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Third Time Lucky? A Comparative Perspective of IMF Programmes in Pakistan, 2000, 2013, and 2023

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Abstract

Pakistan spent much of 2022 mired in economic crisis and in 2023 the IMF arrived to negotiate an agreement, economic reforms in exchange for a large loan. It would be easy to be pessimistic about the prospects of Pakistan completing the 2023 vintage IMF programme and its multitude of conditionalities. Pakistan has signed off on more than 20 such agreements since 1958 and failed to complete all but one of them. There are grounds for optimism. Pakistan responded successfully to both the 2000-01 and 2013-16 IMF programmes in respect to a wide-range of economic and policy variables. This paper draws on a theoretical framework from Mancur Olson – the distinction between 'roving' and 'settled' bandits - to help think about the wider political economy that allowed Pakistan to (briefly) implement successful economic reform during these two periods. This paper uses this theoretical perspective to think about whether Pakistan will successfully complete the 2023 IMF programme. The tantalising conclusion is that Pakistan is more likely to do so if the criminal convictions against Nawaz Sharif are dropped and he is allowed to run for political office in the 2024 general election.

Introduction

Pakistan spent most of 2022 grappling with a severe economic crisis. As seasoned scholars and commentators anticipated, the International Monetary Fund's (IMF) arrival in 2023 marked another predictable chapter to the country's economic crisis. The year witnessed a protracted agreement with the IMF as negotiations unfolded amidst ongoing economic and intensifying political crises. Inflation soared as the political fortunes of former Prime Minister Imran Khan plummeted from leading the country to court and ultimately, imprisonment (as of the time of

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this article). Pakistan hosted an IMF mission in late January 2023, signed off on a new IMF agreement in July, and hosted a follow-up mission in August. It would be easy to be pessimistic about the prospects of Pakistan completing the 2023 IMF program and its multitude of conditionalities. Since 1958, Pakistan has signed off on more than 20 such agreements, yet it has failed to complete all but one.

This paper begins on a slightly more optimistic note, observing that Pakistan successfully implemented the IMF programme of 2000-01 and made a lot of progress in the 2013-16 IMF programme across a broad range of economic and policy variables. The variables examined in this paper include the budget deficit, inflation, non-performing bank loans, the current account deficit, debt service as a share of total exports, short-term debt as a share of total reserves, and total reserves as a share of external debt. Drawing on Mancur Olson's theory of "roving" and "settled" bandits, this paper explores the wider political economy that facilitated Pakistan's brief periods of successful economic reform. By applying this theoretical perspective, we can consider whether Pakistan is likely to complete the 2023 IMF program. Intriguingly, the conclusion suggests that Pakistan's success hinges on dropping the criminal convictions against Nawaz Sharif and allowing him to participate in the 2024 general elections.

Section 2 examines the urgent need for economic reform in Pakistan during 2022 and 2023. Section 3 delves into the history of IMF engagement in Pakistan. Section 4 presents the claim that the reform efforts undertaken in 2000-01 and 2013-16 were successful. Section 5 introduces several well-established economic theories that fail to explain the reform success of those two periods. Section 6 introduces a theory from Olson, distinguishing between "roving" and "settled" bandits, that could help the reform success of these two periods. Section 7 provides a detailed justification for the successful implementation of reforms during these two periods. Section 8 concludes and discusses the implications of these findings for the likely success of the 2023 IMF mission.

Need for Reform in Pakistan

Pakistan endured a severe economic crisis in 2022 and 2023, marked by a sense of urgency for neglected reforms and the looming threat of IMF intervention. During 2022, Pakistan faced a series of economic challenges, including devastating floods, soaring commodity prices exacerbated by Russia's invasion of Ukraine, rising inflation, an unsustainable current account deficit, a sharp depreciation of the Pakistani rupee, and a foreign exchange crisis. In 2023, Pakistan's response to these problems was inconsistent, involving a combination of "monetary tightening, new subsidies, and an informal exchange rate cap. These measures resulted in the depletion of foreign exchange reserves and undermined progress toward planned fiscal consolidation" (World Bank, 2023:1). International commentators offered a smorgasbord of pessimistic projections. The Asian Development Bank forecast inflation to more than double from 12.2 percent in 2022 to 27.5 percent in 2023 (2023a:169). Economic growth was projected to slow from 6 percent in 2022 to 0.6 percent in 2023, and even into 2024, growth was expected to reach no more than 2 percent (2023b:81). Even this anaemic revival into 2024 was predicated on "assuming sustained macroeconomic policies, reform implementation, recovery from supply shocks caused by flooding, and improving external conditions" (Asian Development Bank, 2023a:172). The crisis was forecast to have a real impact on well-being, "with slowing activity, the lower middle-income poverty rate is expected to increase to 37.2 percent in FY23" (World Bank, 2023:1).

An IMF mission to Pakistan in late January and early February 2023 intoned a familiar list of reforms necessary to "regain macroeconomic stability and resume economic growth". The "key priorities" included "strengthening the fiscal position with permanent revenue measures and reducing untargeted subsidies, while scaling up social protection for the most vulnerable and flood-affected populations; allowing the exchange rate to be market-determined to gradually eliminate the foreign exchange shortage; and enhancing energy provision by preventing further accumulation of circular debt and ensuring the viability of the energy sector." (IMF, 2023a).

The World Bank largely concurred, stating that "to facilitate new external financing, regain stability, and establish a base for medium-term recovery, the Government must maintain overall sound macroeconomic management, including a flexible exchange rate and controlling inflation through appropriate monetary policy; increase revenues and rationalize expenditure (including reducing untargeted energy subsidies); and implement trade and private sector reforms to support improvements in investment, competitiveness, and productivity" (World Bank, 2023:1).

