Folder Title:	Pakistan - President Barber Conable Country Files - Correspondence
Folder ID:	1779836
Series:	Country files
Dates:	12/12/1984 - 04/30/1991
Subfonds:	Records of President Barber B. Conable
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ISAD Reference Code:	WB IBRD/IDA EXC-11-49S
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PAKISTAN - Conable

File / Pakistan

Country: PAKISTAN
April 29 @ 2:30 p.m.

Delegation: Mr. SARTAJ AZIZ, Minister of Finance
Mr. R.A. AKHUND, Secy., Econ. Affairs

BACKGROUND

- You met Mr. Aziz during the last Annual Meetings when he was Finance Minister under the caretaker government.
- New government, which took office in November 1990, moved quickly to adjust oil prices and reactivate adjustment effort with particular emphasis on accelerating industrial investment, deregulation and privatization and putting the financial sector reform back on track.
- Also tackled revenue-sharing and water allocation among provinces -- too long-standing and divisive issues.
- Serious delays, however, in tackling the fiscal situation which prevented reestablishing a satisfactory macro program that could be supported by the Bank and Fund.
- Bank pressure resulted in price increases in March for power, transport and natural gas as required under Energy Sector and Transport Investment Loans.
- Just completed IMF mission with Bank participation; believe agreement on PFP and third-year SAF is possible this summer, provided the government takes requisite steps (fiscal and monetary), and has a sound FY92 budget.
- Bank lending has averaged $700m annually over past several years. In FY91, Bank has committed $300m (3 operations) and plans to commit $380m more (6 operations) on the assumption that macroeconomic and structural adjustment program will be back on track.
- $200m Emergency Adjustment Loan (Gulf Assistance Program) has slipped to FY92 due to delays in government actions. However, we are making supplemental loans for $150m this fiscal year.

POINTS TO MAKE TO DELEGATION

1. Congratulate the Minister on the steps taken to speed up deregulation and privatization, settle long-standing inter-provincial issues and renew Pakistan's adjustment effort.

2. Stress the importance of establishing solid macroeconomic framework and reaching early agreement with the IMF. This requires fiscal and other demand-management measures. Underscore that Bank could not provide quick-disbursing support (including tranche releases), without sound macro framework and IMF agreement.

3. Long Term Development and Poverty Reduction should not be neglected. Bank believes Pakistan must accord much higher priority to social development. Have decided that future size of lending program and level of IDA allocation will depend upon progress achieved on this front, including better implementation performance on existing projects.

4. Express appreciation of Government's emphasis on greater self-reliance, but also note urgent need for increased development spending. Recent progress in solving water rights issues and new revenue-sharing agreements with the provinces will facilitate such investments.

THE WORLD BANK/IFC/MIGA
OFFICE MEMORANDUM

DATE: April 25, 1991

TO: Mr. Barber B. Conable

THROUGH: Mr. Moeen A. Qureshi, OPNSV

THROUGH: Mr. W. A. Wapenhans, EMNVP

FROM: Michael H. Wiehen, EM1DR

EXTENSION: 33000

SUBJECT: PAKISTAN - Your Meeting with the Minister of Finance

Background

1. You will be meeting with Mr. Sartaj Aziz, Minister of Finance, Economic Affairs, Planning and Development, of Pakistan, on Monday April 29, 1991. You previously met Minister Aziz during his visit to Washington for the 1990 Annual Meetings. At that time, he was Finance Minister under the caretaker Government, but has since been reappointed to the same post following the October 24 elections. The Minister has been attending the Asian Development Bank annual meetings in Vancouver, and is here in Washington to attend the Development Committee meeting. From Washington he will be proceeding to the Pakistan Consortium meeting which takes place in Paris on May 2 and 3. Minister Aziz is expected to be accompanied by Mr. R. A. Akhund, Secretary, Economic Affairs Department.

2. At the time the new Government took over in early November 1990, Pakistan faced increasingly serious fiscal and balance of payments difficulties stemming from slower than expected progress in carrying out its adjustment program, including slippage in meeting fiscal targets. These difficulties were exacerbated by the Gulf Crisis and delays in passing through the increase in international oil prices. Given the absence of a sound macro-economic program and insufficient progress in meeting key performance targets, no purchases were made under the IMF standby arrangement during 1990. The IMF therefore allowed the standby to lapse and delayed agreement on the third year of the SAF. At the same time, the lack of progress on macro-economic matters and delays in taking price and other policy actions required under the Bank's adjustment operations in the energy and financial sectors, resulted in our postponing release of second tranches for each of these operations.

Recent Developments

3. Upon taking office, the new Government moved quickly to adjust oil prices (increased by an average 41 percent in November), while also taking steps to reactivate the adjustment effort, with a particular emphasis on accelerating industrial investment,

deregulation and privatization (including, so far, virtual elimination of investment and import licensing, and sale of one nationalized bank) and putting the financial sector reform program back on track. In fact, the overall thrust of the Government's reform program suggests a substantial break with the traditional policy stance, reflecting the new Prime Minister's approach and background as a private industrialist. As part of this approach, several committees were established with private and public sector participation to address economic issues. The Government also reconvened two committees with Federal and Provincial representation to tackle longstanding and politically divisive issues concerning revenue sharing and water allocation. As a result, agreements have been reached on apportioning the Indus water between the provinces and establishing a revised framework for revenue sharing between the Federal Government and the provinces. Finally, the Government has been emphasizing the need for self-reliance, i.e. less dependence on external support.

4. In spite of these promising developments, for which the Government should be complemented, there were serious delays in tackling the fiscal situation. The November oil price increase was not immediately followed by required price increases for natural gas and power tariffs as mandated by the new oil prices (and by the Energy Sector Loan conditionality). Similarly, the railway tariff increase was also delayed. These delays further compromised an already weak fiscal situation, with an expected deficit above the PFP/SAF targets, low development spending, and with defense expenditures high at about 7 percent of GDP. Given the delays in further price increases and lack of other action on resource mobilization issues, no progress was made for several months in reestablishing a satisfactory macro program that could be supported by the IMF and the Bank.

5. An initial breakthrough came in late March when, partly as a result of strong Bank pressure, the Government raised power, transport and natural gas prices to levels adequate to meet requirements under the Energy Sector Loan and Transport Investment Loan. Since then, an IMF mission, with Bank participation, returned to Pakistan for further discussions with the Government on macro economic prospects, including the proposed FY92 budget, and to initiate work on a new PFP framework and the third year SAF. This mission has just completed its work. Its overall conclusions, as conveyed to us in summary form from the field, are positive, in that IMF and Bank staff believe that an agreement will be possible in the coming months, provided the Government: i) takes the recommended steps to strengthen the fiscal and monetary outcome for FY91, and ii) puts in place a sound FY92 budget. Another IMF/Bank mission would return to Pakistan in late June to review the outcome of the measures to be put in place during the remainder of FY91, assess the FY 92 budget, and finalize the PFP and third year SAF arrangement.

Bank Assistance

6. Over the past several years the Bank has provided substantial support to Pakistan (averaging US$700 million per year). During the current FY we have approved three operations to date (totaling about US$ 300 million) and plan to take six more to the Board, totaling close to US$380 additional. We have continued to provide this substantial level of support on the assumption that the macro-economic and structural adjustment program would be put back on track. Assuming that an IMF agreement is reached, we would be able to provide substantial additional balance of payments support in early FY92. This would include disbursement of the second tranches of the two sector loans (US$120 million) and the proposed US$200 million Emergency Adjustment Loan (EMAL) as part of the Gulf Crisis assistance program (which we have had to slip into FY92 due to delays in Government action). A proposed US$200 million Trade/Industry Sector Adjustment Loan is also planned for late FY92. We would hope to be able to take the EMAL to the Board by end August or early September, assuming early agreement is reached with the IMF and the Bank on the PFP and macro-economic framework for FY92. The loan amount of US$200 million would include SDR 60 million in IDA funding coming from the Gulf Assistance program and would also likely have Japanese co-financing, possibly at a similar level. In summary, a high level of fast disbursing resources are linked to reaching a satisfactory agreement with the IMF and the Bank on a macro-program.

Key Points

7. In your conversation, you should congratulate the Minister for the important steps which the Government has taken to speed up deregulation and privatization, settle long standing inter-provincial issues, and renew Pakistan's adjustment effort. These are most encouraging. However, there is much more to be done and you should stress the crucial importance of taking the fiscal and other demand management measures required to establish a solid macro-economic framework and reach an early agreement with the IMF. You should underscore the fact that without a sound macro framework and IMF support, the substantial quick disbursing assistance programmed for FY92, including the tranche releases, would not be possible. We expect that the Consortium, at the meeting next week, May 2 and 3, will also convey the same message, namely the importance of taking adequate fiscal measures and reaching agreement with the IMF.

8. Politically, the Government seems stronger now than three months ago (because the divisive impact of the Gulf war is over). Therefore more can now be done. The Government is proud of its initiatives and has been complaining of IMF/Bank insistence on 'old' quantitative targets and not enough attention to the new structural initiatives. However, getting the macro-balances right is a pre-condition and getting IMF endorsement will be crucial. The Government's emphasis on greater self-reliance is to be encouraged.

However, this goal will not be feasible without reestablishing and maintaining a sound macro-economic framework. Finally, the progress in solving water rights issues (which had blocked new hydro-power projects) and new revenue sharing arrangements with the provinces open the way for urgently needed increases in development spending that will require high levels of support from the Bank as well as the rest of the donor community.

cc: Mr. Hasan, EMNVP
EM1 Management Team
EM1CO Pakistan Team
Messrs: El Maaroufi, Wall (EM1PA)

GTPark

1) $620m or $700m?
2) Social sectors (Fam. Health)
3) [illegible]?

THE WORLD BANK/IFC/MIGA

OFFICE MEMORANDUM

Mr. Sandstrom

DATE: April 30, 1991

TO: Files

FROM: Michael H. Wiehen, Director, EM1

EXTENSION: 33000

SUBJECT: PAKISTAN: Meeting of Mr. Conable with Pakistan Finance Minister

1. On Monday, April 29, 1991, the Finance Minister of Pakistan, Mr. Sartaj Aziz, called on Mr. Conable. The Minister was accompanied by the Pakistan Ambassador to the United States, Mr. R. Akhund, the Secretary EAD, Mr. Arshad Farooq of the Pakistan Embassy, and Messrs. Al Sultan and Faruqi of the Executive Director's Office. Also present were Messrs. Sandstrom and Wiehen.

2. Mr.Conable welcomed the Minister. He said that the last time they had met the Minister was representing the Caretaker Government, and he welcomed him now as a member of the new Government.

3. Mr. Conable then explained that the Bank had decided some months ago that lending to Pakistan should be reduced to much lower levels unless the Government put a viable reform and stabilization program in place. He said that the lending levels envisaged for the current fiscal year (about $680 million) were being processed on the assumption that Pakistan would come to terms with the IMF and the Bank shortly, and that the third year SAF/PFP program would be agreed in the very near future. He stressed in particular the need for Pakistan to enforce strict budget discipline and to do much more than in the past both on the revenue and expenditure side. He added that the Bank and the Fund were agreed in their assessment of the current situation, and the measures that needed to be taken, and he expressed his strong hope that the Government of Pakistan would take the necessary measures forthwith. He said that the Emergency Adjustment Loan, even though the Emergency had almost disappeared, was now being processed for conclusion sometime later this summer; that it had been delayed considerably by delays in price adjustments by the Government; and that the Bank was prepared to process other adjustment operations after EMAL provided the necessary stabilization decisions were taken by the Government and the stabilization actually takes place.

4. The Minister thanked Mr. Conable for receiving him and his delegation. He said the Fund had written a very good and positive report on Pakistan's performance during FY91 (in fact, that report was more favorable than the Bank's Economic Memorandum); the budget deficit in FY91 was now likely to be about 5.8% (as compared to the target of 5.5%); that the Fund mission would return to Pakistan in late June to review the outcome of FY91 and to review the budget for

FY92; and that a report to the Fund's Board would be completed in July. Indeed, he said the outline of the program for FY92 had been agreed with the Fund/Bank mission. He added: "We are back in business with the IMF".

5. As to the measures to be taken by Pakistan, the Minister explained that the Government had stopped recruitment of new staff throughout the Government as of now, but other than that, no other measures, especially revenue measures, could be taken now, just six weeks before the new budget for FY92; that all the necessary revenue measures would be in the new budget, which would be proposed in early May and finalized by the Parliament before the end of June. As to the specific measures to be taken in the FY92 budget, the Minister mentioned specifically structural changes in the tax system which were most important but unfortunately would have a somewhat delayed effect on the tax take. He explained that the drain on the budget had been started in the '70s, with the nationalization programs, and that it was very difficult to disentangle those measures now, but that the Government was determined to carry through their program of disinvestment and privatization. He said Pakistan would soon be a "semi-open economy". He concluded his explanation by saying that the present growth rate, good as it was, was clearly not enough to finance their needs, and that a higher growth had to be achieved.

