DAWN

Managing external debt

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PAKISTAN'S debt has crossed Rs100 trillion raising doubts about the stabilisation programme's veracity. First, it's not advisable to use absolute amounts or per capita debt. The correct way is to use indicators that relate public debt stock and debt servicing to national income, exports of goods and services, revenues, total foreign exchange earnings and foreign exchange reserves to gauge the future capacity to discharge these obligations.

To begin with, clarify the various definitions that have created a lot of confusion in laymen's minds. Pakistan's total debt and liabilities consist of public debt and private debt. Public debt accounted for 91 per cent of the total stock of outstanding debt and liabilities on June 30, 2026. The remaining 9pc is the private debt mostly to borrowers abroad, for which the government has no fiscal obligation. However, the State Bank of Pakistan (SBP) has to provide foreign exchange to service this debt.

Within the gross public debt, the government's share was almost 92pc while the balance was owed by public enterprises but guaranteed by the government. Borrowing from the IMF is also included in the gross public debt, although it is the SBP's liability. The total debt and liabilities is made up of borrowings in rupees from the SBP, banks, national savings schemes, prize bonds, Sukuk etc., and borrowings in foreign currency from multilateral institutions such as the World Bank, ADB, IDB, bilateral governments or global financial markets in the form of Eurobonds or Sukuk.

Rupee-denominated borrowing is termed 'domestic debt' and foreign currency-denominated borrowing 'external debt'. Domestic debt risks are different from those of the external debt. Lumping them together is analytically incorrect. While both create debt-servicing liability for budgetary purposes and thus affect fiscal balances, the risk profile of each is quite different. Domestic debt has to be paid in rupees, which can be printed, or the central bank can acquire those obligations on its balance sheet by creating reserve money. It involves creating possible inflationary pressures but there is no risk of default — a real threat in case of foreign currency-denominated debt. Countries that have suffered debt crises have faced solvency and liquidity risks in servicing their foreign currency loans. Risks from domestic debt include rollover risk, interest rate risk, and crowding out of private-sector credit. Here, we'll focus largely on external debt and liabilities and its servicing.

The reform journey to increase exports, investment and productivity must be accelerated.

Pakistan's external debt and liabilities amount to $139 billion, of which public sector debt accounts for almost two-thirds and the private sector one-third. In the public sector, direct government debt is 80pc of the total. What are the diagnostics of vulnerability indicators of the stock of EDL and debt-servicing capacity? First is the break-up between medium- and long-term and short-term loans. In our case, the ratio is: 88 MLT and 12 ST. Official liquid reserves are enough to cover the ST loans and loans maturing during the year. However, the rollover of friendly country deposits next year will go up to $12bn again. Second is concessionality — the average interest rate, years to maturity, and proportion of fixed rate loans. The higher the element of concessionality, the stronger the safety valve. Fifty per cent of loans are concessional, showing a downward slide from the past ratios. Other stock indicators don't look healthy. Third, EDL-to-GDP ratio has moved from 24pc to 31pc in the last decade. Fourth, EDL-to-export of goods and services too has worsened — from 210 to 340. Fifth, EDL-to-foreign exchange earnings shows an upward movement from 100 to 168 — not a satisfactory trend. Sixth, EDL-to-foreign exchange reserves has shot up alarmingly from 350 to 750, despite a build-up of reserves in the last two years.

Debt-servicing indicators show that external debt servicing-to-GDP has risen from 1.7pc to 4pc, while EDS-to-exports of goods and services has more than doubled from 18pc to 44pc. So has EDS-to-foreign exchange earnings from 10pc to 22pc and EDS-to-foreign exchange reserves from 37pc to 98pc.

This picture shows that to exit the IMF programme after October 2027, palliative measures are needed over the next two years to relieve the debt situation and build up capacity to absorb shocks. There are four levers to reduce the ratios: a) faster growth of exports and foreign exchange earnings; b) faster GDP growth in US dollars; c) lower current account deficits; and (d) lower interest and refinancing costs via concessional financing and maturity extension.

Assuming 4pc GDP growth in FY27-29, inflation contained at 6.5pc, fiscal deficit of 2.9pc and primary surplus of 2pc, the target should be to bring the debt-to-GDP ratio to 60pc and external debt-to-GDP ratio to 25pc by FY29 by implementing these policy measures: a) export of goods to reach $40bn rather than $36bn — a $4bn increase; b) import of goods to reach $76bn instead of $79bn — savings of $3bn; c) export of services to move up to $12bn instead of $11bn — a $1bn increase; d) workers' remittances to go up to $46bn instead of $43bn — an increase of $3bn; and e) an FDI of $3.7bn rather than $2.7bn — a jump of $1bn.

The reform journey to increase exports, investment and productivity must be accelerated. The list of delayed and deferred decisions is long. To mention a few — reducing the tax burden and overregulation of manufacturing and export, upgrading oil refineries, third-party access to oil exploration companies, introduction of weighted average cost of gas, opening up retail electricity and gas business to the private sector, elimination of cross-subsidy from industrial to domestic consumers rather than targeting through BISP, the ML-I railway track (announced in 2015), the Sukkur-Hyderabad motorway, increased share of railway freight traffic, tax collection under agriculture income tax, property tax, GST on professional services, operationalising Exim Bank for export financing and insurance, streamlining FBR's export facilitation scheme, expeditious refunds to exporters, increasing productivity of smallholder agriculture, financial access for SMEs, agriculture, low-cost housing, and SEZs for CPEC 2.0. The announcement and implementation of the industrial policy can help achieve the outlined increases and savings in the external account.

The amount of $12bn can be used for liquidating the bilateral deposits if they are not swapped for equity in long gestation investment projects or their maturities are not extended to the long term. By FY29, the removal of this Damocles sword over our heads should be able to moderate the vulnerability indicators discussed earlier. We don't have to seek another loan from the IMF and can regain our economic sovereignty.

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