Pakistan’s economic dependence on China is dangerous

Something is rotten in the state of Pakistan’s external finances. One would think that Pakistan, the home of the flagship project of China’s trillion dollar Belt Road Initiative, would have an overflowing external account. It is early days yet, but so far the China-Pakistan Economic Corridor’s economic consequences have been disastrous. The World Bank recently warned Pakistan it would face an external financing crisis next year. It noted the country would need $17 billion to cover a rising current account deficit and debt payments. The State Bank of Pakistan, the country’s central bank, had sounded a note of alarm earlier when the current account deficit for the 2016-17 fiscal year unexpectedly jumped 149% from the previous year – from less than $5 billion to over $12 billion.

There is little evidence of Chinese munificence in Pakistan’s foreign exchange reserves and trade figures. Pakistan’s foreign exchange reserves have fallen to $13.8 billion in September, the lowest since 2013. And partly because its improving connectivity with China is resulting in a flood of imports, its trade deficit has widened dramatically. While China is by far the largest source of foreign direct investment in the country, this is less impressive when one realises Pakistan attracted a total of $2 billion in FDI last year. While an improvement on the previous year, it is less than half of what the country used to attract even five or six years ago. At a time the world is flush with cheap capital and the Pakistan economy is growing at over five per cent a year, the lack of foreign investment is more than a bit surprising. Even China’s $ 800 million plus investment flows are hardly eye-popping.

There are a number of reasons for Pakistan’s financial condition. It has long depended on the foreign exchange earned from remittances, flows which have halved as the Persian Gulf economies slow down. The restrictions of some Gulf states on Pakistani migrant labour is also part of the story. But what may be most telling is the lack of serious attempts to attract foreign capital. Pakistan’s establishment seems to have concluded that the CPEC will provide for all of their economic needs and that, therefore, they need not actually do the hard work of reforming their economy. For example, to save the Pakistani rupee from crashing, the country has twice run to China this year alone and borrowed $ 1.4 billion. The question is how long Beijing is prepared to be so generous or what price will it extract in return.

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