India. From India's point of view, Pakistan's relentless indulgence in a ruinous arms race can prove to be beneficial.

Pakistan should translate the catastrophic COVID-19 crisis to an opportunity for undertaking reforms in its economy, polity, and foreign and security policy. Failing this, the country will face the prospect of further deterioration in its economy. The increase in poverty and unemployment will fuel political and social unrest; this, in turn, could destabilise the government and threaten whatever democratic progress Pakistan has made so far.



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