Pakistan: Options after the floods

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Shortage of funds leaves little room for the government other than either to slash development budget or seek foreign debts.

Cameras are turning off, newspapers spaces squeezed, official visits to flood areas reduced to almost none and attention by political parties and civil society groups is diminishing. Images of poor flood victims have already faded away from TV screens and reports from flood-hit areas and temporary shelters have almost taken out daily programmes. Lingua franca of policy forums has changed and already shifted to other government activities.

Thirteen million people are left to deal with their own pressing problems. It is also true that flood victims may find ways to cope with the situation and live a life with fewer demands. We know the reality will not change for a long time to come.

The economic and social effects will not go away for years to come and human miseries will remain for generations to suffer. The first and foremost effect of these floods will come in agriculture production cycle that is dependent on crops and health of those crops. Early signs of food, vegetables and fruit shortage in the market are being felt strongly by consumers. The next cycle will emerge after the Kharif crop is ready to be transported to the market.

The flooding has inflicted serious damage to the economy, posing another challenge for a cash-strapped government struggling to keep economic recovery on track amid high inflation and relentless insurgency. Assistance from the International Monetary Fund and other foreign institution will likely help Pakistan avoid bankruptcy as it tries to cope with the damage.

But the revival of agriculture and rehabilitation of farmers may take some time as the federal government and international community have not provided funds for the purpose. The total losses to the agriculture sector, estimated thus far, stand at about Rs43bn — with losses at Rs34bn and Rs7.35bn in the crops and livestock sectors respectively. A few billions more losses have been incurred by other agriculture sub-sectors for destruction or damages to assets and infrastructure.

Inundation of vast agricultural lands, destruction of irrigation channels and of thousands of tones of ready-to-use-seeds would not only impact crop production in the coming season but is likely to lead to food shortage and food inflation. The loss of around 0.2 million animals is very troubling in that farmers were deprived of source of income but it also would lead to shortage and price hike of animal-products like meat and milk.

Farming community faces a potential shortage of seeds and fertilizers in coming months. With thousands of tons of wheat and maize seeds having been washed away by floods and the wheat growing season to start next month, the government can also consider procuring and providing wheat seeds to farmers free of cost. Farmers have no seeds or money to buy the costly seeds from private vendors. If the problem is not solved immediately, there would be poor wheat crop which entails food security risk.

The increasing debt burden of farmers also needs immediate attention. Agriculture loans of all farmers, especially small and landless sharecroppers, should be written off or at least interest thereon should be remitted. The government should give easy farm and non-farm loans to small farmers to increase their incomes.

The economic distress triggered by the floods has radically changed gradually stabilizing the economic picture of Pakistan. Earlier this summer finance managers of the country predicted that economic growth may be slow, but some of the conditions will improve down the line. Maybe the crops will yield better results, they said. But less than three months into the financial year, all of them are worried that Pakistan's economic outlook is descending into chaos after the floods that caused widespread destruction.

The worst affected part of the economy is agriculture — which directly or indirectly provides jobs to more than half of Pakistan's population. Some government estimates say that the losses could be worth $43 billion, though external experts put the estimate more conservatively between $8-15billion. Whatever the final toll, it is clear that the losses have hit Pakistan's economy significantly.

Floods have forced the government to scale down expectations of Pakistan's overall economic growth to a range as low as 0-0.5 percent in the financial year, sharply below a target of up to 4.5 percent. Annual inflation is expected to jump to more than 18 percent, up from a target of below 10 percent.

The key challenges include an expected contraction of agriculture by more than 8pc, after more than a quarter of Pakistan's farmland was flooded and some of the main crops destroyed. The losses from agriculture have wider repercussions for Pakistan's economy, including trade and current account deficits that will be significantly higher due to increased food imports, and a budget deficit expanded by emergency government subsidies to put farmers back to work.

The economic loss will translate into "massive job losses" affecting thousands of families' incomes, which may have serious social implications. The overall performance of agriculture will be "much lower" this year and next year. The losses may have a snowball effect on manufacturing, services and export sector. Early signs of economic downturn are already visible in recent price hike and recession.

At issue is also the future of Pakistan's relations with some of its main foreign lenders, notably the IMF. In late 2008, Pakistan was forced to sign a two year loan of just over $10 billion, to tide over an expected balance of payments crisis. Even though the loan disbursement will be completed only by the end of 2010, the economic losses from floods have added to Pakistan's economic and financial woes.

The government has already begun negotiations with the IMF, to ease conditions tied to the existing loan or to refinance it with a new loan with easier terms but with little success so far. But recent assessment that economic performance is already off-track — even before the flood-related losses occurred — has increased strong criticism from critics over Pakistan's chronic failure to reform its economy.

Fiscal deficit for the last financial year (July 2009-June 2010) rose to 6.3pc of GDP, up from the government's target of 5.1pc, in an indication of continued mismanagement.

At the heart of the challenge lies a long-term failure to reform Pakistan's tax collection infrastructure, which has contributed to the missed targets for the fiscal deficit. In a country of about 180 million, less than one percent pay income tax and tax collectors repeatedly focus on this narrow group.

Market participants warn that without a forceful effort at financial prudence, the economy will deteriorate further. "Unless the fiscal issues are resolved conclusively and the budget situation improves and improves once and for all, Pakistan’s economic outlook will go through periodic challenges.

The need to mobilise domestic resources, especially after the floods, has already prompted finance managers in Islamabad to plan for a one-time tax for flood relief on members of Pakistan’s most affluent classes.

The number of people living below the poverty line will likely rise to 40pc of Pakistan’s population, up from about 33pc before the floods, a desperate situation which needs urgent measures.

There are fewer options for the Pakistani leadership as they have to cut down on their routine non-developmental expenditure. The shortage of funds in the wake of less enthusiastic international donations leaves little room for the government other than either to slash development budget or seek expensive foreign debts as has been witnessed in post-flood situation in the country. While the former harms development prospects as less development budget means less development and facilities for the people, the latter increases foreign debt burden and the budget deficit besides disturbing the balance of payments.

By Irfan Mufti