Insights for Change

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Exit Strategy From the IMF Programme

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The International Monetary Fund's (IMF) executive board is set to meet next week to discuss the approval of a three-year Extended Fund Facility (EFF) for Pakistan ending in the fiscal year 2027-28 — the 24th time the country is going to enter into an agreement with the lender.

There seems to be a broad consensus that it is in Pakistan' s best interests to exit from the IMF programme. The reasons are quite obvious — the loss of autonomous decision-making by the sovereign, inability to set its own priorities and their phasing, timing and sequencing, and getting out of a straitjacket framework of short-term performance criteria, structural benchmarks agreed with the IMF.

The moot question is how to translate this rhetoric into a credible strategy as many such promises have been made in the past but never fulfilled. The imperative prerequisites are that we achieve durable political stability, tackle security concerns and are willing to take tough extraordinary actions uninterruptedly without succumbing to pressures from vested interests. Next, we have to move away from generalised, vague and contradictory statements of intentions and move towards achieving verifiable, quantifiable and measurable targets.

The compelling reason for approaching the Fund and other creditors is to fill in the external financing gap of $25 billion resulting from the current account deficit and repayments of principal amounts.

So, the main goal of this exit strategy ought to be to take actions in the next three years that by FY28 this amount is reduced and the ratios of external debt to GDP, external debt to total foreign exchange earnings, external debt servicing to export earnings, and external debt servicing to foreign exchange reserves are brought down to manageable levels. On the domestic debt side, we have to focus on debt servicing payments as a percentage of total revenues.

Working around these targets, the main endeavour is to work systematically on enhancing the capacity to generate additional net foreign exchange earnings compared to the current levels. Pakistan has registered a negligible current account deficit in FY24 and less than 1 per cent in last four years except 2022. The objective is to turn it around into a surplus of $6-9bn by FY28. Is this feasible or, as naysayers would argue, kite flying?

Exports of goods recorded a 14pc growth rate of merchandise exports in August. (In FY22, the increase was 26pc). If this average rate of 14pc is maintained for the next four years,

$50bn of exports can be earned by Fy28.

Foremost, the problems faced by the exporters, for example in obtaining refunds, competitive energy prices, tax incentives, etc are quickly resolved. Textile exports should raise the ratio of manmade fibre. The focus should shift from five traditional sectors to every exportable sector. The Export-Import Bank should begin providing supplier and buyer's credit, pre-shipment and post-shipment finance to non-traditional and value-added sectors. IT exports and other service exporters are provided reliable and fast connectivity and the flow of skilled manpower is expanded.

The standards and quality assurance procedures are digitalised, trade flows facilitated through a national single window, new markets are penetrated supported by Export Development Fund (EDF), exchange rate is kept stable and new free trade agreements (FTAs) are negotiated tilted in favour of Pakistani exports. Investment in Reko Diq should be geared up to start flow of export revenues. Tariff rationalisation would enable the exporters to become part of global supply chain, particularly to China, while liberalising the domestic markets and ensuring competition bringing the consumer prices down.

At least four special economic zones have to be made fully operational to attract the Chinese companies planning to relocate their labour-intensive export industries and other investors from Gulf Cooperation Council (GCC) countries. A 1pc increase in participation in supply chain is accompanied by an equal increase in per capita income. Being connected to global supply chains provides access to new technology, new markets and makes the domestic ecosystem vibrant.

Large export firms should invest in their labour to raise their productivity. I have observed during my visits that some of the progressive firms are already doing so as the business case is quite obvious. Two-thirds of incremental returns from increase in productivity accrue to the owners making their products competitive in international markets.

Exports of IT services are estimated to hit $6bn and this should be able to neutralise the deficit on balance on services. Targeting workers' remittances at 10pc annually (as the number of workers abroad is expanding fast and growth rate in FY24 was 10.7pc) to reach $45bn seems feasible through the provision of performance-linked incentives to the banks and the exchange companies.

Foreign Direct Investment and disbursements form the existing pipeline of multilateral and bilateral loans making a conservative estimate could be $6bn. Therefore, the total earnings would amount to approximately $100bn, or $95bn if there is some shortfall.

As tariffs and non-tariff barriers are reduced, import restrictions are completely unwound, merchandise imports are projected to be $83bn by FY28 assuming an annual growth rate of 12pc. (The latest growth rate is 7pc). Adding unrestricted payments on interest, remittances and dividends of $8bn, the current account can have a potential of generating surplus of $6-9bn that can be utilised to redeem and repay one-year deposits and short-term liabilities.