6. In response to Mr. Conable's question "what next?", the Minister explained briefly the Government's strategy, especially in the social sectors, where the social indicators of Pakistan had fallen far behind those of comparable countries. Mr. Conable expressed his surprise that the Bank's lending program this year contained "only one project in the social sectors - namely the Family Health Project". Mr. Wiehen explained that in fact the Bank was supporting this year alone three innovative projects in the social sectors - Family Health, Rural Water Supply and Microenterprise. Mr. Conable added that the level of IDA funds the Bank could make available to Pakistan depended largely on the quality of the social sector activities of the Government. The Minister assured Mr. Conable that there would be plenty of opportunities for the Bank to spend large sums of IDA on such projects in the future. He used this opportunity to report to Mr. Conable on the recent award of the National Finance Commission.

7. Mr. Wiehen explained what the Bank was planning to do in the social sectors as well as in the environment field.

8. The Minister then also told Mr. Conable about the recent historic agreement on the sharing of the Indus waters and added that this new situation would allow and indeed call for massive new investments in the water sector, and he asked for the Bank's help in identifying and resolving all the issues related to this, institutional, technical, federal-provincial, etc. He said very much support was needed from the Bank, both financial and technical assistance.

9. In conclusion, the Minister noted the fact that Mr. Conable was about to retire from the Presidency of the Bank, and he expressed his and his country's gratitude for all the support the Bank, under Mr. Conable's stewardship, had given to Pakistan. Mr. Conable thanked the Minister for his sentiments and assured him that his successor, Mr. Preston, would certainly take a keen interest in the relationship with Pakistan.

cc: Messrs. Qureshi
Wapenhans (o/r)
Chopra (Acting RVP)
Sandstrom
P. Hasan
El Maaroufi
EM1 Management Team

MW/ec

THE WORLD BANK/IFC/MIGA
OFFICE MEMORANDUM

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DATE: November 29, 1990

TO: Files

FROM: Michael H. Wiehen, Director, EM1 MHW.

EXTENSION: 33000

SUBJECT: Meeting of Mr. Barber B. Conable with the new Ambassador of Pakistan

1. On Wednesday, November 28, 1990, Mr. Najmuddin M. Shaikh, the new Ambassador of Pakistan, called on Mr. Conable. The Ambassador was accompanied by Messrs. Hosny, Executive Director, Farooqui, Advisor to the Executive Director, and Farooq, recently appointed Economic Minister at the Pakistan Embassy, previously Advisor to the Executive Director. Messrs. A. Khanna and Wiehen were also present.

2. Mr. Conable welcomed the Ambassador; he said he was looking forward to working with the new Government; and that he was confident that Pakistan, under the wise guidance of President Ghulam Ishaq Khan, would quickly address its economic problems. The Ambassador explained that the new Government had a solid majority and would be able to take decisive action, as was needed.

3. He then commented on, and expressed his country's gratitude for, the good relations between Pakistan and the Bank. Mr. Conable said that quite clearly a number of very tough economic decisions were needed. He referred to the forthcoming visit of Mr. Qureshi to Pakistan and expressed his hope that a major program of actions would be discussed and quickly agreed and implemented. The Ambassador cited the decisions already taken (fuel price pass through, the General Sales Tax, the capping of tariffs at 95%) and commented that the public had taken those decisions remarkably well.

4. Mr. Conable then said that it was extremely important that Pakistan quickly agree on a new program with the IMF. He explained that the Bank of course was independent and would make its own decisions, but that Pakistan clearly needed access to the resources of both institutions. The Ambassador replied that a joint IMF/Bank mission was just starting in the field, and expressed his hope that the mission's work would lead to quick assistance by the Bank. He explained that the Gulf crisis had made it impossible to meet the objectives of the previous IMF program, in particular the budget deficit reduction, that oil prices were now much higher, that remittances were down, and that reabsorbing all the returnees had added substantial costs. Mr. Conable replied that the Bank was flexible in its response to problems caused by the Gulf crisis but that we needed a good program of economic measures before we could provide significant assistance. He acknowledged the particularly difficult position of Pakistan and promised that the Bank would be "accommodative" but said again that a good economic program was absolutely needed. The Ambassador requested specifically that the Bank consider making the Emergency Adjustment

operation (EMAL) available without conditionality, in response to the crisis, and allow speedy disbursement, but Mr. Conable replied that all depended on the quality of the government's own measures. He referred in this context, in addition to the EMAL, to our efforts to agree on higher cost sharing ratios, acceleration of project implementation and disbursements, and to an acceleration of the projects presently being prepared for Board presentation. Mr. Conable added that the Gulf crisis shocks were no reason to abandon the long-term development plans, even though some countries - and Pakistan probably among them - were close to the margin even before the oil crisis.

5. In closing, Mr. Conable said that in the past the Ambassador of Pakistan had been an effective and active channel between the Bank and the Government of Pakistan, and he expressed his hope that that would remain the case in future.

cc: Mr. Barber B. Conable
Mr. Moeen A. Qureshi
Mr. W.A. Wapenhans
Mr. Abdallah El Maaroufi, RMP
EM1 Management Team

MHWiehen:ec

THE WORLD BANK
Washington, D.C. 20433
U.S.A.

BARBER B. CONABLE
President

December 3, 1990

His Excellency
Sartaj Aziz
Minister of Finance, Planning
and Economic Affairs
Government of Pakistan
Islamabad

Dear Mr. Minister:

I would like to take this opportunity to extend my congratulations on your appointment as Minister of Finance, and to acknowledge your letter of November 15, 1990.

We were pleased to learn of the new Government's strong commitment to reestablish a viable macro-economic framework and to continue with the structural reforms initiated over the past few years, including moving ahead with the reforms being supported by the Bank's sector adjustment lending. Accelerating the adjustment process is clearly a high priority and we look forward to working closely with the Government in these matters.

With respect to Bank assistance in reacting to the impact of the Gulf crisis, we are planning a mission for the second week of December to expedite preparation of the proposed Emergency Adjustment Operation. I trust that the Government will be able to move quickly to take the macro-economic policy and adjustment measures needed to enable the Bank to accelerate processing of this operation. We are also continuing our review of projects that could possibly benefit from increased cost sharing.

As you know, Mr. Moeen Qureshi will be visiting Pakistan next week and I trust that he will discuss with you and other senior officials both the Government's plans for addressing macro-economic issues and the Bank's potential help to Pakistan in this process.

Sincerely,
(Signed) Barber B. Conable
Barber B. Conable

Cleared with and cc: Mr. Qureshi
Mr. Wapenhans
Mr. Wiehen

GTPark

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MINISTER

MINISTER FOR FINANCE, PLANNING AND ECONOMIC AFFAIRS GOVERNMENT OF PAKISTAN

D.O.No. 0710-FM/90

Islamabad, the 15th Nov.1990

Dear Mr. Conable,

Thank you very much for your letter of 12th October in which you indicated the Bank's likely response to the adverse impact on Pakistan of the Gulf crisis.

2. Since I met you last in September, at the time of the Annual Meetings, general elections have been held in Pakistan. A new government is now in place. This government is not only fully committed to the programme of restructuring the economy in Pakistan in accordance with the policy objectives worked out with the Bank and the Fund in the PFP but to go beyond that in order to achieve a fully industrialised viable economy during its tenure. We, therefore, hope to work with you in defining new medium term structural reform benchmarks to achieve these objectives during the life of this government. Indeed, we realise that re-enforced policy initiatives will be essential to cope with changing economic environment created by the Gulf crisis. These would be required also to conform to the new government's commitment to accelerate the pace of growth within a viable macro-economic framework, in particular a viable external payments position supported by rapid growth of export-oriented industry.

3. The new government, as the Bank fully appreciates, faces a number of difficult challenges. It expects to move swiftly to meet those. The new general sales tax has already been put in place. Exchange rate flexibility is being maintained in order to keep our exports competitive. Consequently, exports during the first four months of the current fiscal year have registered a growth of 24%. We have raised petroleum prices by 42% and consequential price adjustments are now being processed. Having made these adjustments we intend to move on and address the problem of the budget deficit effectively. On trade policy we will continue to follow a policy of liberalisation and fulfill our commitments. We have already initiated the process of extensive deregulation to create a liberal environment to facilitate rapid industrialisation and flow of foreign investments. On both those counts the new government expects to make important decisions in the coming weeks. We intend also to explore avenues of resource mobilisation and to contain public sector expenditure

through disinvestment and privatisation.

4. In responding to the three proposals contained in your letter of 12th October, I would like to indicate how the government expects to move. First, work has been initiated on putting together a project which will focus on income generation, shelter and employment opportunities for returning workers from the Gulf. We will be prepared to discuss different aspects of this project with your mission in early December. Second, we are analysing the preliminary ideas contained in Mr. Wiehen's detailed letter of 17th October regarding a fast disbursing loan. Our anxiety is that such a project, if it is to serve the purpose for which it is being put together, should fully disburse within the current fiscal year. Accordingly, I would request you to send your appraisal mission for this project to Islamabad as early as possible. We are ready to discuss all its aspects. Finally, we are at present revising the Bank's portfolio of ongoing projects with a view to considering the possibility of increasing disbursement as well as the Bank's cost sharing ratios. We expect to be in touch with your Resident Mission here in this regard.

5. The new government intends also to move ahead with important policy decisions involving the Bank's policy adjustment lending. In particular we expect to take some important decisions regarding the financial sector loan, which we consider fundamental to reforms in the banking and fiscal sector envisaged by the present government.

6. Pakistan has had a long and fruitful relationship with the Bank. The new government hopes that this will continue to flourish in the years to come.

With regards,

Yours sincerely,

Sartaj Aziz.

(SARTAJ AZIZ)

Mr. Barber B. Conable,
President,
The World Bank,
Headquarters: Washington D.C.
USA.

THE WORLD BANK/IFC/MIGA

OFFICE MEMORANDUM

Mr Conable:

Barber: I would appreciate your indicating the following to the Ambassador
(1) While you are sympathetic to Pakistan's current situation, it is clear that Pakistan needs to take some determined steps to strengthen its fiscal and b.o.p. situation, and reach early agreement with the IMF.
(2) You expect to get a report from me following my discussions with the new Pakistani ~~[illegible]~~ Government on what steps the Govt proposes to take.
(3) You will review the situation after my return regarding the scale and timing of Bank support.
Moeen 11/20

DATE: November 20, 1990

TO: **Mr. Barber B. Conable**, President

THROUGH: Mr. Moeen A. Qureshi, SVPOP MAQ
Mr. W. A. Wapenhans, EMNVP

FROM: Michael H. Wiehen, Director, EM1 HW

EXTENSION: 33000

SUBJECT: **Meeting with the New Ambassador of Pakistan**

11:45 am

1. You will be meeting with the recently appointed Ambassador of Pakistan, Mr. Najmuddin M. Shaikh, on November 28. The Ambassador met previously with Mr. Wapenhans and Mr. Wiehen in early November for a more detailed briefing on the Bank's program in Pakistan. The Ambassador's principal interest in those meetings was to discuss the Bank's response to the Gulf crisis. We expect that in his meeting with you, the Ambassador will once again stress Pakistan's need for urgent assistance. The Finance Minister's letter to you dated November 15 (in response to your letter of October 12 regarding possible Bank actions to address the Gulf crisis), expresses the new Government's commitment to rapidly tackle macro-economic and adjustment issues, while also stressing the need to move quickly to alleviate the impact of the Gulf crisis.

Background

2. Over the past year Pakistan experienced increasing internal political difficulties and growing ethnic violence, leading to the dismissal of Prime Minister Benazir Bhutto and her cabinet in early August, the appointment of an interim caretaker government, and elections on October 24, 1990. The elections resulted in a major victory for the Islamic Democratic Alliance over the Pakistan People's Party, headed by the former prime minister. A new government, headed by Prime Minister Nawaz Sharif, took office on November 9, with the Finance Minister under the caretaker government, Mr. Sartaj Aziz, retaining his post.

3. Even before the Gulf crisis, although overall economic performance in FY 90 has been satisfactory, with real GDP growing at about 5 percent and inflation contained at 6 percent (but rising), Pakistan faced increasingly serious fiscal and balance of payments difficulties. At the same time, progress in carrying out structural reforms agreed with the Bank and the IMF under the PFP/SAF framework was much slower than expected. The Government has also been unable to meet some of the performance targets under its standby program with the IMF, which was allowed to lapse. The Gulf crisis has exacerbated Pakistan's economic difficulties, particularly on the external side.

Assuming an average price of oil of $29 per barrel, petroleum imports would increase by $660 million in FY90/91. In addition, workers' remittances are expected to decline by about $200 million in FY90/91.

