UNIVERSITA' DEGLI STUDI DI PADOVA

DIPARTIMENTO DI SCIENZE ECONOMICHE ED AZIENDALI "M.FANNO"

CORSO DI LAUREA MAGISTRALE IN ENTREPRENEURSHIP AND INNOVATION MANAGEMENT

TESI DI LAUREA

"HOW LIMITED AMOUNT OF FOREIGN RESERVES AND CURRENT ACCOUNT DEFICIT IS CONSTRAINING THE GROWTH OF PAKISTAN?"

RELATORE:

CH.MO PROF. LORENZO FORNI

LAUREANDA: RIDA TARIQ

MATRICOLA N. 2005939

ANNO ACCADEMICO 2020 – 2022

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INTRODUCTION

The primary objective of this study is to present a rationalised concept of foreign currency and current account deficit and how each of them affect the significant economic problems that the country is currently experiencing, such as a fluctuation of exchange rate, imbalance financial circumstances, and the government's frustration with its inability to exert control over the domestic money market. The "exchange rate" describes how much of a unit of a foreign currency can be purchased over a specified period with a unit of local currency. The rate of exchange, in more precise terms, is a conversion factor that establishes the rate at which currencies fluctuate in value. While the volatility of exchange rates suggests that the exchange rate is influenced by the supply and demand of a particular country's currency, the fastest-moving price on the currency market will ultimately set the exchange rate.

The presence of foreign money and solid exchanges lower growth in the economy because exports are more expensive, consequently reduced demand for exports. Imports are cheaper, forecasting higher demand for imported products. Consumption of goods and services, trade & services together account for most of the economy's output and significant growth. Pakistan's economic structure is more similar to that of middle-income countries in East and Southeast Asia than it is to that of the poorest countries on the Indian subcontinent, according to the World Bank.[1] The relationship between exchange rate and economic progress is obviously significant. The exchange rates of several developing nations have implicitly or explicitly fixed their own exchange rates to the currency of another country and whose inflation rates are higher than of the foreign country. Devaluation frequently results in recession and inflation, which pushes the economic situation of a country into an inflation devaluation spirals, resulting in a significant reversal in the pace of economic progress. Other developing nations grow at a blistering pace and frequently experience the opposite of this pressure upon their currencies. A high rate of economic growth is associated with a high rate of investment as well as a high rate of export growth. Banking system intervention in the currency market and developed foreign reserves leading to successful exports would result in current account surpluses, which will put pressure on the currency's nominal appreciation rate. Even if the intervention preserves the exchange rate stability, unsterilized intervention leads in inflation, and the exchange rate appreciates regardless of fixed exchange rate.

[1] The World Bank is a global financial organization that offers grants and loans to governments in low- and middle-income nations so they can carry out major projects.

Currency depreciations have an impact on policymakers' actions as well as the quantity of exports and imports in a given period of time. It also has an impact on the allocation of items for manufacturing, reserve money, exports, imports, and the balance of payments, among other things. Exchange rate volatility gives opportunities for domestic investors to buy in foreign currency to earn bigger profits, resulting in depreciation of the domestic currency and an appreciation of the foreign currency. Furthermore, the volatility of the exchange rate has a direct impact on the pricing of exported goods, reserve money, manufacturing products, and the growth rates of these industries. Trading and investing systems minimise the difference between the actual as well as expected value of the exchange rate. It is supported by traders and investors who prefer volatile exchange rates that allow them to maximise their profits by taking advantage of price fluctuations (Javed & Farooq, 2009).

1.1. Foreign Currency and Economic Growth

When exchange rates fluctuate, the value of imported items, particularly domestic ones that rely on import parts and raw materials, will fluctuate in value. Furthermore, exchange rates have an impact on investment performances, rate of interest, and inflation and they can even have an impact on the labour market and the real estate industry. When the dollar price increases, the price of domestic products and services rises, while the comparable price of international goods and services lowers. The shift in price levels will result in a fall in exports and an increase in imports from other countries.

The economic consequences of exchange rate fluctuations are one of the most contentious topics discussed in academic literature. Over the past few decades, the relationship between exchange rate changes and economic growth has emerged as the main important research subjects. In accordance with conventional wisdom, there is a strong association between fluctuations in the exchange rate and economic growth. As a result, depreciation of the local currency following an increase within exchange rate, affects both relative prices of exports and imports, encourages exports while diminishes imports. Thus, the rise in the value currency also converts the desires of foreigners who enter the nation and drive the import of goods and services into the country. This is true to the extent that a rise in exchange rates increases net export volume, which in turn has a positive impact on economic growth as a result of an increase in total demand. Structural economists, on the other hand, contend that the exchange rate & economic growth have an inverse relationship. Because the basic structure of production in developing nations is heavily dependent on imported capitals and intermediate products, a rise in exchange rates makes import manufacturing inputs more expensive and, as a result, has a negative impact on economic growth.

1.2. Current Account Deficit and Economic Growth

A current account deficit is a caution that an economy is unable to keep up to its competitive lead. Consumers prefer to purchase less expensive imports rather than consume more expensive domestically produced goods. During a period of rapid economic growth, import volumes normally increase, and if export volumes are insufficient to keep pace with the increase in imports, the account balance will be in debt. In contrast, if imports drop and exports, to stronger economies, increase during a downturn, the account balance will show a surplus. A country that has a big current account deficit is at risk and the value of its currency deteriorates in the short term. If there are insufficient capital inflows to cover the deficit, the currency rate will decrease in order to reflect the imbalances of foreign cash flowing into and out of the economy. A decline in the value of the currency will result in inflationary pressures for consumers and businesses that rely on the importation of raw materials. In the case of a current account deficit, foreign obligations rise in proportion to the deficit. At first glance, a current account deficit may appear to be just a deficit in the purchase of goods. However, the interest payment on the capital surpluses causes the deficit to grow over time, increasing the amount of money owed. Foreigners make investments in the United States of America, and they receive interest or dividend payments as a result of their investments. These dividends are reflected as a debit here on current account balance sheet. As a result, the longer the imbalance persists, the greater the amount of capital gains and dividends debits that will accrue over time. This means that in the future, the economy will be forced to attract capital in order to pay off from the investment returns that has been generated. In addition, there is a deficit in products and services (Sahin et al., 2014).

1.3. Impact of Foreign Currency and Current Account Deficit on Economic Growth

Pakistan's economic woes are becoming more severe, as evidenced by the country's shrinking foreign reserves, rising debt, ancient devaluation of the currency, and escalating trade deficit forcing the country to borrow money from foreign sources such as the International Monetary Fund and Saudi Arabia once more. During first five months of the fiscal year, the trade imbalance has increased by an astounding amount, amounting to more than 117.25 percent. Between July and November 2021, the merchandise trade deficit increased to $20.746 billion, an increase over the previous year's figure of $9.549 billion. When considering only the period July to November 2021, the current-account deficit increased to more than $5.08 billion (or 4.7 percent of GDP), primarily due to an increase in imports that outpaced decreases in exports. An important factor contributing to the dramatic increase in import costs is the disturbance in the supply chain that has resulted in a spike in commodity prices, as previously stated. Additional

factors contributing to this downward trend include the importation of raw resources, capital equipment, and grocery chain products with inelastic demand, all of which have increased in recent years. Exports increased by 27 percent to $12.365 billion in July-November 2021, compared to $9.747 billion in the same period the previous year, but the effect of this rise appears to have been insufficient to increase foreign exchange reserves to allow imports to be more easily procured. The objectives shall include analysing the impact of foreign currency and current account deficit on the economic growth of Pakistan, which are as follows:

- To investigate the impact of foreign currency on the economic growth of Pakistan.
- To explore the impact of current account deficit on the economic growth of Pakistan.
- To suggest the policy implications.

TECHNICAL LITERATURE REVIEW

Balance of Payments and Exchange Rates: A Historical Overview

In this chapter, I have analysed past trends of the foreign trade in Pakistan as well as highlighted the major imports and exports structure from the past to the current times. The role of balance of payments, exchange rate and current account balance in a country's economic growth, has also been highlighted.

2.1. Past Trends in Foreign Trade of Pakistan

The current drop in Pakistan's foreign trade is largely due to the global economic recession. However, it is incorrect to assert that there is no escape from it or that the effects of the Western recession on less developed countries would inevitably be as terrible as they were in the 1930s of the present centuries. In fact, since 1929, the entire global economy has undergone radical upheaval. The underdeveloped nations can now be constructively rescued from the impacts of an industrial crisis in the West by factors and forces that, if properly employed. In addition to having a global scope, these variables and forces also exist within the underdeveloped nations themselves. For instance, in most of these nations have begun large programs of land reform and fundamental development and are currently politically independent or semi-independent. They have also made significant progress in the post-war era toward the development of manufacturing industries based on the use of local raw materials, which has greatly decreased their reliance on Western markets for the sale of its basic commodities. On the other hand, there are enormous areas like China, the U.S.S.R.[2], and Eastern Europe that are distinctly beyond the sphere of the global crisis and are essentially immune to the negative impacts of an economic depression in the West. In 1929, when the U.S.S.R. was still in the early stages of her economic rebuilding and unable to provide alternative markets for raw commodities in a significant scale, this predicament did not exist. (Tufail, 1958)

This does not imply that the only way to reverse the concerning trends in our international trade is to alter its course. Indeed, there are numerous and different factors that contribute to our current problems in foreign trade, necessitating a multifaceted approach to their resolution. At the same time, it must be emphasized that the primary cause, which is represented by the global recession, requires a unique approach. In fact, Pakistan's foreign commerce is trapped in a hamster wheel. A decrease in imports was forced by a decline in exports, which had a negative

[2] The Soviet Union, officially the Union of Soviet Socialist Republics, was a transcontinental country that spanned much of Eurasia from 1922 to 1991.

impact on our sales abroad. To aid the nation in emerging from its current predicament, this vicious spiral must eventually be broken. Breaking it would be simpler on the import side than the export. To put it another way, the nation's import trade needs to be reorganized. It must be acknowledged that our import trade has undergone very little planning, if any at all. Undoubtedly, given the deteriorating exchange position, it was the proper decision to lower its overall quantity. Giving the import schedules an industrial bias was also the right move. But none of this was sufficient. Despite strict government regulation, our limited exchange resources kept being used in the wrong directions. As a result, the decline in private imports forced the government to stop furthering commercial and industrial development, which resulted in a severe decline in the nation's economic activities. (Tufail, 1958)

2.2. Historical Overview of Exports in Pakistan

Significantly, we have been importing very little from the currency area that generates the majority of our earnings, while purchasing extensively from the regions that generate very tiny sums of foreign cash. In other words, we have been spending money from one area on the other. Since Pakistan's inception, countries outside the dollar and sterling zones have provided us with more foreign currency than the two regions combined. This will be evident from the subsequent table of numbers. (Tufail, 1958)

(In Million Rupees) *

Total export earnings from	1948-49	49-50	50-51	51-52	52-53	53-54	54-55	55-56
Sterling and dollar areas combined	380.5	390.8	938.5	875.5	516.2	540.3	640.3	942.4
Countries outside the dollar and sterling areas.	423.9	478. 8	1,369.0	1311.3	825-6	762.2	576.4	956.3

Table 1: Total Export Earnings (1948-1956)

Source: State Bank of Pakistan

The preceding table demonstrates that, except for the year 1954-1955, annual export earnings from the world outside the dollar-areas have always exceeded those from the two dollar-areas. Even during 1954-1955, the "outside world" brought us more trade than the two regions combined. In 1956-57, we earned a total of 787.7 million rupees from the dollar and pound areas combined, while our export earnings from the rest of the globe totalled 873.8 million rupees. (Tufail, 1958)

It is important to remember that developing countries must purchase capital goods and intermediate inputs for domestic manufacturing, which helps them generate an exportable surplus as well. As a result, placing a strong emphasis on reducing the trade deficit may actually work against them. In Pakistan, both imports and exports rose greatly between FY01 and FY05, but both decreased dramatically between FY06 and FY08. The decline in export growth was much greater than the decline in import growth, which widened the trade deficit. This may be the case because the ability to produce an exportable surplus is dependent on imported raw materials, or it may have been the result of State Bank of Pakistan's demand management strategies, particularly its changes to policy rates and signals to the money market. A considerable fall in import growth during FY07 as a result of a slowdown in credit to the private sector, or monetary tightening, was compensated by an increase in export growth in FY08 instead. The State Bank of Pakistan was able to reduce some import demand, but undoubtedly at a price. However, despite rising commodity and energy prices in FY08, imports growth picked up again, and the gap between import and export growth dramatically expanded. In FY07, the current account deficit increased by one percentage point from FY06 to 5.2 percent of GDP (US$7.5 billion). During July to May of FY08, it had already attained 7.6% of GDP. The paradox was that official circles failed to respond with any effective policy. (Zafar-ul-Hassan, 2008)

The slowdown of export growth is particularly important since it shows how poorly changes have been implemented in the past and how poorly targeted programs have worked. While the structure of exports has mostly remained unchanged, the content of imports has changed significantly in recent years. All declarations of export diversification turned out to be empty platitudes; both the products and the destinations of exports remained highly specialized. In the post-quota liberalization period, the share of the textile industry in total exports fell by approximately 5 percentage points while the share of other industries increased by around the same amount. Over time, the textile industry has benefited from excessive official favoritism, which has resulted in a weak industrial base for the nation. The industry lacks competitiveness and has received significant subsidies. The majority of the investment was made in the spinning sub-sector, which was less export-intensive, but it turned out to be a disaster despite the government providing it with enormously generous concessionary financing facilities. Serious structural problems with Pakistan's exports must be resolved, mostly by the sector itself, with the government serving as a facilitator. The reasons for structural flaws in the textile industry include:

1. Low value added and poor-quality products fetching low worldwide prices

2. Relative to Pakistan's rivals, significant depreciation of recently installed machinery.

3. Use of power-guzzling, underproductive, and expensive to maintain machinery

4. Increased input waste raises the price of production.

5. The business sector makes few or no attempts to raise worker skill levels.

6. The industry makes little investment in R&D.

7. Export houses don't have the capacity to fulfil large orders or satisfy client demands for style, design, and delivery dates.

For these reasons, it would be a bad idea to waste further resources trying to increase textile exports. The federal budget for 2008–2009 correctly ignored pressure from the influential textile lobby and does not provide the industry with any new incentives. The rupee's decline may turn out to be advantageous for the textile industry. (Zafar-ul-Hassan, 2008)

	FY 00	FY 01	FY 02	FY 03	FY 04	FY 05	FY 06	FY 07	FY08*
Food Group	9.4	8.6	8.6	10.6	10.0	8.6	9.4	9.3	14.0
Textile Group	65.6	64.1	63.5	65.2	65.7	59.4	60.2	60.9	55.8
Other Manufactures Group	13.7	15.1	18.8	16.7	15.7	17.7	16.4	14.3	18.9
All Other Items	11.3	12.2	9.1	7.5	8.6	14.3	14.0	15.5	11.3
Total	100	100	100	100	100	100	100	100	100

* July-May

Source: Federal Bureau of Statistics

Table 2: Structure of Exports (2000-2008)

In the first eleven months of FY08 (July to May), non-traditional, non-textile products accounted for 100% of total sales. However, the export of goods based on technology was still almost non-existent. Products exported ranged from basic things like sporting goods and medical and surgical supplies to a small amount of software. There was basically no value-added or knowledge-based component. Lack of sufficient markets for its goods is another failing of Pakistan's export business. Only four nations account for more than half of exports, indicating a small export base. Trade diplomacy hasn't worked: Pakistan could have negotiated for more market access in the aftermath of 9/11, but this didn't seem to be a priority for policymakers. In reality, the nation has missed numerous chances in the past where it could have used its political influence to negotiate for perks and market access. Pakistan's diplomats have not been successful in promoting trade since the assignment of trade or commerce officials in embassies across the world is based more on political or military connections than talent. (Zafar-ul-Hassan, 2008)

2.3. Historical Overview of Imports in Pakistan

Our imports have been virtually monopolized by countries in the pound and dollar zones, primarily the sterling zone. It is vital to clarify that, for import reasons, sterling area is synonymous with the United Kingdom. In fact, the United Kingdom has been the largest single drain on our foreign exchange resources, both in terms of imports and other forms of foreign payments. Even with a severe shortage of foreign currency, we continued to increase our purchases from the sterling area. This is evidenced by the following statistics about private and government imports over the past four years. It will be remembered that our exchange position began to deteriorate throughout the following years.

	Private imports	Government imports
1953-54	365.7	...
1954-55	510.0	261.6
1955-56	473.3	333.8
1956-57	533.9	523.0

*Table 3: Private & Government Imports (1953-57) *Figures are in Million Dollars**

Source: State Bank of Pakistan

As for the dollar area, private imports have decreased while government imports have increased.

Commercial year	Private	Government
1953-54	71.1	44.1
1954-55	65.5	74.6
1955-56	50.0	79.5
1956-57	52.8	210.3

*Table 4: Dollar area private and government imports (1953-57) *Figures are in Million Dollars**

Source: State Bank of Pakistan

On the other hand, imports from the rest of the world (i.e., nations outside the dollar and sterling sectors, such as West Germany and the Communist countries) have been dropping from year to

year, even though this region has generated most of our export earnings. From Rs. 890.1 million in 1951-52 to Rs. 475.4 million in 1953-54 and Rs. 297.6 million in 1953-54, the value of private imports from this region of the globe decreased. The next year, they decreased even further to Rs 262,7 million. In 1955-1956, imports increased to Rs. 311.5 million, but in 1956-1957, they decreased to Rs. 282.7 million. Imports on the government's tab demonstrate a lack of strategy in our overseas commerce. Despite the extremely precarious exchange position, government imports increased from Rs. 488.8 million in 1953-54 to Rs. 535.9 million in 1955-56, and then to Rs. These imports may have been decreased through a variety of methods, including a decrease in defence spending. (Tufail, 1958)

While the majority of Pakistan's imports consist of manufactured products with high prices and low-income elasticity of demand, more than three-fifths of the country's merchandised exports are made up of textiles. As a result, unless domestic demand declines, imports will certainly increase, widening the trade deficit. In Pakistan, periods of great economic expansion are accompanied by periods of significant current account and trade deficits. This serves as a reminder of the crucial notion that, as has occurred in the majority of developing nations, reducing the trade deficit by restricting or lowering imports will restrain economic growth. Like its exports, Pakistan's imports are similarly heavily concentrated on a small number of goods: machinery, oil and petroleum products, chemicals, equipment for transportation, edible oil, iron and steel, fertilizer, and tea. 85 percent of all imports during the first eleven months (July-May) of FY08 fell into these eight import categories. Regarding origin, Pakistan's imports are similarly very specialized. Over the past ten years, the top importers have been the USA, Japan, Kuwait, Saudi Arabia, Germany, the UK, and Malaysia. These seven nations continue to supply over 40% of Pakistan's imports. The top import providers continue to be Saudi Arabia, the United States, and Japan. (Zafar-ul-Hassan, 2008)

Pakistan's imports' composition has changed significantly in recent years. Between FY01 and FY05, petroleum imports as a percentage of total imports decreased, but they significantly increased over the next three fiscal years, increasing by over 10 percentage points. The more concerning trend is the roughly 10-percentage-point reduction in the raw material and machinery groups, which is more than offset by an increase in the "others" category, which includes luxury and non-traditional commodities like mobile phones.

A downturn in the economy is implied by the decline in raw material and machinery imports. The share of consumer durables in the import basket is finally stabilizing, which may make State Bank of Pakistan delighted, but its monetary tightening may have had a greater impact on the investment cycle than on consumer demand. Between FY03 and FY06, Pakistan's imports

increased at an average rate of 29% annually because of the country's robust economic expansion, which also led to an increase in investment and imports. In FY07, import growth dropped to a normal level, but in FY08, it sharply increased once again as a result of an extraordinary increase in oil import bills and a few one-time factors, including imports of wheat and fertilizer.

	FY00	FY01	FY02	FY03	FY04	FY05	FY06	FY07	FY08*
Machinery Group	14.5	15.0	16.9	18.2	21.2	21.8	21.4	15.5	14.5
Petroleum Group	27.2	31.3	27.1	25.1	20.3	19.4	23.4	24.0	28.1
Raw Materials	14.0	12.9	14.5	13.9	14.2	15.8	16.2	10.3	8.1
Food Group	10.8	9.2	8.0	8.0	6.6	6.8	7.2	6.2	10.8
Consumer Durables	4.9	4.2	4.4	5.9	5.8	6.9	7.7	6.7	7.2
Others	28.7	27.3	29.1	28.9	31.8	29.2	24.1	37.2	31.3
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

* July-May

Source: Federal Bureau of Statistics.

Table 5: Structure of Imports

In FY07, import growth dropped to a normal level, but in FY08, it sharply increased once again as a result of an extraordinary increase in oil import bills and a few one-time factors, including imports of wheat and fertilizer. The outcome has been a significant increase in Pakistan's trade and current account deficits this year, which has led to catastrophic macroeconomic imbalances. Government should place the highest priority on correcting imbalances by reducing aggregate demand through suitable policies. (Zafar-ul-Hassan, 2008)

Imports increased by 29.6% to $35.9 billion during the first eleven months of FY08, with a particularly large increase in the purchase of petroleum products as well as imports of food and raw materials. In the same time period, imports of goods other than oil and food increased by 18.5 percent and by 22.4 percent, respectively. In the current fiscal year, imports in the food category increased by 51.3 percent, mostly due to unexpected imports of wheat totaling $860 million and an unusual increase (71.5 percent) in imports of edible oil caused by the skyrocketing price of palm oil on the global market. Food imports made up 11% of all imports but were responsible for 16.01% of the increase in imports for the current fiscal year. In the first eleven months of FY08, machinery imports only slightly increased (11.0%), reaching $5.2 billion. The imports of mining, construction, and other machinery all increased significantly within the machinery category by 38.2 percent, 33.1 percent, and 9.9 percent, respectively. The country's continuing building and electricity projects are to blame for the increase in imports of

these diverse categories of machinery. Despite representing 14.5 percent of all imports, the equipment group made up only 6.3 percent of this year's overall import growth.

