



With Us or Without Us: extended interviews

Interviewer: Edward Stourton

Interviewee: Moeen Afzal, Secretary-General of the Pakistani Ministry of Finance

STOURTON: Where were you and how did you hear about the events of September the 11th.

AFZAL: Well actually I was in the finance minister's room and, as it happens, we were having a meeting on economic issues with the prime minister of Azad Jammu and Kashmir. The finance minister had a television going in his office, and that's where we saw the terrible events in New York that day.

STOURTON: Can you provide us with an account of the days that followed 11 September?

AFZAL: Well obviously everything changed and we realised very early in Pakistan that in a diplomatic, in an economic, and political sense, things were going to change pretty fast, and, because of its regional position, Pakistan would be, in a sense, very closely involved with what happened as a result of 11th September.

STOURTON: Were there certain meetings you had to attend, was there a feeling of crisis here?

AFZAL: Well the fact was, as you probably know, the decision was made very early by General Musharraf in consultation with his cabinet colleagues and the security council, to throw Pakistan's full weight behind the coalition in their fight against terrorism. Of course that was followed by internal meetings for us in the finance ministry, trying to weigh up the consequences of 11 September on Pakistan, plus of course as you recall we had visitors from all over the world wanting to know about Pakistan's economic progress, problems, prospects, and so in a sense it was a very busy time.

We were at that stage negotiating the final stages of a three year medium term, you know programme, with the IMF. We just completed successfully the standby and this was the PITF, and so in a sense, within a couple of weeks, we had to work out the short term and medium term effects on the Pakistani economy and see how this would impact us on the trade side and on the fiscal side because we had to go and negotiate with the fund. In fact the fund were to come here and because of travel advice you know they couldn't, so we had to spend two weeks in Washington then in early October finalising the programme.

STOURTON: Among those visitors who came were Colin Powell, can you tell us about the list of seven demands put up by Colin Powell and Richard Armitage?

AFZAL: Well no I don't think I'd be able to really say very much about that, that was...

STOURTON: Could you tell us about the lists of seven demands put up by Colin Powell and Richard Armitage?

AFZAL: No I think you, you're probably referring to the recent visit of Richard Armitage and Colin Powell, which came in the wake of the stand-off with India, which was fundamentally political and connected with the military aspects of the situation on the LOC and the borders with India. No I wouldn't be able to say anything about that.

STOURTON: Could you just describe the financial situation here in Pakistan before the events of 11 September?

AFZAL: Yes, you see there is a view which I think is very misleading, that Pakistan was in a very serious economic crisis which somehow eased up after 11 September because of the assistance we got from some of the major donors. I think that's incorrect.

Pakistan was, in fact, in a very difficult economic situation in the last two or three months of 1999 at about the time General Musharraf took over, and the government went through a very, very prolonged, comprehensive and strong reform programme which was both a stabilisation programme and an economic reform programme. And, sometime around July/August 2001, we had meetings with the IMF and the World Bank and both of them publicly announced support for the programme, and a transition for Pakistan from the standby into the PITF facility, to be financed by the IMF over three years, and both had also agreed to provide us with special assistance through a third and final round of Paris Club (an informal group of donor governments), so in fact the situation had already improved considerably. So what I mean exactly is that the foreign exchange reserves increased much more substantially in the year before 11 September than they did in the nine or ten months after. And of course 11 September itself, in the short term by which I mean nine months to a year after, we estimate would cost us a lot in terms of production, in terms of lost exports, in terms of lost revenues, and that's now been borne out by the facts.

STOURTON: And in simple terms, in layman's terms, what were the main kind of problems facing Pakistan before 11 September, was it lack of foreign investment, was it lack of industry?