Results of IMF engagement

A passing familiarity with Pakistan's previous engagement with the IMF would likely lead to pessimism regarding the country's ability to implement IMF-mandated reforms. As of February 2020, Pakistan had signed 22 agreements with the IMF and failed to complete 21 of them. The exception was a Standing Arrangement of US$596 million, signed in November 2000 under the military government of General Musharraf and running until September 2001 (IMF, 2023b).

One means of quantifying this failure is to focus on tax revenue. In 2000, the IMF approved a Stand-By Credit for Pakistan of US$596 million, regarding which, the IMF's Managing Director indicated that the "budget target is to be achieved through increased tax collections, a widening of the tax base, improved tax administration, and strict expenditure controls." (IMF, 2000). In 2003, the IMF approved a loan of US$123 million. The IMF's Managing Director was quoted as saying "This will require forceful pursuit of reforms aimed at simplifying the tax system and broadening the tax base, including through the elimination of a number of tax exemptions, to reduce distortions and the potential for corruption" (IMF, 2003). In 2009, the IMF completed a review of a US$11.3 billion loan to Pakistan. At the time, the Deputy Managing Director was quoted as saying "A durable solution to the problem of low tax revenue should start with the early implementation of Value Added Tax (VAT) and the ongoing tax administration reform" (IMF, 2009). In 2010 the Deputy Managing Director of the IMF said, "Achieving the 2009/10 fiscal target will require strong efforts, including from the political leadership. Resolute continuation of tax collection efforts, tax administration reform, and expenditure restraint" (IMF, 2010).

These four quotes are not exceptions, but rather are entirely typical of the conditionalities imposed by the IMF. A more comprehensive list of 18 such examples can be found in McCartney (2015). Figure 1 shows the practical outcomes of these promises: Tax revenue in Pakistan barely changed between 2000 and 2021, fluctuating within a narrow band between 9 and 11 percent of GDP. Consequently, in 2021 (9.56 percent), tax revenue was lower than in 2000 (9.45 percent).

Two Success Stories: 2000-2001 and 2013-2016

As noted in Section 2, Pakistan only fully completed the conditionalities attached to one IMF program, the one launched in 2000. However, if we examine a broader range of macroeconomic indicators, we can extend the list of successes to two. Although two is not a large number out of the twenty occasions in which Pakistan has engaged with the IMF, it is at least adequate for a comparative perspective. Pakistan managed to implement economic reforms sufficiently to ensure that the main macroeconomic indicators quickly moved in the right direction after both 2000 and 2013. We introduce these two programs in this section and provide a more comprehensive justification for why they can be considered "successes" in Section 6.

In 2000 Pakistan received US$596 million from the IMF, which went to the then-newly installed military government of the late General Pervez Musharraf. At the time, IMF appeared to be optimistic about the prospects for reform and declared, "The new government, shortly after assuming office in October 1999, announced that it would make a clean break from the past by forcefully implementing reforms to address these long-standing structural problems facing the economy. They set forth a wide-ranging reform agenda aimed at reducing poverty, improving governance, and sustaining a high rate of economic growth." (IMF, 2001:6).

The IMF did acknowledge, however, that looking at past engagements with the IMF, performance in Pakistan had been disappointing. "Policy implementation and economic performance have been disappointing. Tax revenue performance has repeatedly fallen short of programme targets, public sector indebtedness—both external and domestic—has continued to rise, the external position has remained fragile, and economic growth has been low, while the number of people living in poverty has increased and Pakistan's social indicators remain weak." (IMF, 2001:6).

In 2013 Pakistan requested US$6.68 billion from the IMF through an Extended Fund Facility. Whereas previously the IMF had heralded the arrival of a reforming military government, in 2013 they praised the merits of a newly installed democratic civilian government. "The convincing win provides a strong mandate to implement a bold reform agenda required to lift Pakistan's growth potential, which deteriorated significantly over the past decade" (IMF, 2013:1).

The IMF did acknowledge Pakistan's reform history, saying "the programme carries significant implementation risks given Pakistan's track record" (IMF, 2013:2), but noted that these risks were "mitigated by critical upfront actions and even phasing of Fund disbursements, as well as by the strong electoral mandate and commitment to reform of the new government" (IMF, 2013:2).

Theories of Reform that Do Not Fit Pakistan

This paper seeks to explain why and how the reform episodes in 2000-01 and 2013-16 were relative successes. Economic theory and case studies of reform have generated various possible explanations, most of which do not fit these two Pakistan case studies. These theories include IMF conditionalities, democracy and dictatorship, a discredited former regime, and a developmental state.

IMF Conditionalities

The IMF intends and various scholars support the use of conditionalities as a buttress to strengthen the reform drive of recipient governments. Turning to the IMF is often a last resort when other sources of commercial or low-interest credit have dried up, and there is no alternative. The Cold War bipolarity, in which countries such as China and the USSR offered donor support as a distinct ideological alternative to the US, has since collapsed. Loans from the IMF, especially when phased over time (as in 2013) can serve as a reward for adhering to reforms. An IMF program often signals intent and seriousness to other potential donors, who may offer assistance contingent upon adherence to the IMF program. However, this explanation does not help with regards to our two Pakistan case studies, both of which were subject to IMF conditionalities, as were the numerous failed reform efforts noted in Section 3.

Democracy and Dictatorship

Other scholars have focused on the nature of the political system, investigating whether democracy or dictatorship is more effective in implementing radical, IMF-style policy reform. Some have noted that democracy often leads to more fitfulreforms, because of the greater need to avoid imposing costs on politically influential groups. For example, India's reform process in the 1990s has been described as "a process of change that was not so much gradualist as fitful and opportunistic", with India evidently possessing a "strong consensus for weak reforms" (Ahluwalia, 2002:86). Conversely, democratic countries may be better equipped to foster coordination and cooperation among various groups. Consistent with these arguments, evidence suggests that countries with greater civil liberties and political rights during the 1970s were more resilient to the global economic shocks and slowdown in global growth in the mid-1970s, experiencing lower declines in economic growth when their trend rate of growth changed (Rodrik, 1997). Moreover, the volatility of economic growth tends to decrease following democratization (Rodrik and Wacziarg, 2005). However, this debate has limited relevance to our case studies, which compare successful adjustment under a dictatorship (Pakistan in 2000), followed by a democratic government (Pakistan in 2013).