Petroleum-related imports saw an unprecedented increase of 52.2 percent, totalling $10.1 billion. Despite making up 28.1% of all imports, the petroleum group was responsible for 42.2% of the year's growth. The prices of Petroleum, Oil and Lubricants (POL) products have skyrocketed, which has contributed to the boom in petroleum growth. In contrast to prior years, imports of consumer durables decreased by 3.9% in the first eleven months of the fiscal year 2008. Consumer durables made up 7.2 percent of all imports, but their contribution to import growth was negative by 1.3 percent. The first eleven months of FY08 had a 6.5 percent increase in raw material imports, which made up 8.1 percent of all imports. Fertilizer imports increased by 193.1 percent, 12.3 percent, 74 percent, iron, steel, plastics, and scrap, which together account for 45 percent of all raw material imports.

	July-May		% Change	Absolute Increase	Point Cont. in Import Growth	% Cont of absolute increase in imports
	FY07	FY08				
Total imports	**27743.2**	**35943.3**	**29.6**	**8200.1**	**29.6**	**29.6**
Food Group	**2556.5**	**3867.5**	**51.3**	**1311.0**	**4.7**	**16.0**
Machinery Group	**4697.3**	**5213.1**	**11.0**	**515.9**	**1.9**	**6.3**
Transport Group	**931.3**	**870.1**	**-6.6**	**-61.2**	**-0.2**	**-0.7**
Petroleum Group	**6632.0**	**10094.2**	**52.2**	**3462.2**	**12.5**	**42.2**
Textile Group	**1389.8**	**2206.1**	**58.7**	**816.2**	**2.9**	**10.0**
Agri Chemicals Group	**3956.5**	**5259.7**	**32.9**	**1303.2**	**4.7**	**15.9**
Consumer Duables	**2685.5**	**2581.1**	**3.9**	**-104.5**	**-0.4**	**-1.3**
Electric Mach & App.	594.3	676.4	13.8	82.1	0.3	1.0
Road motor Vehicles	1288.8	1207.3	-6.3	-81.5	-0.3	-1.0
Mobile Phones	802.4	697.4	-13.1	105.0	-0.4	-1.3
Raw Materials	**2749.8**	**2927.7**	**6.5**	**177.9**	**0.6**	**2.2**
Others	**2144.5**	**2923.8**	**36.3**	**779.3**	**2.8**	**9.5**

Table 6: Major Contributors to Increase in Imports

At a time when the price of fertilizer on the worldwide market had increased by approximately 50%, the tremendous rise in fertilizer imports was unexpected. Pakistan bought nearly 2 million tons in the first eleven months of FY08, a rise of 58% from the 1.2 million tons it imported in the same period last year. It is unclear why such big amounts of fertilizer were imported while the nation's consumption of the substance did not increase from the previous year. The import bill for the nation increased by $490 million as a result of an unprecedented rise in fertilizer imports that cannot be justified by the performance of the nation's agricultural crops this year. 2.2 percent of this year's increase in imports was attributable to raw material imports.

Contrary to prior trends, imports of telecom products remained mostly at the $2.1 billion level from the previous year, indicating that the current expansion period of numerous cellular

carriers has reached saturation. Despite making up 5.9% of all imports, the 0.3% gain in overall imports this year was barely noticeable due to telecom imports. It is crucial to remember that the strong economic growth that boosted domestic demand and expanded investment was the primary driver of the jump in imports from 2003 to 2006. But this year's import growth was not caused by a structural change in demand; rather, it was brought on by higher global commodity prices, including those for crude oil and palm oil, as well as one-time increases in the imports of wheat and fertilizer. Just the imports of edible oil and petroleum products increased this year's imports by 47%. The import of fertilizer and wheat contributed an additional 18.7 percent. Together, these four goods made for two-thirds of the increase in imports for this year. (Zafar-ul-Hassan, 2008)

2.4. Current Export Structure of Pakistan

Pakistan ranked 65th among all exporters in 2020 with a total export value of $25.5B. Pakistan's exports have decreased by -$1.42 billion over the past five reporting years, from $27 billion in 2015 to $25.5 billion in 2020.

Bed linen, table linen, bathroom linen, and kitchen linen account for the majority of recent exports ($3.61 billion), followed by rice ($2.14 billion), suits, ensembles, jackets, blazers, trousers, bib and brace overalls, breeches, and shorts ($1.8 billion), suits, ensembles, jackets, dresses, skirts, divided skirts, trousers, bib and brace overalls ($1.06 billion), and jerseys, pullovers, cardigans, waistcoat United States ($4.04 billion), Germany ($2.13 billion), China ($1.97 billion), United Kingdom ($1.73 billion), and United Arab Emirates ($1.09 billion) are Pakistan's top export markets. (OEC, 2020)

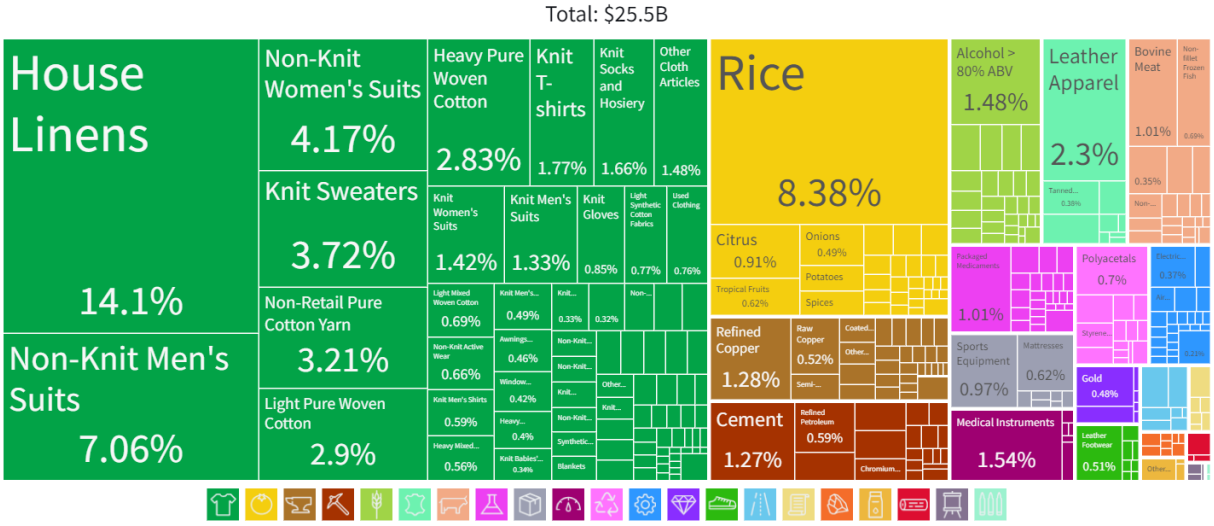

Figure 1: Current Exports of Pakistan

Source: Data from BACI HS6 REV. 1992 (1995 - 2020)

2.4.1. Service Exports of Pakistan

Pakistan exported services valued $5.77B in 2019. Other commercial services ($1.47 billion), computer and information services ($1.29 billion), government services, n.i.e. ($1.21 billion), transportation ($854 million), and personal travel ($492 million) were Pakistan's main exports in 2019. (OEC, 2019)

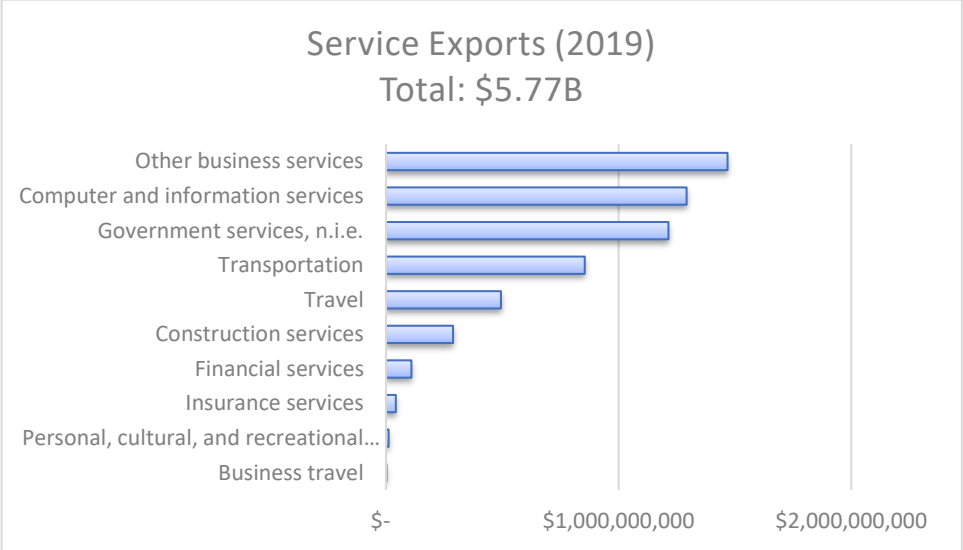

Table 7: Service Exports of Pakistan (2019)

Source: Data from UN Comtrade United Nations International Trade Statistics Database

2.5. Current Import Structure of Pakistan

Petroleum gases and other gaseous hydrocarbons ($2.24B), palm oil and its fractions ($2.15B), petroleum oils and oils obtained from bituminous minerals ($1.92B), and cotton that has not been carded or combed ($1.68B) are Pakistan's top imports, with the majority of these goods coming from China ($14.7B), the United Arab Emirates ($5.34B), and the United States ($2.78B).

Pakistan was the 49th-ranked trading destination in the world in 2020 thanks to imports worth $50.5 billion. Pakistan's imports have changed by $401 million over the last five reporting years, rising from $50.1 billion in 2015 to $50.5 billion in 2020. Pakistan was the largest importer of tea ($646 million), nickel ($259 million), waste and scrap of these materials, jute and other textile base fibres (not flax, true hemp, and ramie), raw or processed but not spun; tow and waste of these materials, including yarn waste and garneted stock ($43.6 million), and

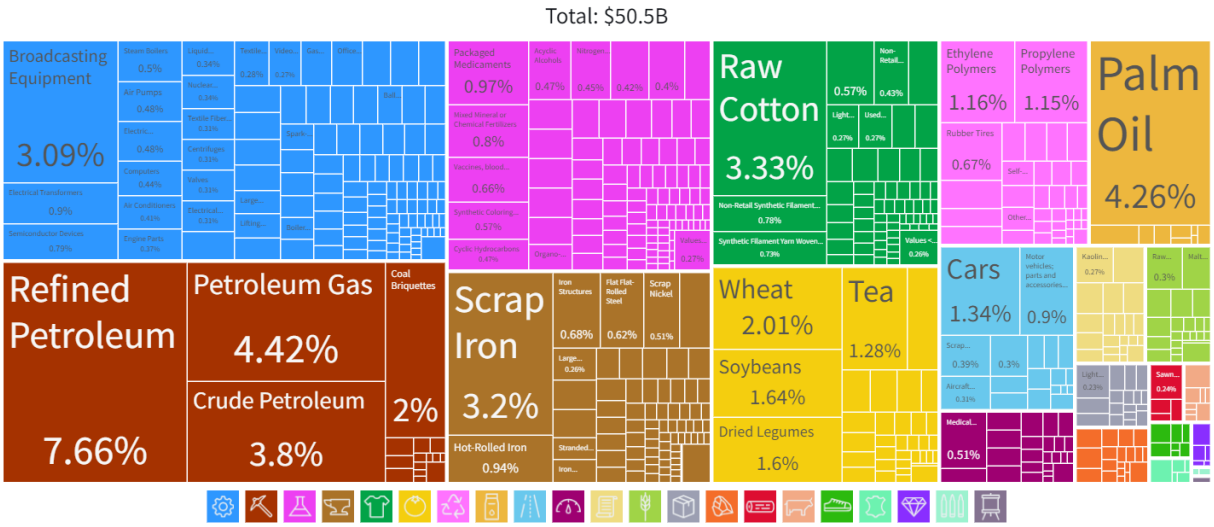

Figure 2: Current Imports of Pakistan

Source: Data from BACI HS6 REV. 1992 (1995 - 2020)

yarn that has been metallized, whether or not gimped, of textile yarn, strip, or the like of heading no. 5404 or 5405. (OEC, 2020)

2.5.1. Service Imports of Pakistan

Transportation ($3.55 billion), Other business services ($2.54 billion), Personal travel ($1.63 billion), Construction services ($501 million), and Computer and information services ($426 million) were Pakistan's top five services imported in 2019. (OEC, 2019)

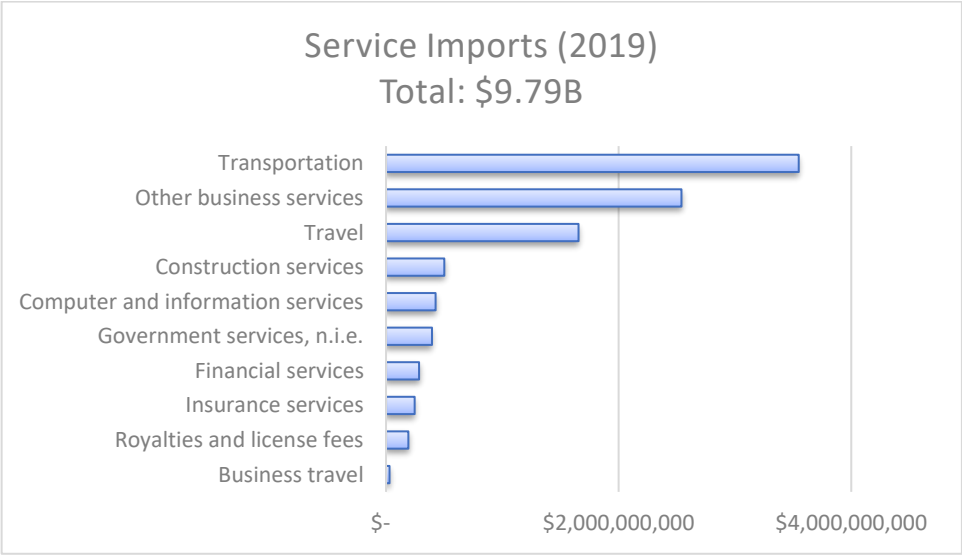

Table 8: Service Imports of Pakistan (2019)

Source: Data from UN Comtrade United Nations International Trade Statistics Database

2.6. Balance of Payments

According to data from the State Bank, we have always had a deficit in our balance of payments with the sterling area, mostly due to our reliance on imports from the United Kingdom. In fact, fifty to sixty percent of our total annual imports have originated from the sterling region since the end of the partition. In recent years, the deficit in payments balance with the sterling region has been as follows:

Commercial year	Deficit in Million Rupees
1948-49	460.3
1949-50	354.5
1950-51	95.6
1951-52	557.7
1952-53	556.3
1953-54	362.5
1954-55	209.2
1955-56	195.5
1956-57	562.5

Table 9: Balance of Payments Deficits (1948-1957)

Source: State Bank of Pakistan

In contrast, our balance of payments with the rest of the world outside the pound and dollar zones has always been rather positive. (Tufail, 1958)

Development revolves around the balance of payments. It shows how trade and finance are intertwined and exposes how a particular economy interacts with the global economy. The fundamental barriers to industrialization that developing nations encounter are what cause their balance-of-payments crises, and they also show why those barriers are so entrenched. The point of convergence for a country's trade and financial flows is its balance of payments. A statement of all a country's dealings with the rest of the world for a specific time period is referred to as its "balance-of-payments." It comprises government activities, money flows, the buying and selling of products, services, presents, and other items. The capital account and the current account are frequently used to categorize economic activity. Unlike capital account flows, which involve movements in the ownership of both foreign and local assets, current account flows are predominantly made up of goods and services (i.e., in foreign-held domestic assets and domestic-held foreign assets). A "balance-of-payments" issue arises when the decline in demand for a nation's currency is so severe that it puts downward pressure on the value of the

currency. The ensuing depreciation makes it difficult for people to buy basic commodities and disturbs market operations. Governments frequently take action to avert this negative pressure, especially if they are devoted to upholding a tight exchange rate. Balance-of-payments problems can be caused by both established and less common factors. A rapid and significant growth in a country's trade deficit is a common reason for balance-of-payments crises. Such a rise may take place, for instance, if unfavourable weather significantly lowers export revenues and crop yield of important export commodities. Another well-known instance is when a surge in oil prices causes a country's import costs to skyrocket. The result is the same, a fast decline in demand for domestic currency relative to foreign currency, whether the abruptly expanded trade deficit is brought on by reduced export revenues or a greater import bill. (Chantal, 2000)

Table 10 demonstrates that Pakistan's trade balance was negative despite a three-year current account surplus (FY01 to FY04). Economic growth during this time was less than it had been in more recent years, from FY05 through FY08.

(Million $)

ITEM	FY03	FY04	FY05	FY06	FY07	FY08[P]
Current account balance	**4070**	**1811**	**-1534**	**-4990**	**-6878**	**-14016**
Current account balance without off. transfers	**3165**	**1300**	**-1784**	**-5696**	**-7403**	**-14443**
Goods: Exports f.o.b	1097 4	1245 9	1448 2	1655 3	1727 8	20125
Goods: Imports f.o.b	1133 3	1373 8	1899 6	2499 4	2698 9	35411
Trade Balance	-359	-1279	-4514	-8441	-9711	-15286
Services (Net)	-2	-1316	-3293	-4430	-4170	-6302
Services: Credit	2712	2644	3319	3769	4140	3590
Services: Debit	2714	3960	6612	8199	8310	9892
Income (Net)	-2211	-2207	-2386	-2667	-3582	-3905
Income: Credit	170	187	437	784	940	1613
Income: Debit	2381	2394	2823	3451	4522	5518
Of which :Interest Payments	1277	1057	1037	1248	1417	2156
Balance on Gds & Serv. & Inc	-2572	-4802	- 1019 3	- 1553 8	- 1746 3	-25493
Current Transfer (Net)	**6642**	**6613**	**8659**	**1054 8**	**1058 5**	**11477**
Capital Account and Financial Account	**661**	**-1252**	**1131**	**6071**	**1044 9**	**8778**
Capital Account,	**1133**	**82**	**685**	**241**	**304**	**69**
Financial Account	**-472**	**-1334**	**446**	**5830**	**1014 5**	**8709**
Dir. Invest. In Rep. Econ.	798	951	1525	3521	5140	5153
Other Investment Assets	449	-669	-1352	148	-585	397
Other Investment Liab.	-1453	-1885	-281	1246	2421	3198
Monetary Authorities	-51	2	-5	0	-1	490
General Government	-1419	-1792	574	769	1308	2315
Disbursements	1389	978	2163	2238	2669	3485
Amortization	2788	2744	1558	1446	1339	1149
Overall Balance	**5254**	**781**	**-410**	**1334**	**3730**	**-5780**
Reserves and Related Items	**-5254**	**-781**	**410**	**-1334**	**-3730**	**5780**
SBP Reserves(Excl. CRR & Sinking Fund)	**9529**	**1056 4**	**9805**	**1076 5**	**1334 5**	**8577**

Table 10: Summary Balance of Payment

2.7. Current Account Balances and Deficits

An important measure of an economy's basic strength is the current account balance. The current account balance changes offer important information regarding changes in macroeconomic policy and reactivity to autonomous shocks. Fluctuations in this variable are closely related and transmit information about the intentions and expectations of all economic agents in an open economy. (Zafar-ul-Hassan, 2008)

A country that has a current account deficit is one that imports more products and services than it exports to overseas markets. A current account deficit may occasionally not be detrimental to a nation's economy if external debt is utilised to fund successful projects. An expanding current account deficit in the country's economy causes an increase in the supply of that nation's currency on the foreign exchange markets. Imports outnumber exports, causing expenditure to leave the economy in order to purchase imports. A current account deficit might be a warning that an economy is losing its competitive advantage. Consumers prefer to purchase less expensive imports rather than consume more expensive domestically produced goods. The current account deficit, in accordance with the intertemporal perspective, is the result of forward-looking dynamic saving and investment decisions that are influenced by expectations of productivity growth, government expenditure, interest rates, and a number of other factors. (Calderon et al., 2000)

It may be necessary to examine structural aspects of the economy, such as levels of economic development, demographics, and consumption and production structures, to conduct a long-term evaluation of the current account. These elements affect the current account balance and, consequently, the savings rate. Usually, as nations go to the next stage of development, they import capital, resulting in current account deficits. After 9/11, Pakistan's current account deficit, which had previously averaged 5.0 percent of GDP, sharply decreased and even saw three years of surpluses. In place of the periodic devaluations of the 1990s, the Pakistani rupee appreciated during this time. But over the past two or three fiscal years, current account deficit has started to resurface and has already reached dangerous levels. The growing trade deficit in both goods and services was the main contributor. The initial phase of easy monetary policy and the expansionary fiscal policy implemented over the course of the last five years since FY04[3] have helped to spark a surge in demand for imported products, particularly consumer durables. The level of consumption has increased significantly in recent years, despite

[3] Fiscal year of 2004.