4. Since taking office, the new Government has raised petroleum prices by about 40 percent and has announced its intention to take other macro-economic actions. An IMF/ Bank mission to discuss, and hopefully reach agreement on, the third year PFP/SAF program will be in Pakistan beginning in late November. We are hopeful, therefore, that the Government will expedite efforts to address Pakistan's macro-economic difficulties, while accelerating efforts to carry through with the structural adjustment process already underway. At the same time, the Government must expedite efforts to tackle its underlying development issues, especially the need to give much higher priority to the social sectors and the need to continue developing basic infrastructure.

Talking Points

5. You should stress the importance of early actions by the new Government to address Pakistan's balance of payments and fiscal difficulties, including agreement on revised PFP/SAF targets, since this will be key to obtaining additional balance of payments support from the Bank and other donors. Satisfactory progress on macro-economic issues as well as accelerated efforts to put in place previously agreed structural reforms in energy and the financial sectors, would also enable the Bank to proceed with disbursement of the second tranches of the Energy Adjustment and Financial Adjustment operations. In this context, the Finance Minister's letter indicating the new Government's intention to proceed rapidly to tackle key economic issues is most welcome, and we look forward to continuing to work closely with the new administration.

6. With respect to the Gulf crisis, your letter of October 12 to Finance Minister Aziz outlined a number of possible actions. Perhaps the most important is an Emergency Adjustment Operation for $250 million (including $60 IDA). On the assumption that agreement is reached quickly to put the Government's macro-economic program back on track, including appropriate revenue measures, we would be able to complete the appraisal of the emergency operation by early 1991 and take it to the Board before the end of FY91. In addition to the emergency adjustment operation, the Bank is also reviewing steps that could be taken to accelerate disbursements of on-going investment projects. As noted in the Finance Minister's November 15 letter, we look forward to early discussions with the new Government in both of these areas.

7. Although macro-economic issues are clearly very high on the new Government's agenda (and rightly so), you may also want to underscore the Bank's concern that the Government give equally high priority to tackling medium term development issues. In this context, you may want to stress the importance the Bank attaches to the Government's formulation and implementation of a longer term development

strategy which emphasizes the social sectors, especially expanding primary health care, including family planning, and basic education. The Bank is willing to increase IDA lending to Pakistan by $50 million to $250 million per annum for the next three years, provided the Government gives higher priority to the social sectors. The Bank is going ahead, at the Government's request, with preparation of a social sector action plan to assist the Government's efforts in this area.

8. The Bank's FY91 program for Pakistan includes 7 projects for a total of $745 million (of which $250 million is IDA). In addition to the proposed Emergency Adjustment Operation, these include: Corporate Restructuring of the gas pipeline utility (already approved by the Board); Scarp Transition II (salinity control and reclamation in agricultural production areas); Rural Water Supply and Sanitation; On-Farm Water Management; Micro-Enterprises; and Domestic Energy Resources Improvement project.

GTPark

The World Bank/IFC/MIGA
O F F I C E   M E M O R A N D U M

DATE: 26-Nov-1990 03:09pm

TO: Sven Sandstrom (SVEN SANDSTROM)

FROM: June Nemeyer, EXC (JUNE NEMEYER)

EXT.: 81146

SUBJECT: MAQ Note re Meeting with New Amb. of Pakistan

As requested, here is MAQ's note to BBC:

"I would appreciate your indicating the following to the Ambassador:

(1) While you are sympathetic to Pakistan's current situation, it is clear that Pakistan needs to take some determined steps to strengthen its fiscal and b.o.p. situation, and reach early agreement with the IMF.

(2) You expect to get a report from me following my discussions with the new Pakistani Government on what steps the Government proposes to take.

(3) You will **review the situation after** my **return** regarding the scale and timing of Bank support."

THE WORLD BANK
Washington, D.C. 20433
U.S.A.

BARBER B. CONABLE
President

October 12, 1990

His Excellency
Sartaj Aziz
Minister for Finance, Planning
and Economic Affairs
Government of Pakistan
Islamabad

Dear Mr. Minister:

Thank you for your letter of September 13, 1990 in which you requested the Bank's assistance in addressing the adverse impact of the Gulf crisis. During the recent Annual Meetings we had the opportunity to discuss with you the problems which Pakistan is facing, the Government's intentions and policy response, and the possibilities of Bank support. We recognize that the Gulf crisis has placed a significant additional burden on the Government both in terms of the need to re-absorb large numbers of migrant workers and the balance of payments impact of higher oil prices and reduced workers' remittances. We are prepared to take the following steps to assist Pakistan in addressing these issues.

Firstly, we propose to start preparation of a project for alleviating the problems resulting from the arrival of repatriated workers. As suggested during the Annual Meetings discussions, this project could focus on income generation, shelter and employment opportunities. The target group of such a project could extend beyond the returning workers.

Secondly, we are reviewing the project portfolio with a view to identifying projects where disbursements of Bank/IDA funds could be accelerated. Of course, increasing the cost sharing ratios will have a significant impact only if the Government effectively addresses the implementation problems which have slowed down disbursements on virtually all Bank-financed projects.

Thirdly, as regards quick disbursing assistance, we have begun to design an emergency operation which would support a policy package to address the objectives of reducing the country's vulnerability to external shocks and improving the efficiency of domestic resource allocation. Such an operation will require a viable macroeconomic framework, in line with the policy objectives and targets defined in the existing Policy Framework Paper. It would, of course, be most helpful if this were done by reaching an agreement with the International Monetary Fund about a new program. Bank staff is already at work and has exchanged views with your staff on the elements of such a policy package that we believe are necessary to ensure a balanced response to the present terms-of-trade shock. A crucial element of the policy package would be, in our view, to protect the development expenditures, and I would like to stress again the importance of the social sectors in this context.

I hope that through these proposals, the Bank will be able to contribute to the re-establishment of a sound and sustained growth process in Pakistan.

Sincerely,

Barber Conable

Barber B. Conable
President

The World Bank
Washington, D.C. 20433
U.S.A.

File

MOEEN A. QURESHI
Senior Vice President, Operations

October 12, 1990

Mr. Wiehen

Re: Pakistan CSP

Mr. Conable's note on Pakistan should not be interpreted to mean that we are required to cut the Operations program at this time. Elections are to be held on the 24th of October. After that we will know whether the new government is prepared to pursue an adjustment program with the Bank and Fund. On the basis of conversations with Mr. Aziz, I have every expectation that if the existing caretaker government is reelected, they will be prepared to adhere to the adjustment program. If, on the other hand, Ms. Bhutto's party gets elected, they can be expected, based on earlier conversations, to also implement the program. There is, therefore, no action needed at this time. We should review the matter in eight weeks. I have discussed this issue with Mr. Conable.

MAQ

cc: Messrs. Wapenhans, Sandstrom, Bock, Grilli

Revised
Senior Management Brief

1990 ANNUAL MEETINGS BRIEF

Name of Country: PAKISTAN   Date: September **19**, 1990

Meeting with: Mr. Sartaj Aziz, Minister for Finance, Economic Affairs, Planning and Development and Governor of the World Bank
Mr. I.A. Hanfi, Governor, State Bank of Pakistan
Mr. Saeed A. Qureshi, Secretary, Finance
Mr. Qazi M. Alimullah, Additional Finance Secretary (Development Finance Division)

Population: 110m (mid-1989)   Estimated Growth Rate: 3.1% (65-89)
GNP per capita: $365 (1989)

		($m)		($m)
Total Commitments to date:		7,171.20	FY90 Commitments:	825.80
Bank (no. of operations and value)	73	4,020.89	Disbursements:	535.26
IDA (no. of operations and value)	111	3,150.41	Amortization:	63.55
Total Undisbursed:		3,117.84/a	Net Disbursements:	471.71
Lending Program: FY91-92		1,401.20		

Summary Data	Average FY85-89	FY90
GDP Growth %	6.2	4.9
Export Growth /b	13.1	5.3
Import Growth /b	2.6	0.0
Current Account Deficit (% GNP)	4.0	4.0
Gross Debt Service Ratio	25.6	25.8
Annual Inflation Rate (average)	6.0	6.0

Aid Group Meeting: Consortium
Last Meeting: April 17-18, 1990
Last Article IV Consultation: September 1990
Next IMF Visit: N.S.

/a Includes FY90 commitments that are not yet effective.
/b Goods and non-factor services in constant Pakistan Rupees.

Part I: Background

Bank lending to Pakistan has increased substantially over the last few years and is coming close to the exposure thresholds. Pakistan's social indicators remain dismal and underscore the need for Government action in the social sectors which we will request and support. Bank strategy, as approved by the Operations Committee in July 1990, supports a stronger focus on longer-term development issues, in particular human resources, basic services and productivity increases. Support for the PFP/SAF adjustment is a necessary condition for base case lending of $700 million per year. Within that Bank/IDA ceiling, the IDA share could go up from $200 to $250 million a year, for the next three years, provided the Government gives higher priority to the social sectors, by redefining its strategy for social development and improving performance. You may want to repeat the Bank's request that the Government prepare a social development action plan and express our willingness to help with it.

The caretaker government that was appointed in August 1990, has not taken any action to put the macroeconomic program back on track or to address the impact of the Gulf crisis. While overall economic performance in FY90 appears satisfactory with real GDP growing at 5% and inflation contained at 6%, there are serious slippages in the implementation of macroeconomic and structural reforms. In particular, the budget deficit which was reduced from 7.3% of GDP in FY89 to 6.6% of GDP in FY90, fell short of the 6.3% target, owing mainly to an overrun in defense spending. The budget deficit for FY91, which already exceeds the SAF/PFP targets, would increase by another 1.3% of GDP, if the increase in international oil prices is not fully passed on to consumers. The impact of the Middle East crisis (higher oil prices and lower remittances) would also increase the external current account deficit by $750 million or more in FY91. In view of the breach of two end-June performance criteria, slippages in the implementation of the program and the Government's unwillingness to take adequate corrective measures, the IMF staff will recommend to let the current standby lapse and to postpone the third-year SAF, possibly to FY92. Thus, the basis for additional fast-disbursing adjustment lending or even for releasing the second tranches of ongoing sector adjustment operations (ESAL and FSAL) does not exist.

In a letter addressed to Mr. Conable, the Minister of Finance has requested emergency assistance from the Bank, and the Government has approached most of the other donors as well. A return to a satisfactory macroeconomic performance by the caretaker government would allow us to react with quick-disbursing assistance; in the absence of a macroeconomic program, we propose to accelerate disbursements under existing project loans and to prepare an income/employment generation project. You could also offer Government our assistance through calling an early meeting of the Pakistan Consortium to mobilize and coordinate resources.

Part II: Issues Likely to be Raised by the Delegation

1. Request for Emergency Assistance

Part III: Issues to be Raised by Senior Management

1. The Government's Development Strategy

Attachment: Biographical Information
FY90-95 Lending Program

Senior Management Brief
Country: Pakistan
September 19, 1990

1990 Annual Meetings
Briefing Paper

I. Background

A. Political Developments

1. Pakistan went through substantial political difficulties in the past year which led to a change of government in August 1990. Since coming to office in December 1988, the Government of Prime Minister Benazir Bhutto had experienced problems. It barely survived an end-1989 motion of no-confidence as some of its parliamentary alliances unraveled. Meanwhile, the conflicts between the federal government and two of the provincial governments became more bitter, with Punjab, which accounts for 60% of population, being controlled by the opposition. Maintenance of law and order deteriorated as long-standing ethnic rivalries intensified and violence increased seriously in Karachi and rural Sindh.

2. On August 6, 1990, the President of Pakistan dismissed Prime Minister Bhutto and her Cabinet on charges of corruption, nepotism, and misuse of power. Ghulam Mustafa Jatoi, leader of the opposition, was appointed Prime Minister of an interim government until the next general election, announced for October 24, 1990. The President also declared a state of emergency, which remains in effect. Charges of abuse of power have been filed against Ms. Bhutto, and the President has set up special courts with power to disqualify her and PPP leaders from participating in the October elections and from public office for seven years.

3. After assuming office, the interim government indicated that the change in government did not imply a shift in economic policy. It requested the Bank to send missions to Pakistan as scheduled, and the Fund was asked to proceed with its standby program review and SAF/PFP mission as foreseen. The latter mission visited Pakistan (with Bank participation) in early September and concluded that the SBA program was off-track and that the interim government was not able to agree to take corrective measures at this time. As a result the SBA arrangement will lapse and the third-year SAF will not be made available to Pakistan for the time being.