A Discredited Former Regime

Economic reform may be facilitated when an incoming government can attribute economic and social problems, as well as the short-term costs of reform, to a discredited former regime. This was one factor that enabled rapid and systemic change in the socialist transitionary economies of the 1980s (China) and 1990s (the former Soviet Union, and Central and Eastern Europe). To some extent, the military government under Musharraf was able to do so in Pakistan in 1999. The military coup was justified on the grounds of the perceived corruption and incompetence of the democratic civilian governments of the 1990s, three of which had been dismissed by the Pakistani President. The incoming Pakistan Muslim League government under Nawaz Sharif in 2013 similarly attempted to blame the outgoing Pakistan People's Party under Asif Zardari for economic problems, in a traditional democratic manner. There is limited scope for this argument, particularly regarding why Pakistan was able to implement successful reforms in 2000-01 and 2013-16. Pakistan in 2000 and 2013 was markedly different from the transition economies of the 1980s and 1990s. These transitionary economies were undergoing a systemic shift from closed, state-run, and planned socialist systems to open-market, private sector economies. In many cases the political system had transitioned from authoritarian to democratic. These were examples where a discredited political regime and economic system could be blamed for current economic problems and any associated costs of reform. In 2000, Pakistan witnessed the rise to power of a military government, the same military that had been at the centre of Pakistan political life since at least the 1950s and had seized power through military coups in 1958 and in 1977, ruling for a decade in both instances. the third military coup in 1999 was not particularly novel. The Muslim League, which came to power in 2013, was the successor to the Muslim League which was the party of independence in the 1940s and came to power in 1947. Nawaz Sharif and the Muslim League had formed the national government between 1990-93 and 1996-99.

A Developmental State

Other scholars have argued that a "strong state", regardless of whether it is democratic or dictatorial, is essential for promoting market-oriented economic reform and overcoming the entrenched special interests that benefit from government intervention. The market-oriented reforms implemented by Prime Minister Margaret Thatcher in Great Britain during the 1980s are often cited as an example (Gamble, 1988). This idea has been generalised by scholars of developmental states, who seek to explain the economic success of countries such as Japan, South Korea, and Taiwan, and China, as a product of effective and developmentally oriented states (Leftwich, 1995). Some authors have suggested that the incoming military government of General Pervez Musharraf in 1999 attempted to make the civil service more autonomous from politicians, more technocratic, and more development-oriented. General Musharraf appointed Shaukat Aziz (then senior manager at the Citibank) as Finance Minister. Aziz put together a team of international bankers and former/current employees of the World Bank and IMF, including Ishrat Husain, a former director for central Asia at the World Bank who was appointed governor of the State Bank of Pakistan (SBP). Aziz became Pakistan's most important minister and was given the freedom and mandate to tackle the financial crisis, often bypassing the prime minister. At the time, military rule was viewed as a benefit, insulating the state and empowering a technocrat to implement long-term, tough economic reforms (Khanna, 2010). The World Bank's "Government Effectiveness" index "captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. Estimate gives the country's score on the aggregate indicator, in units of a standard normal distribution, i.e. ranging from approximately -2.5 to 2.5." Figure 2 shows that there were brief, slight improvements in government effectiveness around 1999-2000, a deterioration soon after, an improvement between 2003 and 2006, a slump after 2006, and some signs of an improvement in 2013, though from very low levels. At no point between 1999 and 2013, did Pakistan have an effective, East-Asian style government.

A Theory of Reform that Does Fit: Mancur Olson, Roving Bandits, and Settled Bandits

This section introduces the Roving vs Settled Bandit theory of Mancur Olson. According to this theory, all politicians are bandits and seek to benefit themselves and their networks through "theft". When facing imminent loss of office, the most profitable option is to raid the state's coffers. However, in a more stable political environment with a long-term tenure, promoting economic growth by protecting the property rights of investors becomes more lucrative. This section introduces the Olson theory and explains how Pakistani politics shifted from "roving" to "settled bandits" in the 1990s compared to the 2000s.

The Olson Theory

Mancur Olson provides a useful framework. Olson assumed all politicians to be "bandits" seeking to maximise their personal wealth and power by using political office. When facing imminent and certain loss of office (being a long way behind in the opinion polls with an election looming), a politician would have no incentive to consider future societal output, becoming a "roving bandit" (Clague et al, 1996). Whenever a politician faces a higher likelihood of losing power or a shortened time horizon, they may be tempted to expropriate assets from businesses, households or farmers. Short-term tax yields are often less than the capital value of expropriated assets. In the 1990s Pakistani politicians faced uncertain and likely brief tenures in office. This incentivized them to grab wealth for themselves and their networks as quickly as possible, making them "roving bandits". A quick plunder and subsequent departure was the political maxim.

Investment is essential for growth, but returns on investment may take time. This means that a politician with a long-term perspective will try to convince constituents that their assets are protected from theft by others and expropriation by the politician themselves (Olson, 1993, 2000). This paper argues that politics in Pakistan shifted toward greater stability and longevity after 1999. However, this did not indicate a change in the politicians of the military dictatorship or subsequent democracy. They still sought to maximise their wealth and power; they were still "bandits". The incentives for politicians changed. For those with extended tenure, maximizing personal wealth and benefits for their networks involved taking a more regular and predictable income share while incentivizing businesses to expand production over the longer term (Olson, 1993; 2000).