State Bank of Pakistan[4]'s attempts to curtail it by tightening monetary policy. In comparison to real GDP growth of 5.8 percent, real consumption growth in FY08[5] was 8.5 percent. Consumption made up 118 percent of the GDP growth. (Zafar-ul-Hassan, 2008)

Pakistan, like the majority of transitional countries, is dependent on the current account deficit because it has played a significant role in driving its present higher rate of economic growth. The sustainability of the deficit, however, is a crucial issue that has to be examined. The demand for durable goods, which are primarily imported, as well as growth in the financial and telecom industries, are the main drivers of the current growth pace. All of them contributed significantly to inflows and the current account deficit. (Zafar-ul-Hassan, 2008)

The fall of the rupee was accelerated by inflationary pressures, endangering Pakistan's demand control strategies. To keep the population gathered around the poverty line from slipping below it is a herculean undertaking for policymakers. The current growth pace must be maintained to keep these populations from slipping to a very low quality of life. Only a stronger growth trajectory might reduce poverty or, at the very least, stop it from increasing, and give more weight to the negative repercussions of such a strategy in a nation like Pakistan. (Zafar-ul-Hassan, 2008)

2.8. Foreign Currency Reserves Shortage in Pakistan

The policymakers believed that foreign currency deposits could be the solution to the economy's low rate of saving and investment, as these deposits could serve to mobilize both domestic and foreign savings. However, the rise in potential savings from foreign currency deposits did not lead to a boom in investment. Rather, these short-term foreign liabilities helped fund substantial fiscal and external current account deficits for a longer length of time than would have been possible otherwise.

Consequently, the nation was burdened with a debt overhang problem, which significantly hampered its long-term growth potential. Pakistan's experience demonstrates the significance of public debt sustainability for maintaining economic stability and growth and highlights the difficulties borrowing governments face in determining what are appropriate debt levels, i.e., those that can be sustained, particularly in economies with a high of dollarisation. The analysis seeks to identify the most significant structural flaws in negatively the financial system, with a

[4] Pakistan's national bank is known as the State Bank of Pakistan. Prior to the bank being nationalized and having its functions significantly expanded on January 1, 1974, its original 1948 State Bank of Pakistan Order constitution remained largely unchanged.

[5] Fiscal year of 2008.

special emphasis on how short-term foreign liabilities have degree impacted the conduct of financial policies[6]. (Abbas & Iqbal, 2006)

Throughout the 1980s and 1990s, Pakistan had chronic balance of payments issues as a result of expansionary financial policies and deficiencies in the structure of the external sector.

Year	GNI growth (Percent)	Inflation (End-of Period)	Current Account Deficit (Percent of GDP)	International Reserves (Months of Imports of G&S)	REER (Percentage Change)	Official Exchange Rate (Rupees per Dollar)
1973	24.33	23.07	–1.40	5.93	n.a.	9.88
1974	29.90	26.66	–10.04	3.60	n.a.	9.88
1975	28.42	20.90	–9.18	2.09	n.a.	9.88
1976	18.72	7.16	–6.33	2.65	n.a.	9.88
1977	16.40	10.13	–4.12	2.30	n.a.	9.88
1978	21.42	6.14	–4.53	1.77	n.a.	9.88
1979	11.13	8.27	–4.28	0.83	n.a.	9.88
1980	20.54	11.94	–3.25	1.26	n.a.	9.88
1981	19.18	11.88	–2.86	1.52	12.46	9.88
1982	16.16	5.90	–1.27	2.34	–8.39	12.84
1983	15.53	6.36	–1.84	4.03	–3.42	13.50
1984	13.77	6.09	–3.57	2.20	2.12	15.36
1985	11.12	5.61	–2.66	1.58	–6.60	15.98
1986	8.90	3.51	–1.73	1.58	–17.48	17.25
1987	9.53	4.68	–2.60	1.15	–11.02	17.45
1988	15.71	8.84	–3.45	0.83	–1.50	18.65
1989	13.10	7.84	–3.59	1.00	–6.39	21.42
1990	11.78	9.05	–3.54	0.60	–6.54	21.90
1991	16.83	11.79	–3.33	0.98	–1.82	24.72
1992	17.02	9.51	–4.30	1.18	–1.43	25.70
1993	10.27	9.97	–4.81	1.56	–0.35	30.12
1994	16.55	12.37	–3.61	3.77	–2.24	30.80
1995	20.12	12.34	–5.54	2.09	–0.65	34.25
1996	12.39	10.37	–6.44	0.69	–1.96	40.12
1997	14.01	11.38	–4.22	1.35	3.08	44.05
1998	10.14	6.23	–3.19	1.33	–3.47	45.89
1999	9.78	4.14	–2.79	2.01	–5.72	51.78
2000	7.53	4.37	–1.89	1.71	1.18	58.03
2001	7.67	3.15	0.42	4.12	–6.95	60.86
2002	8.55	3.29	4.14	8.31	3.95	58.53
2003	14.70	2.91	3.27	9.27	–4.94	57.22
Period Averages						
1973–79	21.47	14.62	–5.70	2.74	n.a.	9.88
1980–89	14.35	7.27	–2.68	1.75	–4.47	15.22
1990–99	13.89	9.72	–4.18	1.56	–2.11	34.93
2000–03	9.61	3.43	1.49	5.85	–1.69	58.66

Table 11: Basic Economic Indicators (1973-2003)

Source: World Economic Outlook and International Financial Statistics Database

[6] The focus on foreign currency deposits is not intended to "put too much blame" on them as a cause of Pakistan's problems; rather, by limiting the analysis to a few key factors, it is hoped to provide a more in-depth analysis of certain core issues that are frequently discussed in policy discussions but could benefit from a more rigorous treatment.

Over fifty percent of the nation's exports were comprised of cotton and cotton-based items, which represented a restricted export base. In the past, workers' remittances were a considerable share of overall exports; nevertheless, they fell in the 1990s and became a less significant source of foreign exchange profits; however, this trend has reversed in recent years. The dramatic swings in these remittances mirrored changes in the economic, political, and other situations in both the host nations and Pakistan. The recurrent current account deficits had been covered in part by foreign direct investment and portfolio capital, but more so by the build-up of short-term foreign liabilities due to the FCDs and foreign aid by bilateral and multilateral donors. (Abbas & Iqbal, 2006)

2.9. Synopsis of Indebtedness in Pakistan

World War II introduced several new occurrences and organizations to the world. We are well acquainted with inflation, rationing, and black marketing. Prior to the end of the war, however, the four principal nations, collectively known as the Allied Powers, mapped out the new form of the globe as well as their respective territories. At the conclusion of the war, the United Nations were established. The 1944 Bretton Woods Conference established the International Bank for Reconstruction and Development (IBRD or World Bank) and the International Monetary Fund (IMF). The United States was, without a doubt, the wealthiest nation in the group. It assumed the position of political and economic leader for the majority of the world. It offered to be the host nation for all three major international organizations and provided the required facilities. During the decades following World War II, the United States provided help to Europe via the Point Four Programme and Marshall Plan. After World War II, economists created the discipline of Development Economics. The Keynesian idea of 'autonomous' investment resulting in increased employment, income, and 'induced' investment proved useful. This might be accomplished most effectively through economic aid to "encourage" economic development in comparatively poorer nations. There was, in a sense, enlightened self-interest. The countries receiving help would purchase goods from the United States and other aid-giving nations. There was occasionally "Tied Aid"[7] to secure the advantage to help donors when economic aid was provided to countries that required and sought it. Obviously, the United States and other donor nations had their own perspectives when determining which countries should be assisted. In any case, we may like to know how much and from whom Pakistan got foreign help. IBRD and its affiliates were active, as were wealthy nations such as the United States. International Finance Corporation (IFC) and International Development Association (IDA) are

[7] Foreign help that must be spent on items and services offered by firms from the country delivering the aid or a chosen group of countries is called tied aid.

IBRD's two most prominent affiliates (IFC). The first organisation, IDA, provides very low-interest loans in the form of service fees. IFC, the second affiliate, directs private sector investment from wealthy nations to private businesses in underdeveloped nations. (Mohammad, 1993)

We've chosen 1970 and 1991 as our two benchmark years for convenience. Thus, there are two phases: one prior to 1970 and one after to 1971, i.e., the loss of East Pakistan. Prior to 1970, or the first phase, the time is split according to the Five-Year Plan. The first subdivision is Pre-Plan (July 1955), followed by First Five-Year Plan, Second Five Year Plan, and Third Five Year Plan. Let's now examine the initial step. It may be noted that in the early years, "aid" signified "help" or "gifts." However, loans were also provided. These loans were deemed "assistance." IBRD was intended to be a development bank. Therefore, it provided loans like a typical bank would. Obviously, its actions were impacted indirectly by the interests and thinking of the host nation (USA). This may be inevitable. IBRD loans were also deemed a form of 'assistance'. In the early years of Pakistan, there was a larger share of 'gifts' than loans. Gradually, the posture changed. Grants became a small portion of help, while loans comprised the majority. The circumstances looked like this:

	Pre-Plan Period (upto July 1955)	**First Five Year Plan (1955-60)**	**Second Five Year Plan (1960-65)**	**Third Five Year Plan (1965-70)**
Grants	**$ 251.1m**	**$ 575.9 m**	**$ 345.4 m**	**$ 193.1 m.**
Loans	**$ 121.0m**	**$ 417.0 m**	**$ 2,023.3 m**	**$ 52,507.0 m.**

Table 12: Grants and Loans (1995-1970)

Source: Government of Pakistan Central Statistical Bureau

Up to 1970, the grants totalled 1,365,6 million US dollars. The United States contributed 955.1 million dollars to the total amount of grants awarded prior to 1970. In terms of percentage, the United States' share was 70%. Other donor nations were Canada, the United Kingdom, Australia, and New Zealand, among others. The ratio of grants to total aid during the Pre-Plan period (up to July 1955) was 70 percent, while the ratio of loans was 30 percent. By the Third Five Year Plan (1965-1970), the grant-to-loan ratio was 31% for grants and 69% for loans. In terms of loans, the total amount of loans disbursed and outstanding in 1952-53 was barely one million dollars. In 1959-60, outstanding loans totalled 145 million US dollars. In 1969-70, the outstanding loans were 2,959 million USD. Clearly, a substantial proportion of outstanding loans originated from IBRD and its affiliates. As of 30 June 1970, international agencies held 21,3 percent of total outstanding debt. IBRD loans totalled 332 million U.S. dollars. IDA loans

totalled 269 million US dollars. The total amount of IFC loans was 10,7 million dollars. The total amount of loans from IBRD and its affiliates was $612,2 million. However, individual country loans were also significant. As of 30 June 1970, outstanding loans from the US government and its agencies were 1,212.5 million dollars. The American portion of international aid or loans was 41.5% of the total foreign loans. This is a rather high proportion of foreign aid and loans. Economic reliance is connected to political friendship. The borrowing nations, or the beneficiaries of foreign loans or help, must alter their policies or actions to meet the requirements of the lending or aid-giving countries. The lending or aid-providing nations give priority to "friendly" nations that share their values and policies. These countries who give or lend help view it as a "political favour." A "favour" must be "reciprocated." The receivers of foreign loans or international help are, ironically, extremely indebted. Any new loan or aid entails a growth in cumulative debt as well as debt service, which is a budgetary burden in addition to a foreign exchange outflow. The sum of loans from international agencies and loans from the United States and its agencies accounts for approximately 63 percent of all outstanding loans. After these two sources, Germany, the United Kingdom, and Japan would be additional key lenders or "help suppliers." (Mohammad, 1993)

Until the middle of 1970, Pakistan was internationally regarded as one of the most effective recipients of foreign help during its initial phase. Other developing nations should emulate Pakistan, according to international organizations. During the decade of the 1960s, economic management was effective. Misuse or "leakage" of 'aid' monies, corruption, and even bribery did not represent a significant issue throughout that decade. Even inflation as a concern was nearly non-existent. In the sense that the rate of inflation was under control, the economic environment was relatively stable. There was also political stability, which contributes to economic growth, and competent economic administration. It is a commonly held belief that dictatorships and unbroken continuation of the system are conducive to economic progress. However, economic growth makes little progress when there is an excessive amount of 'democracy' or 'parody of democracy' and heavy politicking. Korea serves as a model. It is a regrettable compromise. However, if there is a true democracy and the leadership is in the hands of honest, committed, and capable individuals over an extended length of time, there may be good and stable economic outcomes. Malaysia is a wonderful example. Briefly, the outstanding foreign debt (or foreign aid) in 1952-53 equalled one million dollars. As of 30 June 1970, at the conclusion of the Third Five Year Plan, the sum was $2,91 7.8 million USD. This is a significant increase in 17 years. However, the burden was not as great as it would be in coming years. In the second phase, which began in the middle of the 1970s, there was a far greater

increase in foreign debt and foreign aid. We've chosen 1974-1975 as a baseline for the second phase. After the fall of East Pakistan in December 1971, the significant depreciation of the rupee in May 1972, and the widespread nationalization, this was in some ways a regular year. In 1974-1975, foreign aid and debt totalled 4,796 million USD. By 1991-92 (another 17-year span), it had risen to $16,481 million USD. In the table below, we compare the numbers from 30 June 1970 and 30 June 1991. The names of the lenders are also listed as follow.

Donors	(Million Dollars) 30 June 1970	30 June 1991
Total All Sources	2,917.8	151,470.8
I. International Agencies	623.3	6,502.8
IBRD (World Bank)	332.5	1,808.7
International Development Association (IDA)	269.0	2,171.9
International Finance Corporation (IFC)	10.7	39.3
International Fund for Agricultural Development (IFAD)	—	88.4
Asian Development Bank (ADB)	11.1	2,394.5
II. US Govt. and Agencies	1,212.5	2,974.9
US AID	1,087.1	1,499.3
US EXIM Bank and Others	67.7	409.6
PL 480	57.5	1,066.0
III.Other Countries		
Canada	78.3	516.1
USSR	63.8	242.8
UK	201.0	35.1
Germany	268.1	1,263.8
France	49.3	394.4
Japan	188.9	2,137.8
China	49.1	171.3
IV.Muslim Countries and Institutions	NA	617.6
Saudi Arabia	—	265.0
Abu Dhabi	—	103.0
Kuwait	—	101.9
OPEC Fund	—	50.1
Islamic Development Bank (IDB)	—	39.9

Table 13: Foreign Aid Loans Outstanding

Source: Government of Pakistan Central Statistical Bureau

It would be of interest to investigate the origins of foreign help in the form of loans. In 1970, international organizations accounted for 21,3 percent of total loans, while the United States contributed 41,5 percent. The position was reversed in 1991. International organizations contributed 42% of the total, while the United States contributed just 19%. There were three causes for this reversal. One explanation was the progressive decline in the US economy's growth rate and overall economic strength. The second cause was the development and expansion of new international organizations. New source was the International Fund for Agricultural Development (IFAD). IDA and IFC then extended their activities as IBRD affiliates.

June 1991 data suggest a sizeable loan from the Asian Development Bank (ADB). In reality, ADB loans (2,394,5 million US dollars) outpaced IBRD loans (World Bank). The ADB has been generous. The third reason is that other nations, particularly Japan, had a faster growth rate and a better balance of payments than the United States. The sum of Japan's loan (or help) was $2,137,8 million US dollars. This source contributed fifteen percent of the overall assistance. Interestingly, during the late 1970s and nearly the entirety of the 1980s, Muslim nations and organizations (OPEC Fund and Islamic Development Bank) were both grant and loan donors. In terms of loans, 4% of Muslim nations were represented. As previously said, the 'grants' component of foreign assistance increasingly diminished, and foreign aid eventually came to represent foreign loans. (Mohammad, 1993)

2.9.1. IMF Funding Provisions to Pakistan

The International Monetary Fund (IMF), established in 1944, was responsible for ensuring exchange rate stability and providing temporary support (under Stand-By Arrangement) to member states experiencing short-term balance of payments difficulties. The Fund created additional medium-term support facilities (i.e. SAF, ESAF, EFF, and PRGF) in recognition of the fact that short-term assistance is insufficient to handle certain challenges, such as emergent crises and structural vulnerabilities. A member utilizing IMF resources under these conditions must agree to a reform and stabilization program with the Fund. The disbursement of funding is contingent to IMF-imposed conditions. Pakistan is one of the IMF's "prolonged customers"; it stayed on the IMF's support program for more than twenty-five years, nearly continuously between 1988 and 2004. (The new Arrangement adds two more years). Table 13 lists the eight medium-term agreements negotiated between 1980 and 2004. The first six agreements (1980-1998) were terminated prematurely owing to Pakistan's failure to meet certain conditions. Despite extremely stringent requirements set by the IMF, the previous two agreements (SBA 2000 and PRGF 2001-2004) were implemented effectively (i.e. under SBA 56 against average normal conditions of 19 and under PRGF 81 against 45 in similar arrangements with other countries during the period). Pakistan chose to skip the last payment and terminate the PRGF Arrangement prior to December 2004 due to its improved external situation as a result of debt reduction arrangements, 9/11-related aid, privatization revenues, and increased remittances. The broad goals of the Arrangement were deemed to have been attained. In addition, the budget deficit and external debt ratio decreased. Inflation fell below 4 percent from 2001 to 2004. (re-emerging in later years and reaching 9 percent in 2005). (Fasihuddin, 2009)

Arrangement	Date of Arrangement (expiration)	Amount (SDR million)	Disbursement (SDR million)	Signed during rule of
EFF	24-11-80 (23-11-83)	1268.00	1079.00	Ziaul Haq
SBA	28-12-88 (7-3-90)	273.15	194.48	Benazir Bhutto
SAF	28-12-88 (27-12-91)	382.41	382.41	Benazir Bhutto
SBA	16-9-93 (15-9-94)	265.40	88.00	Nawaz Sharif
EFF/	22-2-94 (21-2-97)	379.10	123.20	
ESAF	22-294 (21-2-97)	606.60	172.20	
SBA	13-12-95 (31-3-97)	562.59	294.69	Benazir Bhutto
EFF/ESAF	20-10-97 (19-10-2000)	454.92 682.38	113.75 265.37	Nawaz Sharif
SBA	29-11-2000 (30-9-2001)	465.00	465.00	Pervez Musharraf
PRGF	7-12-2001 (5-12-2004)	1033.70	861.42	Pervez Musharraf

Table 14: IMF Support to Pakistan (1980-2004)

Source: IMF

Particularly in the areas of trade, interest rate management, and capital account liberalization, structural changes have advanced. In several regions, progress remained slow. Despite tax changes, the tax-to-GDP ratio remained low at 11%, but the quasi-fiscal deficit produced by subsidies and loans to public utilities remained elevated (1 percent of GDP). Although social indices improved, they remained well below intended levels. Upon completion of the PRGF Arrangement, the authorities asserted that they had broken the "beggar's bowl" and would no longer require IMF assistance in the future. The assertion was more rhetorical than factual. Initially, the IMF-established path was to be adhered to even after the completion of assistance Arrangements, and its progress was monitored through the Fund's annual Article IV consultation. Second, many World Bank/Asian Development Bank-supported measures (such as banking sector and tax changes) were intended to adhere to the IMF's guidelines. Thirdly, despite the absence of a support agreement with the IMF, the economy was more vulnerable to foreign development and remained highly reliant on external resources. During 2005-2008, Pakistan was obligated to adhere to the IMF's agenda despite the absence of any financial support agreements. (Fasihuddin, 2009)

RESULTS AND DISCUSSION

In this chapter, I have managed to link the current account deficits to a country's economic growth and well-being, following that, I have analysed and compared among Pakistan and other developing nations. I have highlighted what other developing nations have done to handle their deficits and what areas we are lacking in. Furthermore, the plausible causes of this current account deficit have been discussed and why Pakistan has not been able to exterminate these causes after all.