B. Economic Performance

4. Overall economic performance in FY90 appears satisfactory with real GDP growing at about 5% and inflation, as measured by the CPI, contained at 6%. There are some indications, however, that GDP growth will have to be revised downwards and that inflation has accelerated in the second half of FY90 resulting in a 10% increase over the 12-month period ending July 1990, due to an expansionary domestic credit policy. The fiscal deficit was reduced from 7.3% of GDP in FY89 to 6.6% of GDP in FY90, but fell short of the target of 6.3% of GDP. While revenue and development expenditure were roughly on

target, the expenditure overrun is the result of higher defense spending. The external current account deficit declined from 4.6% of GNP in FY89 to 4% of GNP in FY90; exports, imports, and workers' remittances were at targeted levels. The accumulation of reserves was less than targeted and remained at a low 3.8 weeks of imports at end-June 1990.

5. The recent IMF/Bank mission found that little progress has been made in the area of structural reforms. Legislation for the general sales tax has been introduced, but its implementation has been delayed until October or November 1990. Substantial questions remain about the coverage and form of the tax. While there has been progress in some areas, financial sector reform is running behind schedule. The introduction of an auction system for government securities is still several months away; the authority of the State Bank of Pakistan to regulate non-bank financial intermediaries has not yet been implemented; and, while the Bhutto Government had declared its intention, in principle, to fully privatize two commercial banks, this decision is being held in abeyance by the caretaker government. In trade policy, the Government reduced non-tariff barriers and maximum tariff rates, but not to the extent agreed under the program. Industrial policy reform also proceeded at a slow pace with marginal deregulation of industrial investment, an increase in major administered prices, and an increase of most concessional interest rates to positive levels.

6. The Gulf crisis is weakening Pakistan's balance of payments position and could create a financing gap for at least two years. The recent IMF/Bank mission estimated that, on the basis of an oil price of $24/barrel for FY91 and no adjustment in domestic energy prices, the current account deficit would rise to 4.6% of GNP compared to a program target of 3.2% of GNP. Petroleum imports would increase by $550 million, while workers' remittances would decline by $200 million. The balance of payments gap would amount to $600 million without any reserve buildup. The increase in international oil prices would add 1.3% of GDP to the budget deficit which already exceeded the SAF/PFP target of 5.5% of GDP by 0.7% before the crisis. Energy price increases of 41% would be needed to reduce the deficit to about the program level.

7. Under these circumstances, the IMF staff will recommend that the Government not be allowed to make the final purchases under the SBA before it expires on November 30, 1990. An IMF mission had visited Pakistan in May 1990 to review progress on the SBA and assess the status of the SAF/PFP program. The Fund did not complete its review mainly owing to the uncertainties about the fiscal outcome for FY90 and the impact of policy changes taken or about to be taken in the FY91 budget. The IMF Board granted an extension of the standby agreement from end-June to end-November 1990. The IMF mission which visited Pakistan in September 1990, will recommend to let the current standby lapse since two of the performance criteria for June (credit) were not met and since there have been slippages in the implementation of the program. They also recommend to proceed with a shadow program or have no program at all for FY91, and to prepare the third-year PFP and SAF program for FY92.

II. Issues Likely to be Raised by the Delegation

(1) Request for Emergency Assistance

8. In addition to their letter to Mr. Conable requesting increased Bank assistance, the Government has approached the donor community with a request for emergency assistance. The Government estimates that it would need $1.1 billion to support the balance of payments and finance the evacuation of Pakistanis from Kuwait and Iraq. Requests have been made to Japan, the United States ($500 million each), the United Kingdom, Canada, Switzerland ($300 million each), Germany, France ($250 million each), Italy, Netherlands ($200 million each), Sweden ($150 million) and Norway (amount unspecified). The letter addressed to Mr. Conable makes the following proposals for Bank assistance: increase the quick-disbursing component of the Energy Sector Loan, include such a component in the Transport Sector Loan and increase the amount of the proposed Industry and Trade Adjustment Loan by $100 million to $300 million, provide emergency assistance of $250 million, and help with the resettlement of Pakistanis from Kuwait and Iraq.

9. We expect the delegation to bring up the need for balance of payments support to face the impact of the Gulf crisis. <u>You may want to express the general willingness of the Bank to help, and to remind the delegation that maintaining a high level of Bank assistance would require an adequate macroeconomic adjustment and structural reform program, agreed with the Bank and the Fund. In particular, early action is needed to increase petroleum product prices to fully reflect the international price increases</u> and, thus, mitigate the impact of the Gulf crisis. The Government would also need to take policy actions in the fiscal area and in financial sector reforms to put the macro-program back on track. In response to Mr. Aziz' letter, <u>you may want to mention that</u>:

- <u>in the absence of a macroeconomic program, we would not be able to provide quick-disbursing assistance through new operations or through increased amounts for these components in ongoing operations. We would not be able to release the second tranches of the ESAL and the FSAL, even if all sectoral conditions are met</u>;

- we are looking into the possibility to accelerate disbursements under existing projects and to advance preparation of new projects;

- <u>we are also thinking about special emergency assistance through an income/employment generation project</u> which could be modeled on the Afghan refugees project;

- <u>we would be prepared to call an early meeting of the Pakistan Consortium to mobilize resources and coordinate aid flows</u>.

III. Issues to be Raised by Senior Management

(1) The Government's Development Strategy

10. You may wish to inform the delegation that we attach great importance to the Government's formulation and implementation of a longer-term development strategy which emphasizes increased attention to the social sectors. The Bank would be willing to increase IDA lending to Pakistan by $50 million to $250 million per annum for the next three years, provided the Government gives a higher priority to the social sectors. This would require that the Government formulate a social development action plan, which we are willing to help prepare, and that performance in the social sectors improve through increased recurrent and investment expenditures. In addition, the size of the overall Bank lending program would depend on the Government's implementation of a sound development strategy.

PAKISTAN

Biographical Information

Mr. Sartaj Aziz

Federal Minister for Finance, Economic Affairs
and Planning & Development
(and Governor of the World Bank)

Mr. Sartaj Aziz was born in February 7, 1929. After obtaining a Degree in Commerce from the Punjab University, he proceeded to Harvard University (USA) where he earned a Master's Degree in Public Administration (Economic Development). He joined Government service in 1950 and started his international career in 1969 with important posts in FAO and IFAD. Mr. Sartaj Aziz returned to Pakistan in 1984 and was entrusted with the portfolio of Food, Agriculture and Cooperatives in the Federal Cabinet as Minister of State. He was taken as Minister in the Federal Cabinet on June 9, 1988 with the portfolio of Food, Agriculture and Cooperatives and served until December 1988. Since then, Mr. Aziz has been a senator and, in August 1990, was appointed Minister for Finance, Economic Affairs, Planning and Development in the caretaker government.

Other Members of the Delegation

1. Mr. R.A. Akhund
   Secretary, Economic Affairs Division

2. Mr. I.A. Hanfi
   Governor, State Bank of Pakistan

3. Mr. Saeed A. Qureshi
   Secretary, Finance

4. Mr. Qazi M. Alimullah
   Additional Finance Secretary
   Development Finance Division

5. Mr. M. Ashraf Janjua
   Economic Advisor
   State Bank of Pakistan

September 18, 1990

PAKISTAN

FY90-95 Lending Program

(In $ Million)

Sector	Actual FY90	Projected FY91	FY92	FY93	FY94	FY95	Total
Agriculture							
Agriculture Research II	57.3						57.3
Agriculture Credit	150.0						150.0
SCARP Transit II		20.3					20.3
On Farm Water Mgt. III		80.6					80.6
Agric. Sector Environment (S)			50.9				50.9
Punjab Salinity Drainage			75.0				75.0
Integrated Hill Farming				81.3			81.3
Baluchistan Irrigation (S)					50.9		50.9
On-Farm Water Mgt IV					70.0		70.0
Command Water Mgt. II (S)						70.0	70.0
Irrigation System Rehab III						70.0	70.0
Sub-Total	207.3	100.9	125.9	81.3	120.9	140.0	776.3
Industry							
Micro-Enterprises		79.0					79.0
Industry & Trade Adjustment (S)			200.0				200.0
FSAL II/IIC IV				200.0			200.0
Telecoms				100.0			100.0
ISIL					100.0		100.0
Financial Sector Investment						100.0	100.0
Sub-Total	0.0	79.0	200.0	300.0	100.0	100.0	779.0
Infrastructure							
Transport Sector	184.0						184.0
Rural Water		134.8					134.8
Karachi Port Moderniz.		70.0					70.0
Sindh Urban Development			100.9				100.9
Shelter (S)				71.3			71.3
Punjab Urban Environment (S)					102.6		102.6
Highways V					65.0		65.0
Transport						125.0	125.0
Provincial Administration (S)						35.0	35.0
Sub-Total	184.0	204.8	100.9	71.3	167.6	160.0	888.6

PAKISTAN

FY90-95 Lending Program

(In $ Million)

Sector	Actual FY90	Projected FY91	FY92	FY93	FY94	FY95	Total
Population & Human Resources							
Sindh Primary Education	112.5						112.5
Family Health (S)			30.5				30.5
Basic Education			76.2				76.2
Education				56.0			56.0
Health					101.6		101.6
Education						100.0	100.0
Sub-Total	112.5	0.0	106.7	56.0	101.6	100.0	476.8
Energy							
Rural Electrification	160.0						160.0
Transmission Extension	162.0						162.0
Corporate Restructuring		130.0					130.0
Domestic Energy		160.0					160.0
Private Sector Energy II			160.0				160.0
Small Scale Hydro				100.0			100.0
Energy Sector Investments				150.0			150.0
Thermal Power					150.0		150.0
Energy Conservation (S)						100.0	100.0
Thermal Power						100.0	100.0
Sub-Total	322.0	290.0	160.0	250.0	150.0	200.0	1372.0
Other							
Technical Assistance IV (S)					5.1		5.1
Sub-Total	0.0	0.0	0.0	0.0	5.1	0.0	5.1
Grand Total	825.8	674.7	693.5	758.6	645.2	700.0	4297.8

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12-Sep-90

FY90 Lending Program

FY91-94 Lending Program: 7/31/90

FY95 Lending Program: CSP

1990 ANNUAL MEETING BRIEF

PAKISTAN

1. Meeting Time and Place: Sunday, September 23, 1990, at 2:30 PM, International Finance Corporation, Room I-12-015.

2. Representing Pakistan:

Hon. Sartaj Aziz	Minister of Finance, Economic Affairs and Planning and Development
Mr. I. A. Hanfi	Governor, State Bank of Pakistan
Mr. Saeed Ahmed Qureshi	Finance Secretary
Mr. R. A. Akhund	Secretary, EAD
Mr. Qazi M. Alimullah	Additional Finance Secretary (Development Finance)
Mr. M. Ashraf Janjua	Economic Adviser, State Bank of Pakistan
Mr. Mueen Afzal	Economic Minister and Financial Adviser, Embassy of Pakistan, Washington, D.C.

3. Representing IFC:

Sir William Ryrie
Mr. Judhvir Parmar
Mr. Wilfried E. Kaffenberger
Mr. Jemal-ud-din Kassum
Mr. Daniel F. Adams
Mr. Declan Duff
Mr. C. John Pott
Mr. Khalid Mirza

4. Issues or Discussion Topics to be Raised by IFC:

(a) Expansion of Operations:

- IFC made progress during the year (FY90) on building the portfolio. The Board approved US$40.33 million, including US$3.24 million in equity. This year's pipeline (FY91) will need considerable strengthening.

- IFC would like an increased share of the Bank Group's assistance to the Pakistan private sector in future. Pakistan can derive significant benefit from taking a larger share of IFC's worldwide activities.

- IFC's strategy in Pakistan is to increase commitment levels and to broaden the sectoral base of investments. The Corporation will continue financing suitable private sector energy projects, but will seek to diversify our investment into other areas, with a focus on financing higher value added projects.

(b) Areas for Investment:

- IFC's portfolio has been heavily weighted in the past toward energy projects. We are making considerable efforts to diversify the portfolio into higher value added projects in areas such as general manufacturing on light engineering industries and in textiles on higher quality cotton products and synthetic fibers.

- We are actively seeking investments in the light engineering sector where Pakistan has some comparative advantage. Promising areas are automotive component industries, metal working and fabrication, electrical goods and telecommunications.

- In textiles, we are examining several projects which will improve overall quality and introduce new technology. Emphasis will be placed on export potential.

- Given recent developments in the Middle East, the large investment needs and the considerable import bill for petroleum, the Corporation will continue to finance oil and gas development projects. We are also reviewing several project proposals for urea manufacture from local gas.

- Other promising areas are power, cement, health care, agri-business and hotels.

- The Corporation is increasing its capital markets activities. In FY90 the Corporation invested in the First International Bank and in early FY91 the Board approved an investment in the Housing Finance Corporation of Pakistan. We will continue our institutional building activities with special emphases on equity finance companies, discount houses, stock-brokerage companies, etc. CMD continues to provide ad-hoc assistance to the Ministry of Finance and the Corporate Law Authority on various aspects of capital market development. IFC would be interested in assisting GOP to formulate rules to regulate non-bank financial institutions (housing finance companies, investment banks and leasing companies).