AFZAL: Well actually the problems we faced really do not relate to 11 September. I think the economic problems were structural problems which had, unfortunately, been a consequence of a number of things done or not done in the previous 15 years, and I mean from about the mid eighties to about right up to the year 2000. Now that meant we had not gone in for structural reforms, our revenues were weak, and governance issues were there, there were policy inconsistencies, but fundamentally we were facing a recurring balance of payments crisis, shortages of foreign exchange, and a lot of fiscal indiscipline. Now these things are exactly the areas that General Musharraf's government addressed, and a year and a half after he took over, that's by about June/July 2001, I think we had successfully initiated the programme of both reform and stabilisation. The current account had been brought under control, the fiscal deficit was under control, exchange rate stability had been achieved, and the results were

building up. There were of course problems also of domestic savings, which is related very directly to investments. As external savings had ceased to flow because of our debt problems in the early 1990s, we basically had to raise domestic savings, and we had not addressed that issue until the last year or two, so 11 September, in a sense, provided us both with, what I'd call, a short term problem and difficulties in terms of lost production, lost exports, lost revenues, but gave us an...

STOURTON: ... How seriously had sanctions affected you?

AFZAL: The sanctions, coming as they did in June 98, affected us very seriously. Pakistan had lived with very thin low foreign exchange reserves, equivalent to about two, three weeks of imports which is very dangerous for any country, and Pakistan is a country which was relying very heavily on the flows of funds from the multi-lateral agencies, and of course some bi-lateral assistance, so when sanctions were imposed on all new lending, as it was called, it meant really we were faced with a default situation on our extended account, and that is exactly what happened, Pakistan had to go to the Paris Club.

STOURTON: What can you tell us about the visits of Tony Blair and Colin Powell, and the kind of things that were discussed?

AFZAL: Well actually the visits of these leaders and a host of others from Western Europe basically focused, as I recall it, on first of all coming really to signal support for Pakistan and the government of General Musharraf, because of the vital role Pakistan was playing as a part of the coalition. But also they and their colleagues looked very closely at some of our economic concerns; they studied the strength of our programme and agreed to provide us with appropriate support in the Paris Club, and in terms of trade access, and also in terms of technical assistance, which we needed, and that has been coming since then. But we feel, of course, that this is based not just on largesse by the donor community, but on the strength of a pretty good programme, because Pakistan has been facing difficulties, it's not completely out of the woods now, but I think it's very much on the way to stabilisation and beyond - to a stage of economic revival and much more rapid growth.

STOURTON: What did Pakistan ask the Americans to give them, and what did the Americans actually offer?

AFZAL: Well we never asked them, as I recall it, the decision the Pakistan government made with General Musharraf ...was that we are taking this decision [to support the coalition against terrorism] because it is above all in Pakistan's interests and morally the right thing to do. We did point out when we were asked that we were facing an acute debt crisis, and there were difficulties connected with economic growth and, well, the US government very generously provided us immediately with grant assistance and then, of course, they agreed to provide us with some debt reductions which I think will come in the next year. Simultaneously the European Union came in with some grant assistance, and with some very generous trade access, because we said that if you do want to ever see a strong Pakistan, then a strong Pakistan will come with a stronger economy, with stronger reserves. I think the government never asked for anything like military assistance, which I think may have pleasantly surprised them, and so that's the way it's worked out since then.

STOURTON: How much difference has the lifting of sanctions and the offer of various financial aid packages made to the economy of Pakistan?

AFZAL: I think it's made a big psychological difference, but we are not yet seeing the results of that, and I'll tell you why. As I see it, for one we still have problems on the Afghanistan front, I mean in the sense that this Al Qaeda business is not yet over, Afghanistan's reconstruction is yet to start. As we speak we still don't know how things will turn out in Afghanistan. Simultaneously we had the stand-off with India, which we hope will gradually ease, but all this accompanied by a few terrorist acts have certainly not made the investment climate more inviting for either the domestic or the foreign investment community. However, I am convinced that in the medium term, that's in the next couple of years, as these regional problems begin to ease, I think they will help us tremendously. Why? Because the removal of sanctions means that the business investment community, whether it's Western, Eastern or Middle Eastern, feel much more comfortable and I think the very fact that the sanctions are off also means that a psychological barrier or a weight has gone.