3.1. Current Account Deficit and Economic Growth

The current account balance appears to be a complex issue in economics. However, the current account is the point at which international economics and political realities intersect in nations that spend significantly more abroad than they get. When countries run big deficits, companies, trade unions, and legislators are sometimes eager to accuse trading partners of engaging in unfair tactics. Several aspects are under dispute, including the definition of a current account deficit or surplus and the several methods for calculating a current account balance. (Atish & Uma, 2020)

The current account represents the difference between the value of exports and imports of goods and services. A deficit indicates that a country imports more goods and services than it exports; however, the current account also includes net revenue (such as interest and dividends) and transfers from abroad (such as foreign aid), which are often a tiny portion of the total. In this context, a current account deficit frequently draws the ire of protectionists, who, apparently forgetting that one of the key reasons to export is to be able to import, consider exports "good" and imports "bad." (Atish & Uma, 2020)

Current account is also the gap between national (including public and private) savings and investment. Therefore, a current account deficit may imply a low amount of national savings relative to investment, a high pace of investment, or both. A current account deficit may be natural for capital-poor emerging nations that have more investment possibilities than they can afford to pursue due to low levels of domestic savings. Although recent research does not imply that emerging nations with current account deficits grow quicker, a deficit may stimulate faster production growth and economic development (perhaps because their less developed domestic financial systems cannot allocate foreign capital efficiently). In addition, private capital flows often from emerging to developed economies in actuality. In relation to their gross domestic product (GDP), very poor nations often have huge current account deficits that are supported

by state subsidies and loans. Does the length of a country's current account deficit matter? When a nation has a current account deficit, it accrues liabilities to the rest of the world that are supported by financial account flows. These will eventually need to be repaid. If a country fritters away its borrowed foreign cash on expenditure that delivers no long-term economic advantages, its capacity to repay—its fundamental solvency—could be called into doubt. This is because a government must be willing and able to earn (eventually) sufficient current account surpluses to return what it has borrowed to fund current account deficits in order to remain solvent. Consequently, whether a country should run a current account deficit (borrow more) depends on the size of its foreign liabilities (its external debt) and on whether the borrowing will finance an investment with a higher marginal product than the interest rate (or rate of return) it must pay on its foreign liabilities. But even if the country is intertemporally solvent — that is, its present commitments will be met by future income — its current account deficit may become unsustainable if it cannot acquire the required funding. A typical criticism of economics is that every issue is answered with "it depends." True, economic theory informs us that whether a deficit is desirable or bad depends on the reasons that cause it, but economic theory also tells us what to look for when evaluating the acceptability of a deficit. (Atish & Uma, 2020)

If the deficit represents an excess of imports over exports, it may be symptomatic of competitiveness issues. However, because the current account deficit also indicates an excess of investment over savings, it may also indicate a highly productive, expanding economy. If the deficit is due to poor savings rather than high investment, it may be the result of irresponsible fiscal policies or excessive consumption. Or, it might be the result of completely reasonable intertemporal trading, possibly as a result of a transitory shock or a shift in population. It makes little sense to call a deficit "good" or "bad" without understanding which of these factors is at play. Deficits reflect underlying economic tendencies, which may be favourable or unfavourable for a nation at a given moment. (Atish & Uma, 2020)

According to neoclassical economists, fiscal deficits are detrimental to economic growth (Bernheim, 1989). This is due to the fact that the deficit will increase a person's total lifetime consumption by moving taxes to future generations. If all economic resources are in use, a rise in consumption implies a decline in savings. To restore equilibrium to the capital markets, interest rates must rise. This implies that a prolonged deficit will eventually "crowd out" private capital accumulation and, in turn, reduce economic development. Diverse empirical investigations have been conducted to clarify these contradictory statements. The study of the connection between economic growth and budget deficits dates back to Martin and

Fardmanesh's work (1990). Using cross-sectional data from seventy-six industrialized and developing nations between 1972 and 1981, the authors examine the effect of various fiscal variables on economic development. These variables consist of the government fiscal deficit, expenditures, revenues, non-tax revenues, gross capital formation, and population growth. According to the results of the cross-sectional linear regression, the deficit and tax income have a negative effect on economic growth, whereas government spending has a positive effect. Furthermore, by splitting nations into low-, middle-, and high-income categories, the study indicates that only middle-income countries have a negative association between fiscal deficit and economic growth. (Wee-Yeap Lau & Tien-Ming, 2019)

Tan (2006) explores the dynamic relationships between budget deficits, inflation, and economic growth in Malaysia from 1966 to 2003 by focusing on a single country. The analysis identifies unidirectional causality between fiscal deficit and money supply, and between money supply and prices. The article concludes that monetization of a budget imbalance could have an inflationary effect on the economy.

If a current account deficit is financed by borrowing, it is seen less sustainable. This is due to the fact that borrowing is unsustainable over the long run and will burden governments with high-interest payments. In 1998, for instance, Russia was unable to pay its international debt. Other emerging nations, like Brazil and African nations, have encountered similar repayment difficulties. Large interest payments leave little capital for investment in countries. (Tejvan, 2019)

An extremely big balance of payments imbalance may eventually cause international investors to lose trust. Therefore, there is always a chance that investors would withdraw their funds, resulting in a sharp decline in the value of your currency (devaluation). This might result in a reduction in living standards and decreased investor confidence. A sustained current account deficit may indicate reliance on consumer spending, and that the economy is becoming imbalanced between sectors and between short-term consumption and long-term investment. For instance, the United Kingdom has a large proportion of its GDP devoted to consumer spending and comparatively low levels of investment, particularly in the manufacturing sector. This emphasis on domestic consumption might have negative long-term repercussions by reducing investment in production. Germany, which has a current account surplus and is typically thought to have higher levels of economic investment, might be contrasted with the United Kingdom. A current account deficit may indicate that the economy is losing its competitiveness and the currency rate is overpriced. (Tejvan, 2019)

3.1.1. Thirlwall's balance of payments constrained growth model or Thirlwall's Law

The concept of economic growth restricted by the balance of payments is known as the Thirlwall model. According to the Thirlwall model, a rise in the income elasticity of import demand (π) decreases the rate of growth of the equilibrium product with regard to the balance of payments. Observe that the causality in this model runs from exports to the product, which is why, contrary to traditional theories of economic growth, it is believed that a rise in external demand is a significant contributor to economic growth. Thirlwall and Hussain (1982) investigated an expanded model that permits uneven international trade and capital flow over the long term. Additionally, their research on developing nations yielded data that supported this enlarged new model. (Anuradha, 2017)

Thirlwall's law (named after Anthony Thirlwall) states that if long-term balance of payments equilibrium on current account is required and the real exchange rate remains relatively stable, then a country's long-term growth can be approximated by the ratio of the growth of exports to the income elasticity of demand for imports (Thirlwall, 1979). Thirlwall's balance of payments constrained growth model or Thirlwall's Law is frequently referred to as the dynamic Harrod trade multiplier result, following Roy Harrod's (1933) static foreign trade multiplier result that $Y = X/m$, where Y is national income, X is exports, and m is the marginal propensity to import, which is derived under the same assumptions as Thirlwall's Law (O'Hara, 1999). The assumption of balance of payments equilibrium on current account can be loosened to allow capital flows, however at realistic quantities of sustainable flows (such as 3% of GDP), capital flows have minimal empirical impact on the growth projections of the basic model. Since 1979, the concept has been rigorously evaluated with widespread endorsement from both industrialized and developing nations. The model offers an alternative to the supply-side models of neoclassical growth theory, which are closed economy models without demand restrictions. In the Thirlwall model, the ultimate growth limitation is a lack of foreign exchange or export growth that can be accommodated by factor suppliers. Changes in economic growth, not changes in relative pricing in international commerce, are what stabilize the balance of payments.

3.2. Impact of Current Account Deficit on Pakistan's growth

Pakistan's output growth rate has averaged 5.3% per year during the 1960s, while productivity growth has averaged 2.5%. In the 1950s and 1960s, Pakistan transitioned from a weak agrarian economy to one that was quickly industrializing; nevertheless, it has never since reached sustained growth rates comparable to those of the Asian Tigers or, more recently, China. For the next decade, the Poverty Reduction Strategy (Ministry of Finance, 2007) has projected a

GDP growth rate of 7–7.5% each year. The issue that inevitably arises is whether this is achievable or an overly ambitious objective. If the former, what policy actions are required to guarantee this result? If the latter is the case, what inhibits growth? Recurrent crises in the current account of the balance of payments are a significant issue for Pakistan's economy. When Pakistan's output growth rate increases, and this is not attributable to a rise in the growth of its exports, the outcome is a balance-of-payments problem. In fact, recent trends in Pakistan's economy indicate that the most significant impediment will likely be an underperformance in export growth and the resulting balance-of-payments issues (Felipe & Lim, 2008). Particularly concerning are the altering mix of production and the escalation of sizable deficits in current and fiscal accounts. The current account deficit increased to 8.4% of GDP in 2007–08. This has precipitated a severe balance-of-payments problem. As a result, Standard & Poor's and Moody's reduced Pakistan's credit rating. This has had significant effects on international borrowing. (Felipe et al., 2010)

In the past, as in the present, current account deficits have been partially funded by short-term foreign borrowing, which is extremely volatile and carries the risk of capital flight and exchange rate collapse. In prior years, positive net capital inflows avoided a balance-of-payments crisis. According to Felipe and Lim (2008), a balance-of-payments deficit is not necessarily a bad thing. If the capital flows are utilized for constructive investment, there is no need for alarm. Specifically, if the funds are utilized to boost export performance and increase the competitiveness of industries that compete with imports, this may be sufficient to achieve a future improvement in the current account. (Felipe et al., 2010)

This is not the situation with Pakistan at the present time. According to Felipe and Lim (2008), "in the case of Pakistan, the current deficit implies poor export growth... and, eventually, export competitiveness issues." The continuous current account deficit of Pakistan does not indicate a highly productive economy." The collapse of export growth is at the heart of the current situation, which does not speak well for future growth. Only Afghanistan, the Kyrgyz Republic, Mongolia, Sri Lanka, Turkmenistan, and Uzbekistan have seen lower export growth rates than Pakistan during the 1960s. There is an immediate need for a dramatic reorganization of the economy, so that exports are not so dependent on textiles, and towards the production and export of manufactured goods with a greater income elasticity of demand. In November 2008, the crisis had gotten so severe that Pakistan was compelled to enter an IMF programme and borrow $7.6 billion in order to avoid defaulting on its national debt. From March to November 2008, the rupee lost 20% of its value. As a loan condition, the Fund usually requires budgetary discipline from recipient nations (i.e., a lower budget deficit with a rapid move to a balanced

budget). This will surely lead to a reversion to a slower growth pace. To prevent recurring balance-of-payments crises, the growth rate must be maintained continuously below the growth in productive potential. (Felipe et al., 2010)

Likewise, the Pakistan Economic Survey 2007–08 (p. xvii) suggests that the government's main goal should be "repair of imbalances by reducing aggregate demand through suitable measures." In other words, despite the high unemployment rate and the harm it would do to investment, the proposed solution for the balance-of-payments issue is to slow economic development. This would unquestionably address the problem, as slower growth in production would limit the rate of increase of imports, but the growth of exports is mostly influenced by the expansion of international markets and would thus be unaffected by the slowing of domestic growth. In this regard, Pakistan is approaching or is now suffering a balance-of-payments limitation on its economic growth. However, the solution is not to cut aggregate demand, but rather to implement measures that would boost export growth and so eliminate the balance-of-payments restriction. (Felipe et al., 2010)

The fundamental premise of the balance-of-payments limited growth model is that, in the long term, no nation can develop faster than the pace associated with a balanced current account, unless it can finance ever-increasing deficits. In fact, if imports expand faster than exports, the current account deficit must be funded by borrowing from abroad, often in large part by an increase in short-term capital inflows; but this cannot continue forever. Thirlwall's paper is the seminal one (1979). The reason why this is not sustainable is obvious. If the growth in net inward financial flows exceeds the growth in GDP, then the ratio of net foreign debt to GDP will necessarily increase. There is a maximum magnitude at which this ratio may grow before international financial markets get anxious about the prospect of private and, especially in less-developed nations, public default. If the majority of borrowing is on a short-term basis, capital flight may occur, leading to a collapse of the currency rate. This will not only result in capital losses in foreign currency (most notably US dollars) for domestic assets controlled by foreigners (the lenders), but it will also result in serious local liquidity issues. This is especially true for a great number of developing nations, as international borrowing by banks and corporations is typically denominated in a foreign currency, typically the US dollar. As the exchange rate plummets, it becomes increasingly difficult for domestic enterprises to get domestic capital to finance their debt and day-to-day operations, frequently resulting in catastrophic outcomes. (Felipe et al., 2010)

The precise net foreign debt-to-GDP ratio at which it becomes difficult for a country to borrow on international financial markets will vary from country to country, depending on the health

of its underlying economy and the perceived risk of government default. The United States, for instance, may run a significantly greater deficit as a proportion of its GDP than most less-developed nations, yet even the magnitude of the United States' current account deficit is limited. (Felipe et al., 2010)

Consequently, there is a growth rate that a country cannot surpass for an extended period, as doing so will result in immediate balance-of-payments issues. This is the "equilibrium balance of payments growth rate." Simply said, an increase in a country's growth rate because of domestic demand management measures boosts the growth of imports via the import demand function, but export growth, which is mostly influenced by growth in the country's outside markets, is unaffected. (Felipe et al., 2010)

The following is a Pakistan's growth in terms of GDP as well and the world's growth itself.

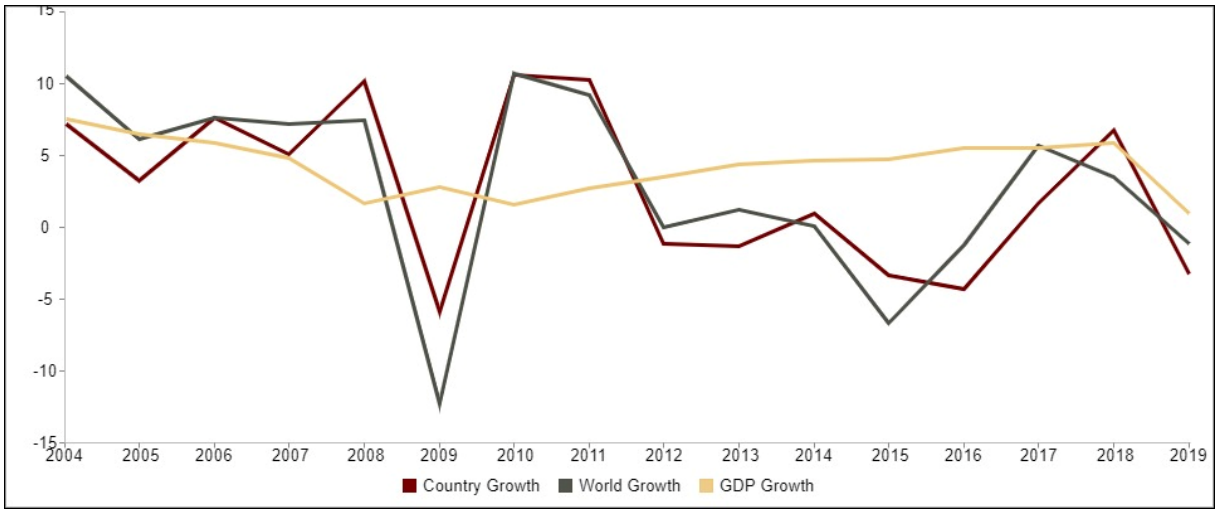

Figure 3: Pakistan Country Growth v/s World Growth V/S GDP Growth

3.3. Comparisons between Pakistan and other developing nations (Turkey, India, Sri Lanka)

In this section, I have compared some of the important indicators used to study the international position of a country. They are the following:

- Current Account

Current Account equals the total of the trade balance (exports minus imports), net factor income (such as interest and dividends), and net transfer payments (e.g., foreign aid).

The last current account for Pakistan was recorded as USD -4323 million with reference to June 2022 while that of Turkey was USD -6468 million.

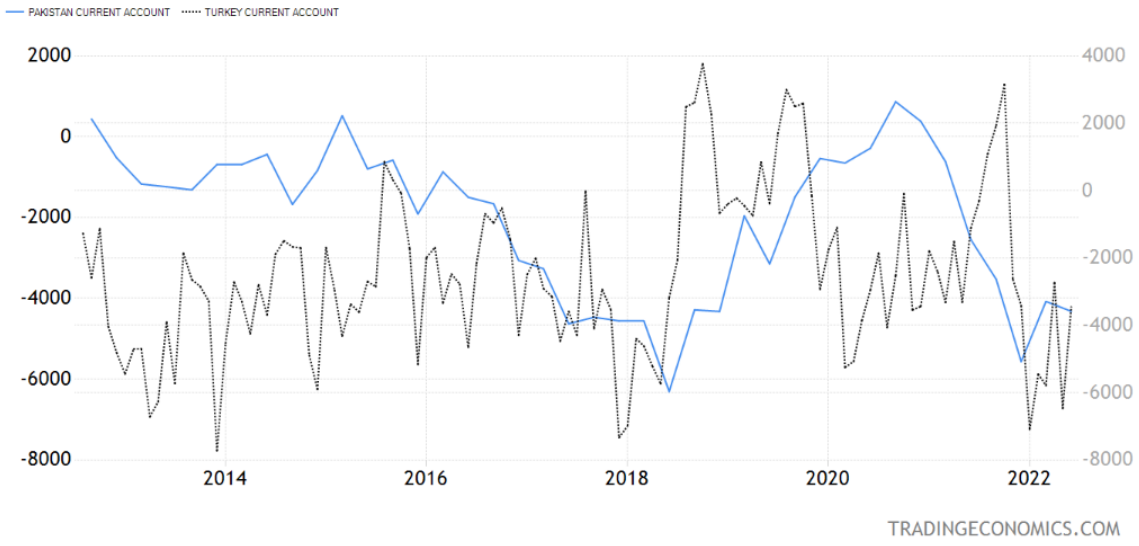

Figure 4: Current Account (Pakistan and Turkey)

Source: State Bank of Pakistan and Central Bank of the Republic of Turkey

The last current account for Pakistan was noted as USD -4323 Million with reference to June 2022 while that of Sri Lanka was USD -1331 million with reference to March 2022.

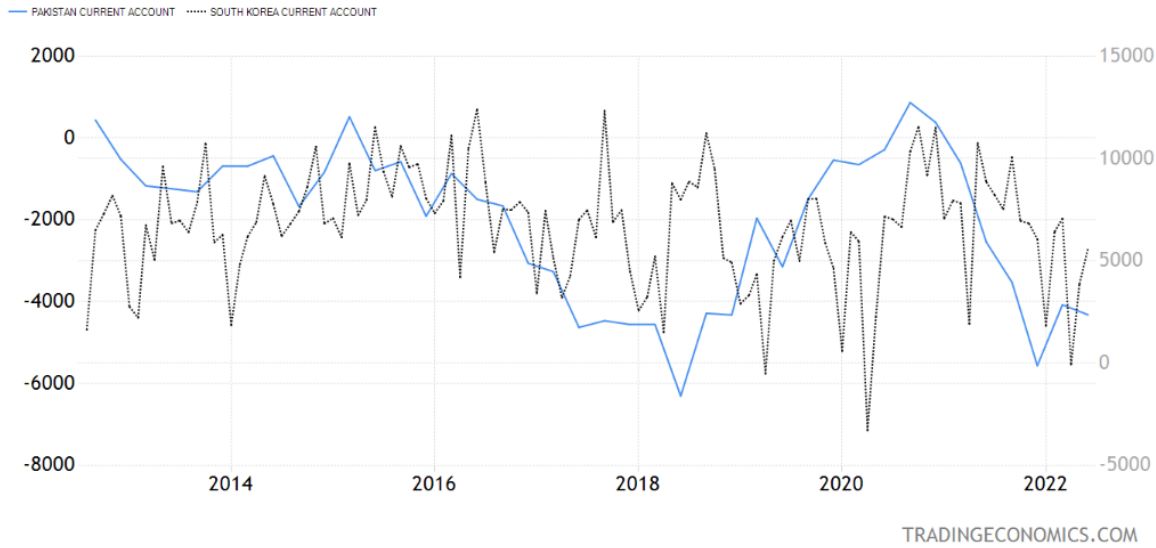

Figure 5: Current Account (Pakistan and Sri Lanka)

Source: State Bank of Pakistan and Central Bank of Sri Lanka

The last current account for Pakistan was logged as USD -4323 Million with reference to June 2022 while that of India was USD -13400 million.

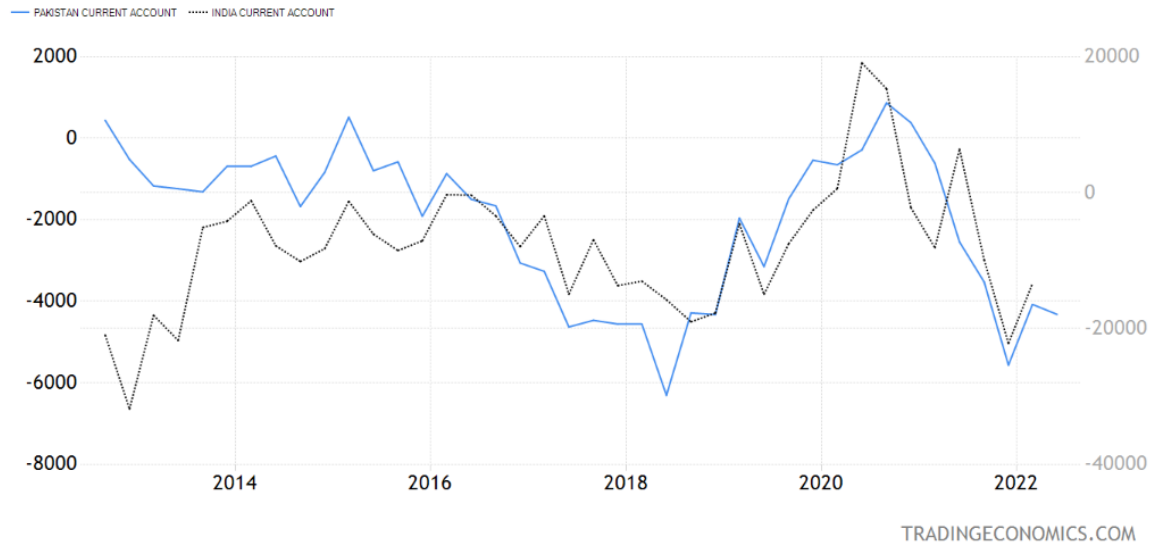

Figure 6: Current Account (Pakistan and India)

Source: State Bank of Pakistan and Reserve Bank of India

- **Current Account to GDP**

The Current account balance as a percentage of GDP indicates the level of a country's international competitiveness. Typically, nations with a significant current account surplus have an export-driven economy with a high savings rate but poor domestic demand. Conversely, nations with a current account deficit have robust imports, low savings rates, and high personal spending rates as a proportion of disposable earnings.

The last figure recorded for Pakistan was -0.6 percent of GDP as of June 2021 and that of Turkey as -1.7 percent of GDP in December 2021.

