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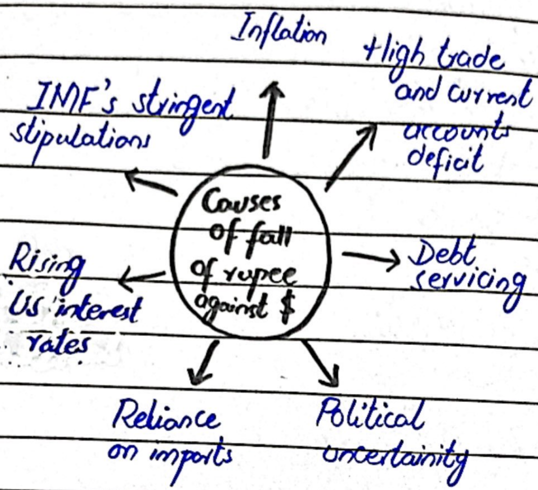
Rupee has been seen going down the slope as its falling against dollars with each passing day. What factors are responsible for soaring dollar rate? Write possible wayouts to stablize the currency?

1/ Introduction

The Pakistani Rupee has been on a downward trend, depreciating against US dollar at an accelerating rate. This going down is driven by many factors including high trade deficit, reliance on imports, low foreign direct investment and rising of global interest rates. To address this situation it is crucial to explore underlying reasons and consider strategies to stabilize currency.

2/ Causes of Rupee fall against US dollar



(A) High Trade and Current accounts deficit

Pakistan has been facing significant trade deficit due to high imports and less exports, Leading to trade defict. This results in higher dollar outflow and less dollar inflow.

$\boxed{\text{\$ inflow}}$ → Trade deficit 17.7 billion dollar → $\boxed{\text{\$ outflow}}$

↓ $ 25.7 billion — $ 43.4 billion ↑

$\boxed{\text{FY 2023-24}}$

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(B) Debt servicing causes fall of rupee

Debt servicing requires significant dollar outflows, reducing reserves and weakening rupee. On average **36%** of budget is allocated to debt servicing.

FY 2022-23

The total budget was **9 trillion pkr** and **4.7 trillion pkr** was allocated to debt servicing.

(C) Reliance on imports leading to dollar outflow

Pakistan depends highly on imports. With rising global prices, especially of oil, demand for dollar increases, driving rupee down.

July-March FY2024: Imports of Petroleum products were 11,047 thousand tonnes

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(D) Political uncertainity deters foreign direct investment

Political uncertainity creates an environment of risk, leading to low foreign direct investment, weakening the rupee.

July - April FY2024

FDI inflows = $1.5 billion

(E) IMF's stringent stipulations devaluing rupee

IMF has set rule for Pakistan that difference between dollar's exchange rate in interbank of Pakistan and open market should not exceed **1.25%**. The State Bank of Pakistan has to maintain a strict difference. If dollar demand is high but can not be met in open market, it creates supply gap. People try to seek dollars from Black Market where rates can be even higher, indirectly pressuring rupee down.

(F) Inflation impacts Currency confidence

Faced with historically high inflation people tend to hedge against rupee's fall by keeping savings and pensions in dollars. This increases dollar demand and value and weakens rupee.

Source:-

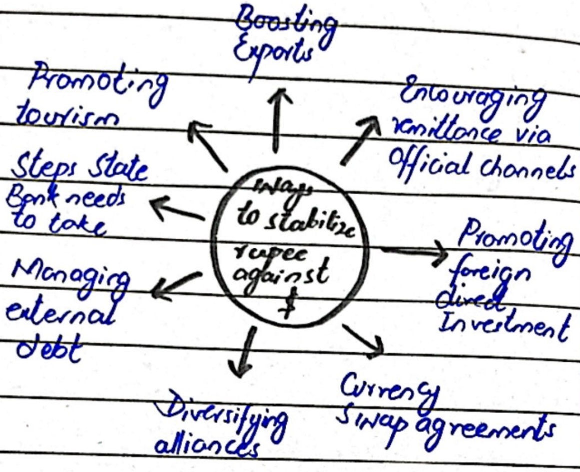
Economic Survey of Pak 2023-24

Inflation in May 2024 = 11.8%

(G) Rising US interest rates draws investors away

Higher interest rates in US attract global investors seeking better returns leading to capital outflow from Pakistan.

3/ Possible Solutions to stabilize the Rupee



(A) Boosting Exports and reducing imports

Enhancing exports and reducing dependence on non essential imports can balance trade and stabilize rupee.

(B) Promoting foreign direct investment through incentives

Attracting FDI by offering tax incentives can bring dollars to Pakistan, supporting rupee.

(c) Encouraging remittances through official channels

Streamlining remittance processes and lowering transaction fee can increase dollar inflows, strengthening rupee.

(d) Currency Swap Agreements can strengthen Rupee

Currency swap agreements during bilateral trade can help Pakistani rupee to stabilize.

Currency swap agreement (for 3 years)

China's Central Bank $\xrightarrow{\text{30 bn Yuan}}$ State Bank of Pak

State Bank of Pak $\xrightarrow{\text{Rs 1.18 trillion}}$ China's Central Bank

Source:- (The state council) PRC (16 oct 2024)

(E) Managing external debt can stabilize rupee

Renegotiation debt terms and cautious borrowing can lower debt servicing

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costs.

(F) Diversifying alliances

Pakistan should look forward to strengthen its tie with oil exporting countries at friendly prices.

(G) Steps state Bank of Pakistan needs to take to strengthen rupee

States Bank of Pakistan should take proactive measures in commonikating to market in order to mitigate unnecessary panic driven dollar purchases, assuring stability.

(H) Promoting tourism can increase inflow of foreign currency

Promoting Pakistan's tourism sector could provide a steady flow of forign currency, supporting rupee.

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4/ Conclusion

The conundrum of devaluation of rupee is mainly due to trade deficit, debt servicing, reliance on imports, inflation and low foreign direct investment. This ailment can be cured by attracting foreign investment, promoting tourism, restructing external debt, currency swap agreement and boosting exports.