COUNTRY BRIEF

PAKISTAN

A. Current Strategy and Work Program

a) Expansion of Operations

- o IFC made progress in FY90 in building the portfolio. The Board approved US$40 million of new investments, including US$3 million in equity. With held commitments of US$100 million, Pakistan now ranks tenth in IFC's portfolio with 2.1%.

- o This year's pipeline (FY91) was reasonable and should result in higher investment volume provided political uncertainties do not lead to large scale deferral of private sector investment plans.

- o We intend to increase the focus on projects which are wholly private sector owned, broaden the sectoral base of investments and increase disbursement levels.

- o However, IFC is facing increasing competitive pressure in larger projects. Other institutions are apparently prepared to price aggressively and to require less clarity of lenders' rights.

- o To support our expansion effort, we are substantially increasing our promotion among medium- and smaller-sized groups, on a systematic basis, and are currently considering a number of good prospects in the US$5-10 million range where IFC has a role to play.

b) Areas for Investment

- o IFC's portfolio has been heavily weighted in the past toward energy projects. Whilst maintaining coverage in this sector, we are also making efforts to diversify the portfolio into areas such as light engineering and textiles.

- o In the light engineering sector, where Pakistan has some comparative advantage, promising areas are automotive component industries, metal working and fabrication, and electrical goods.

- o In textiles, we are examining several projects which will improve overall quality and introduce new technology in both cotton products and synthetic fibers. Emphasis is being placed on export potential.

- Given recent developments in the Middle East, the large investment needs and the considerable import bill for petroleum, the Corporation will continue to finance oil and gas development projects. We are also reviewing several project proposals for urea manufacture from local gas.

- Other promising areas are power, cement, health care, agri-business and hotels.

- The Corporation is increasing its capital markets activities. In FY90, the Corporation invested in the First International Bank and in early FY91 the Board approved an investment in the Housing Finance Corporation of Pakistan. We will continue our institutional building activities with special emphasis on equity finance companies, discount houses, stock-brokerage companies, etc. CMD continues to provide ad-hoc assistance to the Ministry of Finance and the Corporate Law Authority on various aspects of capital market development. IFC would be interested in assisting GOP formulate rules to regulate non-bank financial institutions (housing finance companies, investment banks and leasing companies).

- GOP had earlier expressed interest in a FIAS review of the foreign direct investment climate. FIAS is in process of discussing the timing for a first mission.

B. Project Approvals and Pipeline

1. Approvals (FY87-FY90)[a/]

Approvals ($ Million)	FY87	FY88	FY89	FY90
Number of Projects	4	6	2	3
Loan	11.8	101.0	-	37.09
Equity	7.5	0.0	2.6	3.24
Total	19.2	101.0	2.6	40.33

a/ Includes transactions of Capital Markets Department and Energy Unit.

2. Last Year's Approvals (FY90)[a/]

Approvals	Net IFC Investment Loan	Equity	Total	Project Cost ($ Million)	Activity
Pak Suzuki Motor Co. Ltd.	15.14	-	15.14	92.60	Automobile manufacturing
Rupali Polyester Ltd.	21.95	2.55	24.51	89.00	Petrochemicals/textiles
First International Investment Bank	-	0.69	0.69	4.76	Merchant bank
	37.09	3.24	40.34	186.36	

a/ Includes transactions of Capital Markets Department and Energy Unit

3. This Year's Pipeline (FY91)

Project	Net IFC Investment	Project Cost ($ Million)	Activity
a) Asia II Investment Department			
High Probability			
Attock Refinery	5.60	20.00	Petroleum refinery
Exxon Chemicals	18.50	74.00	Urea fertilizer
Shifa International Hospital	7.50	35.00	Hospital
Colony Denim	7.00	28.00	Textiles
Polyron	5.00	17.05	Petrochemicals/textiles
Crescent Denim	9.00	35.60	Textiles
Low Probability			
Pak Telecom/Alcatel	10.00	37.80	Telecom
Fauji Electric	35.00	250.00	Power
Hab River	n.a.	n.a.	Power
Mari Gas	n.a.	n.a.	Energy
Pak Saudi Fertilizer	n.a.	n.a.	Fertilizers
Hawkins/Tenasco	n.a.	n.a.	Power
b) Capital Markets			
High Probability			
Housing Finance Corporation	5.60	44.05	Housing finance
Industrial Leasing Corporation	5.0	5.0	Leasing
Equity Finance Corporation	1.15	5.75	Mezzanine financing
Low Probability			
Prudential Discount House	n.a.	n.a.	Discount house

C. Environment for IFC Activity

(Further details are given in Appendix 2)

- o Pakistan's overall economic performances has been relatively strong during most of the 1980's. However, by early 1988, its considerable economic achievements were being threatened by a growing fiscal deficit, an increasingly vulnerable balance of payments position and distortions in domestic costs and prices.

- o GOP, in consultation with the IMF and the Bank, responded to these problems by initiating a medium-term (3-year) structural adjustment and reform program (a PFP) beginning late 1988, aimed at achieving balance of payments viability while maintaining a satisfactory growth performance.

- o Implementation of the program has broadly been on track as regards liberalization of the trade regime, tariff rationalization, industrial incentives, and domestic credit restraint. Discussions on the Third-Year PFP (FY91-93) had been initiated with Ms. Bhutto's Government.

- o A worrisome outcome of the past year (FY90) was the lack of progress on reducing the fiscal deficit (an overall deficit of 7.2% versus about 7.3% in FY89) because of the political situation in Sind and Kashmir which prompted increased defense expenditure.

- o It is possible that the dismissal of Ms. Bhutto's Government could erode some of the macroeconomic stability achieved over the past two years, but it is unlikely that there would be any rollback of the structural reforms and liberalization initiatives introduced during Ms. Bhutto's period of office.

- o The recent developments in the Middle East could have far more serious consequences for Pakistan. Imports of petroleum and petroleum products comprise about 17.5% of total imports and each $1.0/barrel increase in the international oil price effectively increases the petroleum import bill by $65-70 million (foreign exchange reserves were US$504 million at end-July 1990).

- o Increased oil prices, reduced remittances and generally higher import prices, will exert severe pressure on the balance of payments and reserves positions. Pakistan's narrow export base will be particularly vulnerable to a slowdown in the economies of her main trading partners.

- o There are no indications yet as to whether the Government will seek balance of payments support through IMF arrangements or whether the Bank and other donors are considering providing stabilization suppport.

- o The Bank's FY91-FY95 strategy for Pakistan proposes a real decline in lending and a shift in lending toward agriculture and the social sectors and away from industry and DFIs.

1990 ANNUAL MEETING BRIEF

PAKISTAN

1. Meeting Time and Place: Sunday, September 23, 1990, at 2:30 PM, International Finance Corporation, Room I-12-015.

2. Representing Pakistan:

Hon. Sartaj Aziz	Minister of Finance, Economic Affairs and Planning and Development
Mr. I. A. Hanfi	Governor, State Bank of Pakistan
Mr. Saeed Ahmad Qureshi	Finance Secretary
Mr. R. A. Akhund	Secretary, EAD
Mr. Qazi M. Alimullah	Additional Finance Secretary (Development Finance)
Mr. M. Ashraf Janjua	Economic Adviser, State Bank of Pakistan
Mr. Mueen Afzal	Economic Minister and Financial Adviser, Embassy of Pakistan, Washington, D.C.

3. Representing IFC:

Sir William Ryrie
Mr. Judhvir Parmar
Mr. Wilfried E. Kaffenberger
Mr. Jemal-ud-din Kassum
Mr. Daniel F. Adams
Mr. Declan Duff
Mr. C. John Pott
Mr. Khalid Mirza

4. Issues or Discussion Topics to be Raised by IFC:

- o The IFC office in Islamabad is now fully staffed and will be highly instrumental in the expansion of our promotional efforts.

- o We appreciate GOP's assistance in remittance of our Pakistan Paper Corporation Ltd. settlement.

- o Now that the Federal Shariat Court has assumed exclusive jurisdiction to examine and decide whether or not any banking or fiscal law or practice is contrary to Islamic Injunctions, the question of enforceability of interest remains an acute problem. Even though certain petitions have now been filed by the Chairman of the Islamic Revolutionary Movement challenging fiscal payments and interest, no determination has been made by the Federal Shariat Court. We are of course continuing to rely on certain assurances provided by GOP but these are recognized as being interim arrangements and our dialogue with GOP will therefore continue to find a more permanent resolution of this problem which will be needed in any large financial transaction, particularly where a syndicated loan is involved.

PAKISTAN

STATEMENT OF IFC INVESTMENTS AS OF JUNE 30, 1990

(US$ MILLIONS)

FISCAL YEAR	OBLIGOR	BUSINESS	ORIGINAL INVESTMENT Equity	Loan	Total	IFC HOLDING Equity	Loan	Total	TOTAL Undisb. (Incl/Part.
1958	Steel Corp. of Pakistan	Iron & Steel	0.00	0.63	0.63	0.00	0.00	0.00	0.00
1959	Adamjee Industries Ltd.	Textiles	0.00	0.75	0.75	0.00	0.00	0.00	0.00
1961/65	Gharibwal Cement Ltd.	Cement	0.42	5.25	5.67	0.00	0.00	0.00	0.00
1963/64/ 75/87/89	Pakistan Industrial Credit & Investment Corporation Ltd.	DFC	3.63	0.00	3.63	0.59	0.00	0.59	0.00
1965/80/82/ 87/88	Packages Limited	Paper Products	1.01	26.00	27.01	0.62	6.19	6.81	0.00
1965	Crescent Jute Products Ltd.	Textiles	0.11	1.84	1.95	0.00	0.00	0.00	0.00
1967	Pakistan Paper Corp. Ltd.	Paper	2.02	5.38	7.40	0.00	0.00	0.00	0.00
1969/89	Dawood Hercules Chemicals Ltd.	Fertilizer	2.92	18.30	21.22	2.92	17.30	20.22	5.00
1979	Fauji Foundation	Polypropylene Bags	0.00	1.78	1.78	0.00	0.00	0.00	0.00
1979	Attock Refinery Ltd.	Chemicals & Petrochemicals	0.76	15.00	15.76	0.61	0.00	0.61	0.00
1979	Milkpak Ltd.	Food Processing	0.35	2.40	2.75	0.00	0.00	0.00	0.00
1979/82/84	Pakistan Oilfields Ltd.	Chemicals & Petrochemicals	1.28	14.00	15.28	1.03	0.00	1.03	0.00
1980 /b	Premier Board Mills Ltd.	Particle Board	0.00	2.70	2.70	0.00	0.00	0.00	0.00
1981	Habib Arkady Ltd.	Food & Food Processing	0.16	3.15	3.31	0.17	2.10	2.27	0.00
1982	Asbestos Cement Industries Ltd.	Cement & Construction Material	0.50	3.50	4.00	0.00	0.00	0.00	0.00
1983/85	Pakistan Petroleum Ltd.	Chemicals & Petrochemicals	1.56	104.50	106.06	1.56	13.81	15.37	0.00
1985	National Development Leasing Co.	Money & Capital Market	0.37	5.49	5.86	0.00	0.00	0.00	0.00
1986	Mari Gas Company Ltd.	Chemicals & Petrochemicals	0.00	46.53	46.53	0.00	5.14	5.14	0.00
1987/89	Anglo-Suisee	Chemicals & Petrochemicals	6.80	0.00	6.80	1.60	0.00	1.60	1.61
1988 b/	Fecto Cement	Cement & Construction Materials	0.00	18.58	18.58	0.00	0.00	0.00	0.00
1988	Millat	Tractors	0.00	4.90	4.90	0.00	5.54	5.54	0.00
1989 b/	Shams Textile	Textiles & Fibres	0.00	2.76	2.76	0.00	0.00	0.00	0.00
1989 b/	Suraj Cotton	Textiles & Fibres	0.00	2.76	2.76	0.00	0.00	0.00	0.00
1989	Hala Spinning	Spinning Plant	0.00	3.26	3.26	0.00	2.99	2.99	0.00
1990	Pak Suzuki	Automotive	0.00	15.56	15.56	0.00	15.56	15.56	15.56
1990	Rupali Polyester	Textiles	2.00	20.10	22.10	2.00	20.10	22.10	22.10
1990	FIIB	Capital Markets	0.68	0.00	0.68	0.68	0.00	0.68	0.68
	TOTAL		24.57	325.12	349.69	11.78	88.73	100.51	44.95

a/ Includes transactions of Capital Markets Department and Energy Unit.

b/ Subsequently cancelled.