Pakistani Politics: From Roving Bandits in the 1990s to Settled Bandits in the 2000s

The military governments that took power in 1958 and 1977 each lasted more than a decade. The 1999 military takeover ousted former Prime Minister Nawaz Sharif, who went into exile. The new president, General Pervez Musharraf—responsible for the said takeover—faced the prospect of a similarly extended tenure in office.

The nature of civilian democracy and its return to Pakistan after 2008 require further justification. In the 1990s, Pakistani governance was characterized by minority-led coalitions that consistently failed to complete a five-year term in office. These coalitions included the Pakistan People's Party (PPP)-led four-party "Democratic Alliance" (1988-90), the Pakistan Muslim League-Noon (PML-N)-led nine-party "Islami Jamhoori Ittehad" (IJI) alliance (1990-93), and the subsequent PPP (1993-96) and PML-N (1997-99) governments. The PPP-led "People's Democratic Alliance" (PDA) also proved short-lived. The PML(N)-led IJI alliance was promoted by Pakistani intelligence agencies to unite various supporters of President General Zia-ul Haq, who died in August 1988 (who came to power by overthrowing Zulfikar Ali Bhutto's civilian PPP government). The alliance survived under various guises and fluctuating membership throughout the 1990s. The largely urban and Karachi-based Muttahida (formerly the Muhajir) Qaumi Movement (MQM) party was a shifting alliance partner. It switched between the PPP and PML-N based on its own internal political compulsions. The first three governments of the 1990s were dismissed by the President for corruption and maladministration. The last one was overthrown in a military coup. The PML-N's victory in 1997 was the only national-level majority for a single party in Pakistan during the 1990s.

The 2000s saw the gradual stabilisation of a two-party coalition system, where governments were only removed by the electorate or through constitutional means. The 2008 PPP administration completed its full five-year term, the first since 1971. The 2013 PML-N victory heralded Pakistan's first ever democratic transfer of power after a full term in office. The PML-N went on to complete its five-year term in office and was ousted at an election (2018) by the Pakistan Tehreek-e-Insaf (PTI) party headed by the cricketer and philanthropist Imran Khan. PTI lost its majority in parliament and a subsequent parliamentary vote of no confidence, which in turn led to the resignation of Imran Khan as PM, and his replacement by Shahbaz Sharif and the PML-N.

A significant indicator of increasing political stability in the 2000s was the evolving role of independent members of parliament (MPs) in national elections. Independent MPs, often with a local power base and prior party affiliations, increasingly won seats. The victories frequently led to negotiations with established political parties, typically the majority party, for various benefits such as financial payoffs or ministerial office in exchange for support.

Independent candidates often demonstrate flexibility in joining and leaving ruling coalitions, which can weaken party attachment and the stability of party rule. In the 1988 elections in Pakistan, independent candidates played a pivotal, role, winning 48 of 217 seats and 22.12 percent of the vote. Many of these candidates were local notables who had been denied tickets by the main political parties (PPP or PML-N), leading them to run as independents. The party-political system lacked the robustness to retain these candidates within the system to work for party interests. Since 1988, the role of independent candidates has steadily declined, with seats won dropping from 48 in 1988 to 27 in 2013 and plummeting to 13 in 2018. The vote share for independent candidates experienced an even sharper decline, falling from 22.12 percent in 1988 to a negligible 3.8 percent in 2018. These small, often one-person, parties represent single constituencies and have little incentive to consider the wider social costs of any benefits they secure for their narrow interests. Special interest groups, which significantly influence government policies, have minimal incentive to consider the social costs of the redistributions they obtain. A typical lobby in the United States represents less than 1 percent of the country's income-earning capacity, leading it to stop advocating further redistribution only when the social costs exceed the benefits by a factor of one hundred (Olson, 1993).

The nature of the political leadership in Pakistan strengthened the impact of the "settled" nature of the ruling bandits. In Pakistan, Asif Ali Zardari headed the PPP and became President in 2008. It was widely assumed that Zardari's son, Bilawal Bhutto, would eventually take over the party leadership. Bilawal was the son of former Prime Minister Benazir Bhutto, who in turn was the daughter of former Prime Minister Zulfikar Bhutto. Nawaz Sharif, the Prime Minister, and his brother, Shahbaz Sharif, the Chief Minister of Punjab, were both first-generation politicians. However, they had various sons and daughters who were speculated to become the next generation of democratic-dynastic political leaders of the PML-N. The perception of ruling leadership in Pakistan during the 2000s extended beyond that typical of a five or ten-year period in office. In both countries, the leadership had an incentive to act as settled bandits to pass on the benefits of long-term policy orientations to their dynastic family successors.

In Pakistan, the nature of political competition is crucial; to win office, politicians must form winning coalitions. The number of competitors a party faces in a first-past-the-post system influences the size of the constituency a politician must appeal to in order to secure a majority. If there are only two effective parties or alliances, each needs a majority to win the seat, which compels a party to build broad alliances across social groups. In such cases, politicians will seek a more encompassing interest (Olson, 1993). However, as the number of competitive parties increases, a party requires an increasingly smaller coalition to win the seat. For example, in the Lok Sabha elections in India between 1957 and 1991, a winning party needed 55 percent of the vote in districts with two competitive parties, compared to 38 percent in districts with three or more effective parties. Empirical evidence shows that multi-party systems in India spend less on public goods relative to targeted goods and salaries (Chibber & Nooruddin, 2004). Evidence from India also indicated that the successful implementation of the National Rural Employment Guarantee Act (NREGA) in Andhra Pradesh (Khosla, 2011) and in Rajasthan (Gupta & Mukhopadhyay, 2014) was linked to close two-party competition for power at the state level. A study of 3,701 country-years from 107 countries investigates whether electoral rules and the form of government affect economic growth. The results show no robust impact of presidentialism or parliamentarism on economic growth. However, there is robust evidence of a positive and substantial, impact of proportional representation (PR) electoral rules on economic growth. This is partly due to the propensity of PR systems to generate broad-interest policies, such as universal education spending, property rights protection, and free-trade, rather than special interest economic policies (Knutsen, 2011).