By FY 29 these can be brought down to zero. Together with other flows in the financial account (e.g. NPCs, portfolio investment, purchases from the market), this would result in foreign exchange reserves to $20bn by FY28 as projected by the IMF. These are point estimates but sensitivity analysis should further refine these estimates and make them robust.

On the import side, why a 12pc target is

proposed? It is because if we take a multipronged approach, this would be the outcome. POL and RLNG are the largest import items. Oil and gas exploration and development companies — particularly the foreign companies — should be incentivised both through remunerative pricing, a facilitative regulatory environment where they do not have to run to the ministry or the regulator for securing permission at each stage.

These companies want to invest $5bn but are waiting for changes in the policy. The CCI decision to offload 35pc of their production to third parties has not yet been implemented. It is hard to comprehend that once constitutional bodies such as CCI or NEC or high-powered coordination bodies such as SIFC make decisions, why there is foot-dragging in implementing those.

Similarly, the refinery policy is lingering on for the last four years coming across one stumbling block or the other. Pakistan badly needs a petrochemical complex as the downstream industries would benefit from these raw materials. Saudi Crown Prince Mohammed bin Salman had announced his commitment to this project four years ago, but it is now going through another feasibility study while the previous studies have been shelved.

RLNG contract with Qatar should be revised in 2026 as the demand for the imported fuel for power is on a downward curve. Power distribution and gas companies should be opened up to competition at retail level. Russian and Chinese companies were interested in setting up a new steel mill with a capacity of 3 million tonnes that would replace imports used by the auto and white goods and other industries.

A country with the largest contiguous irrigated system has been importing food items amounting to $10bn. A smart agriculture policy should be able to save $ 6-7bn. The government has to discontinue fixing prices for wheat, sugar cane and cotton and procuring wheat and selling it at below market prices. Compare this to maize and rice, the unregulated commodities which have increased their output significantly exporting surplus.

By removing government interventions, wheat, sugar and cotton would no longer be imported. Oil seed cultivation should be another priority area. Meat, poultry, fruits and vegetables, fisheries and milk have high potential for exports, but these are fragmented and there is no champion either at the federal or provincial level to act as their facilitator. My calculations show that these commodities can add $2bn by FY28 if the problems faced by them are quickly resolved.

FDI has to be screened and only those investments which are export-oriented, bring in technology transfer and generate employment should be given the incentives comparable to those in our regional competing countries.

A question which arises frequently is: who would manage this highly ambitious agenda given our bleak past track record of implementation? The SIFC has proved to be a useful platform for coordination, problem-solving and monitoring and should assign targets to each implementing agency, review the progress periodically and remove the hurdles if any.

Actions rather than speeches would establish credibility and restore investor confidence. The above strategy has to be accompanied by many reforms on domestic side which would form a separate discussion piece. Both external and domestic reforms, if implemented seriously, would allow Pakistan to raise its present growth speed limit from 4pc to 6pc, which is badly needed. Failing this, the country would again be knocking at the

doors of the IMF in September 2028.

Domestic Reforms

The country requires a comprehensive three-year action plan for domestic reforms, in addition to solidifying external accounts, to ensure a smooth exit from the International Monetary Fund (IMF) programme and transition to a self-sustained, non-inflationary growth path.

The broad contours of such reforms are quite well known. What is needed is to build a consensus among political parties, federal and provincial governments, and the private sector.

Key elements of the plan should be finalised with timelines, responsibilities and milestones, and must be approved by parliament to ensure continuity, consistency and predictability — the missing elements responsible for the poor track record of previous reform efforts.

Government must focus on increasing investment, controlling fiscal deficits, devolving services, addressing energy crisis and reforming civil services

The reform agenda should focus on raising the investment-to-GDP ratio to 20 per cent by FY28, containing a fiscal deficit of 5pc of GDP and a primary surplus of 3pc, devolving basic service delivery to local governments, overcoming the energy crisis, and reforming civil services.

Investment in Key Sectors

Public sector investment through its own budgetary resources has to move up to 5pc through fiscal consolidation measures. Public-private partnerships and private investment have to escalate to 15pc by doubling credit to the private sector, especially SMEs, farmers, and sectors such as construction, housing and tourism.

The main reason the country keeps getting into a balance-of-payments crisis is that the domestic productive capacity in industry and agriculture falls short of aggregate demand when it crosses the 4pc growth barrier and results in higher imports. To remove this constraint, agriculture, industry and export sectors must be expanded through investment and productivity gains to make them competitive.

Private equity and venture capital funds, development finance institutions, takafuls, insurance companies, and pension and endowment funds must be reinvigorated to participate in both equity and debt capital market transactions.