PAKISTAN: Portfolio Movements[a/]
June 30, 1990
(US$ millions)

	FY86	FY87	FY88	FY89	FY90
1. Disbursed Portfolio					
Beginning Balance	39.04	55.15	49.76	45.72	48.11
+ Disbursements	13.92	3.61	3.14	10.01	16.31
- Repayments	4.84	4.74	6.84	5.60	9.12
- Prepayments	00.0	7.24	0.00	0.00	0.00
- Investments Sold	0.00	0.25	1.08	0.00	0.24
- Write-offs	0.00	2.02	0.00	0.00	3.11
+ Currency Revaluation	7.03	5.25	0.74	(2.02)	3.62
Ending Balance	55.15	49.76	45.72	48.11	55.57
2. Undisbursed Portfolio					
Beginning Balance	13.75	15.26	13.47	34.87	26.95
+ Commitments	23.91	6.80	23.36	29.07	40.72
- Disbursements	13.92	3.61	3.14	10.01	16.31
- Cancellations	11.61	3.46	0.00	23.57	5.52
+ Currency Revaluation	3.13	(1.52)	1.17	(1.31)	(3.19)
Ending Balance	15.26	13.47	34.87	26.95	42.65
3. Held Portfolio					
Beginning Balance	52.79	70.41	63.23	80.59	75.06
+ Commitments	23.91	6.80	23.36	26.97	40.72
- Repayments	4.84	4.74	6.84	5.60	9.12
- Prepayments	0.00	7.24	0.00	0.00	0.00
- Investments Sold	0.00	0.25	1.08	0.00	0.24
- Write-offs	0.00	2.02	0.00	0.00	3.11
- Cancellations	3.48	11.61	0.00	23.57	5.52
- Currency Revaluation	10.16	3.73	1.91	(3.33)	0.43
Ending Balance	70.41	62.23	80.59	75.06	98.22
4. Held Portfolio as % of IFC's Held Portfolio	2.95%	2.26%	2.39%	1.86%	2.07%

a/ Excluding transactions of Capital Markets Department and Energy Unit

PAKISTAN: Portfolio[a]
June 30, 1990
(US$ millions)

	FY87	FY88	FY89	FY90
1. Loan Portfolio				
Number of Companies	7	9	11	9
Amounts Held	54.9	72.6	67.1	88.7
Amounts Disbursed and Outstanding	41.8	38.1	40.4	48.1
Prepayment and Cancellations	10.7	0.0	23.6	5.8
Non-Accruing Loans				
Number	2	2	2	1
Principal Outstanding	7.7	7.7	7.7	2.1
% of Loan Portfolio	18.4%	20.2%	19.1%	4.4%
Total Specific Provisions	2.5	3.6	5.0	0.7
2. Equity Portfolio				
Number of Companies	8	8	7	8
Amounts Held	8.3	7.9	8.0	9.5
Amounts Disbursed and Outstanding	8.0	7.6	7.7	7.5
Dividend Income	1.3	0.6	1.1	0.9
Capital Gains	0.2	1.0	0.0	0.6
Specific Reserves	1.4	2.8	0.2	0.1
3. Approvals				
Number of Projects	2	6	-	2
Loan	11.8	101.0[b]	-	37.09
Equity	0.2	0.0	-	2.55
Total	12.0	101.0	0.0	39.64

a/ Excluding transactions of Capital Markets Department and Energy Unit.
b/ Includes $74 million equivalent in PSO and PPLIII which was subsequently dropped.

PAKISTAN: Sectoral Distribution of Held Portfolio
June 30, 1990
(US$ millions)[a]

Sector	Loan	Equity & Quasi-Equity	Total	Percentage
Automotive/Accessories	15.56	-	15.56	15.8
Capital Markets	-	-	-	-
Cement/Const. Materials	-	-	-	-
Chemicals/Petrochemicals	-	-	-	-
Development Financing	-	0.60	0.60	0.6
Energy	18.95	3.2	22.15	22.6
Fertilizers	17.30	2.92	20.22	20.6
Food and Agribusiness	2.1	0.16	2.26	2.3
Industrial Equip./Mach.	5.54	-	-	5.6
Iron and Steel	-	-	-	-
Manufacturing (Other)	-	-	-	-
Mining	-	-	-	-
Pulp, Paper and Timber	6.19	0.62	6.81	6.9
Services (Other)	-	-	-	-
Shipping	-	-	-	-
Textiles	23.09	2.0	25.09	25.5
Tourism	-	-	-	-
Total	88.73	9.5	98.22	100.0

[a] Excluding transactions of Capital Markets Department and Energy Unit

ECONOMIC DEVELOPMENT AND PROSPECTS

- Pakistan's overall economic performance has been relatively strong during the 1980s. Continuous improvements in economic policies, coupled with increased demand for goods and services in the Middle East, have been the major contributors to the impressive real GDP growth of 6.5% per annum since 1984. Growth of key sectors has been satisfactory, with agriculture, services and industry averaging 4.1%, 7.1% and 7.5%, respectively, over the 1981-89 period. External debt servicing difficulties have been largely avoided and inflation has been moderate. During this time, Pakistan was also able to care for more than three million Afghan refugees.

- These economic achievements became increasingly threatened by three structural problems: a large fiscal imbalance (8.6% of GDP by 1988) which could trigger balance of payments problems and accelerate inflation; a vulnerable external current account (the deficit averaged 3.6% of GDP in FY84-FY88); and distortions in domestic costs and prices.

- GOP responded to these problems by initiating a medium-term (three-year) adjustment and structural reform program beginning in December 1988, aimed at achieving fiscal and balance of payments viability while maintaining satisfactory growth performance. The program, which is being supported by the IMF (with a 15-month Standby and three annual arrangements under the Structural Adjustment Facility) and by higher Bank lending, can be considered successful. It is now close to the end of its second year of implementation (December, 1990). A Second-Year Policy Framework Paper (PFP; FY90-92), which lays out the policy intentions under the program, was reviewed by the Executive Directors of the Bank and the Fund in December 1989. Discussions on the Third-Year PFP (FY91-93) had been initiated with Ms. Bhutto's Government.

- Preliminary results for FY90 show a mixed economic performance. The greatest success has been in achieving further macroeconomic stability through a reduction of inflation (down to 6%) and strengthening of the balance of payments position (a current deficit of 4.1% of GDP against 4.6% in FY89) while maintaining a reasonable rate of overall economic growth (5.2%). However, these improvements are somewhat fragile, even without the most recent domestic and external developments.

- External reserves remain uncomfortably low (at $604 million, June 1990) and the overall level of investment is also too modest to sustain long-term growth and social progress. Some progress has been made in financial sector reform but the pace is slow, and the thrust towards privatization seems to have weakened. The most worrisome outcome of the year was the lack of progress in fiscal policy (an overall deficit of 7.2% versus about 7.3% in FY89). The cause does not appear to be bad economic management, but rather the political situation in Sind and Kashmir which prompted increased defense expenditure. The 1990/91 Budget contains a fiscal deficit reduction strategy, but hopes of controlling the deficit could be ruined by further increases in defense spending, actions of the interim Government and/or the successor Government and/or developments in the Middle East.

- The past fiscal year (FY90; July 1-June 30) witnessed disquieting developments at the eastern border and considerable domestic political confrontation which carried over into early FY91 with President Ghulam Ishaq Khan's dismissal of Prime Minister Benazir Bhutto on August 5, 1990 and the declaration of a state of emergency. The President has constituted an interim Government, led by Mr. Ghulam Mustafa Jatoi. Elections have been set for October 24, 1990.

- It is possible that the dismissal of Ms. Bhutto's Government could erode some of the macroeconomic improvements achieved over the past two years. However, a rollback of the structural reforms and liberalization initiatives (as embodied in the Bank/IMF Policy Framework Paper (PFP), 1989/90 to 1991/92) introduced during Ms. Bhutto's period of office, is unlikely since they were in large part designed and endorsed by the Government of the late General Zia and there does not appear to have been any political or civil opposition to the measures.

- Recent developments in the Middle East could potentially have far more serious consequences for Pakistan.

  - In 1988/89, imports of petroleum and petroleum products (Rs18.509 billion or US$974 million) accounted for about 14% of total imports. In the first nine months of FY90 (July-March), imports of petroleum and petroleum products (Rs18.997 billion or US$883 million) comprised 17.5% of the value of total imports. Roughly 60% of the oil imports were from Kuwait, 23% from Saudi Arabia and 11% from UAE.

  - Assuming oil prices were to average $24/barrel over the next 12 months (versus an average of $16/barrel paid during the previous 12 months), the increase in the import bill for petroleum and petroleum products would effectively use up most of the country's foreign exchange reserves. Each US$1.0/barrel increase in the international oil price will effectively increase Pakistan's petroleum import bill by US$65-$70 million.

  - International petroleum prices are also likely to affect the prices of other imported products such as chemicals, dyes and chemical fertilizers which together account for about 14% of total imports.

  - Workers' remittances are also certain to be affected. In FY89, workers' remittances totalled $1.897 billion, of which 68% was from the Middle East. About 13% of remittances from the Middle East originate in Kuwait, and almost 60% from Saudi Arabia. A slowdown of remittances will have consequences for the balance of payments position and displaced Middle East workers will add to the employment and social problems.

- o A cause for some concern is that IFC's operations are coming into increasing competition from other official and semi-official sources of direct private sector financing. ADB's new private sector focus has made them one of the major term lenders in Pakistan. Newly created AFIC is also becoming a major player. CDC, although not as large a lender, has also opened a new office in Pakistan.

- o The Bank's Country Strategy Paper for Pakistan (FY91-FY95) proposes shifts in the Bank's strategy and approach to assisting Pakistan's development effort. Several of these shifts are likely to work in the Corporation's favor.

  - The proposed Base Case lending scenario of $700 million annually, which would total $3,402.5 million over the five-year period FY91-FY95 represents a real decline in Bank lending over the previous five-year period (FY86-FY90, $3,483.4 million). Even with this normally constant lending level, the Bank will face problems of managing its exposure within Bank guidelines (the Bank's share in long-term debt outstanding and disbursed was about 10% in 1990 and is projected to rise to 14% by 1999. The Bank's share in debt service will rise from 12% over the same period). Bank lending may also be limited by Pakistan's ability (in certain sectors) to absorb more external loans. There are about $8 billion in undisbursed funds from external loans.

  - The Bank (CSP) proposes that once the current account deficit is brought down to sustainable levels, other official sources (notably ADB and Japan) and the private financial markets would provide a larger share of financing relative to the Bank. Sector investment loans would serve as the instruments for achieving further sector policy reforms and for promoting institutional reforms.

  - The Bank will continue suppport for GOP's medium-term adjustment and structural reform program, but will now also develop a longer-term development program, with appropriately matched investments. These investments will tend to be focussed on the social sectors, rural development and agriculture.

  - There appears to be a shift away from both Bank financing of the industrial sector through direct investments and Bank financing of the private sector through financial intermediaries, toward increased emphasis on the social sectors. The emphasis on lending for energy development is maintained. It should not escape notice that funds from major Bank loans and credits made to industry and DFIs in the previous five years will be available for commitment and thus compete with other sources.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: December 20, 1989

TO: Mr. Michel Camdessus

FROM: Barber B. Conable

EXTENSION: 72001

SUBJECT: PAKISTAN - Policy Framework Paper 1989/90-1991/92
Summary of the Discussion of the Committee of the Whole
December 18, 1989

Attached is the summary of the discussion of the Committee of the Whole held on December 18, 1989 on the Pakistan Policy Framework Paper.

Barber B. Conable

Attachment

PAKISTAN POLICY FRAMEWORK PAPER, 1989/90-1991/92

CHAIRMAN'S SUMMARY OF DISCUSSION BY THE COMMITTEE OF THE WHOLE

The Committee of the Whole reviewed the second-year Policy Framework Paper for Pakistan on December 14, 1989. The Directors noted with approval the Government's commitment to adjustment and commended the Government for progress already made in adopting the structural reforms laid out in the PFP, including trade liberalization. These steps should strengthen economic competitiveness and encourage private economic activity, including direct foreign investment. However, they expressed concern about the slippages in the fiscal area and, in particular, about the large external current account deficit in FY89 and low external reserves.

Directors noted that the Government's ability to adjust the external current account more rapidly had been affected by the deterioration in the terms of trade. They emphasized the need for both structural reforms and active demand management to reach the current account deficit target by FY92, one year behind the original schedule. In the past fiscal year, it was noted, the Government had responded to the terms of trade difficulties by depreciating the real exchange rate further and tightening monetary policy. These measures, together with the Government's trade policy reforms, should result in a broadening of the export base.