Evaluation of 2000-01 and 2013-16

This section provides empirical evidence to support the claim in section 4 that economic reforms undertaken by Pakistan, after engaging with the IMF, were sufficient for macroeconomic indicators to move swiftly in the right direction after 2000 and 2013. It also provides the evidence to support the theoretical framework of the Olson thesis from Section 6, which suggests that greater stability and longevity in Pakistani politics, as seen in 2000 and 2013, resulted in improved macroeconomic management. The variables discussed in this section include the budget deficit, inflation, non-performing bank loans as a share of total loans, the current account deficit, debt service as a share of total exports, short-term debt as a share of total reserves, and total reserves as a share of external debt. These variables are common to IMF programs in Pakistan and are critical for ensuring sustainable economic growth.

Figure 1 shows that the general stagnation of tax revenue across 2000 to 2021 masks moderate increases during both 2000-2001 and 2013-2016. Tax revenue as a share of GDP was stable at around 9.5 percent in both 2000 and 2001, then increased to 10.3 percent in 2003. The tax ratio increased from 9.8 percent in 2013 to 11.19 percent in 2016. However, these increases were not sustained as the tax ratio declined after 2003 and 2018.

Figure 3 shows that the budget deficit was sharply reduced between 2000-2001 (-4 to -3 percent) and 2013-16 (-8.4 to -4.42 percent). However, in both cases, this progress was not sustained, and the budget deficit increased afterward.

Figure 4 illustrates that inflation decreased in 2000-01 (from 5 to 3 percent) and 2013-16 (7.2 to 3.8 percent). Yet, as with the budget deficit, reforms were not sustained, leading to an increase in inflation after 2003 and 2015.

Figure 5 shows that problematic lending by the banking system was successfully addressed in both 2000-2001 and 2013-2016. In 2000-2001 non-performing loans initially increased from 19.5 percent to 23.4 percent of GDP, but then sharply declined to 6.9 percent of GDP by 2006. Between 2013 and 2016 non-performing loans declined from 13 percent to 10 percent, before showing an increase after 2018.

Figure 6 shows that the current account balance was well managed during both 2000-2001 and 2013-16. Between 2000-2001 the current account balance increased from 0 percent to 2 percent of GDP, further improving to 5 percent in 2002, before deteriorating rapidly. In 2013-2016, the balance was maintained between -1 to -2 percent of GDP, but there was a sharp deterioration after 2016.

Figure 7 shows that debt service as a share of exports of goods, services, and primary income, remained stable at around 28 percent between 2000-01, then fell sharply. It declined from 22.7 percent in 2013 to 15.7 percent in 2016, before rising sharply again.

Figure 8 shows that significant progress was made in reducing the ratio of short-term debt as a share of total reserves (a proxy measure of financial vulnerability) during both 2000-01 and 2013-16. The ratio declined from 72.8 percent in 2000 to 31.1 percent in 2001, and from 60.8 percent in 2013 to 32.3 percent in 2016. However, the ratio subsequently increased after 2009 and 2016.

Figure 9 shows that total reserves as a share of total external debt increased during both 2000-2001 and 2013-2016. The ratio increased from 6.3 percent in 2000 to 13.1 percent in 2001, and from 12.7 percent in 2013 to 29.4 percent in 2016. The ratio subsequently declined, after 2007 and 2016.

Conclusion and Discussion: Implications for 2023

It would be easy to adopt a pessimistic view regarding Pakistan's ability to fulfil the conditions of the 2023 IMF programme. Pakistan has failed to complete all but one of the more than twenty IMF programs it has entered into since 1958. However, this paper takes a slightly more optimistic perspective, arguing that Pakistan responded successfully to both the 2000-2001 and 2013-2016 IMF programs across a wide range of economic and policy variables. This paper draws on Mancur Olson's theoretical framework—specifically the distinction between 'roving' and 'settled' bandits—to explore the broader political economy that enabled Pakistan to briefly implement successful economic reforms during these two periods. This paper used this theoretical perspective to explain why Pakistan was better able to implement economic reform in both 2000-2001 and 2013-2016. The explanation offered here is that Pakistani politics shifted from roving to settled bandits in the 2000s compared to the 1990s. Politics in Pakistan during the 2000s was characterized by greater stability and longevity in office. This stability provided politicians, both dictators and democrats, with the incentive to adopt a long-term perspective and implement the economic reform measures requested by IMF.

After eight months of protracted negotiations, amid loud media commentary, and inflation reaching 30 percent, the IMF Executive Board approved a US $3 billion Stand-by Arrangement for Pakistan in July 2023 (IMF, 2023c). The new IMF loan acknowledged that Pakistan had been buffeted by a "difficult external environment" which included "devastating floods", but also acknowledged that much of the crisis resulted from domestic "policy missteps". Together, these forces "led to large fiscal and external deficits, rising inflation, and eroded reserve buffers" (IMF, 2023c). The package of reforms Pakistan agreed to implement in exchange for the loan was a familiar one. It included "fiscal adjustment", "protecting critical social spending", a "return to a market-determined exchange rate", "an appropriately tight monetary policy aimed at disinflation", and "further progress on structural reforms, particularly with regard to energy sector viability, SOE governance, and climate resilience" (IMF, 2023c). Unsurprisingly, there was a ritual emphasis on taxation, the "anticipated improvement in tax revenues is critical to strengthening public finances, and eventually creating the fiscal space needed to bolster social and development spending." (IF, 2023c).

The IMF Managing Director emphasised the importance of implementation: "The authorities' new Stand-By Arrangement, implemented faithfully, offers Pakistan an opportunity to regain macroeconomic stability and address these imbalances through consistent policy implementation." (IMF, 2023c).

