

**NATIONAL BUDGET 1990-91:
ECONOMY POLICY PERSPECTIVE**

PRESS CONFERENCE

Islamabad

26 May 1990

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1. The Federal Budget for 1990-91 is due in the first week of June. The budget, which lays the fiscal policy of the Government, basically guides the course of economic activities in the following year, though it also exerts some long term effects through new taxation measures and development schemes.
2. The fiscal mismanagement has now become a norm rather than an aberration. The process of fiscal policy formulation has gradually drifted out of the hands of our planners and now firmly rests in the hands of international lending institutions. Nation's economic sovereignty has been seriously compromised and the present regime must be taken to account for that. With this, let me warn in clear and categorical words that it may not be surprising if sooner or later the country meets the same fate which is met by some of the Latin American countries, where after such take over's economic conditions have fast deteriorated into hyper-inflation and bankruptcy.
3. No doubt, we are still far away from this kind of a scenario. However, there is nothing in sight which could indicate any reversal from following this course. This budget is being presented in this perspective and we must lay the ground work for reversing the present state of fiscal mismanagement. To this end it will be useful to correct perceive the fundamental economic problems the nation is facing at the moment.
4. In the last two years the country has lost the price stability that it has maintained during most of the decade of 80's. Although price indices have depicted much lower rates of inflation, the common perception puts the rates anywhere between 12-18 percent. Apart from fiscal mismanagement, the basic cause of this inflationary trend is the decline in the productive activity as well as in the level of investment. Both of these are confirmed by a decrease in the GDP, which has averaged around 5a percent during the last two years, against the average of over 5 percent achieved in most of the 80's. This is despite the fact that no major natural calamity has hit the agriculture sector which has performed generally well during these two years.
5. The most important reason behind the decrease in production is the continuously deteriorating law and order conditions in Sind, particularly in the industrial cities of Karachi and Hyderabad. It is difficult to estimate the amount of lost production on this account, but it is significant enough to reflect both in the decreased amount of manufacturing output as well as revenue collections (during March 1989- March 1990, the total revenues including surcharge on gas and petroleum increased by only 6.8 percent compared to the growth rate of 18.4 percent in 1989-90).

6. The investment climate has been affected by the standing problem of huge Government borrowings from the domestic market at exorbitant interest rates. Even though the rate of interest on Khas Deposit has been lowered, it still remains the most effective instrument of resource mobilization for the Treasury. The non-bank borrowings are constantly depriving the private sector from obtaining the needed funds for their planned investment. The presence of high rates of return on such scheme' also acts as a disincentive for investors who would not want to take the trouble of setting up industrial units.
7. Unless the trend of declining production and investment is arrested the country would face stronger inflationary pressures in which case the possibility of an accelerating inflation cannot be ruled out. These are further strengthened by the fact of continuous depreciation in the exchange value of the Rupee affecting cost of imported inputs.
8. The most poignant reflection of fiscal mismanagement is the emergence of a permanent deficit in the Federal Budget. Of course the problem has evolved over the last decade, but the fact remains that except for the last two years there has always been serious concern shown by the policy makers and efforts were made to reverse the trend. For example in the budget for 1988-89, a small surplus was envisaged and it was planned that during the 7th Plan period the current account deficit would be completely eliminated. However, all this was changed after the assumption of power by the present Government. The problem of current account deficit is becoming acceptable to the fiscal managers of the Government. The only concern is to maintain the overall deficit within the limits imposed by the IMF. And whatever evidence is so far available, there is no hope to meet that too in the current fiscal year, while the prospects of striking a deal with IMF are dismal.
9. It is estimated that year the current account deficit, without discretionary measures, would be anywhere Rs. 15-23 billion. This would make overall deficit in the range of Rs. 70-77 billion. Undoubtedly, an unbearable economic hardship would be inflicted on an already burdened people with this kind of gross fiscal mismanagement. Even worse, there would be no hope that tomorrow would be any better. For the entire development budget is financed through domestic and foreign borrowings, and the mounting public debt would pose a greater fiscal problem in subsequent years in the form of rising interest payments.
10. It is difficult to over-emphasize the seriousness of the problem of fiscal mismanagement. It has already drifted out of our hands and in the absence of concerted efforts for its rescue it will permanently rest in alien hands.
11. The problem of budget deficit is basically a problem of mismatch between revenue and expenditure. The Government' has not been able to mobilise the needed resources to meet the growing demand on its expenditure. The growth of Government revenues has stagnated

around 16-18 percent of GDP while the expenditure has continued to rise, which obviously gives a rising deficit in the current account.

- 12.** The stagnant level of revenues is the basic result of a highly inefficient system of taxation that is totally incapable to meet the demands placed on it. In fact, the system has not been designed as instrument of resource mobilization. It is essentially an instrument of repression and harassment in the hands of the Government. It is characterized by a complete disregard of ability to pay and heavily biased against the poor sections of the population by its overwhelming concentration in the form of regressive indirect taxes. The entire system of taxation is rampant with loopholes and exemptions reducing drastically the effectiveness of the system.
- 13.** A number of commissions have been set up in the past, -but not a single report was ever implemented to reform the system. The report of the National Taxation Reforms Commission of 1985 is the most recent of all. Two Committees of the Parliament have also prepared reports on the Commission's report. These reports, particularly the Committee of the Senate, have conclusively shown that the present system of taxation is totally incapable to meet the resource mobilization needs of the country and unless major revamping and restructuring to the system is done along the suggested line in the near future, the state of fiscal mismanagement would worsen beyond repair.
- 14.** It is ironic that in the face of such grave dangers that the country is facing in its fiscal policy, the present Government has not shown any desire to make use of the NTRC report and the Reports of the Senate Committee. Rather it has gone to compromise country's sovereignty by assigning the revenue collection to foreign agencies and is planning to introduce yet another complex General Sales Tax law without cleansing the oppressive ability of taxation machinery. This would be highly unproductive. The legislation should be adopted with the consensus of both the parliament and the business community and preferably should form part of a general plan to reform the taxation.
- 15.** The other side of fiscal mismanagement is the continuously rising Government expenditure in the face of declining rate of (built in) growth in revenues. The Government expenditure has increased to more than 20 percent of GDP, There is no justification of at least rising expenditure when the corresponding increase in revenues cannot support.
- 16.** The rising level of expenditure is in fact a manifestation of yet another evil in our society: the unbridled proliferation of Government institutions and influence in our public life. Since the time of Nationalization, the Government has become the single all too important political and economic giant in the country. At present consumes more than 25 percent of GDP. Its regulatory and directs influence is all pervasive. There is absolutely no economic activity which could be pursued without the active involvement of one or more of