Directors stressed the importance of strengthening the fiscal situation and increasing revenues. Although the revenue/GDP ratio was expected to fall temporarily in FY90, it was noted that the Government was making progress in resource mobilization, and had in fact intensified the structural reform of the tax system in FY90. Besides expanding the coverage of the existing sales tax and extending excise taxes to services, it had also broadened the income and profit tax base and raised administered prices. It was also on schedule in preparing for the introduction of a generalized sales tax in July of next year. In addition, it had converted a large number of specific customs duty rates to ad valorem rates. While noting the steps already taken, Executive Directors emphasized the importance of enhanced determined action to reduce the fiscal deficit and strengthen the revenue base.

In view of Pakistan's need for infrastructure and social investments, the reduction in the Government's investment/GDP ratio in FY89 was disappointing. Executive Directors pointed to the need to prioritize investments and noted, in particular, the need for special programs in the social sectors, given Pakistan's relatively poor social indicators.

Several speakers expressed concern about the social impact of the program. It was noted that, in the past fiscal year, the Government had taken steps to shield the lower income population from the full burden of adjustment. Increases in electricity and natural gas prices were lower for the smallest consumers, and the Government did not pass on the full cost of wheat and edible oil imports to the population. Having an additional year to reach the macroeconomic targets was acknowledged as helpful to the Government in minimizing the cost of adjustment. Directors also drew attention to the importance of drawing up a comprehensive environmental program and noted with approval that steps to this end had already been taken.

Directors commented on the Government's progress in privatization and improving the efficiency of parastatals. Note was made of the progress in private sector power generation and in the financial area, where the Government had sanctioned six private investment finance companies and was actively exploring ways to privatize part of the nationalized banking system. Steps were also being taken to restructure some of the other important public sector companies.

Finally, Directors stressed the need to consolidate and extend reforms, despite Government's continuing political and economic difficulties. Several Directors referred to Pakistan's need for external assistance and to the substantial support that was being provided by the donor community to Pakistan. Directors confirmed that in view of the heavy burden of indebtedness, and the impact of worsening terms of trade, Pakistan will continue to need substantial external assistance in support of its adjustment program.

COUNTRY: <u>PAKISTAN</u>

DELEGATION:
Mr. V.A.Jafarey, Adviser to Prime Min. (Finance)
Mr. I.A. Hanfi, Governor of State Bank
Mr. H. Minwala, Adviser to Prime Minister
Mr. R.A. Akhund, Financial Secretary

<u>Friday 9/29 @ 9:15 a.m.</u>

BACKGROUND
- Despite many political strains and other problems, Ms. Bhutto's Government appears secure for the near future.
- Committed to carrying out the July 1988 adjustment program (IMF/Bank) inherited, but likely to breach FY89 fiscal and current account targets.
- Adjustment effort needs strengthening, notably in raising fiscal revenue.
- May 1989 Bank/Fund program review was incomplete; continued in September.

POINTS TO BE MADE TO THE DELEGATION

<u>Adjustment Program</u>: In order for the Government to meet fiscal targets, not only must non-development expenditures be contained, but Government must aggressively mobilize additional resources through changes in the tax structure.
- Inquire about the prospects for broadening the tax base.
- Also, revenue raising by provinces themselves.

<u>Development Strategy</u>: Express some concern that Government has still not articulated a coherent development strategy. Also understand a 6-point program to fight poverty is being prepared.
- Inquire how the Government plans to follow up on the Population Report discussed at April Consortium meeting.
- How does the Government intend to expand family planning programs in the face of expenditure cuts (5% in real terms in FY90).

IF DELEGATION MENTIONS...

<u>Prime Minister's Interest in Bank Assistance</u> on a variety of problems.

YOU MAY INDICATE that these matters are being reviewed by Bank staff and a comprehensive reply to the Prime Minister is under preparation.
- Regional staff can provide further details.

FY89 Commitments:	$949.4 million	**GDP Growth:** 5.1% (1989); 6.6% (84-88)
Disbursements :	$471.5 million	**Lending Program (FY90-91):** 1,738.0 m.
Amortization :	$ 81.9 million	

1THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: September 20, 1989

TO: Mr. Moeen A. Qureshi, Senior Vice President, Operations

THROUGH: Wilfried P. Thalwitz, Vice President, EMENA

FROM: H. Eberhard Köpp, Director, EM1

EXTENSION: 33000

SUBJECT: PAKISTAN: Annual Meetings Updating Note

1. The change in the leadership of the Pakistan Delegation and the results of the recent IMF/Bank mission to Pakistan are given below. A shorter updating note for Mr. Conable is also attached.

Change in the Pakistan Delegation

2. The Government has advised us that Mr. Ihsanul Haq Piracha, Minister of State for Finance, has replaced Mr. Jafarey as head of the delegation. Biographical information about Mr. Piracha and a list of other members of the delegation are attached for your information.

Update on IMF/Bank Mission

3. The recent Fund/Bank mission to Pakistan (August 26 to September 12) was inconclusive:

- The mission was unable to complete the review of the program for FY89. Review of the performance criteria proper revealed almost 100% compliance, and policy measures were adopted as planned in most areas (including trade, financial and other sectors). However, the mission and GOP could not agree on the magnitude of the FY89 budget deficit. Although revenues seem to have been on target, the mission thinks that the fiscal deficit for FY89 exceeded the targeted 6.7% of GDP by about one percent of GDP. (This calculation, which must still be confirmed, is derived from financing estimates.) The Government disputes this finding. Because of the absence of direct estimates of expenditure at the time of the mission, the issue could not be settled then.

- There is no agreed program yet for FY90. Here again, the major issue is expected fiscal performance. Although the IMF/Bank team agrees with GOP's estimates of revenue yields, it feels that such a modest revenue effort will unduly constrain expenditures. Furthermore, GOP's current proposals imply a drop in the revenue to GDP ratio from 18.1% in FY89 to 17.6% in FY90. Using more realistic expenditure assumptions, the mission calculates a gap of about Rs 7 billion (about 0.8% of GDP), if GOP is to reach an overall deficit level of

6% of GDP in FY90. A menu of possible revenue measures, including an increase in the excise tax on petroleum, was proposed by the mission. The authorities were not ready to consider more than token actions, primarily because of fear of political repercussions.

4. Discussions will continue at the Annual Meetings. The Government has been requested to come with a reconciliation of the FY89 budgetary and financing numbers, and additional revenue measures for the current year. If an understanding emerges during the Meetings, the Fund will go back to Pakistan in mid-October, in order to finalize the FY90 program for presentation to the Executive Directors in December 1989. Although progress on reaching an agreement has been slower than initially anticipated, both the GOP and IMF/Bank maintain a strong interest in continuing discussions.

5. Suggested Discussion Points at the Annual Meetings. Although we expect the Government to clarify its budget position at separate meetings with the Fund and the Region, we suggest that you reiterate the importance of continued fiscal adjustment in your meetings with the Delegation. As part of the discussion, we suggest that you:

- acknowledge the awkward situation facing the Government vis a vis the Fund and the Bank. Although the formal review process has not yet been completed, GOP seems to have technically met virtually all of the Fund's performance criteria and adopted the major policy measures in the PFP for FY89. However, there is a strong prima facie case that it exceeded the fiscal deficit target for FY89 by perhaps one percent of GDP, thus requiring a stronger adjustment effort for FY90.

- recognize the political difficulties associated with additional revenue efforts. We realize that the Prime Minister is already facing a difficult domestic situation, with several recent challenges to her authority. In addition, the continuing Afghan war has left Pakistan with the task of feeding and housing additional refugees and inadvertently transferring, through private traders, wheat and other food staples to Afghanistan, thus worsening its own budget and balance of payments. All of this compounds the difficulties of undertaking new resource mobilization measures, which are justified by the macro situation.

- emphasize the importance of maintaining the revenue/GDP ratio, in order to permit growth in development spending. In this period prior to the introduction of a value added tax, slippage in the revenue/GDP ratio would be highly undesirable by compromising future growth.

- emphasize the difficulties of letting development expenditures slip. We have been told that project implementation in all sectors except energy is slowing down; left unaddressed, this slippage could undo many of the positive benefits of the Government's policy reforms.

6. The Bottom Line. All of this suggests that fiscal performance is problematic and its improvement is required to meet short-term requirements of the IMF program and to avoid undermining longer-term development prospects. Introducing new revenue measures, however, will be extremely difficult and run counter to the Prime Minister's announced position against introducing "mini-budgets." Nevertheless, the Bank should express its willingness to work with the Government to identify feasible options.

Attachments

LYap:bd

PAKISTAN

Biographical Information

Mr. Ihsanul Haq Piracha

Minister of State for Finance, Economic Affairs and Planning and Development (Governor of the IMF)

An MNA from Sargodha, Mr. Ihsanul Haq Piracha was born in April 1934. Mr. Piracha is a law graduate. A prominent businessman and industrialist, he has held high positions in various industrial organizations. He has also been the president of the Rawalpindi Chamber of Commerce and Industry seven times. He also served as Chairman of the Municipal Committee, Bhera, Distt. Sargodha. He was elected as Senator in 1985 as technocrat from Punjab. He was also elected as Member of the Punjab Provincial Assembly in 1970. In 1977, he was re-elected MPA and held the portfolio of the Minister in charge of Communication and Works until the imposition of Martial Law. In 1988, he was appointed as Minister of Transport in the Caretaker Cabinet of the Punjab but resigned to join PPP and take up his MNA position.

Other Members of the Delegation

1. Mr. A.G.N. Kazi
   Deputy Chairman, Planning Commission

2. Mr. K. M. Chima, Secretary
   Economic Affairs Division

3. Mr. R. A. Akhund, Financial Secretary

4. Mr. Qazi M. Alimullah, Additional Secretary
   Finance Division

5. Mr. M. Ashraf Janjua, Economic Adviser
   State Bank of Pakistan

6. Mr. Zulfiqar Ali Khan, Ambassador
   Embassy of Pakistan

7. Mr. Mueen Afzal, Economic Minister and F.A.
   Embassy of Pakistan

8. Mr. Nasim Qureshi, Commercial Counsellor
   Embassy of Pakistan

September 20, 1989

PAKISTAN: Annual Meetings Update for Mr. Conable

Change in the Pakistan Delegation

1. The Government has advised us that Mr. Ihsanul Haq Piracha, Minister of State for Finance, has replaced Mr. Jafarey as head of the delegation. Biographical information about Mr. Piracha and a list of other members of the delegation are attached for your information.

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- The mission was unable to complete the review of the program for FY89. Review of the performance criteria proper revealed almost 100% compliance, and policy measures were adopted as planned in most areas (including trade, financial and other sectors). However, the mission and GOP could not agree on the magnitude of the FY89 budget deficit; according to preliminary mission calculations, the actual deficit appears to have exceeded the target by about one percent of GDP.

- There is no agreed program yet for FY90. Here again, the major issue is expected fiscal performance.

3. Discussions will continue at the Annual Meetings. The Government has been requested to come with a reconciliation of the FY89 budgetary and financing numbers, and additional revenue measures for the current year. If an understanding emerges during the Meetings, the Fund will go back to Pakistan in mid-October, in order to finalize the FY90 program for presentation to the Executive Directors in December 1989. Although progress on reaching an agreement has been slower than initially anticipated, both the GOP and IMF/Bank maintain a strong interest in continuing discussions.

4. Suggested Discussion Points at the Annual Meetings. Although we expect the Government to clarify its budget position at separate meetings with the Fund and the Region, we suggest that you reiterate the importance of continued fiscal adjustment in your meeting with the Delegation. As part of the discussion, we suggest that you:

- acknowledge the awkward situation facing the Government vis-à-vis the Fund and the Bank. Although the formal review process had not yet been completed, GOP seems to have technically met virtually all of the Fund's performance criteria and adopted the major policy measures in the PFP for FY89. However, there is a strong *prima facie* case that it exceeded the fiscal deficit target for the year.

- recognize the political difficulties associated with additional revenue efforts.

- emphasize the importance of maintaining the revenue/GDP ratio, in order to permit needed growth in development spending.

- emphasize the difficulties of letting development expenditures slip.

5. The Bottom Line. All of this suggests that fiscal performance is problematic and its improvement is required to meet short-term requirements of the IMF program and to avoid undermining longer-term development prospects. Introducing new revenue measures, however, will be extremely difficult and run counter to the Prime Minister's announced position against introducing "mini-budgets." Nevertheless, the Bank should express its willingness to work with the Government to identify feasible options.

Attachment

Conable.Pak

PAKISTAN

Biographical Information

Mr. Ihsanul Haq Piracha

Minister of State for Finance, Economic Affairs
and Planning and Development
(Governor of the IMF)

An MNA from Sargodha, Mr. Ihsanul Haq Piracha was born in April 1934. Mr. Piracha is a law graduate. A prominent businessman and industrialist, he has held high positions in various industrial organizations. He has also been the president of the Rawalpindi Chamber of Commerce and Industry seven times. He also served as Chairman of the Municipal Committee, Bhera, Distt. Sargodha. He was elected as Senator in 1985 as technocrat from Punjab. He was also elected as Member of the Punjab Provincial Assembly in 1970. In 1977, he was re-elected MPA and held the portfolio of the Minister in charge of Communication and Works until the imposition of Martial Law. In 1988, he was appointed as Minister of Transport in the Caretaker Cabinet of the Punjab but resigned to join PPP and take up his MNA position.