STOURTON: How much has the Afghan war actually cost Pakistan?

AFZAL: Well I think we haven't actually quantified it in actual figures and data, but I think the cost is tremendous. I mean if you just look at it, it's now been what, over 20 years, I think we still have 2.2 million Afghan refugees in Pakistan, so it's been a problem not just in a social sense, which has also been there, especially in the north west frontier and parts of Olotestan, but the physical problem of feeding them, the environment has lost out, there's been a tremendous impression on infrastructure, not just roads or water supply but things like schools, hospitals, dispensaries, so that's been one obvious and very large effect. Then there's the fallout within Afghanistan, we've had initially, the war with the Soviet Union and then we had this whole business of what's known as the "Kalashnikov Culture" coming in, because we had all sorts of outfits from Afghanistan, from the Middle East, from North Africa, from everywhere fighting out there, which in a sense, some of that has flowed into Pakistan, so it has created problems. It's been a very difficult, difficult time really but I think the cost has been frankly, very, very highto actually quantify it.

STOURTON: And what about the cost of the fighting in Afghanistan since 11 September?

AFZAL: Yes we have been, as you know, providing assistance within Pakistan's borders to the coalition, and that has been costing us a fair amount of money. Not just providing logistical support, but providing protection - providing security forces along the borders of Afghanistan. Now some of those were in the process of being removed to the eastern front because of the problems with India, but all in all we have estimated, and this can vary from month to month, that the cost is maybe around one billion rupees a month, of this.

STOURTON: What's that in dollars?

AFZAL: In dollars that would be, oh the equivalent of about \$170/180 million a month.

STOURTON: And what other factors are included in that, is that falling investment, is that inflation?

AFZAL: Well the effects of all this, the first thing which got affected very badly were our exports. Why? Because as soon as Afghanistan erupted, many buyers, prospective buyers in Europe and the United States in particular, who were not familiar with the Pakistani environment thought that well, war in Afghanistan means that Pakistan is in the war zone. A lot of orders were cancelled in places like Lahore and Karachi, which had very little to do with what was happening in Afghanistan. Then we had the war risk insurance coming in, lots of airlines discontinued their services, freight charges were increased, and of course, there is always the psychological factor, even for Pakistani investors. I was looking at our excise revenue figures the other day, and for things like cigarettes, Pepsi cola, Coca Cola, the consumption went down for those three or four months, now it's picking up again. So exports went down, we feel that GDP itself, the output actually went down, and then we had, of course, the additional costs on defence, which as you know are not the most productive way of spending government money, and then finally our revenues. Our tax revenues have probably suffered to the extent of 5 to 10 billion rupees during this year.

STOURTON: What do you think the future prospects for Pakistan's economy are, and what assistance from America and Europe would you like to see?

AFZAL: Well I think frankly many of us who worked with this government as a part of a team to get Pakistan out of its great economic muddle, which was centred around I would say three or four areas, (one was debt, the next was poverty, the third was governance, and fourth, you could call it a sort of lack of confidence among Pakistanis and among prospective investors about the quality of management in Pakistan) now those were the three or four major areas.

I think in this government we have dispelled the view that economic management will continue to be poor in Pakistan, so we've swung that around. And today, as I speak to you, our inflation for the last three years has been on an average at 3%, this year's it is 2.5%. Our current account, which used to be in deficit by over 4% and for the last two years was in deficit below 2%, is now actually in surplus. Interest rates are coming down, exports are growing, so apart from the fact that our GDP growth has been lower than what we wanted it to be, and one of the prime factors for that was the two years of severe drought with which we are familiar, and of course 11 September, that's picking up again now.

