

## PAKISTAN INTERNATIONAL DONORS' CONFERENCE

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### I. INTRODUCTION

1. On behalf of the IMF, I want to offer my heartfelt condolences and sympathy to those who lost family or were hurt in this tragic event. As a Pakistani, the earthquake has affected me personally. The loss of lives and the suffering caused by the earthquake have been truly enormous. The Government of Pakistan, and the Pakistani people, have responded quickly, aided by the international community, through the agencies of the United Nations and directly. But the challenges posed by the sheer magnitude of the suffering and devastation, combined with the remoteness of the area and winter setting in, are huge. Further support is therefore very much needed, both for the ongoing relief efforts and for rebuilding. This conference here today provides potential donors with the opportunity to assure Pakistan of support at this difficult time. As a representative of the International Monetary Fund I would like to assure the authorities that the Fund is ready to assist Pakistan, with policy advice and help in updating the authorities' macroeconomic framework, as well as with financial support and technical assistance.

### II. RECENT ECONOMIC ACHIEVEMENTS

2. Let me briefly draw attention to some of Pakistan's economic achievements over the last few years, to get a picture of where the country stood before it was hit by the earthquake. These earlier achievements are now well known around the world, but it is worth reiterating the main points:

- First of all, persistent implementation of sound economic policies and broad-based structural reforms over the last five years has paid off, with the economy recovering convincingly from the crisis of the late 1990s. Growth reached almost 8½ percent last fiscal year, among the highest levels in the world.
- Fiscal consolidation and reform, coupled with international financial assistance, have put the budget on a sound footing and have resulted in an impressive reduction in Pakistan's debt burden, with the government debt-to-GDP ratio declining by 30 percentage points from its peak of 90 percent a few years back.
- Financial sector reform, privatization, trade liberalization, and deregulation have fundamentally transformed the economic landscape in Pakistan. They have improved private sector confidence, contributing to large inflows of remittances and foreign investment, and ultimately to higher growth.

- Personal incomes have risen, room for social spending has been increased, and, as a result, various health and education indicators, such as literacy rates, school enrollment, and immunization ratios, now show a significant improvement.
  - To some extent, the price of this economic success has been a pick up in inflation and a shift of the current account into a deficit. In response, the State Bank of Pakistan tightened its monetary policy, and this change in stance seems to have started to show effect.
3. All in all, Pakistan's prospects were very favorable. The country's successful re-entry in the international capital markets attested to its economic success. Even more importantly, Pakistan was much better placed than at any time during the past decade to absorb a major shock, as now posed by this massive earthquake.

### III. THE ECONOMIC IMPACT OF THE EARTHQUAKE

4. This brings me to what might be the impact of the earthquake on Pakistan's economy and how it has affected the overall outlook. The earthquake clearly had a devastating impact on the northern parts of the country. We know that, in addition to the large loss of lives, almost all houses, hospitals, schools, and other buildings and infrastructure in the area have been destroyed. Some 3 million people have been left without shelter. Recovery and relief efforts are estimated by the United Nations to cost some \$1½ billion. The rebuilding of lives will take time and much more money. The reconstruction cost are estimated at \$3½ billion over the next three years according to the assessment prepared jointly by the World Bank and the Asian Development Bank, with the help of the government and many other international organizations.

5. The earthquake is expected to have some adverse impact on Pakistan's overall economy, at least in the short run. It is true that the affected region accounts for a fairly small fraction of the country's output. Pakistan's main economic infrastructure—factories, ports, financial centers—was mostly unaffected. Similarly, Pakistan's main crops—cotton and wheat—are mostly grown in other parts of the country. Still, with economic activity having been virtually wiped out in the directly-hit areas, there will be some dampening impact on growth. Together with a somewhat less buoyant harvest of crops like cotton, growth in 2005/06 could be some ½ to 1 percent lower than the 7 percent projected prior to the earthquake. Eventually, however, as rebuilding activities get underway, growth may strengthen. Natural disasters destroy assets, and the process of restoring assets results in growth.

6. Relief and reconstruction efforts may result in some price increases. These can particularly occur in sectors where demand was already strong, such as construction, and to the extent that the additional demand cannot be met through higher imports. More of the burden to maintain macroeconomic stability will, therefore, fall upon monetary policy. The State Bank of Pakistan will need to remain vigilant to contain inflation and support the external position as public spending is raised.

7. Obviously, the relief and reconstruction efforts will affect the government budget. The relief and reconstruction efforts translate into an average cost of about 1–1½ percent of GDP per year in the next few years. Much will depend, of course, on the size and phasing of international support and whether this support will come in the form of grants or loans. As the Prime Minister has mentioned, Pakistan’s debt burden has been greatly reduced over the past five years, but at about 60 percent of GDP, the debt ratio is still high and, more importantly, the same holds true for the ratio of debt to government revenues. The provision of grants, rather than loans, at this conference would help to improve this position. At the same time, the authorities aim to redirect some of their development spending in the coming years to the rebuilding process, and the decision to postpone a major defense purchase creates additional room. But I also urge the government to continue to move ahead more forcefully with policies that could generate more resources, such as strengthening taxpayer compliance, broadening the tax base, and improving performance in the energy sector. For the current and next few years, however, the reconstruction efforts will surely put pressure on the fiscal position and could widen the budget deficit on average by about ½ percent of GDP per year. Fortunately, given the budgetary achievements of the past five years, this should not threaten fiscal sustainability.

8. A possible widening of the trade deficit due to the import of relief and reconstruction goods should be largely balanced by additional grants and loans, and possibly also by higher remittances. However, given the scale of operations, some pressures on international reserves could emerge, depending also on the availability and timing of the new grants and loans. As the Managing Director stated during his visit to Pakistan a week following the earthquake, the IMF is also ready to provide financial resources through the Emergency Natural Disaster Assistance (ENDA). ENDA is aimed at meeting foreign exchange financing needs of a country hit by a natural disaster. It is quick disbursing and the government only needs to present a statement on the general economic policies they propose to follow. A balance of payments need has to be demonstrated. ENDA is typically limited to 25 percent of quota, which for Pakistan would be about \$375 million. The maturity of ENDA loans is 3¼–5 years. PRGF-eligible countries, such as Pakistan, can request that the interest rate be subsidized down to 0.5 percent, subject to the availability of subsidy resources.

#### **IV. CONCLUSION**

9. In conclusion, I would like to emphasize that Pakistan’s economic future continues to look bright, despite the recent tragedy. But right now the authorities face the daunting task to address the needs of those affected by the earthquake, most urgently in the short run, by providing shelter, food, and medical care, but also in the longer run, by helping the survivors rebuild their lives. Pakistan needs and deserves the generous support of the international community in fulfilling this task. The IMF stands ready to do its part.