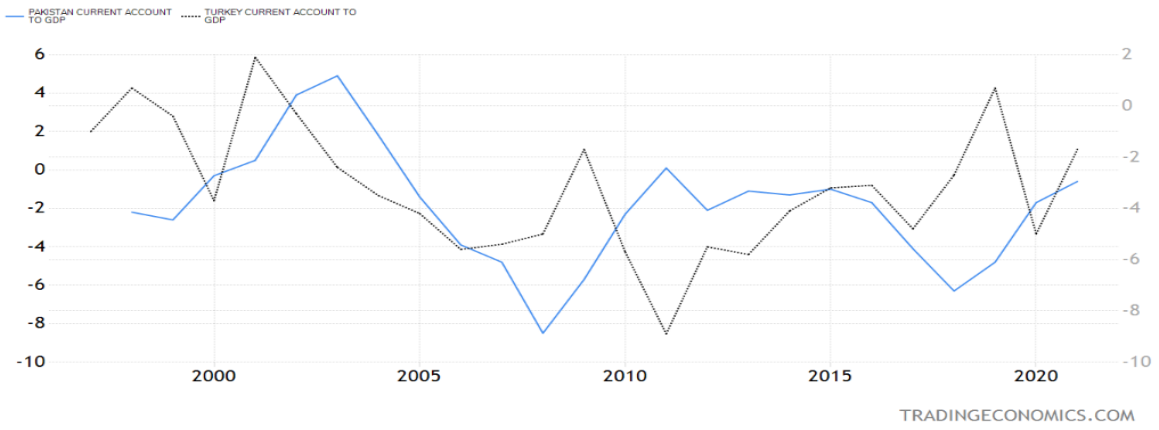

Figure 7: Current Account to GDP (Pakistan and Turkey)

Source: State Bank of Pakistan and Central Bank of the Republic of Turkey

The last number noted for Pakistan was -1.3 percent of GDP Jun 2021 while that of Sri Lanka as 3.5 percent of GDP in December 2020.

Figure 8: Current Account to GDP (Pakistan and Sri Lanka)

Source: State Bank of Pakistan and Central Bank of Sri Lanka

The last figure logged for Pakistan was -0.6 percent of GDP in June 2021 and that of India was 1.7 percent of GDP in December 2021.

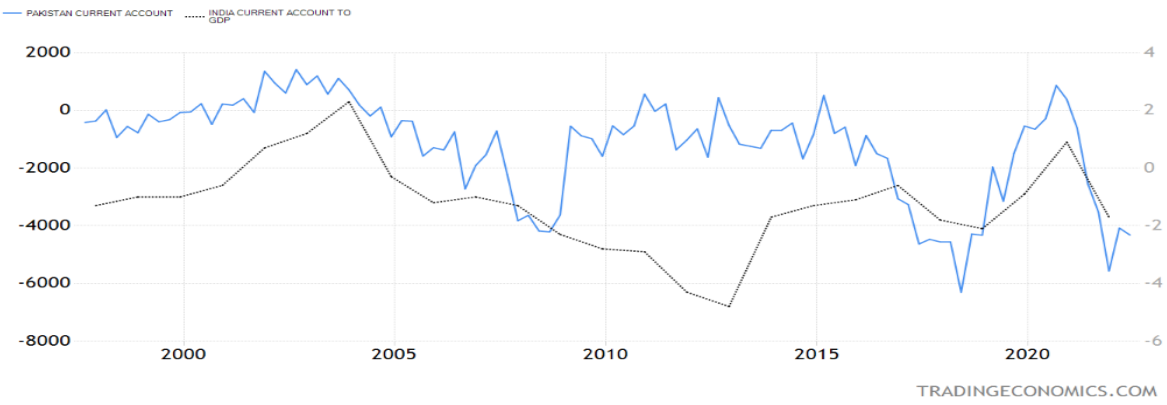

Figure 9: Current Account to GDP (Pakistan and India)

Source: State Bank of Pakistan and Reserve Bank of India

- **Balance of Trade**

Pakistan has maintained a constant trade imbalance since 2003, primarily due to its high energy imports. Since 2012, China has replaced the United States as Pakistan's main commercial partner. In recent years, trade deficits with China, India, the United Arab Emirates, Saudi Arabia, Kuwait, and Malaysia were the largest. The United States, Afghanistan, Germany, and the United Kingdom all report trade surpluses with Pakistan.

The last balance of trade figure was noted as PKR -582869 million for Pakistan in July 2022 and USD -8170 million for Turkey in June 2022.

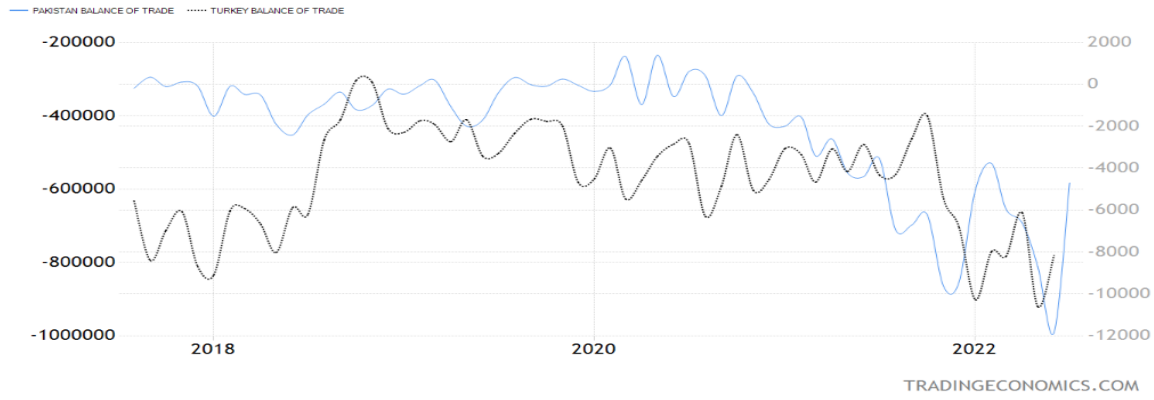

Figure 10: Balance of Trade (Pakistan and Turkey)

Source: State Bank of Pakistan and Central Bank of the Republic of Turkey

It was recorded as PKR -582869 million for Pakistan in July 2022 and that of Sri Lanka as USD 21 million in June 2022.

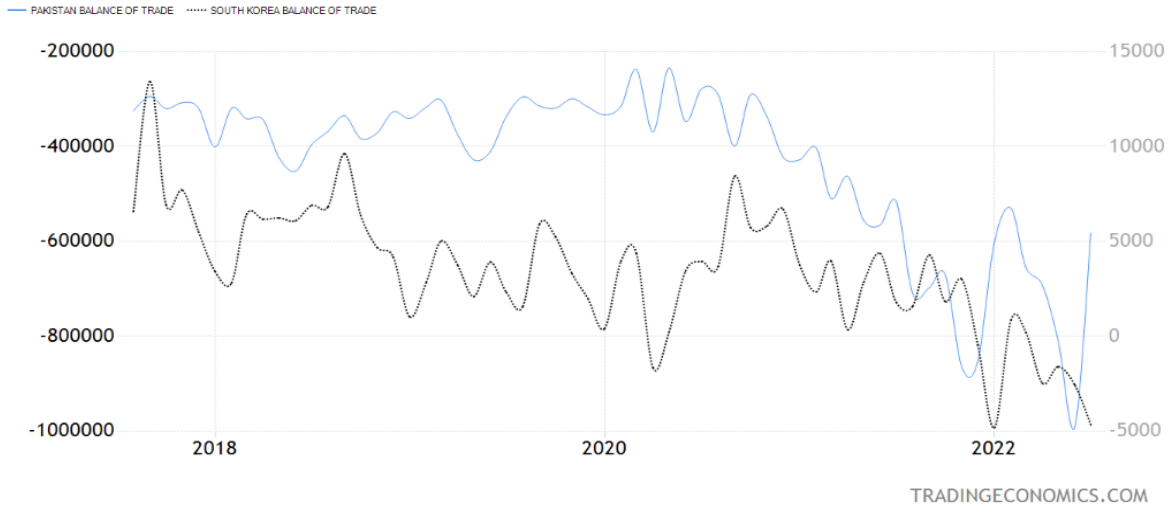

Figure 11: Balance of Trade (Pakistan and Sri Lanka)

Source: State Bank of Pakistan and Central Bank of Sri Lanka

The value was noted for Pakistan as PKR -582869 million in July 2022 and USD -30 billion for India in July 2022.

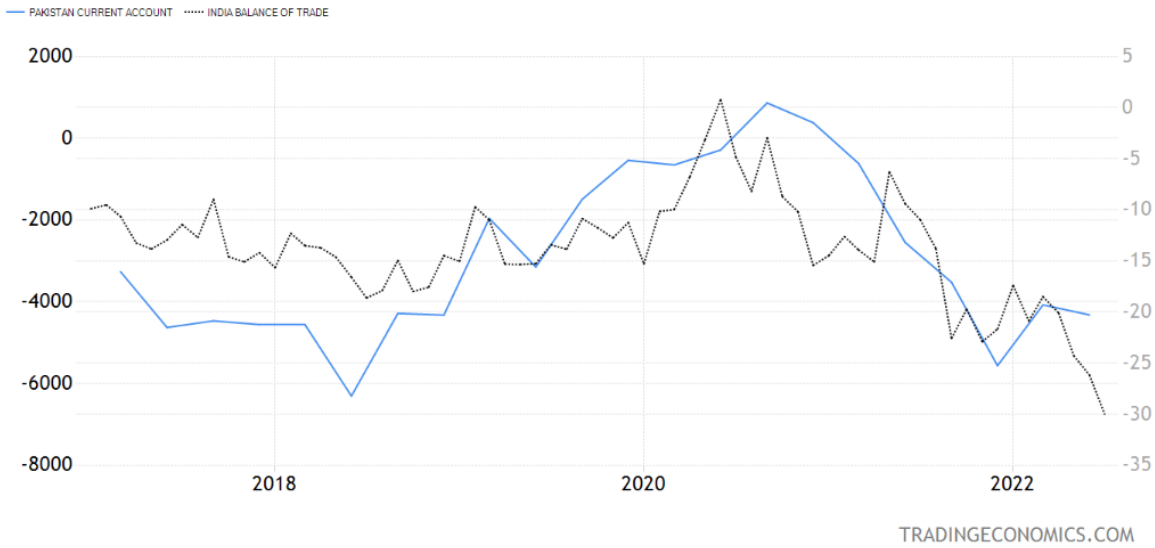

Figure 12: Balance of Trade (Pakistan and India)

Source: State Bank of Pakistan and Reserve Bank of India

- **Foreign Exchange Reserves**

Foreign Exchange Reserves are cash and other reserve assets, such as gold, maintained by a central bank or other monetary authority for the purpose of balancing a country's payments, influencing the foreign exchange rate of its currency, and maintaining market confidence.

The figure was recorded as USD 16406 million in April 2022 for Pakistan and for Turkey it looked like USD 67770 million in August 2022.

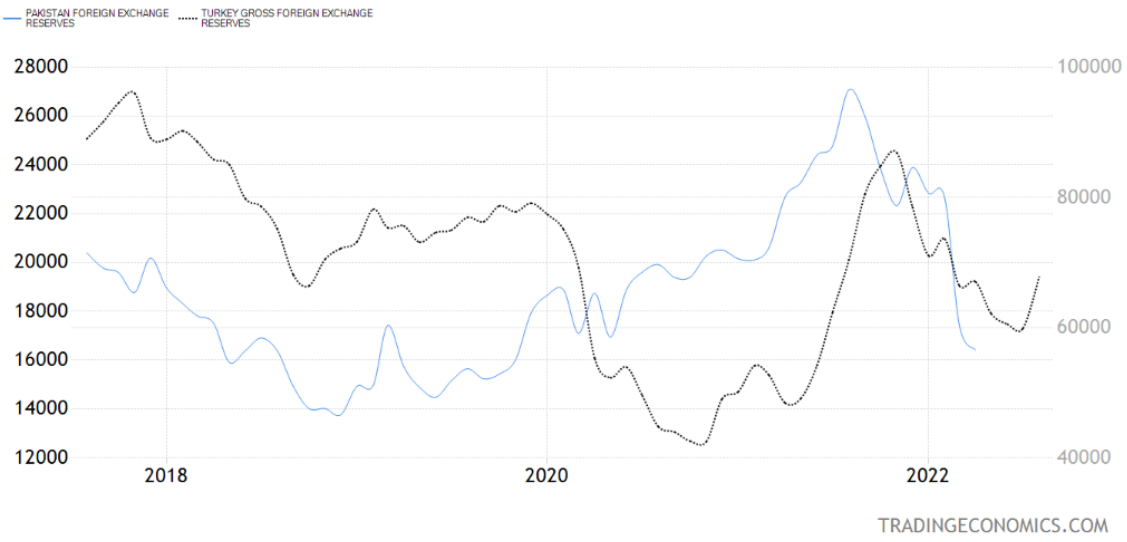

Figure 13: Foreign Exchange Reserves (Pakistan and Turkey)

Source: State Bank of Pakistan and Central Bank of the Republic of Turkey

The value was USD 16406 million in April 2022 for Pakistan and for Sri Lanka, it was recorded as USD 1920 million in May 2022.

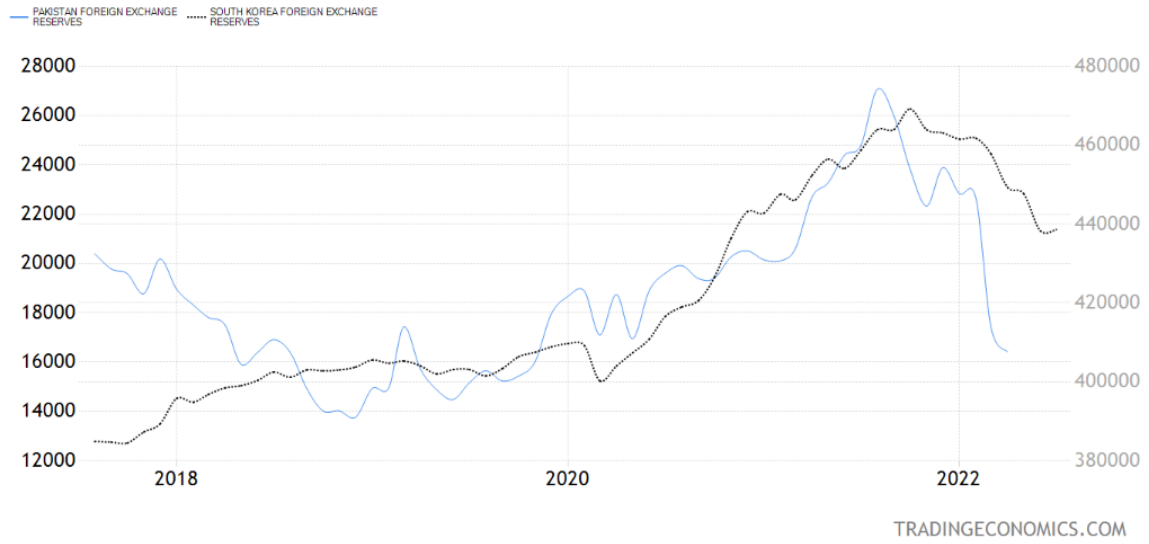

Figure 14: Foreign Exchange Reserves (Pakistan and Sri Lanka)

Source: State Bank of Pakistan and Central Bank of Sri Lanka

The foreign exchange reserves for Pakistan were USD 16406 million as of April 2022 and USD 3104071 million for India in July 2022.

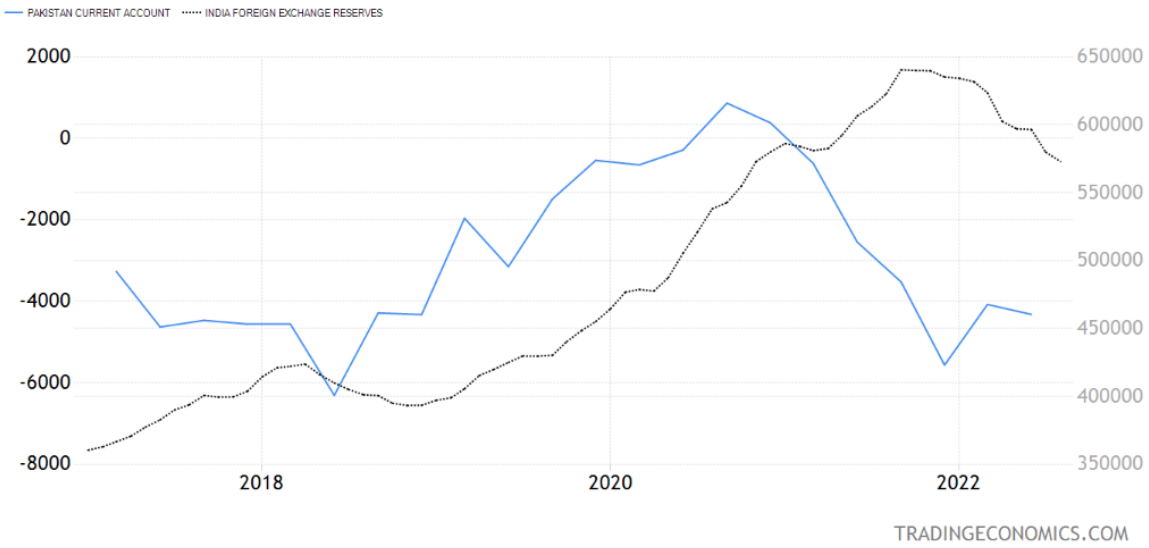

Figure 15: Foreign Exchange Reserves (Pakistan and India)

Source: State Bank of Pakistan and Reserve Bank of India

3.3.1. Current Account Deficit of Turkey and its implications

Many emerging countries have current account deficits because they import a substantial proportion of their production inputs; or, to put it another way, their growth is import-driven. However, this relationship between growth rate and current account deficit is not always

consistent. Especially in nations where economic growth is accompanied with a surplus in foreign trade, improvements in real national income may result in a reduction in the current account deficit. (Telatar, 2007) This will have a beneficial effect on the current account deficit when the export rate rises alongside a drop in production costs and falling costs in a growing national economy. However, the direction of the effect of economic development on a country's current account deficit relies on the proportion of income growth that is saved and spent. If spending exceeds savings, then the current account deficit will grow. Economic growth that is dependent on imports because imported commodities are employed as raw materials, semi-finished products, or capital goods to make export goods, and which therefore increases production, would necessarily lead to an increase in imports and a current account deficit. (Coskun, 2010)

Kasman, Turgutlu, and Konyal (2005), discussing the topic in the context of the Turkish economy, determined that there is a long-term constant correlation between current account deficit, real exchange rate, and economic growth in Turkey, and that an overvalued Turkish Lira has a greater negative impact on current account deficit than economic growth. In a study attempting to establish the existence of a causal link between current account balances and economic growth, deficit, economic growth, and exchange rate, Erbaykal (2007) conducted a causality test using Toda and Yamamoto[8] methodology, concluding that both economic growth and exchange rate contributed to current account deficit. In separate research, Telatar and Terzi (2009) used VAR[9] analysis to analyse the link between the current account deficit and economic development in Turkey. They discovered, based on impulse-response functions, that the current account deficit is negatively correlated with economic growth. There is a statistically significant negative association between the current account deficit and a shock of one standard deviation in growth rate. Ylmaz and Aknc (2011), on the other hand, utilized Granger causality and Johansen cointegration tests to examine the relationships between Turkey's GDP and current account deficit. In this study, a long-term link between GDP and current account deficit was observed, although the Granger causality test[10] revealed unidirectional causality from GDP to current account deficit. Kostakoglu and Dibo (2011) examined the relationship between current account deficit and growth rate in Turkey using the VAR method and impulse-response[11]

[8] The cointegration test validates the presence of equilibrium connections between variables over the long run. If cointegration exists, a long-term equilibrium relationship or ECM is utilized.
[9] Value-at-risk is a statistical measure of the riskiness of financial entities or portfolios of assets.
[10] The Granger causality test is a statistical hypothesis test used to determine if one time series may be used to foretell another.
[11] A impulse-response function explains the evolution of the variable of interest over a specific time range following an initial shock.

functions. They concluded that one unit of GDP shock has a negative impact on the current account balance/GDP ratio, indicating that economic growth led to an increase in current account deficit.

During moments of crisis in Turkey, the ratio of current account deficit to national revenue has reached between 3.5% and 4%, leading to the conclusion that a current account deficit constitutes a crisis if it surpasses a specific threshold number (Erbaykal, 2007). Consequently, changes in current account are viewed as indicators of economic trends and are known to significantly influence economic actions and expectations (Erdogan and Bozkurt, 2009).

Figure 16 displays the annual current account deficit for Turkey.

