

QUESTION NO # 01

What major economic challenges are being faced by Pakistan. What recommendations do you suggest to deal with these issues?

"The economy is the start and end of everything. You can't have successful educational reform or any other reform if you don't have a strong economy."

~ David Cameron

Pakistan an underdeveloped country faces several significant economic challenges that impede its growth and development. These challenges include low economic growth, fiscal deficits, energy crisis, regulatory hurdles, limited access to finance, lack of research and development (R&D), taxation issues, export concentration, infrastructure challenges effectively. A comprehensive approach is needed, encompassing economic reforms, fiscal management, energy sector reforms, regulatory simplification, improved access to finance, investment in research and development, tax reforms, export diversification, infrastructure development and policy consistency. By addressing the challenges

that causes economic crisis and implementing recommended strategies Pakistan can pave the way for sustainable economic growth, enhance its competitiveness in the global market and create a conducive environment for investment and development.

MAJOR ECONOMIC CHALLENGES BEING FACED BY PAKISTAN:

Pakistan has been grappling with a range of economic challenges for several decades. Following are the major economic challenges being faced by Pakistan -

i- FISCAL DEFICIT AND BUDGETARY PROBLEMS IN PAKISTAN:

The fiscal deficit in Pakistan occurs when government's total expenditure exceeds its total revenue. It is an indication of the total borrowing needed by the government. Pakistan has consistently struggled with a high fiscal deficit, leading to increased borrowing and debt servicing costs.

⇒ Causes of Fiscal deficit:

- - Excessive government subsidies:

The government often engages in excessive spending, especially on subsidies and non-developmental expenditures, leading to a widening fiscal deficit.

- - Inefficient Tax collection:

Pakistan's tax collection system is inefficient and

suffer widespread tax evasions, resulting in lower than expected revenues and contributing to the fiscal deficit.

•- Dependence on Borrowing:

The government relies heavily on borrowing to finance its expenditure, which increases debt servicing costs and exacerbates the fiscal deficit.

ii- Budgetary Problems:

The fiscal deficit is a critical economic indicator that reflects government's financial health and its ability to manage its budget effectively. Fiscal deficits contribute to inflationary pressure, crowding out private sector investment by absorbing available funds from the market and also raising debt sustainability. Moreover, budget constraints resulting from fiscal deficits may lead to reduced ~~from~~ funding for essential public services such as healthcare, education, infrastructure, and social welfare programs resulting into the negative impact of the services quality provided to the population.

Persistent fiscal deficits and budgetary problems can erode investor confidence and lead to credit rating downgrades. A low credit rating makes it more expensive

for the government to borrow in the future, further exacerbating the debt burden. The total government debt increased by Rs 58.999 trillion with Rs 36.55 trillion from domestic sources and Rs 22.050 trillion from foreign sources.

ii- Lack of diversification of Export Basket:

.. Overreliance on Traditional Sectors:

Pakistan's export basket is heavily concentrated in a few primary products such as textiles, and agricultural commodities. This overreliance on traditional sectors makes the economy vulnerable to external shocks, global price fluctuations, and market demand fluctuations.

.. Limited Access to High-value Markets:

The lack of diversification limits Pakistan's access to high-value markets that demand specialized or high value-added products.

This restricts the country's ability to tap into lucrative export opportunities and maximize export earnings.

.. Vulnerability to External factors:

Relying on a narrow range of exports makes Pakistan susceptible to external factors.

beyond its control, such as changes in global demand, trade policies of importing countries, and fluctuating in commodity prices. This vulnerability can expose the economy to risks and uncertainties.

•- Reduced Competitiveness:

A lack of diversification can hinder Pakistan's competitiveness in the global market. Without a diverse range of export products, the country may struggle to differentiate itself from competitors, innovate in new sectors and capture emerging market trends.

•- Limited value addition:

Focusing on limited set of export products may restrict opportunities for value addition and product differentiation. Diversification into higher value-added products can enhance export earnings, create employment opportunities and drive economic growth.

iii - Tax Reforms and Revenue Collection challenges.

•- Tax Evasion and Informal Economy:

Pakistan faces significant challenges in revenue collection due to widespread tax evasion, a large informal economy and underreporting of income. Many individuals and large businesses engage in

tax avoidance practices leading to revenue leakages and reduced tax compliance.

A report by the International Growth Centre estimated that tax evasion costs Pakistan PKR 1.7 trillion annually.

•- complex tax system:

The complexity of Pakistan's tax system with multiple taxes, exemptions and loopholes complicates the tax collection process.

Inefficient tax administration and enforcement mechanisms further hinder effective revenue collection.

•- low tax compliance:

Low levels of tax compliance among taxpayers, both individuals and business, contribute to revenue collection problems. Pakistan also struggles with a low tax-to-GDP ratio. According to the Federal Board of Revenue (FBR) reported that the tax-to-GDP ratio was 10.3% as of June 2023.

(source: Federal Board of Revenue)

IV - Energy Crisis and Infrastructure challenges in Pakistan:

•- Energy crisis:

Pakistan faces a persistent energy crisis

characterized by power shortages, inadequate supply and unreliable electricity access. The energy deficit has severe implications for the economy, leading to disruption in industrial production, reduced investment attractiveness, and hindered economic growth. The energy crisis has resulted in a loss of \$82 billion in GDP between 2007 and 2020.

According to the World Bank, the energy crisis in Pakistan is estimated to cost the country \$8.8 billion in GDP losses in 2022-23. This represents 3.8% of GDP.