There are mechanisms built in to help ensure the programme is a success. Pakistan received a US$1.2 billion upfront payment from the IMF, with the remaining to be disbursed over the next nine months, contingent on meeting various targets. The United Arab Emirates and Saudi Arabia also provided significant financial assistance (US$1 billion and US$2 billion, respectively), but their support was contingent on Pakistan reaching an agreement with the IMF (BBC, 2023).

Benighted

An IMF team visited Pakistan in early August 2023 to evaluate progress on the loan conditionalities and contribute to a decision about whether to release a further US $700 million of IMF lending (IMF, 2023d). The team noted that "a nascent recovery is underway, buoyed by international partners' support and signs of improved confidence" and commended Pakistan for the "steadfast execution of the FY24 budget". Even in historically challenging areas the IMF were positive. The IMF team noted, the "authorities are determined to achieve a primary surplus of at least 0.4 percent of GDP in FY24, underpinned by federal and provincial government spending restraint and improved revenue performance supported, if necessary, by contingent measures." While "protecting vulnerable consumers, the authorities implemented power tariff adjustments that were pending since July 2023 and increased gas prices after a long time", and following "passage of the State-Owned Enterprises (SOE) law, the authorities are moving forward with their SOE policy and implementation of their triage plan, including the privatization of select SOEs." (IMF, 2023d).

The successful reforms of 2000-01 and 2013-16 demonstrate that Pakistan can achieve significant progress under both democratic and dictatorial regimes, even with little government effectiveness, but only when incentives are aligned. Applying Olson's theory, we can identify the conditions under which the government would be motivated to implement the current IMF programme. We must assess whether the current government operates in a relatively stable political environment and perceives itself as a long-term ruling entity (a "settled bandit"). The answer to both questions appears to be negative.

The PML-N government led by Shabaz Sharif (Nawaz Sharif's brother) before February 2024, came to power in 2022 after the incumbent Prime Minister was ousted in a vote of confidence. This was the culmination of a period of political instability. The PPP administration (2008-2013) saw Prime Minister Yousaf Raza resign in 2012 due a corruption scandal. His replacement, Mr Haza Khan Khoso, served until the party's defeat in 2013. The PML-N government (2013-2018) was led by Prime Minister Nawaz Sharif until 2017, when he was replaced by Shahid Khaqan Abbasi. Imran Khan led the PTI government from 2018 until his ouster in 2022. The incumbent government, a hastily formed alliance, was tasked with ousting and replacing Prime Minister Imran Khan. The incumbent government under Shahbaz Sharif was facing pressure to implement tough IMF reforms before the February 2024 general election. The leading candidates, Imran Khan (imprisoned and facing legal charges) and Nawaz Sharif (three times former Prime Minister, recently returned from exile and disqualified), were vying for the position. Given the political instability and the likelihood of losing political office, the government's incentives are shifting toward short-term gains, similar to those of a "roving bandit", as per the Olson theory. This could hinder the successful implementation of the 2023 IMF program.

Another trend may alter this trajectory. Nawaz Sharif's return from exile, coupled with his abandonment of opposition to the military, has predictably led to the overturning of his past convictions (Afzal, 2023). This includes his conviction for corruption in the Avenfield properties case (Burney, 2023). There is widespread speculation that the military and other organisations were working to ensure a victory for the incumbent Muslim League in the 2024 elections, while simultaneously undermining the prospects of Imran Khan and the PTI (Afzal, 2023). If this trend gains momentum and the likelihood of a PML(N) victory under either Shahbaz or Nawaz Sharif increases, the incentives faced by the PML(N) government may shift towards those of "settled bandits".

Throughout this paper, "success" has been narrowly defined as the ability to complete a short-term IMF program. The 2023 IMF program, lasting only nine months, would likely require the winner of the 2024 general elections to negotiate another program soon after taking office. Our two case studies of success, 2000-2001 and 2013-2016 were short-lived. Section 7 demonstrated how quickly economic policy and related macroeconomic indicators deteriorated after the completion of these IMF programs. Even the favorable incentives faced by "settled bandits" are insufficient in the Pakistani context to foster long-term, sustainable policymaking.

Upon assuming power, every new government In Pakistan pledged to implement policies that will foster economic growth, enhance social services and alleviate poverty. However, the state's limited resources, due to low tax revenue hinder the achievement of these ambitious goals. Consequently, an increasing number of voters and elites become disillusioned with the government (Lieven, 2011). As the likelihood of re-election diminishes, the government's incentives shift from "settled" to "roving bandits", undermining reform, economic growth and further reducing the chances of re-election.