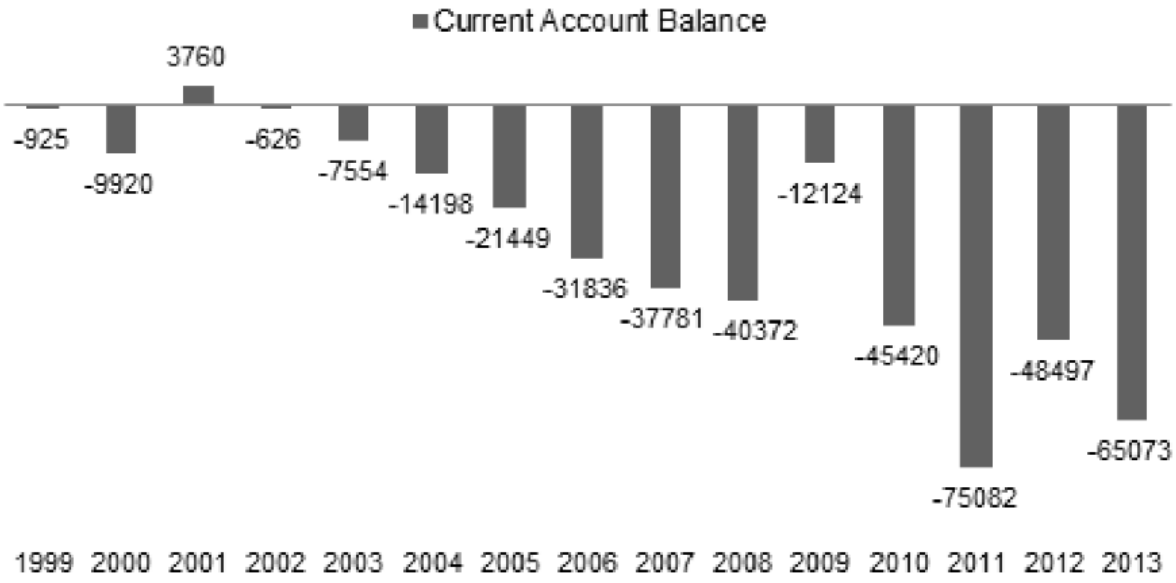

Figure 16: Current Account Deficit (Million Dollars)

Source: Central Bank of Turkey (CBT)

As shown in the above graph, the current account deficit has increased gradually, notably after 2003. As a result of the 2001 crisis, domestic demand decreased, resulting in a current account deficit surplus of $3.7 billion. In the years after 2001, the current account deficit began to rise, and the extent of these deficits expanded progressively until 2009. The effects of the global crisis on local and international demand were apparent beginning in the fourth quarter of 2008, while the current account deficit underwent a precipitous reduction in 2009, falling to -12.1 billion dollars. After 2009, however, the current account deficit began to increase again. In 2011, the current account deficit widened to a total of -75.1 billion dollars as a result of a recovery in home demand. In 2010, international demand was on a downward trend, while local demand rebounded. As a result of CBT's monetary policy implemented in late 2010, domestic

demand slowed with the macroeconomic measures implemented in 2011, which slowed the growth rate in 2012 and consequently led to a decline in imports and was a determining factor in the 2012 reduction of the current account deficit. The increase in the current account deficit in 2013 was mostly due to rising imports and net gold import trends that exceeded historical norms.

The link between growth rate and current account deficit is seen in Figure 17. As seen in Figure 17, the association between growth rate and current account deficit is substantial. This is mostly due to the low ratio of domestic savings to investments in Turkey.

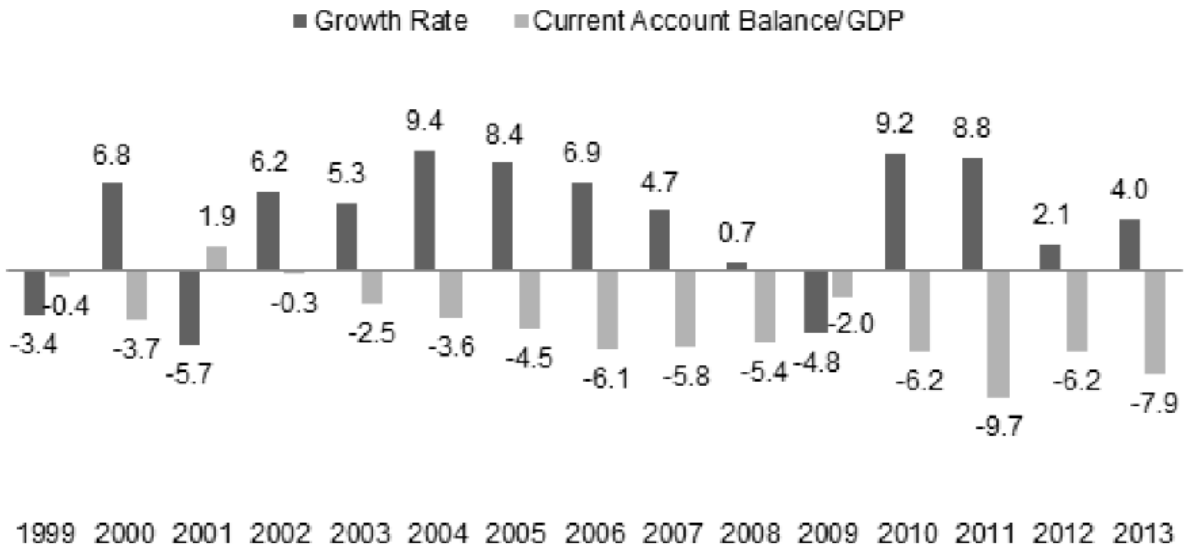

Figure 17: Growth rate and current account balance/GDP (%)

Source: Central Bank of Turkey (CBT) and Turkish Statistical Institute (TSI)

When domestic investments surpass domestic savings, the shortfall is compensated by foreign savings, which is reflected in economic statistics as a current account deficit. Particularly during the period 2001-2007, macroeconomic stability was largely attained, the inflation rate and real interest rates fell, and this resulted in a surge in consumption and investment demand that exceeded national revenue, which was met by foreign deposits (CBT Bulletin, 2009).

The structural characteristics of the economy, which need the import of intermediate products to fulfil the rising total demand, also contribute to the observed substantial correlation between the growth rate and current account deficit, as shown in Figure 16. As a country that imports most of its energy (mostly oil and gas), Turkey's current account deficit is significantly impacted by energy costs, and rising energy prices have a widening effect on current account deficit (CBT Bulletin, 2009)

3.3.1.1. Initiatives to overcome current account deficit

The low per capita family income of $10,000 makes it difficult for families to save. As a result of the Turkish preference for spending, the country has accumulated a current account deficit of 10 percent of GDP. Primarily, it imports fuel, but it also imports chemicals, machinery, and semi-finished items for use in export manufacturing (which are generally very low value added). Automobiles, electrical appliances, textiles, chemicals, and steel are the principal exports of Turkey. The country is a net importer since its export-to-import ratio (the value of items exported relative to the value of products imported) is just 56%.

The Turkish government has recently implemented an investment incentive program to encourage the private sector to create more of the imported critical items and to stimulate the production of commodities with a greater value-added. To encourage investment to impoverished areas, the incentive zones are organized into six regions. Priority will be given to projects that begin before the end of 2012, and incentives will decrease steadily over the following years. Attractive features of the program for strategically vital industries such as steel, chemicals, equipment, and automobiles include:

- Exemption from customs duties.
- Exemption from value-added tax on locally acquired or imported machinery and equipment; Social security premium payment for up to 12 years (the government would subsidize up to 50 percent of the social security premiums generally paid by companies for their employees).
- Regardless of location, fifty percent of the investment is tax-deductible. Depending on the zone, this has the effect of cutting the corporation tax rate to as low as 2 percent. The corporation tax rate will be decreased until it meets the contribution-to-investment rate.
- Interest subsidies on loans up to 50 million Turkish lira (TRY) The loans must have a maximum implementation length of five years and cannot exceed 5% of the investment in fixed assets.
- Allocation of state land (the government will supply the land at no cost for the investment).
- Investment-related building construction is free from value-added tax. (Mete Yüksel, 2021)

3.3.2. Current Account Deficit of Sri Lanka and its implications

Given the small, open, and import-reliant structure of Sri Lanka's economy, the current account deficit is likely a significant macroeconomic indicator for policy decisions and economic performance evaluation. In this context, a thorough comprehension of the dynamic nature of Sri Lanka's current account deficit is crucial in many ways. Since the liberalization of the economy in 1977, Sri Lanka's current account balance has continued to deteriorate. An in-depth empirical investigation of the dynamic behaviour of Sri Lanka's current account deficit might give investors, policymakers, and future researchers with valuable insights. Sri Lanka's current account deficit has persisted over the past three decades. The results indicate that the current account deficit has a positive and significant long-term relationship with government budget, external debt, degree of openness, financial deepening, real GDP growth, and relative income, as well as a significant negative relationship with foreign reserves and exchange rate. (Niranjala & Selliah, 2012)

Since gaining independence, the nation is experiencing its greatest financial crisis. Since the beginning of the year, the rupee's value has decreased due to rising commodity costs, a sluggish tourist industry, and a budget deficit. Due to insufficient international reserves, the Central Bank has been unable to protect the currency, causing the government to default on some debt payments in May and ban imports of essential items. Meanwhile, skyrocketing prices and power outages are stifling economic activity, with the services PMI falling 7.5 points in April and continuing to tumble in May; schools and government offices were forced to close in late June, portending a bleak outlook for future economic activity. In May, a new administration was sworn in, and IMF bailout discussions became its main priority. To this goal, it announced a wide variety of tax hikes in May, which might exacerbate civil discontent and cause the resignation of the president. (Focus Economics, 2022)

Sri Lanka is experiencing its greatest economic crisis since the country's independence from British colonial authority in 1948, and the island nation continues to see daily changes. In May 2022, Prime Minister Mahinda Rajapaksa resigned, opening the way for the nomination of the new PM, Ranil Wickremesinghe. This is merely the most recent of many significant political and economic changes in Sri Lanka over the past several years. The 26-year civil war that concluded in 2009 had a profound effect on Sri Lanka's domestic economy. The 2008 global financial crisis depleted the country's foreign exchange reserves, and economic mismanagement by successive administrations led to budget shortfalls and Balance of Payments (BOP) imbalances. Combined with the rise in government expenditure to implement COVID-19 alleviation measures, the country's increasing foreign debts have structurally damaged the

domestic economy. When the pandemic struck, the country's GDP growth rate had fallen from 8.01 percent in 2010 to (−) 3.56 percent in 2020. (Soumya, 2022)

Sri Lanka is a textbook example of the 'twin deficits' idea, which states that an economy's current account and fiscal account move in the same direction. As evidence of the connection between the two, we have: CA = (SpI) + (T G); where CA is the current account balance, Sp is the total private savings, I is the private investment expenditure, T is the Government tax revenue and G is the Government spending (including transfers), and the total Government savings Sg = (T G) represents the fiscal account balance. Consumption-driven economies combined with large levels of domestic and international debt, as is the situation with Sri Lanka, are characterized by the twin deficits. In this instance, the home economy's surplus demand boosts imports and causes inflation, which makes domestic commodities less competitive on international export markets. (Soumya, 2022)

Since 1970, Sri Lanka's twin deficits on the current and fiscal accounts have progressed in tandem (except for a current account surplus in 1977), but the link between the two has diminished since 2000. (see Figure 18). National savings have generally lagged national investment, although the gap has narrowed over time after reaching a high of 19.8 percent of GDP in 1980, when large-scale public investment programmes were implemented (see Figure 19). (Soumya, 2022)

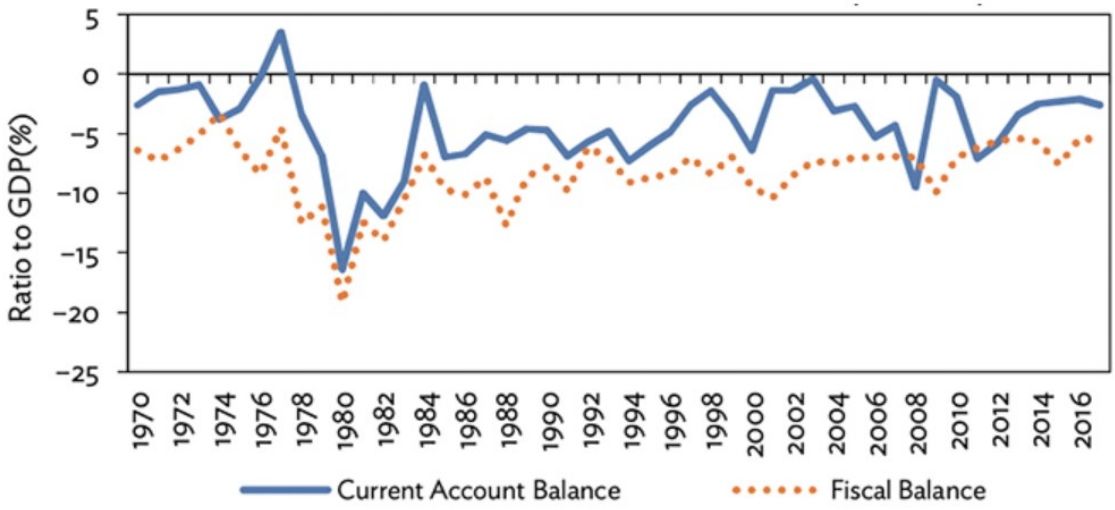

Figure 18: Trends in Sri Lanka's Current Account Balance and Fiscal Balance (1970-2016)

Source: Asian Development Bank, Data from Central Bank of Sri Lanka

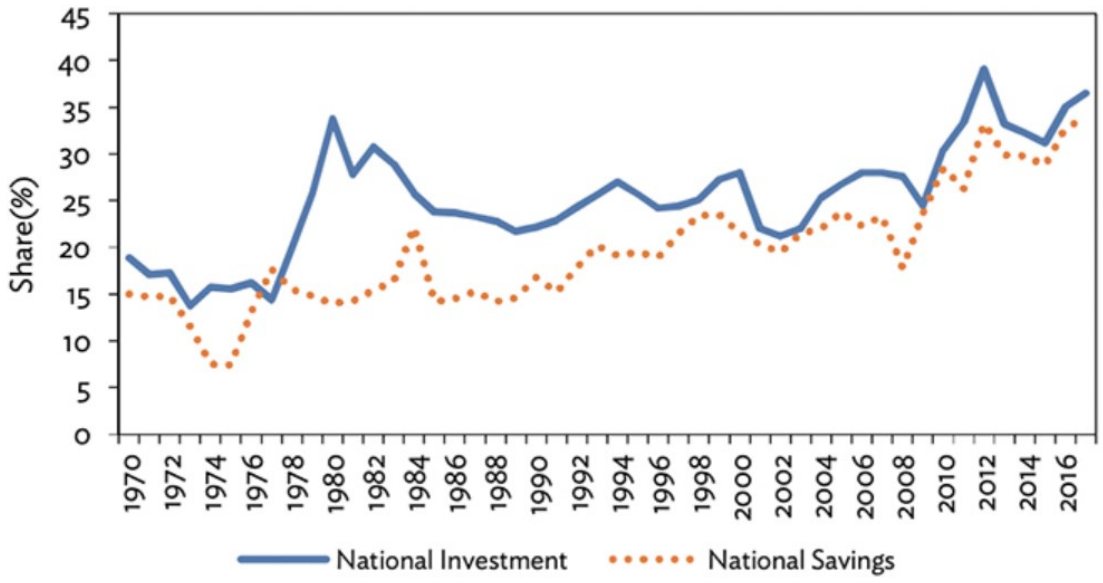

Figure 19: Trends in Sri Lanka's National Investment and National Savings (1970-2016)

Source: Asian Development Bank, Data from Central Bank of Sri Lanka

The occurrence of twin deficits exacerbated Sri Lanka's dependence on foreign debt, making the economy more vulnerable to external shocks like as the COVID-19 epidemic. During the pandemic era, Sri Lanka's Government spending (G) had surged in pace with global expenditures, but tax cuts just prior to the epidemic had significantly reduced tax receipts (T), therefore dramatically increasing fiscal deficits and current account deficits. In fact, Sri Lanka's Balance of Trade has consistently shown a deficit, with a roughly growing tendency over the years (see Figure 20). Sri Lanka's trade deficit reduced from US$ (-)1085 to US$ (-)762 between December 2021 and March 2022, showing a sharp decline in imports due to FOREX depletion and the start of an economic crisis. (Soumya, 2022)

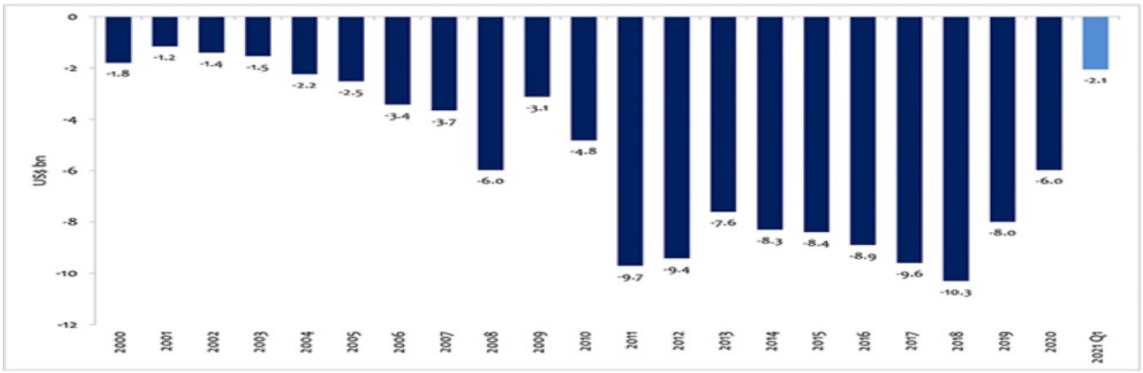

Figure 20: Sri Lanka's Balance of Trade (2000-2021)

Source: Central Bank of Sri Lanka

Historically, Sri Lanka's capital account and current account balances have moved in opposite directions: the former has been in surplus, while the latter has been marked by persistent deficits. There have been a few notable outliers, such as during the financial crisis of 2008-2009, when Sri Lanka's capital account balance dropped catastrophically (see Figure 21). This disparity is characteristic of consumption-driven developing countries that are magnets for incoming capital investments, which provide the FOREX to finance imports to satisfy local demand. (Soumya, 2022)

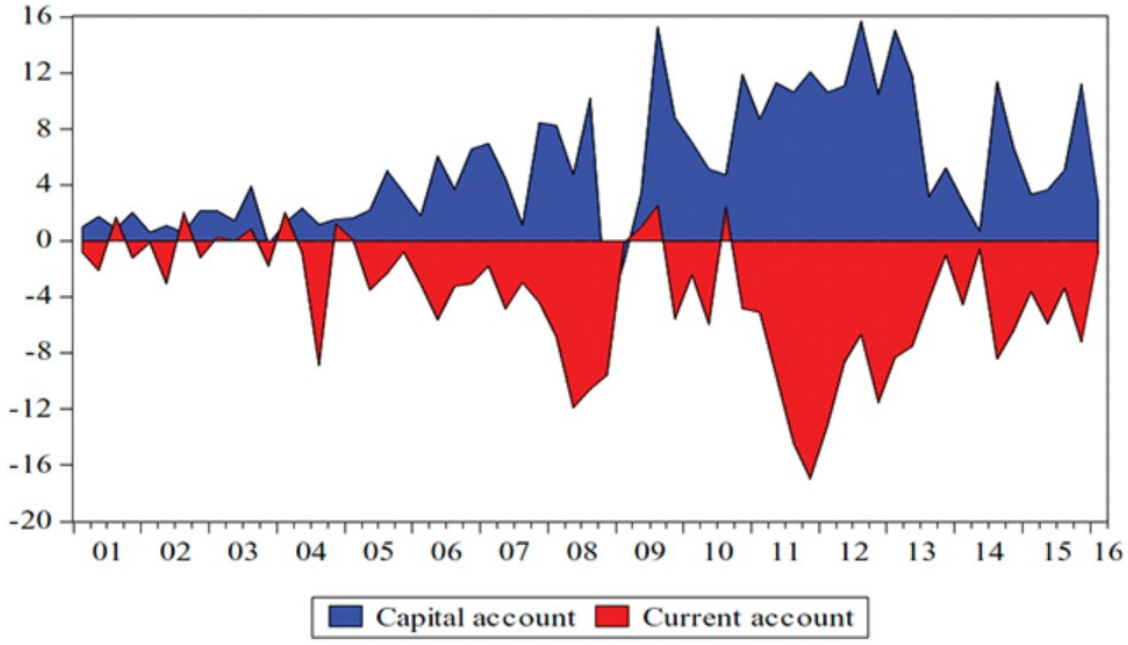

Figure 21: Historical Trends in Sri Lanka's Current and Capital Account Balances (in US$ million)

Source: Maitra[12]

Sri Lanka has had a succession of BOP crises over the past two decades and has needed many bailouts from the International Monetary Fund (IMF). In 2009, the IMF extended a loan contingent upon the reduction of budget deficits to 5% of GDP by 2011. Without any improvement in GDP or exports, the country requested an additional $1.5 billion in debt from the IMF in 2016, along with some new stipulations. The economic health suffered as a result of the IMF package, and the growth rate decreased from 5 percent in 2015 to 2.9 percent in 2019. During the same time period, government revenue decreased from 14.1% of GDP to 12.6% of GDP. Conditions attached to IMF loans are frequently onerous for debtor governments. Despite

[12] Maitra, B. (2018). Dynamics of capital account and current account in Sri Lanka. Journal of International Trade and Economic Development, 27 (1), 74–73.

its acute BOP problem, Sri Lanka did not immediately seek help from the IMF due to its history of sluggish economic recovery. Eventually, though, Sri Lanka returned to the IMF due to desperation. (Soumya, 2022)

3.3.2.1. Initiatives to overcome current account deficit

The end of Sri Lanka's civil war in 2009 raised hopes for fast economic growth, but these aspirations were not realized since Sri Lanka failed to liberalize its economy. Sri Lanka's post-war economic expansion was mostly fuelled by government spending and major debt-financed infrastructure projects, which caused the country's budget deficit to balloon over time as the economy slowed. As institutionalizing fiscal discipline is essential to minimizing a budget deficit, Sri Lanka should analyse and restructure its legal, constitutional, and institutional institutions to implement efficient budget monitoring, parliamentary oversight, transparency, and accountability. Sri Lanka's economy is heavily influenced by the government. Over 500 state-owned enterprises (SOEs) operate in nearly every significant industry. State-imposed pricing have also inhibited the growth of free markets in the nation. Due to poor management, several Sri Lanka's state-owned enterprises (SOEs) incur enormous losses, which exacerbates the government's deficit and debt issues. Reforming SOEs through divestment, downsizing, and closure will instantly boost investor confidence and demonstrate the nation's commitment to reforms. (Thowfeek, 2022)