I think the macro picture is looking good; I think with elections round the corner now, because in another three to four months we'll have a new government - a political and democratically elected government - it will be important for that government, as we see it, to continue with this programme. It's my conviction, having worked with the Pakistan economy for some time, that if the macro framework is right, if the policies are consistent and stable, the private sector in Pakistan is extremely vibrant, and given the continuation of the reform programme with macro stability, I see the prospects as being extremely good. I think we should, in a couple of years, achieve growth rates which we know Pakistan is capable of, which is well over 5% and possibly over 6% per annum. We also think population growth, which has been coming down, should now begin to come down to below 2%. Social sectors which we are concentrating on should show better rates of literacy, better health cover, and we can then see a very quick social change and much more investment.

So I see the prospects as being very good - with one proviso - that we continue with the broad policy initiatives which this government undertook.

Finally, I think we plan to be and we hope to be out of a situation where we continue to rely on the International Monetary Fund. We have a very good relationship with them, and this is in no way meant to say that the relationship is not good in itself, but no country should really be relying continuously on fund assistance, and we think that the present fund programme should be the last one, and we are quite capable of really coming out of it. For instance, our reserves have historically been at levels of anything between 6 hundred million and 1.5 billion, now they are over 5.5 billion, and we hope they will be crossing the 6 billion mark before the end of this month, so the debt, both external and domestic, we are now gradually getting hold of. In fact external debt has reduced from \$38 billion to \$36 billion in the last two years, so I think the prospects are good, the private sector is vibrant, and a continuation of the reform programme should see Pakistan really making much, much more rapid progress than it's done in the last 20 years.

STOURTON:: And what about any particular kind of assistance you'd want from America and Europe?

AFZAL: Well from these states, from Europe and from the multi-lateral agencies, we basically want, over the next two years, continued assistance, concessional assistance in accordance with the requirements we've already indicated. That will see us through to a position where we don't need to rely on the fund in a continuous way.

However, we do need more trade access to the United States, and we will probably continue to rely on bi-lateral assistance and World Bank assistance over perhaps the next decade. But with the emphasis again on technical assistance - assistance for instance on how to tackle the problems of illiteracy, of dropouts at the primary and elementary school level, how to tackle our problems on the medical and health side. So we will need bi-lateral assistance, we will need multi-lateral assistance without the IMF in the next say, five to 10 years, and above all we'll continue to need a lot of investment, and trade access.

STOURTON:: And finally, what's your opinion about the link between economic difficulties in the region and the conditions that give rise to terrorism? And do you think America, in particular, has been ready to address these difficulties?

AFZAL: Yes, well I think actually, you know you asked me earlier about the fall-out of the Afghanistan situation on Pakistan, I think one of the things I didn't mention was the fact that this great pressure of the Afghan refugees and the fall-out of what's been happening in Afghanistan on Pakistan meant greater poverty, frankly. And there was also a failure of successive Pakistani governments to address its own problems - but the result was failure of the public sector and the private sector to provide adequate facilities for education and employment, and the result was of course a lot of this Madrassa culture coming up. Now Madrassa culture is, as you know, basically convents or schools that are found traditionally in Islamic countries. They were actually pioneers of education, but some of these facilities were misused by extremists to train and educate people

with a terrorist bent of mind, and as we all know, poverty, the failure to impart proper broad education and a lack of employment opportunities, can lead to a frame of mind which can be exploited by the extremists. So that certainly was a result of what happened in Afghanistan and Pakistan's own internal mismanagement over a couple of decades of its economy. Now we are addressing this issue broadly in Pakistan, but we are specially interested in some of the areas bordering Afghanistan, both on the frontier and Baluchistan; because these areas are among the poorest; they are tribal, which means they're not fully, politically, legally integrated into Pakistan, and these are areas where literacy levels are still abysmally low. Medical services, infrastructure doesn't exist, so here we have actually put together a programme which the US government and US authorities have shown a lot of interest in. We discussed it with Mr Wolvensen when he was here and the World Bank is willing to in a sense pilot it, put it together and market it, with prospective donors. I think there is interest in it, and that is one of the areas we'll be exploring.

STOURTON: Excellent, thank you so much.