What major Economic Challenges are being faced by Pakistan? What recommendation do you suggest to deal with these issues.

Introduction

In contemporary times, Pakistan faces the challenges of an unprecedented economic crisis. Depleting reserves, declining exports, and reduced economic activities are mounting on to the state's financial instability, with negative socio-economic implications for the general populace. The current crisis has been backed by various domestic and external factors not limited to advanced economics, but also political instability, youth bulge and enviornmental hazards.

Major Economic Challenges being faced by Pakistan

Political Instability

An economy cannot strive without political stability. However, Pakistan has found itself in the midst of political instability since its insception, ~~by~~ as a result of power tussels, deteriorating civil-military relations and populism. Similarly, the successful vote of no confidence in 2022, followed by dissolution of Punjab and kp assemblies ~~revived~~ led Pakistani politics into further instability. Moreover, the launch of protests instigated populism across the state, and the use of force launched by the government further impacted the state's political standing. As a result, the stock exchange was hit, dollar reserves fell and foreign investors left the country. These factors collectively contributed to the challenges faced by Pakistan's economy; however, political instability was the main instigator.

Shrinking Foreign Direct Investments

Factors like political instability have impacted the FDI in Pakistan, resulting in an economic challenge. According to the State Bank of Pakistan, FDI in the fiscal year 2022-23 declined by 25% in comparison to the previous year. Furthermore in an year-on-year basis, the FDI dropped by 58% to $114 million in June 2023, compared to $271 million in June 2022. This factor is significantly impacting the economic might of Pakistan, causing it to have a lower investor interest in the market. This problem is also fueled by the import-led growth and current account plus fiscal deficit of the state.

Balance of Payment Crisis

The shrinking FDI in Pakistan can be linked to its persistant balance of payment crisis, serving as a major factor hindering Pakistan's economic development. The state has maintained a consistent trade deficit every year, with the amount rising to $46 billion in the fiscal year 2022-2023. This is due to the massive imports of hydro-carbon, as in 2022-2023 alone, $23 billion worth of hydro carbons - coal, oil, LNG - were imported. As a result, the state has become ~~entrinch~~ a victim of an economic crisis, where current account defecit is mounting, the value of PKR is declining, and the dependency on loans is increasing.

Reduced Economic Activity

A major factor backing the balance of payment crisis and pushing Pakistan into an economic crisis is the reduced economic activity. Pakistan has faced multiple set backs to industrialization, like the nationalisation of steel, textile, food, and automobile industries. As a result, private sector competition was discouraged, and industrialisation leading to enhanced economic activity was halted after the 1960s. Furthermore, the electricity crisis led to the shutting down of 200 industrial units across Pakistan, like, Toyota, Honda and sports industries. This crisis was further instigated by the shift of 35% of textile units into Bangladesh from 2007-2016, shutting down of 80% of the cottage industry, along with the leather industry in Faisldbad. Thus, lack of industrialisation has resulted in reduced economic activity across the state.

Sluggish Taxation System

Along with the lack of industrial development and inability of ~~maintaing~~ maintaining balance of payments, the taxation system of Pakisan adds further weight to the economic crisis of Pakistan. Pakistan's taxation system is ineffective and leaves out entire sections of the economy. The tax to GDP ratio continues to hover around 10% of the GDP. Furthermore, sectors like agriculture remain undertaxed, despite contributing nearly one fifth of the GDP their tax revenue accounts for less than 1% of the national tax revenue. Reduced revenue is generating a fiscal deficit, whilst negatively impacting the economy of Pakistan.

Pakistan and the Pension Bomb.

Apart from taxation and low revenue, the pension bomb is also hitting the economy of Pakistan. Over the last 12 years, Pakistan's pension's budget allocation has gone up by 500% exclusive of provincial pensions. In Budget 2023, Rs 761 billion were allocated for federal employees, and it was a 25% increase from 2022. The pension budget is adding up as a liability for the economy of Pakistan, which does not have a sustainable future. In other states, pension funds are set up as a retirement benefit, which avoids financial burden on the state. Pakistan is already struggling in terms of balance of payments, industrialisation and taxation, thus pensions are adding fuel to an already str

Flood Damage and Economic Loss in Pakistan

Lastly, Pakistan ~~is~~ has been a victim of various economic challenges, and the 2022 floods created chaos and further economic loss. According to the World Bank, the estimated total damages in Pakistan exceed \$ 14.9 billion, and \$15.2 billion in economic losses. Moreover, 2.2% of the GDP was directly impacted, with the agriculture sector at 0.9%. These damages had spillovers in terms of industry, external trade and service sectors. As, ~~food~~ floods impacted the production of green chilli, rice and cotton, plus the land could not be prepared for future crops. Resultingly, food shortage arised and exports had to be increased, which further impacted the trade deficit of Pakistan, and hindered any potential Development.

How to Deal with the Major Economic Challenges of Pakistan

Imposition of Protectionist Measures

In order to deal with the economic challenges, Pakistan needs to address the balance of payment crisis and trade deficit. An approach towards that direction can be marked as protectionist measures through short-term tariff and non-tarrif barriers. In this manner, local industries can be empowered to meet the local demands. However, the significance of free trade in the liberal world order, along with policies of the IMF and World Trade Organisation, may serve as obstacles in that directions. Hence, other avenues should be explored as well.

Decrease in the import of Hydro-Carbon

Moving forward, in order to address the mounting trade defecit, Pakistan should decrease the imports of hydro-carbons. Instead, in order to meet the local energy needs, local energy projects like dams should be installed. Throug this, imports are expected to be cut by $8-10 billion, which is address 20% of the deficit. Hence, Pakistan needs to invest in energy projects that will meet the hydro-carbon needs of the state.

Increase Production Base

Other than decreasing imports, Pakistan also needs to focus on local production in order to eliminate the need for extensive imports. NO country can transition into predominant exports without industries. Pakistan's strength lies in the textile industry, and the production increased to above $19 billion in 2021. This was a result of reducing electricity cost, subsidaries to import latest machinery. and reduction in GST tax. Such measure should continue, and Pakistan should focus on the electronics industry as well. In

2020, the government decided to form four IT cities in Islamabad, Lahore, Karachi and Haripur. However the progress needs to be sped up. Moreover, manufacturing of ~~mo~~ products should be targetted, since Pakistan is currently only assembling products locally. Similarly, spare parts should be produced in Pakistan for the automobile industry, sports industry should be diversified and on the agriculture front cotton should be revived. Moreover, in order to promote wheat production seed development should be promoted plus modernisation of agricultural techniques. Lastly, livestock should be promoted for leather milk and wheat production.

Acquire loans with easier Terms and Conditions.

The fact of the matter is that Pakistan currently lacks the capacity to develop its industrial might, ~~to~~ and extended loans will be required. However they should be obtained on easier terms and conditions, in order to ~~&~~ retain a financial breathing space for reforms. As, usually, Pakistan traps itself in a cycle of debt, making reforms difficult. Through the acquired loan Pakistan should focus on reforming its industrial and agricultural potential. Moreover, tax and pension reforms should also be undertaken, to reduce the financial burden ~~&~~ on the state.