Private investment has already touched an all-time low due to coercive and arbitrary measures, harassment and threats to existing investors, and an unfavourable business climate. Distinguishing legitimate profit-making from rent-seeking is crucial to attract new investment.

In agriculture, the productivity of small and medium farmers can be boosted by providing certified seeds, fertilisers, pesticides, adequate water, agriculture equipment and credit. Contract farming in certain crops has proved successful and should be encouraged for replication in other crops as well.

Rainwater harvesting can augment water supplies. Warehousing, cold storage, farm-to-market roads, refrigerated vans, and agri malls will help reduce waste, substitute imports and ease inflationary pressures.

The private sector's investment in intermediate goods production must increase, with a focus on industries such as petrochemicals, oil and gas exploration, and engineering goods. Additionally, regulatory reforms should eliminate outdated rules that

hamper business growth.

Strengthening Public Financial Management

On the fiscal side, the country must focus on reducing domestic debt and interest payments to avert future excessive borrowing.

The revenue-to-GDP ratio should be pitched at 15pc, with taxes contributing 12.5pc and non-tax 2.5pc. The breakdown of the Federal Board of Revenue (FBR) and provincial and local taxes would be 10.5pc and 2pc, respectively. The expenditure-to-GDP ratio should be aimed at 20pc, with a big jump in development expenditure to 5pc.

The FBR should drive digitisation to minimise taxpayer interaction, utilise AI-driven analytics, promote digital invoicing and QR codes and simplify tax processes, among other things. Provincial governments can generate additional revenue by collecting agricultural income tax from large landowners and improving urban property tax collection.
Urban immovable property tax should be assessed and collected by the metropolitan or municipal corporations and committees and town councils. Other steps may include cadastral surveys, removal of exemptions, and heavy penalties for non-utilisation of plots.

On the expenditure side, the burden of interest payments would be eased by reducing the policy rate if inflation remains under control. Other savings would accrue from targeted subsidies for food, energy and fertilisers.

Restructuring the federal and provincial governments, reducing surplus manpower, and privatising loss-making state-owned enterprises (SOEs) will also bring considerable savings.

On the development side, increased recourse to public-private partnerships for infrastructure projects should be encouraged. Public expenditure should be raised for research and development in agriculture, industry, climate change, digital infrastructure, technical and vocational training, etc.

Inequitable burden-sharing between the Centre and provinces can be alleviated by adopting an integrated approach to the management of public finances. The budgetary framework and assignments to the federal and provincial governments (without disturbing the NFC award) should reflect national priorities and targets, approved and monitored by the National Economic Council.

Devolution of Local Govts

A common citizen's daily life revolves around livelihood, education of the children, health care for the family, safety and security, clean drinking water, sewerage, transport, etc. Most of these functions are discharged best at the local level.

Mobilisation of local resources is much easier as the perceived benefits are visible. The Constitution has defined the third tier of the government without a separate schedule defining the functions of the local governments.

Such a schedule needs to be inserted in the Constitution. Following that, the NFC award would make allocations for the federal, provincial and local governments separately.
Major cities like Karachi, Lahore and Islam-abad can generate their own revenue through financial decentralisation, while NFC allocations should consider poverty and human capital investment, rather than population size alone.

Energy Sector Reforms

The energy sector has become a major hurdle for industrial and export growth and is unaffordable for middle-income consumers. The transit towards a competitive market for buyers and sellers should be brought to culmination by privatising distribution companies (Discos) or placing them under management contracts, with the returns contingent upon performance-linked indicators.

Private retail companies would work towards increasing the connections for power so that capacity payments are reduced. A politically tough decision to do away with uniform pricing throughout the country would have to be taken.

Targeted subsidies for energy should be managed through the Benazir Income Support Programme (BISP), ensuring only those in need benefit. Expanding transmission capacity, decommissioning inefficient public-sector generation companies, and restructuring gas distribution companies are also critical steps for energy sector reform.

Civil Service Reform

The capacity and capabilities of more than three million civil servants is Pakistan have eroded over time and weakened the institutions of governance. The reforms aimed at producing merit-based competent professionals of high integrity responsive to the public needs have been designed.

The entire civil service structure, from recruitment to compensation, must be modernised, with a focus on reducing unnecessary staff and incorporating domain experts into high-level positions. Equality of opportunity, transparency and promotion and compensation-based performance should be the hallmarks of the modern civil service.

Finally, transitory movements such as a fall in oil prices, increased liquidity or a decline in global interest rates should not deter the policymakers from pursuing the above agenda vigorously and uninterruptedly.

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