Over time, the prominence of the state's position as an employer has likewise expanded. The state employs over 16 percent of the nation's work force, and another 600,000 former state employees are now receiving pensions. In 2021, the government spent 73% of its earnings on wages and pensions for all its employees. Sri Lanka's public sector is overstaffed and inefficient, imposing a substantial and recurrent tax burden. For the state sector to be reformed, it is necessary to reduce employment in the public sector. (Thowfeek, 2022)

Between 1990 and 2020, Sri Lanka's per capita gross domestic product increased from $463 to $3,680, while its tax collection as a proportion of total revenue decreased from 19 percent to 11.5 percent within the same time frame. Sri Lanka's tax structure is extremely regressive, depending heavily on indirect taxes, such as border duties, to pay government expenditures. Regressive tax arrangements exacerbate income inequality by placing a disproportionate burden on the poor, although income taxes, which are more progressive, only account for 25 percent of its tax receipts. In 2019, Sri Lankan President Gotabaya Rajapaksa enacted tax cutbacks that resulted in a 30 percent decrease in government tax collection. This resulted in the greatest budget deficit in the nation's history and decreased its already-low tax base by 33.5% at the time. This sort of tax regime is severely inadequate to fulfil the demands of a

nation on its path to growth, demanding revisions for a progressive tax structure. Sri Lanka's debt problem is daunting, and while the government strives to deal with it, the suggested changes are essential for positive development. These changes are inextricably linked with Sri Lanka's political economy. Reforms have thus far been avoided by successive administrations owing to their political ideology and fears of upsetting the status quo, resulting in the explosive crisis that today threatens the welfare of their population. Even if Sri Lanka is successful in resolving its immediate financial problems, failing to implement these changes to reduce its deficits and reorient its economy raises the likelihood of Sri Lanka relapsing into a similarly undesirable position in the future. (Thowfeek, 2022)

3.3.3. Current Account Deficit of India and its implications

The sharp growth in the deficit on the merchandise trade account is the main reason why India's current account deficit has increased in recent years. Even though India has formalized multiple free trade agreements, export performance has been unimpressive while imports have increased with the growth in gold imports. Ad hoc fixes must be less of a focus for policymakers as they look for methods to solve the domestic economy's flaws. India's external sector has been tethering on the verge of a crisis for the past few years as a result of a substantial worsening of the current account deficit (CAD). The CAD was hardly more than 1% of the gross domestic product (GDP) in 2007–2008, but during the following five years it had reached 5%, which is twice the level that the Reserve Bank of India (RBI) regards as a safe threshold. Not because it was a large percentage of GDP, but rather because of how quickly the deficit had grown to an unsustainable level, India's current account deficit was frightening. The rapid worsening of the merchandise trade account deficit, particularly since the start of the global economic slump, was the cause of the widening of the CAD. The merchandise trade deficit increased from roughly $46 billion in 2005-2006 to $190 billion in 2012-2013, according to data from the DGCI&S (Directorate General of Commercial Intelligence and Statistics) (Table 15). However, the trade imbalance decreased by over 28% to less than $138 billion in 2013–14. This turnaround was brought about by a decrease in imports and a modest increase in exports (as opposed to negative growth in 2012–2013). As a result, the CAD-GDP ratio is probably going to go below 4% in 2013–14. The general trend of a worsening CAD situation was not the product of individual events, but rather the culmination of a number of fundamental flaws in the Indian economy that had grown over the previous few years. (Biswajit & Rao, 2014)

Years	Exports ($ billion)	Growth (%)	Imports ($ billion)	Growth (%)	Merchandise Trade Balance ($ billion)	Growth (%)
2005-06	103.1	...	149.2	...	-46.1	...
2006-07	126.4	22.6	185.7	24.5	-59.3	28.7
2007-08	163.1	29.0	251.7	35.5	-88.5	49.2
2008-09	185.3	13.6	303.7	20.7	-118.4	33.8
2009-10	178.8	-3.5	288.4	-5.0	-109.6	-7.4
2010-11	251.1	40.5	369.8	28.2	-118.6	8.2
2011-12	304.6	21.3	489.2	32.3	-184.6	55.6
2012-13	300.4	-1.4	490.7	0.3	-190.3	3.1
2013-14	312.6	4.1	450.1	-8.3	-137.5	-27.7

Table 15: Growth in Exports, Imports and Merchandise Trade Balance

Source: DGCI&S[13]

In 2012-13, the merchandise trade imbalance hit a record high of almost 11% of GDP, up from 6% in 2005-06. This was so for two reasons. The average increase of India's exports since 2005-06 has been 16%, which is significantly lower than the 24% average between 2002-03 and 2005-06. Two years of negative growth and two years of relatively slow growth led to the reduction in export growth. The second cause of the rise in the CAD was the increase in imports. There were two causes for the increase in imports. Since the middle of the 2000s, India has signed several comprehensive economic partnership agreements (CEPAS), which have resulted in a lowering of tariffs on a wide range of goods. Not surprisingly, India's import-to-GDP ratio increased to about 28% from 2005-06 to 2012-13, because of a roughly 19% average annual increase in imports during that time. Notably, countries like Indonesia, which have historically had very high levels of import intensity, have drastically reduced their import dependence, while Brazil has not allowed the imports-to-GDP ratio to exceed 10%. Two commodity types, gold and crude petroleum and products, contributed to the rise of imports. The growth in gold imports was quite rapid. In 2005-06, gold imports were less than 4 billion dollars, but within six years, they had risen to about 57 billion dollars, or nearly 12 percent of

[13] Directorate General of Commercial Intelligence and Statistics

the import bill. Gold had replaced the "machinery" group, whose proportion of imports plummeted from an all-time high of 18% in 2007-08 to 10.6% in 2012-13, corresponding with the manufacturing sector's slowdown. However, in the preceding fiscal year, following a series of government actions, gold imports plummeted. The proportion of gold in the nation's imports fell to little over 6%, the lowest level in in a decade (Table 16). (Biswajit & Rao, 2014)

Product Groups	2005-06	2007-08	2009-10	2011-12	2012-13	2013-14
Petroleum crude and products	29.5	31.7	30.2	31.7	33.4	36.7
Gold	7.3	6.6	10.0	11.5	11.0	6.4
Machinery	14.4	18.0	12.6	10.5	10.6	10.0
Electronic goods	8.9	8.2	7.3	6.7	6.4	6.9
Pearls, precious and semi-precious stones	6.1	3.2	5.7	5.8	4.6	5.3
Organic and inorganic chemicals	4.7	3.9	4.1	3.9	3.9	3.5
Coal, coke and briquettes	2.6	2.6	3.1	3.6	3.5	3.7
Metalliferous ores and products	2.6	3.1	2.7	2.7	3.1	3.0
Edible oil	1.4	1.0	2.0	2.0	1.9	2.1
Iron and steel	3.1	3.5	2.9	2.4	2.2	1.6
Fertilisers	1.4	2.2	2.4	2.3	1.9	1.4

Table 16: Import of Principal Commodities (% of total imports)

Source: DGCI&S

When gold imports reached extremely high levels, the then-finance minister, Pranab Mukherjee, took the initial moves to curb them. In the budget for 2012-2013, he boosted the gold customs charge to 4%. This action closely followed the switch from a particular duty to a 2% ad valorem tax on gold. The value of gold imported into India in 2012-13 decreased to less than $54 billion, indicating that the steps enacted to restrict gold imports were successful. However, the World Gold Council (WGC) states that India's demand for the yellow metal skyrocketed in the second half of 2012, even though gold imports fell during the first half of the year. According to the WGC, India's gold demand was bolstered in December by predictions that the government will once again hike gold customs duties. This contributed to stockpiling by bullion dealers, jewellers, and individuals who had intended to acquire gold soon but moved ahead their purchases to avoid higher tariffs in 2013. As anticipated by the market, the government adopted two sets of measures in the subsequent fiscal year to restrict gold imports. First, the import tariff on gold was increased from 8% to 10%. The second was a rule limiting gold imports to ten authorized banks and other bodies and businesses. These specified institutions were required to comply with the 80:20 rule, which stipulated that at least one-fifth of every lot of gold imports must be made available for export and the remainder must be used domestically. These regulations had a major effect on gold imports, as indicated by official figures. During 2013-14, the value of gold imports was $29 billion, a decrease of more than

46% compared to the previous fiscal year. However, there are significant uncertainties regarding the effectiveness of the government's gold import limits. According to a recent assessment by the WGC, the fundamental level of demand among Indian consumers remained healthy throughout 2013. This analysis indicates that the substantial fall in legal gold imports into India led to a greater proportion of this demand being satisfied by gold imported through illicit routes (read smuggling). The data lends validity to the widely held belief that gold import limits have no effect on the outflow of foreign currency from the country since they allow hawala dealers to participate. Clearly, the present restrictions on gold imports are not assisting the government in overcoming its foreign payments issues. The government must thus consider a more comprehensive strategy that, on the one hand, examines measures to reduce the demand for gold and, on the other hand, offers efficient tools to prevent gold smuggling. India's exports have suffered due to a combination of the exporters' inability to capitalize on the opening of markets because of the formalization of various free trade agreements (FTAs) during the previous decade and the slack in the global markets as a result of the global economic recession. As a result of the government's adoption of the "Strategy for Doubling Exports in Next Three Years 2011-12 to 2013-14," exports were anticipated to reach $500 billion by 2013-14. This was to be accomplished by a combination of excellent performances by certain industrial sectors and successful marketing and technology initiatives. The industrial sector was unable to increase its position on global markets, hence these hopes remained unmet. From 2005-06 to 2013-14, the proportion of manufactured items in India's export basket fell from 54% to 48%. (Table 17). Regarding manufactured exports, there was consequently a significant disconnect between policy announcements and reality. (Biswajit & Rao, 2014)

Product Groups	2005-06	2007-08	2009-10	2012-13	2013-14
Manufactured goods	53.8	50.0	47.6	46.0	47.8
Of which: Leather products	2.6	2.2	1.9	1.6	1.8
Chemicals and related products	15.2	13.7	13.7	13.8	14.0
Engineering goods	18.7	20.7	18.2	18.9	19.7
Electronic goods	2.2	2.2	3.2	2.8	2.5
Textiles and clothing	15.1	11.3	10.7	8.8	9.7
Petroleum products	11.3	17.4	15.8	20.3	20.1
Gems and jewellery	15.1	12.1	16.3	14.4	13.2

Table 17: India's Exports of Principal Commodities (% of total exports)

Source: DGCI&S

The problem is not limited to a drop in the total percentage of manufacturing in India's export basket; the falling technological content of India's exported manufactured goods should be of even more concern. The proportion of high-tech items in India's industrial exports declined from 28% in 2005-06 to 21% in 2012, a decrease of 6%. At the same time, exports of medium-tech products remained stagnant. Thus, exports of high and medium tech products have decreased from about 60% in 2006 to less than 55% in 2012. (Table 18). Brazil and China have done substantially better than India: their high and medium exports have increased by 68% and 76%, respectively. The expanding economic ties between India and a vast number of its trade partners do not appear to have benefitted the export industry. Through PTAs and CPAs, India has tried to increase its economic integration with a number of nations during the past decade. However, it is unclear if India was prepared to take advantage of the potential presented or to handle the obstacles presented by these accords. (Biswajit & Rao, 2014)

Years	India		Brazil		China	
	High Tech	Medium Tech	High Tech	Medium Tech	High Tech	Medium Tech
2005	24.8	27.6	27.7	39.8	47.5	27.3
2006	28.5	31.3	28.4	39.1	49.6	27.2
2007	25.6	32.4	20.0	44.6	48.9	27.9
2008	24.6	36.8	24.6	43.4	47.3	28.8
2009	26.2	32.2	24.8	42.0	46.7	29.2
2010	22.1	30.4	24.6	42.3	46.0	30.5
2011	21.0	31.4	22.7	45.7	43.7	32.1
2012	21.3	33.4	23.0	44.7	46.7	29.7

Table 18: Technology Content of Exports of Manufacturing (% of exports of manufactured products)

Source: WITS[14] Database

An early evaluation of the PTAs/CEPAs reveals that India has not been able to use these agreements adequately to expand its footprint in its partners' markets. India's exports of goods to its FTA/CEPA partners have risen far more slowly than imports since the middle of the

[14] World Integrated Trade Solution

previous decade, roughly coinciding with the time when the government made the decision to join into the accords. While the average annual increase of exports to FTA/CEPA partners was less than 13%, imports climbed at more than double this pace, 26.6%. (Table 19).

FTA/CEPA Partners	Average Annual Growth between 2005 and 2012	
	Exports by India	Imports into India
ASEAN	30.6	43.1
Australia	31.2	23.4
Canada	14.7	23.2
EU	16.4	18.2
Malaysia	33.1	47.3
New Zealand	16.5	38.6
Singapore	21.4	21.0
Japan	23.0	33.7
Korea	24.0	30.0
FTA partners	12.5	26.6

Table 19: India's Trade Expansion with FTA/CEPA Partners (%)

Source: WITS Database

India's failure to enter its partners' markets means that it continues to be a minor participant in most of these markets (Table 20). Except for Singapore, India's proportion of its partner nation's imports has either remained stable or fallen in every country. In three of these instances, India's proportion of the trading partner's total imports has yet to exceed 1%. Consequently, while India was unable to gain access to the markets of its partner nations, its imports from those nations remained relatively high. This tendency can be better comprehended by comparing the trade balance and exports (Table 21). (Biswajit & Rao, 2014)

Trade Partners	2005	2006	2007	2008	2009	2010	2011	2012
ASEAN	1.5	1.6	1.8	2.1	1.9	2.1	2.5	2.3
Australia	0.8	0.7	0.8	0.8	1.0	0.9	1.0	1.1
Canada	0.5	0.5	0.5	0.5	0.5	0.5	0.6	0.6
EU-27	0.6	0.7	0.7	0.8	0.8	0.9	1.0	0.9
Japan	0.6	0.7	0.7	0.7	0.7	0.8	0.8	0.8
Korea	0.8	1.2	1.3	1.5	1.3	1.3	1.5	1.3
Malaysia	1.0	1.0	1.4	2.0	1.8	1.5	1.8	1.9
New Zealand	0.6	0.6	0.6	0.7	0.9	0.9	0.8	0.9
Singapore	2.0	2.0	2.2	2.6	2.3	3.0	3.9	3.4
Thailand	1.1	1.3	1.4	1.5	1.3	1.2	1.3	1.3

Table 20: India's Share in Imports of its share partners (%)

Source: WITS Database

Trade Partners	2004	2005	2009	2010	2011	2012
World	-30.4	-40.4	-50.7	-58.8	-53.4	-68.9
ASEAN	-13.2	-3.4	-33.9	-29.1	-16.9	-32.3
Australia	-436.5	-492.8	-752.2	-630.6	-540.2	-391.0
Canada	3.9	1.5	-96.5	-65.1	-22.4	-27.2
EU	-3.4	-5.4	-5.5	-2.0	-0.9	-11.6
Malaysia	-112.9	-113.0	-41.6	-68.6	-139.7	-176.8
New Zealand	-12.7	-45.7	-69.9	-245.1	-199.5	-150.5
Singapore	27.1	41.8	10.0	19.9	47.8	42.5
Japan	-60.3	-49.8	-108.0	-72.0	-100.6	-92.7
Korea	-246.8	-190.4	-118.2	-173.0	-171.7	-235.5
FTA partners	-16.4	-16.8	-32.3	-30.5	-28.6	-40.2

Table 21: Trade Balance/Exports

Source: WITS Database

This ratio was over four times more in Australia than in Korea, where it was greater than twice as high. In recent years, India's conditions of engagement with its economic partners have deteriorated. Prior to the commencement of the economic downturn, rises in the trade deficit were mitigated by the favourable balance on the "invisibles" account, to which the surplus on the services trade account and private transfers (mostly workers' remittances) contributed significantly (Table 22, P 44). Nonetheless, both elements were impacted by the poor market circumstances in the major economies. (Biswajit & Rao, 2014)

Years	Services Trade Balance	Investment Income (Net)	Private Transfers (Net)
2005-06	23.2	-5.3	24.5
2006-07	29.5	-6.8	29.8
2007-08	38.9	-4.4	41.7
2008-09	53.9	-6.6	44.6
2009-10	36.0	-7.2	51.8
2010-11	44.1	-17.1	53.1
2011-12	64.1	-16.5	63.5
2012-13	64.9	-22.4	64.3

Table 22: Major Components of the Invisible Accounts ($ Billion)

Source: Reserve Bank of India

In comparison to the average annual growth rate of 15% between 2005-06 and 2012-13 (the most recent year for which data are available), services exports may rise by just g% between 2009-10 and 2012-13 (the most recent year for which data are available) due to a severe decrease in 2009-10. Although positive judgments about the recovery of major economies in 2011-12 led to a considerable increase in net services trade and net private transfers, the momentum was not maintained the following year, as both indices grew by just 1%. Table 22 demonstrates that services exports and remittances are the lifeblood of India's current account, as their contributions have prevented the CAD from ballooning out of control. Consider the export performance of the key service sectors in this context. (Biswajit & Rao, 2014)

Years	Travel	Transportation	Insurance	Software Exports	Business Services	Financial Services	Communication Services
2005-06	13.6	11.0	1.8	40.9	16.1	2.1	2.7
2006-07	12.4	10.8	1.6	42.4	19.7	4.2	3.1
2007-08	12.6	11.1	1.8	44.6	18.6	3.6	2.7
2008-09	10.3	10.7	1.3	43.7	17.6	4.2	2.2
2009-10	12.3	11.6	1.7	51.8	11.8	3.8	1.3
2010-11	12.7	11.4	1.6	42.6	19.3	5.2	1.3
2011-12	13.0	12.8	1.8	43.7	18.2	4.2	1.1
2012-13	12.4	11.9	1.5	45.2	19.5	3.4	1.2

Table 23: Shares of Major Services Sectors in Exports Services (%)

Source: Reserve Bank of India

Since 2005-06, Table 23 displays the share of main service sectors in India's exports of services. Clearly, the proportion of service exports has stayed practically unchanged. Software exports, which encompass both IT services and information technology enabled service (ITES)-business process outsourcing (PO) services, have remained by far the most important component of India's services exports, even though their proportion has decreased from a high of nearly 52% in 2009-10 to just under 45% in 2012-13. The performance of software exports has been mediocre since key markets are plagued with protectionist attitudes due to economic uncertainty. Recent research performed jointly by ASSOCHAM and KPMG revealed the problems facing the IT and ITES-BPO services industry. According to the research, India is losing almost 70% of all additional voice and call centre business to competitors such as the Philippines and eastern Europe. The report concludes that "our rivals will further solidify their position until the local BPO (business process outsourcing) market diversifies its delivery footprint to take advantage of low-cost centres." In light of the fact that IT and ITES-BPO service providers face heavy competition from comparably efficient Asian and European enterprises, it is indisputable that the inability of the services industry to diversify its export

basket might further pressure the current account. Investment income outflows were a significant element in determining the balance of the invisibles account (Table 23). Given that India relies on capital inflows, whatever of their source, to overcome the challenges posed by its massive CAD, this development has significant significance. Since 2010-2011, this component, which comprises income on equity and on debt, has expanded fast. In 2005-06, these outflows were slightly over $5 billion, but by 2012-13, they had surged by more than fourfold to more over $22 billion. A portion of these are reinvested profits, which are offset by a rise in direct investment liabilities. On the longer run, the reinvested earnings will result in significantly bigger future payments without equivalent cash inflows. It is also true that while dividend payments as a portion of investment income have increased dramatically over the past several years, other factors have gained relative and absolute significance. Most of the payments for services consist of miscellaneous products. One such item is the payment for royalties and franchise agreements (Table 24). The upkeep of offices outside of diplomatic posts is a significant but considerably less noticeable expense component. Although the causes for the high increase in expenditures on this account will need to be investigated in depth, it can be noted that this occurrence roughly correlates with India's increasing FDI outflows. (Biswajit & Rao, 2014)

Years	Business Services	Dividends	Royalty Payments	Remittances for Maintenance of Offices Abroad	Business Management and Consultancy Services
2005-06	7.7	2.5	0.6	2.1	1.8
2006-07	15.9	3.5	1.0	4.0	3.5
2007-08	16.6	3.2	1.0	3.6	3.4
2008-09	15.3	3.2	1.7	3.4	3.6
2009-10	18.0	3.8	2.0	3.6	5.4
2010-11	27.7	4.7	2.4	6.1	9.1
2011-12	26.8	4.9	3.2	5.1	9.8
2012-13	30.3	3.4	4.2	5.2	8.1

Table 24: Outflows on the invisibles account in India's BOP ($ Billion)

Source: Reserve Bank of India

Each of the individual items requires thorough inspection. For instance, if the rapidly increasing royalty payments are a result of Indian firms acquiring technology, this might still be viewed as a positive indication. However, if these payments are made by FDI-invested firms to their

overseas parents, this might be reason for worry. This is especially true if these payments are replacements for dividends, either to deny the Indian partners their due share of the profits or to take advantage of the favourable tax treatment applicable to dividend payments. The case of Samsung India Electronics is relevant to this discussion.