The factors contributing to energy crisis includes insufficient energy generation capacity, reliance on costly imported fuels, transmission and distribution losses and inefficiencies in the energy sector.

-- Infrastructure Challenges:

Pakistan's Infrastructure sector faces various challenges including inadequate transportation systems, energy shortages, limited access to reliable telecommunication services, and insufficient logistics networks.

The Global Competitiveness Report 2023 ranked Pakistan 106 out of 141 countries. These Infrastructure deficiencies hinder foreign direct investment (FDI) inflows, impede

industrial growth and constrains ^{economic} growth and development.

Addressing infrastructural challenges is crucial for enhancing connectivity, reducing production costs, and improving the competitiveness of Pakistani Industries in global markets.

V- Unemployment and Underemployment in Pakistan:-

•- Unemployment:

Unemployment remains a significant challenge in Pakistan, with a large portion of the population unable to secure gainful employment opportunities. High levels of unemployment lead to economic instability, social unrest, and reduced living standards for individuals and families.

The unemployment rate is 7.1% in Pakistan. The factors contributing to unemployment include limited job creation, mismatch between skills and job requirements, inadequate investment in labor-intensive sectors and a growing working-age population outpacing job opportunities.

•- Underemployment:

Underemployment is a prevalent issue in

Pakistan, where individuals are employed in jobs that do not fully utilize their skills, education, or potential. Underemployment often results in lower wages, job dissatisfaction, and reduced productivity. Many workers in Pakistan are engaged in informal or low-paying jobs that do not provide adequate income or job security. Out of 71 million total labor force, only 67 million is employed and 4 million unemployed.

VI- Policy Inconsistency Problems:

Policy inconsistency refers to the lack of coherence, continuity and predictability in the formulation and implementation of government policies in Pakistan. Inconsistent policies can create uncertainties for business, investors and other stakeholders, leading to inefficiencies, reduced confidence and hindered growth of economy. Addressing policy inconsistency is crucial for promoting stability, attracting investments and fostering sustainable development in Pakistan.

VII- External Imbalance and Exchange Rate Volatility in Pakistan:

-- External Imbalance:

Pakistan faces a challenges related to external imbalances, characterized by mismatches in its trade, current account, and capital account balances. Persistent external imbalances can lead to vulnerabilities in the economy, including reliance on external financing, fluctuations in foreign exchange reserves, and exposure to global economic shocks. The factors contributing to external imbalance dependency and fluctuations in international commodity prices.

-- Exchange Rate Volatility:

Exchange rate volatility refers to the fluctuations in the values of the Pakistani rupee relative to foreign currencies, such as US dollar and the Euro. High exchange rate volatility can have significant implications for the economy affecting trade competitiveness, inflation rates, foreign investment inflows, and debt servicing costs. Factors contributing to exchange rate volatility include external shocks, speculative activities in the foreign exchange markets, changes in global economic conditions and policy uncertainties.

SOLUTIONS TO DEAL WITH ECONOMIC CRISIS:

* Addressing Fiscal deficit and Budgetary Problems
To deal with fiscal deficit and budgetary problems, Govt. should prioritize spending on essential services, develop a sustainable debt management strategy, strengthen the budgetary process, and implementing policies that stimulate economic growth and develop a comprehensive long-term fiscal plan to address structural issues and promote economic stability for sustainable growth and development.

* Addressing lack of Export-Diversification.
Diversifying the export basket can boom the economy. This can be done by focusing on value addition in existing export sectors to move up the value chain., Identify and target new export markets that offers opportunities for diversification, and by improving trade facilitation.

* Tax Reforms to Address Revenue Collection Problems:

In order to increase revenue collection government should streamline the tax system

by reducing the number of taxes, enhancing tax compliance, improving tax administration, and broaden tax bases resulting in the development of economy.

* Addressing Energy Crisis and Infrastructural reforms.

To tackle the energy crisis and infrastructure challenges effectively, Pakistan needs to adopt an integrated approach that combine short-term measures with long-term strategic planning. This approach should include energy sector reforms such as enhancing energy generation capacity, improving transmission and distribution efficiency, diversifying energy sources and promoting renewable energy resources.

For Infrastructural developments; reforms are prioritize investments in transportation networks, logistic infrastructure, energy generation and transmission.

* Addressing Unemployment and Underemployment

To address unemployment and underemployment government should emphasize on youth empowerment, labor market reforms, job creation, development of skills by investing in education and vocational training.

programs ultimately create a more inclusive and dynamic labor market that provides opportunities for all segments of the population, fosters economic growth and enhances social well-being.

* Addressing Policy Inconsistency problems:

Policy Inconsistency problems are addressed by transparent policymaking, coordination, long-term planning and effective monitoring. Pakistan can create more stable, predictable, and conducive policy environment for business, investors and other stakeholders. Consistent and coherent policies are essential for promoting economic growth, attracting investment and fostering sustainable development in Pakistan.

* Addressing External Imbalance and Exchange rate volatility.

By implementing targeted strategies such as export diversification, foreign exchange reserves management, exchange rate stability and structural reforms; external imbalance and exchange rate volatility can be managed. Pakistan can enhance its economic stability, improve its external position and create a conducive environment for sustainable growth and development.

Conclusion:

Pakistan faces significant economic challenges and addressing these challenges requires a multi-faceted approach that includes job creation, export diversification, policy consistency and infrastructure reforms. By implementing these recommendations, Pakistan can enhance its economic resilience, attract investments and foster sustainable growth. Collaboration between the government, ~~and~~ private and other stakeholders is essential to navigate these challenges and pave the way for a more prosperous and inclusive economy in Pakistan.