Government agencies capable to strangle it to death in almost arbitrary fashion. And all of this is done at the expense of public exchequer.

17. The country badly needs a massive cut in bureaucracy and regulatory functions of the Government. More importantly, there is a dire need for an almost complete ban on future expansion of public sector enterprises in the country. In fact there should be efforts to disinvest the public sector enterprises. It is unfortunate that even though one of the most important promises of the present Government was to privatize the public' sector units, no significant progress has been made so far. The recently announced decision to sell the shares of PIA smack of complete failure of the original thinking, A mere call of about Rs. 250 million share capital through general public could hardly be termed as privatization. If this is what was meant by the whole programme then it does not amount to more than a device to fool the general public.
18. Another manifestation of fiscal mismanagement is the staggering level of public debt. The public debt is the sum of both domestic and foreign debt. The size of the debt which was hardly Rs. 300 billion until 5 years ago has risen exponentially to a level of about Rs. 700 billion. Interestingly, the share of domestic debt in the total has long surpassed that of foreign debt. This is indicative of the heavy reliance Government is placing on non-bank borrowings (mostly through National Savings Schemes) to finance its overall budget deficit.
19. The dangers inherent in such a high level of public debt are reflected in the ever-increasing amount of interest payments which appear in the current account of the budget. This has now become the single most important item in the budget, surpassing the level of defence expenditure. This year it will be above Rs. 60 billion.
20. Incidentally, the continuously rising interest payments reflect a debt-trap in which some confirmation for this view is evident from steep decline in the flow of net transfers in the country, which stood at below 16 percent in 1988-89. Similarly, the gross mobilizations from non-bank borrowings are almost double the net mobilization (i.e. net of retirement; with the addition of interest payments the net mobilization would further decrease.
21. The trends in fiscal policy presently observed suggest that not much is being done to curb the level of public debt. This is a highly explosive situation, which can drift into a collapse of public confidence on Government's real ability to pay its obligations.
22. The solution of the problem lies in fiscal discipline that Government would have to introduce sooner or later. Here again, as we said earlier, the opportunity offered by the extension of Sharia Court's jurisdiction over fiscal matter should not be missed. The repudiation of Riba has the promise of becoming a viable alternative available to the Government for ridding the nation of this fiscal mess. Serious planning to bring about this

transaction to a new monetary and fiscal system represents one of the most pressing challenges of Pakistan's economy today.

23. I also want to warn that the Banking Sector of the country is in the throes of a crisis. There is no merit in ignoring at this situation. World Bank has warned that bad debts swelled to about one percent of the GDP, and have even suspended or line to some of the DFIs. Nationalized banks are showing only through accounting tricks of carrying over bad and unrecoverable debts. The operating costs of banks are unrealistically high and there is a lot of dead even rotten wood that goes to make their work free. Loans are being given on political considerations and represent a dangerous form of corruption. If something is not done urgently, the country is heading towards serious trouble.
 24. Another important issue that can no longer be swiped beneath the carpet is that of economic relationship between the Centre and Provinces. Real provincial autonomy has not been allowed. The un-economic policy of Centre's picking up of provincial deficit has proved to be futile and counter-productive. Proper economic authority as visualized in the Constitution should be transferred to the provinces without delay. National institutions of NFC and CCI should be made operational. Provinces should be given the authority to mobilise their own resources and be responsible for their effective utilization.
 25. The next budget must also squarely face the question of elimination of 'Riba' from the economy. Last five years have been wasted in a criminal manner and whatever progress had begun towards elimination of interest from the economy has been undone. Yet the issue cannot be ignored, particularly in view of the extension of the jurisdiction of the Federal Shariat Court to monetary and fiscal matters due in June 1990. This also constitutes a historic opportune. There is enough evidence to show that Riba is the root cause of fiscal mismanagement in the country. Over-emphasis on financial collateral eclipses the real economic viability of projects. Switch over from an interest-based relationship to an equity-sharing arrangement has the potential of streamlining the economy and ridding it of many of its weaknesses and contradictions.
 26. Finally, I want to pose the question that the PPP Government has now completed 18 months of its rule, almost one-third of its tenure. The next budget would be judged on the criterion of the PPP' manifesto which had assured establishment of a welfare economy with huge expansion of education, increase in literacy from 26% to 90% by 1993, construction of 500,000 cheap houses every year, better health, higher employment, more equitable distribution of wealth and income and greater availability of basic necessities and social amenities to all sectors of the population. Has the country come any closer to the targets? And can it really move in that direction with the fetters (IMF conditionalities) on its feet? The economic managers can no longer avoid answering these questions!
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