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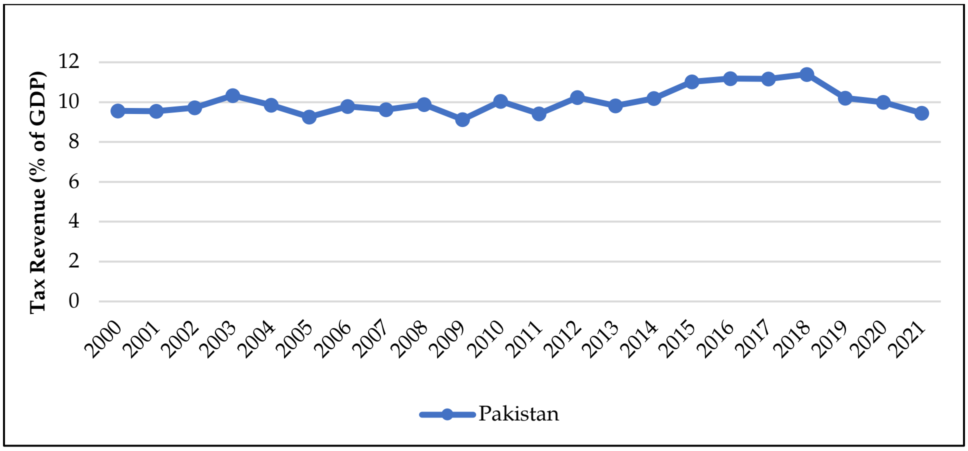
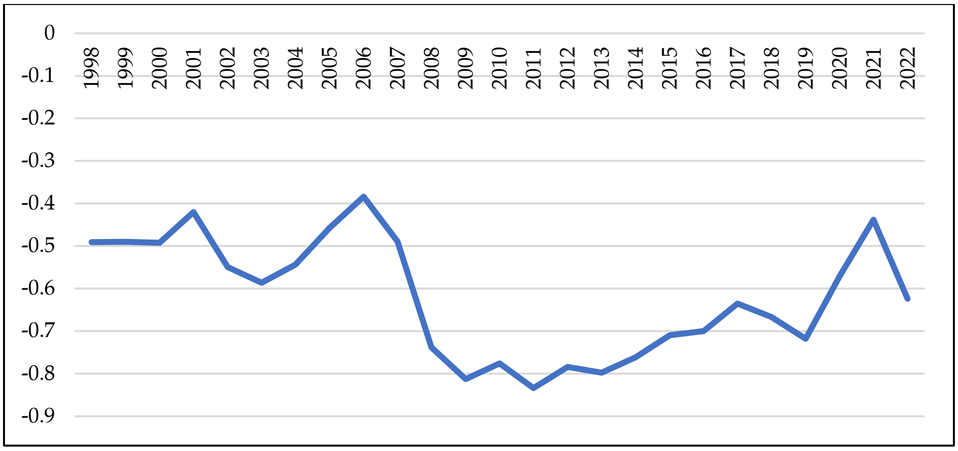
Appendix

Figure 1: Tax revenue (% of GDP), Pakistan 2000-2021



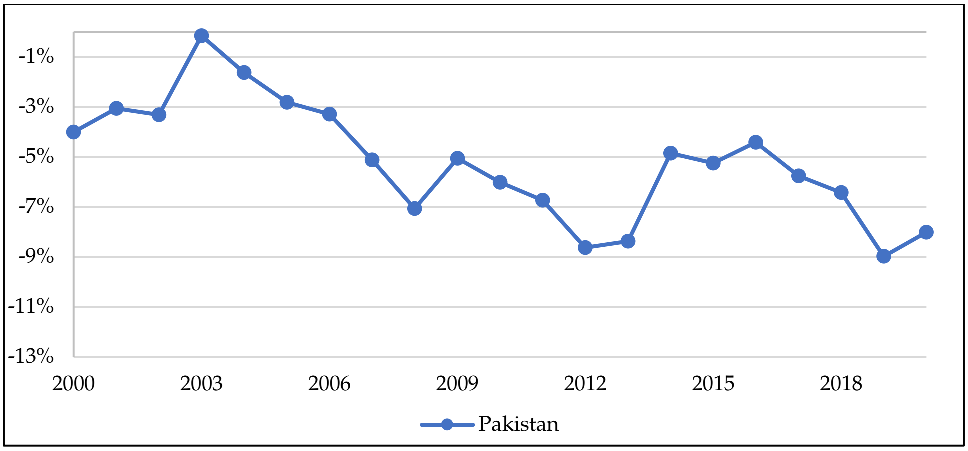
Source: Asian Development Bank (2022)

Figure 2: Government Effectiveness in Pakistan, 1998 to 2022



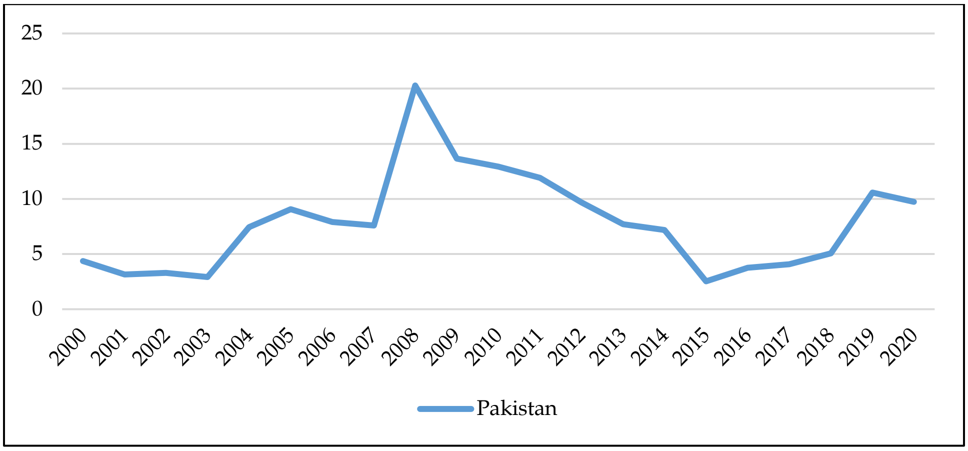
Source: World Bank (2022)