Year	Dividends	Royalty Payments	Imports
2008-09	0	0.7	39.8
2009-10	0	1.0	67.6
2010-11	0	1.1	94.1
2011-12	0	1.5	125.0
2012-13	0	3.0	174.3
Total	0	7.2	500.8

Table 25: Samsung India Electronics: Foreign Exchange Outgo (Rs Billion)

Source: Ministry of Company Affairs

In spite of claiming that "considering the rapidly changing industry scenario and the need to further strengthen the business, your Directors have decided not to propose any dividend," the company paid out Rs 7.2 billion in royalty payments from 2008-09 to 2012-13, compared to Rs 2.2 billion in paid-up equity capital (Table 25). This was in addition to the Rs 1.7 billion in royalties it had previously paid over the previous nine years. In contrast, its imports grew from R 38.9 billion to R 174.3 billion between 2008-09 and 2012-13, surpassing R 500 billion for the whole time. A few other international corporations, such as Maruti Suzuki, Hindustan Unilever, ABB, and Colgate-Palmolive, are included in the discussion over the increase in royalty payments. It is pertinent to highlight that of the 312 manufacturing businesses that paid royalties in 2012-2013 and are covered by the Prowess of CMIE, 746 foreign companies paid roughly 73% of the entire $1.2 billion in royalties. The remainder was produced by 236 more firms. (Biswajit & Rao, 2014)

3.3.3.1. Initiatives to overcome current account deficit

As the current account deficit reaches levels that might leave the Indian economy severely vulnerable, the government will need to find effective remedies quickly as the payments issue threatens to escalate into a debt overhang. India's external debt has more than tripled from 2005-06 to 2012-13, reaching $404.9 billion. Short-term debt contributed significantly to this growth, as its proportion rose from 14% to nearly a quarter of the overall debt stock. The ratio of reserves to foreign debt is another unsettling characteristic. After reaching a high of 138.0% in 2007-08, it dropped precipitously to 74.5% by the end of 2012-2013. The burden of the expanding debt

is also evident in the escalating investment income payments, which are eroding the surpluses attributable to services and remittances. To yet, the government's remedies to the difficulties with foreign payments have been, at best, ad hoc. This strategy must be replaced with one that identifies the root cause of the issue to discover a long-lasting remedy. Consider, for instance, the government's responses to gold imports. As indicated in a previous conversation, The success of these efforts was illusory, as they only transferred gold imports from official to illicit channels since they were unable to impact the expanding demand for gold. (Biswajit & Rao, 2014)

It is a well-known fact that gold's development as an asset class has increased demand for gold in the country. Real estate and equities market volatility have made gold an attractive investment. Gold's actual returns have been strong, making it the best hedge against inflation. In order to reduce the demand for gold, it is necessary to construct alternative financial products that offer genuine rewards. In addition, it has been suggested that the development of new gold-backed financial instruments may be considered to lower the need for actual gold. This contains a WGC proposal to convert gold into a financial asset. Equally crucial is finding a long-term solution to the issue of sluggish export growth, particularly for manufactured goods. Again, the officials' efforts have been short-sighted, since they have made no move to boost the nation's manufacturing base. In 2011, then-finance minister Pranab Mukherjee emphasized the necessity of revitalizing the manufacturing sector. Nonetheless, the National Manufacturing Policy, which was adopted to increase the sectoral share of manufacturing in GDP to at least 25% by 2022 and to enhance global competitiveness, domestic value addition technological depth and environmental sustainability of growth, as well as to increase the rate of job creation, remains in the conceptualization phase. (Biswajit & Rao, 2014)

3.4. Plausible Grounds of Current Account Deficit in Pakistan

Large and persistent trade and current account deficits have been among the hottest subjects among politicians and economists throughout the globe over the past few decades. Current account plays an important part in the economic growth of a nation. It illustrates a country's economic performance, which may aid both local and foreign investors in their investment planning. The causes of a current account deficit include excessive domestic demand, a lack of domestic saving, inflated currency rates, government policy on imports and exports, domestic production capacity and capability, etc. A current account deficit indicates that a country is spending more than it is earning. Its consumers, businesses, and government together spend more on net foreign investments than they gain from local output and earnings. A transient current account deficit does not pose a significant threat to an economy and can be quickly

corrected. However, a substantial and persistent current account deficit is more damaging and a greater concern for an economy, requiring the attention of policymakers and modifications to the right policies. A large and sustained current account deficit can have several negative effects on an economy. A country with a current account deficit consumes more than it generates and buys more than it sells. When domestic demand is strong and domestic manufacturers are unable to meet this excessive demand, the need for imported goods and services grows, ultimately resulting in a rise in the trade and current account deficit. On the other hand, this deficit causes a depreciation of the local currency, which results in an appreciation of the foreign exchange rate. This devaluation of the local currency has a favourable effect on exports, as local goods are now available on overseas markets at a reduced price in foreign currency. The weak local currency also has a detrimental effect on imports, since it makes the import of goods and assets more expensive. If a country does not have sufficient manufacturing capacity to meet the rising overseas demand for its goods, this will influence the import-export balance. Ultimately, the trade and current account deficits rise further. (Gulzar & Hui, 2006)

3.4.1. Workers' transmittals

Workers' remittances play an important role in the economic development of a country. Large and persistent amounts of workers' remittances not only support huge payment balances but also help aid domestic investment. Increase in the volume of workers' remittances helps in reducing the current account deficit. Pakistan's current account balance is highly dependent on the volume of workers remittances. A large and persistent amount of workers remittances always supports huge payments, but these remittances cannot be sustained over a long period of time. Pakistan's current account balance used to suffer from a trend of fluctuating workers remittances since the year of its independence. The position of workers remittances changed after segregation of East Pakistan (Bangladesh) from West Pakistan (Pakistan at present) in 1971. There was a sudden rise in the workers remittances at the end the seventies and the start of the eighties. But this increase did not support a conversion of the current account deficit into a surplus. The event of September 11, FY2001 change the situation and there is a tremendous increase in the workers remittances especially from the United Kingdom, USA, and some European countries. This caused a surplus in the current account balance for the first time since FY 1951. After exports, worker remittances are the second greatest source of foreign cash revenues for Pakistan. It has played a crucial influence in lowering the current account and payments balances. The IMF underlined the significance of worker remittances in the April 2005 World Economic Outlook, noting that remittances may assist enhance a country's growth prospects, preserve macroeconomic stability, decrease the effect of unfavourable shocks, and

alleviate poverty. Families can maintain or raise expenditures on basic consumption, housing, education, and the establishment of small businesses due to remittances. In its economic survey for 2005-06, Pakistan's ministry of finance attributed the widening of the current account deficit to large payments against higher oil import bills due to high global crude oil prices, substantial increases in non-oil imports fuelled by strong demand, and a decline in the growth of net transfers. In addition, increasing freight charges by international shipping lines because of a dramatic increase in global commerce, as well as higher fuel prices and an increase in personal travel due to the rising incomes of middle- and upper-income groups, have contributed to the expanding current account deficit. (Gulzar & Hui, 2006)

3.4.2. Terrorism

During a thorough examination of Pakistan's economy, it becomes obvious that the Pakistani dictatorship gained immensely from September 11th. According to the Centre for Defence Information, Pakistan received around $9 million in help in the three years preceding 9/11. In the subsequent three years, it got $4,7 billion in military aid alone. Before 9/11, Pakistan was on the verge of defaulting on its debt and being labelled a pariah state. Since 2002, Pakistan has seen tremendous economic growth, which the Musharraf administration attributes to the influence of international events following 9/11. In the aftermath of 9/11, Pakistan was granted advantageous conditions, which gave the impression that the economic situation was improving during Musharraf's administration. These included export incentives, such as enhanced EU market access, debt rescheduling, and one-time incentives, such as grants from the United States and Saudi investments. Pakistan confronted the gravest predicament in its history. It appeared that the Pakistani President and officials were the only US representatives threatening the Taliban, and they intended to emphasize that our assistance in the US-led campaign was unequivocal and that we would not allow even our national interest and honour to stand in the way. In just thirteen years, from September 2001 to the present, the United States has lost a large portion of its goodwill and probably all its credibility, primarily due to its foreign policy, its imperialistic attitude of not listening to its allies and its blatant disregard for international law, erosion of its moral ground, and imposition of its own culture and values on others. The United States has left a legacy of hatred, dread, and worry, particularly in the Muslim World, due to its botched diplomacy, imperialistic tactics, and ruthless display of power (Baloch, 2006). The export-led growth theory holds that exports may function as a growth engine, according to economists. It is often believed that export growth is a major factor of an economy's output and employment growth. This so-called export-led growth (ELG) concept is often supported by the following four reasons (Ramos, 2001): First, export growth causes an

increase in output and employment via the international trade multiplier. Second, the foreign currency made accessible by export growth permits the procurement of capital goods, which in turn boosts an economy's productive capacity. Thirdly, the volume and rivalry of export markets result in economies of scale and a quickening of technological advancement in manufacturing. (Majeed, 2014)

3.4.3. Heavy Expenditures; Military & Energy

Militarization competitions, energy consumption, economic growth, and the current account balance all have significant effects on one another. Imports of military equipment and energy, in particular, have a significant effect on a nation's current account balance, depending on whether or not the country manufactures military equipment and possesses energy resources. Countries with insufficient energy resources or a high militarization rate must import energy and military equipment. By draining foreign exchange reserves and expanding trade imbalances, importers of energy and military equipment place a significant load on their current account balance. Negative net exports reduce foreign savings and local investment. In addition, these conditions have a negative impact on the macroeconomic equilibria of the countries, as the distortion of the saving-investment balance leads to a decline in the Gross Domestic Product, disposable income, taxes collected, government budget, demand for loanable funds, etc. Negative impacts on external accounts result from forcing nations to deplete their reserves and borrowing from abroad, which crowds out the trading sector. On the other hand, disarmament or a fall in military expenditures and a reduction in energy dependency from foreign sources do not result in a proportional increase in investments, but energy shocks have negative impacts on the volatility of economic growth and current account. As the prices of military equipment and energy shocks have a substantial impact on net foreign asset positions, however, lowering weapon imports might alleviate foreign reserve scarcity. The economic expansion of these nations may decelerate. Long-term variations in the current account balances of countries might result from an increase in imports of energy and military equipment. Due to the utilization of scarce foreign reserves, military equipment and energy imports impose a significant cost on the economy, resulting in trade imbalances. Debt servicing causes the cost of military equipment and energy imports to increase over time. The militarization race surged after World War II, particularly in the year 2000, and it continues to rise. In oil-importing nations, an exogenous increase in the price of imported energy has a detrimental impact on trade by causing an economic shock that affects production choices. However, the magnitude of this effect is unknown. (Fazıl & Melike, 2022)

3.4.4. Political Instability

In Pakistan, corruption, which is defined as the abuse of entrusted power for private gain, is sadly pervasive. It is impervious to no structure, no tier, and the public sector. It has a massive reach. It has approached every state organ; in addition to the executive, it also has a judiciary legislature. It would not be an exaggeration to say that the Pakistani state is afflicted by this illness and weeping overweight. On the scale of corruption-free governance, the prevalence of corruption in Pakistan is so high that it is neither enviable nor acceptable to the international community. The roots of corruption in Pakistan may be traced back to the colonial era, when the British rewarded nepotism and corruption with land and titles to their loyal subjects (Awan, 2004). Two significant crises had a vital role in the creation of corruption in this region of the world: the spiral in defence-related purchases during and after World War II and the distribution of evacuee property following the partition of India. This was followed in the 1950s by industrial and commercial licences as well as patronage programs such as bonus vouchers and route permits. The nationalization program of the 1970s offered fresh corruption possibilities and spawned a new generation of corrupt government officials. In religious and business circles, the 1980s experienced a rise in corruption. (Umbreen, 2010)

Lack of Accountability	31.68%
Low Salaries	16.54%
Monopoly of Power	16.43%
Discretionary Power	12.61%
Lack of Transparency	9.97%
Power of influential people	4.59%
Red Tapism	4.28%
Others	4.9%

Table 26: Survey on Causes of Corruption

Source: NAB, Government of Pakistan

The reasons of this ailment lie in the socio-cultural political matrix of Pakistani society, which is currently experiencing a loss of value system and identity. According to a 2004 Perception Survey conducted by Transparency International Pakistan, the following factors have been identified as the most significant contributors to corruption, along with an estimate of their respective percentages. The primary purpose of petty corruption is to get access to public services or to circumvent or bend laws and regulations. Public contracting and procurement are impacted by large and moderate levels of corruption. (Umbreen, 2010)

3.4.5. Lack of Skilled Labour

The virtuous cycle of economic growth, job creation, and poverty reduction in Pakistan must be maintained throughout the next decade in order to bring about a permanent and beneficial transformation in our economic environment. In addition to other challenges facing the economy, the noticeable phenomena of developing talent shortages in numerous economic areas have received little attention. In the last few decades, the common thinking among development economists was that expansion of international commerce would boost the demand for unskilled workers in developing nations, offer employment for masses, and eliminate poverty. As the proliferation of new technology has substantially raised the need for skilled labour, real experience has demonstrated that this is only partially true. Recent research on economic rates of return have shown that the incomes of people with advanced degrees and abilities have increased significantly compared to those with high school diplomas or less skills. It has been demonstrated that a skilled workforce is essential not only for maintaining the development engine, but also for enhancing the investment climate and gaining a competitive edge in the global economy. Considering this, the talent shortages facing the Pakistani economy pose a significant threat to its future development and competitiveness. Pakistan has been a major exporter and producer of textiles for over five decades. We should have been a significant worldwide supplier of professional and management manpower to the newly emerging and aspirational developing nations attempting to establish themselves in this sector by now. However, what is the truth? Our companies are snatching experienced and high-performing workers from other competitive companies in the country, hence increasing compensation packages and personnel expenditures. We should have had a vast network of Textile Universities, Colleges, Institutes, Faculties, and Technical Training Facilities that produced world-class professionals, managers, and technicians throughout the whole value chain of the business. A number of these institutions fall short of the requirements necessary for the sector to remain highly effective. Industrial magnates and their associations in Pakistan continue to bark up the wrong tree – extracting concessions, tax breaks, subsidies, low interest rates, etc. – not realizing that they are not tapping the hidden wealth in the industry, i.e., labour productivity gains, organizational restructuring, and revamping logistics, acquisition, delivery, and sourcing methods. The cost reductions and income gains that may be achieved through these methods considerably surpass any government's concessions and subsidies. Relatives and kin should be accommodated under all circumstances, providing they are qualified, trained, and competent. Their passion and loyalty to family-owned businesses are essential, but they must be matched with professional and technical abilities to maximize their productive potential.

CONCLUSION AND RECOMMENDATIONS

4.1. Reforms of Export and Import Structures

We must alter the direction of our imports by purchasing more from countries outside the dollar and sterling zones, especially the U.S.S.R. and other East European nations, as well as China, so that they may purchase more from our country. It is vital to engage into long-term, expansive trade agreements with these nations, stipulating that a substantial portion of imports from them be paid for in Pakistani currency. Any rise in rupee-based purchases with these nations would have an immediate impact on our exports, just as India and Egypt have observed in recent years. This arrangement will also conserve our meagre foreign exchange resources. Concurrently, we require a deliberate and planned reduction in imports from nations with whom we have a trade imbalance. Reductions in government imports are also required to increase private imports, upon which the economic resurgence of the country depends. The industrial tilt of our import quotas should be maintained. We must simultaneously make our import lists more austere by eliminating all luxury products. Much may be written about the Export Incentive Scheme, which has granted exporters of designated goods complete discretion in disbursing the incentive currency. This type of incentive is offered at the expense of the country, since items are exported at extremely low costs and the loss is covered by the purchase of luxuries that can be sold for a profit in the local currency. Thus, the implementation of the system has had a significant impact on both the external worth of our currency and the pricing of the specified items. Therefore, it may be advised that the Export Incentive Scheme's whole structure be altered to permit only the import of industrial necessities. If this restriction cannot be implemented, the nation will be forced to eliminate the program entirely. Briefly, re-planning our import trade is the key to solving the challenge of breaking the vicious loop of declining exports and imports. This is also the most successful strategy for mitigating the effects of the Western economic slump and maintaining a high level of economic activity in the country. (Tufail, 1958)

The present high level of the current account deficit exerts pressures on external borrowing, necessitating a substantial adjustment to Pakistan's external sector over the medium term. From July 2007 to the end of March 2008, Pakistan added over $5.4 billion to its foreign debt pile, the largest amount ever made in a single year. This is producing a future stream of repayments that will likely have a significant impact on the balance of payments. It should be assessed whether: I domestic investment is excessive and/or national saving is inadequate; ii) total domestic spending is excessive and/or total domestic income is inadequate; and iii) domestic expenditure on tradable is excessive and/or domestic output of tradable is inadequate. In

developing nations like Pakistan, a current account deficit is the rule rather than the exception. It is anticipated that it will be maintained at an acceptable level and will not necessitate rapid policy revisions that may derail the economy's growing momentum. Given the structural rigidities and potential of the economy, the threshold level is around 4 percent of the GDP, which should also come from expanding investment rather than declining national savings. The persistence of a high current account deficit over an extended period of time has severe repercussions, including erratic fluctuations in the exchange rate, accumulation of external debt beyond a sustainable level, and the emergence of unwarranted concerns regarding the economy's susceptibility to external shocks. A greater foreign debt load is a significant barrier to growth since debt repayments consume resources that could be used for domestic investment and development. High external debt loads discourage foreign investment because they create a high-risk environment characterized by currency rate depreciation, capital flight, uncertainty among potential foreign investors on the feasibility of profit repatriation, and increased taxes to service loans. The taxes on Pakistan's imports of luxury goods, which have been significantly reduced in recent years, continue to be rather high. It may be necessary to examine the tariff structure for such things as automobiles and mobile phones. (Zafar-ul-Hassan, 2008)

4.2. Investing in Sustainable Energy Production to Lessen Imports

The fact that fossil fuels such as oil are substantially subsidized and the government purchases power from these plants at a premium is a key concern. Subsidizing fossil fuels has as one of its goals the protection of domestic prices from volatile global market swings. In doing so, however, the government hinders the incentive for firms and individuals to adapt to change by adopting alternative, more efficient technology. If energy prices remain constant over time, for instance, consumers will not explore for alternate transportation options or acquire energy-efficient equipment. Pakistan's route to a sustainable energy future is by no means straightforward, yet a solution exists. Although a variety of strategies have been proposed to promote the growth of renewable energy in Pakistan, all of these options would unquestionably require substantial government effort and commitment. Consider the long-term social, economic, and environmental benefits of renewable energy generation for Pakistan's population. Investing in renewable energy technology now will pave the way for a secure energy future in the future. (Mashael, 2010)

4.3. Enhancing Trained Labour and Increasing Education Budget

A vast majority of businessmen considers the shortage of skilled manpower as big a problem as their rising cost of production, and it affects their global competitiveness as much as the

energy crunch or the security conditions do. To overcome the skill shortages, many manufacturers have instituted on-the-job training at their factories. One of the country's largest home textiles and garments exporters, for example, spends a substantial amount of money to train industrial stitchers for his units. But he still doesn't have enough trained stitchers to meet his requirements. Obviously, individual efforts are not enough to fill the skill gap in the economy. (Nasir, 2015)

Captive exports in terms of both areas and goods must be varied, and unconventional items must be promoted to unconventional markets. Knowledge-based exports are notably absent from the nation's export portfolio. Pakistan must establish a solid industrial base utilizing cutting-edge technologies and quality standards. For the development of a high-tech industrial base, skilled labour and investments in human capital are required. Education of high caliber and skill development should be stressed. In addition, the traditional emphasis on merchandise exports must be widened; increasing services exports has the potential to increase foreign exchange gains. Pakistan has a competitive advantage in tourism and information technology services, and it should prioritize gaining outsourcing contracts from developed nations. Negotiating labour market prospects in East Asian economies and Middle Eastern nations can also increase remittances. In this sense, the productivity of Pakistani labour should be increased through the provision of excellent apprenticeships and training. (Zafar-ul-Hassan, 2008)

The combination of these initiatives would reduce the country's trade imbalance and assist restore its current account deficit's sustainability.

SUMMARY

In this paper, I have used secondary research methods to describe the historical overviews, and trends of balance of payments & exchange rates have been discovered with reference to Pakistan. The patterns of foreign trade have been elaborated along with the current imports and exports structure of Pakistan. The major commodities being exported such as bed linen, table linen, bathroom linen, kitchen linen, rice, suits, ensembles, jackets, blazers, trousers, bib and brace overalls, breeches, and shorts, suits, ensembles, jackets, dresses, skirts, divided skirts, trousers, bib and brace overalls and jerseys, pullovers, cardigans, waistcoat are also highlighted. Petroleum gases and other gaseous hydrocarbons, palm oil and its fractions, petroleum oils and oils obtained from bituminous minerals, cotton, tea, nickel, waste and scrap of these materials, jute and other textile base fibres were the key imports of Pakistan. The earnings as a result of these trade in the past and in the current time have also been discussed. The path leading to consistent current account deficit and limited foreign exchange reserves has directed Pakistan into indebtedness which has made the country to borrow money from the International Monetary Fund (IMF). It has hindered the economic growth of Pakistan; this paper comprises the impacts of current account deficit on economic growth confirmed by Thirlwall's studies and the vivid comparison with other developing nations. The role of current account deficit in other developing lands and initiatives to overcome this disparity have also been suggested here. In the following segment, probable causes of why the current account deficit in Pakistan arose in the first place have been deliberated. These included heavy expenditures on energy reserves, militarization, political instability, lack of skilled labour etc. In the preceding section, some I have suggested some recommendations that can be taken to diminish this current account deficit which has been constant since the last decades. These can be making reforms in the import and export structure, lowering taxes, investing in local enterprises, reverse engineering small-scale projects, encouraging skilled labour, providing trainings to labour, spending more on education, minimizing expenditures on warfare and military weapons, increasing education budget, investing in sustainable ways to produce renewable energy, and bringing accountability in the political system.

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