Figure 3: Budget deficit as % of GDP, Pakistan 2000-2020



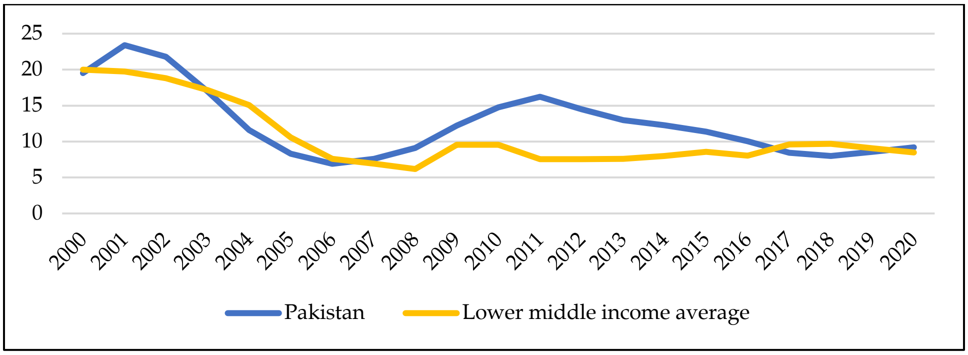
Source: Pakistan Bureau of Statistics

Figure 4: Inflation, Consumer Prices (annual %), Pakistan 2003-2019



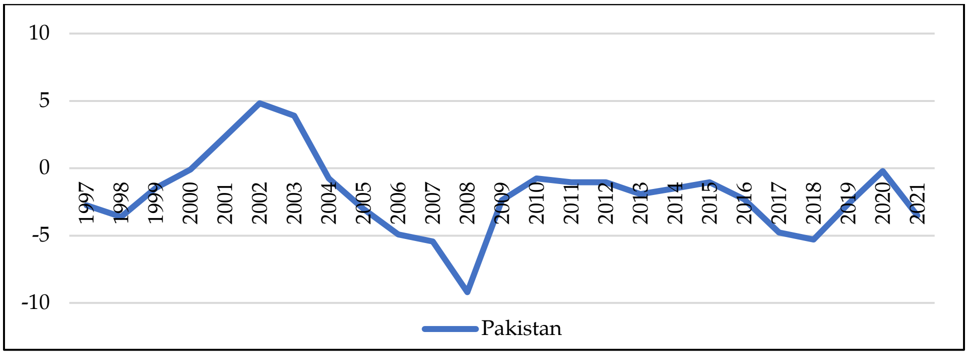
Source: World Bank (2022)

Figure 5: Non-performing loans (NPLs) in the Banking System as % of total loans, Pakistan and Lower-middle income countries 2000-2020



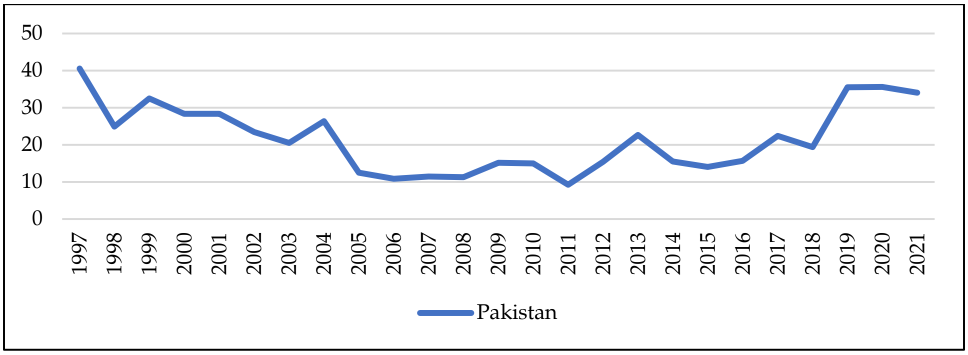
Source: International Monetary Fund (2022)

Figure 6: Current account balance (% of GDP), Pakistan 1997-2021



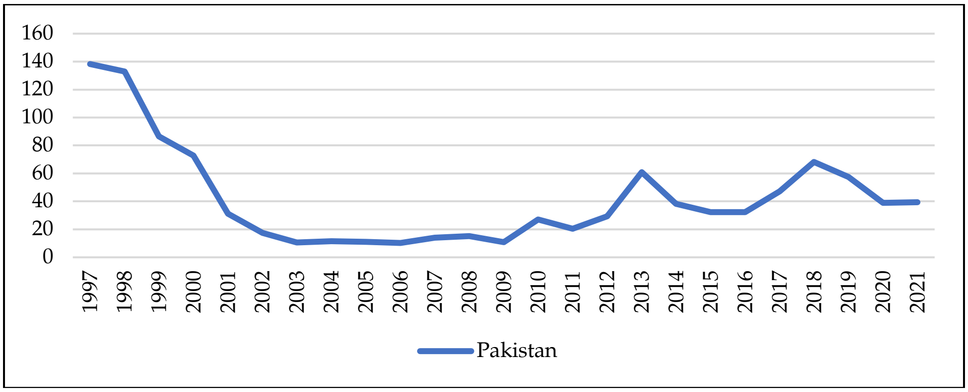
Source: World Bank (2023)

Figure 7: Total debt service (% of exports of goods, services and primary income), Pakistan 1997 to 2021



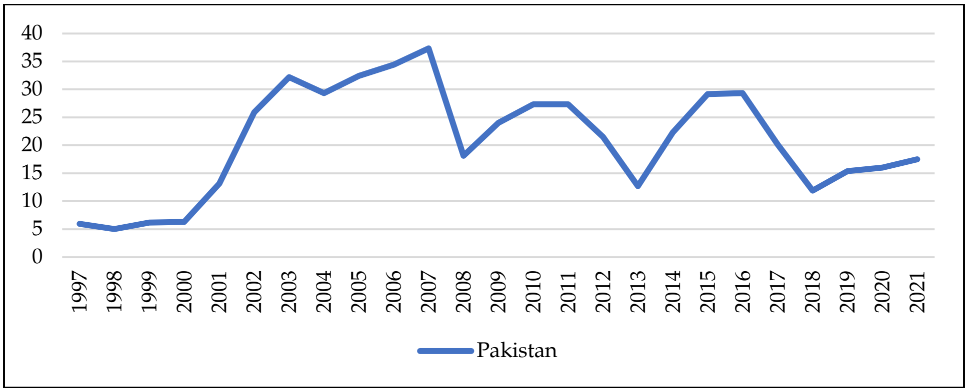
Source: World Bank (2023)

Figure 8: Short-term debt (% of total reserves), Pakistan 1997 to 2021



Source: World Bank (2023)

Figure 9: Total reserves (% of total external debt), Pakistan 1997 to 2021



Source: World Bank (2023)