Other Members of the Delegation

1. Mr. A.G.N. Kazi
   Deputy Chairman, Planning Commission

2. Mr. K. M. Chima, Secretary
   Economic Affairs Division

3. Mr. R. A. Akhund, Financial Secretary

4. Mr. Qazi M. Alimullah, Additional Secretary
   Finance Division

5. Mr. M. Ashraf Janjua, Economic Adviser
   State Bank of Pakistan

6. Mr. Zulfiqar Ali Khan, Ambassador
   Embassy of Pakistan

7. Mr. Mueen Afzal, Economic Minister and F.A.
   Embassy of Pakistan

8. Mr. Nasim Qureshi, Commercial Counsellor
   Embassy of Pakistan

September 20, 1989

1989 ANNUAL MEETINGS BRIEF

Name of Country: PAKISTAN   Date: August 25, 1989

Meeting with: Mr. V.A. Jafarey, Governor of World Bank and Adviser to Prime Minister (Finance)
Mr. I.A. Hanfi, Governor of State Bank
Mr. H. Minwala, Adviser to Prime Minister
Mr. R.A. Akhund, Financial Secretary

Population: 102.5m (mid-1987)   Estimated Growth Rate: 3.1% (65-87)
GNP per capita: $350 (1987)

		($m)		($m)
Total Commitments to date:		6,355.86	FY89 Commitments:	949.40
Bank (no. of operations and value)	69	3,403.39	Disbursements:	471.50
IDA (no. of operations and value)	107	2,952.47	Amortization:	81.90
Total Undisbursed:		2,771.51	Net Disbursements:	389.60
Lending Program: FY90-91		1,738.00		

Summary Data	Average FY84-88	FY89
GDP Growth %	6.6	5.1
Export Growth	13.1	1.7
Import Growth	3.7	2.9
Current Account Deficit % GDP	3.9	4.9
Gross Debt Service Ratio	23.8	27.8
Annual Inflation Rate	5.4	10.3

Aid Group Meeting: Consortium
Last Meeting: April 20-21, 1989
Last Article IV Consultation: December 1988
Next IMF Visit: August 1989

Part I: Background

Despite some of the serious political strains of the past year, Prime Minister Bhutto's Government appears secure for the near future. The Government has maintained its commitment to the economic adjustment program agreed to in July 1988. Nevertheless, deteriorating terms of trade and expenditure overruns are likely to have caused FY89 external and fiscal current account deficits to be above program targeted levels. A Bank/Fund mission review of the program is scheduled to be completed on September 10 and an updating note will be prepared.

Part II: Issues Likely to be Raised by the Delegation

1. Cooperation and Relations

Part III: Issues to be Raised by Bank Management

1. Adjustment Program
2. Development Strategy and Program

Attachments: Five-Year Lending Program: FY90-94 (FY89 Actual)
Biographical Information

Senior Management Brief
Country: Pakistan
August 25, 1989

1989 Annual Meetings
Briefing Paper

I. Background

A. Political

1. The euphoria with which the Government of Prime Minister Bhutto came to power eight months ago has, as might have been expected, been dampened by economic and political realities.

2. The Government has found a significant gap between the resources required to finance the programs so generously promised by the Pakistan People's Party (PPP) during the heat of last Fall's political campaign and the resources that are now available. In addition, it has found it difficult to translate the PPP's political rhetoric and goals into viable operational programs. A continued failure to deliver on promised programs is likely to erode the Government's popular support.

3. Pakistan's national cohesion, which has been a traditional source of concern, has been subject to further strains over the last eight months. The most populous Province, Punjab, is in the control of the opposition Islamic Democratic Alliance. The Prime Minister has also lost her parliamentary allies in the two smallest Provinces, Baluchistan and the Northwest Frontier Province. Even in Sind, which PPP controls, support of the Prime Minister by some of her political allies has been weakened as a result of her inability to stem ethnic conflicts. The result is that the Provinces and the center Government frequently work at cross purposes and federal programs are often obstructed.

4. Pakistan has been encountering two persistent threats to its security. The first is largely, but not exclusively domestic in origin and has been growing, while the second is external and appears to be diminishing. The first is the problem of urban and rural crime and violence in Karachi and other areas of Sind. In recent months the number of kidnapings, robberies and murders have significantly increased. The second threat is the Afghan conflict which although continuing without resolution in sight, appears to be causing fewer border incidents and acts of terrorism within Pakistan. The continued presence, however, of three million Afghan refugees in Pakistan remains an economic and political problem.

5. Despite the Government's many problems, the political opposition has not succeeded in mounting an effective political challenge to the Prime Minister. In addition, the Prime Minister has remained sensitive to the concerns and interests of the military establishment, who thus far have been content to remain outside of the political arena. Although the Government does not appear to be facing any immediate threats to its continued existence, it is not clear that it has as yet firmly established itself.

B. Economic

6. In order to arrest deteriorating economic trends (an increasing fiscal deficit which reached 8.5% of GDP in FY88, and an external current account deficit of 4.4% of GDP in the same year) the previous Government entered into a major adjustment program in July 1988 which was supported by the IMF and World Bank . The new Government under Ms. Bhutto quickly committed itself to carry out the adjustment program after assuming office in December 1988.

7. The Government has been conscientious in adhering to the adjustment program. Nevertheless, overruns in some expenditure categories such as defense and subsidies, are likely to have caused the FY89 fiscal deficit to be above the targeted level of 6.5% of GDP (final FY89 figures are not yet available), although the deficit is still likely to be considerably below FY88's 8.5%. In addition, in the course of FY89 the Government was confronted with a terms of trade shock which was reflected in a higher than expected current account deficit of the balance of payments.

8. In view of the deterioration in Pakistan's terms of trade and the likelihood of a delayed fiscal adjustment, the IMF and Bank are recommending that the country be given an additional year to reach the end-year program targets for the fiscal deficit and the external current account deficit. Nevertheless, the Government still will have to strengthen its adjustment effort and reinforce fiscal measures especially on the revenue side in order to reach these revised targets. However, the Government's FY90 fiscal strategy, as indicated by the budget approved by Parliament in June, relies heavily on containing expenditures. This is being done by nominally freezing military and administrative expenditures, marginally reducing allocations to the provinces, and holding development expenditure increases to slightly above the level of inflation. New revenue measures recommended in the budget were modest, amounting to about 1.1% of GDP. In addition to the undesirably low level of development expenditures, which should be viewed as a holding action until the new revenue measures take full effect, the budget raises the question of the attainability of the tight expenditure targets and the willingness of the Government to take corrective actions should overruns occur.

9. A Fund/Bank team visited Pakistan in May 1989 to review the adjustment program. It was unable to conclude the program review, since agreement was not reached on a viable fiscal scenario. Discussions between the Government and the Fund/Bank team resumed in Pakistan in late August and are scheduled to be completed by September 10. The information contained in this brief will be updated as soon as the mission produces relevant findings.

II. Issues Likely to be Raised by the Delegation

10. Cooperation and relations. Unless the current Bank/Fund mission evaluating the adjustment program results in a negative evaluation of program progress, it is unlikely that the Government will raise any contentious issues with you. Cooperation and relations with the Bank and the Government have been good and the Government has appeared satisfied with the content and level

of Bank lending. The Government would prefer a higher level of IDA financing, but the issue has been discussed with the Bank on several occasions and there is an understanding of the limitations on IDA resources. Bank economic and sector work have been well received and there is an appreciation of the Bank's role in chairing the Pakistan aid consortium. When Mr. Qureshi met with the Prime Minister in August, she expressed interest in receiving Bank assistance, much of it technical assistance, in dealing with a variety of problems, including education reform, establishment of women's centers incorporating family planning, employment, the feasibility of a tunnel linking the northern areas to the rest of the country, and public administrative reform. All of these matters are being reviewed by Bank staff and a comprehensive reply will be sent to the Prime Minister, advising her of the assistance that the Bank might be able to offer. (A copy of the reply will be available in an updating note.) If a question on this matter arises, it may be referred to the regional staff.

III. Issues to be Raised by Senior Management

(1) The Adjustment Program

11. It is likely that the fiscal targets of the adjustment program were not met in FY89 (see para. 7 above). Just how far the fiscal deficit exceeded program targets, the occurrence of other problems in the program and what modifications to the program may be required will be determined in the Bank/Fund review scheduled to be completed on September 10. As stated above, an updating note on the findings of the mission will be issued. However, no matter what the findings of the mission may be, it is virtually certain to recommend that in order for the Government to meet program fiscal targets and maintain a healthy growth in development expenditures, the Government will not only have to continue to curtail non-development expenditures, but it will also have to move more aggressively in mobilizing additional resources through changes in the tax structure. You may wish to emphasize the Bank's support for such policy recommendations and inquire about the prospects for the introduction of measures which would broaden the tax base and encourage provincial authorities themselves to raise revenues to finance provincial expenditures.

(2) Development Strategy and Program

12. In February this year the Bank held a program review meeting with the Government in Pakistan. The Government stated in the meeting that its development strategy had not as yet been fully articulated, but that it would be framed within the People's Party Manifesto, the SAF agreement with the IMF, the Seventh Five-Year Plan, and the planned budget statement. It was further stated that a six-point program to fight poverty was in preparation. Unfortunately, we have seen little progress on the adoption of a development strategy or priorities. In part, this has been related to the Government's preoccupation with macroeconomic matters, but in part it has also been due to a lack of economic leadership (the Prime Minister is still holding the Finance and Planning portfolio). The issue of leadership is a serious one and was raised by Mr. Qureshi with the Prime Minister during his recent visit to Pakistan. Although raising the leadership issue directly with the delegation

may not be possible, you may wish to inform it of the Bank's concern that the Government still does not have a clearly articulated and coherent development strategy. In this regard, you may also inquire about how the Government intends to pursue the recommendations that were contained in the Population Report which was discussed at the April consortium meeting. Specifically you may ask about the Government's plans to integrate population activities into the provincial Secretariats of Health and the Ministry of Health, as well as to how the Government intends to expand programs for family planning in the face of expenditure cuts in family planning activities of approximately 5% in real terms in the FY90 budget. We currently have under discussion with the Government a Women in Development Paper. The paper contains recommendations to increase investment in human infrastructure (education and health) as it affects women, for the removal of discriminatory laws and regulations, and for the provision of credit and marketing schemes to assist women entrepreneurs and workers. An update note will be prepared reporting on the Government's reactions to these and other recommendations. You may wish to follow up on these points in your discussion with the delegation.

PAKISTAN
FY90 - FY94 Lending Program
(in $ million)

Sector	Actual	----------Projected----------					Sector
	FY89	FY90	FY91	FY92	FY93	FY94 1/	Total
Agriculture							
Flood Restoration	40.0						40.0
Ag. Sec. Ln.	200.0						200.0
Priv. Tubewell	34.4						34.4
Agric Res. II		55.0					55.0
Agric Credit VII		150.0					150.0
Agriculture Env. Sector			50.0				50.0
On Farm Water Mgt			50.0				50.0
SCARP Trans. II (S)				50.0			50.0
Punjab Sal. Drg. (S)				75.0			75.0
ASAL II				150.0			150.0
Baluchistan Irrig. (S)					50.0		50.0
Grain Storage II					20.0		20.0
ASAL III					100.0		100.0
Agriculture					100.0		100.0
Sub-Total	274.4	205.0	100.0	275.0	270.0	0.0	1124.4
	(3)	(2)	(2)	(3)	(4)	0	(14)
Population & Human Resources							
Sind Primary Education		100.0					100.0
Family Health			30.0				30.0
Education Quality (S)				75.0			75.0
Education Unidentified					55.0		55.0
Sub-Total	0.0	100.0	30.0	75.0	55.0	0.0	260.0
	0	(1)	(1)	(1)	(1)	0	(4)
Infrastructure							
Karachi Water II	125.0						125.0
Transport Sector		200.0					200.0
Karatchi Port		103.0					103.0
Rural Water (S)			120.0				120.0
Shelter			70.0				70.0
Sind Cities				50.0			50.0
Highways VI					50.0		50.0
TSAL II					100.0		100.0
Urban Unidentified					50.0		50.0
Sub-Total	125.0	303.0	190.0	50.0	200.0	0.0	868.0
	(1)	(2)	(2)	(1)	(3)	0	(9)
Energy							
Energy Sec. Ln. II	250.0						250.0
Privatization of SNGPL		100.0					100.0
Rural Electrification		160.0					160.0
Transmission Extension		160.0					
Domestic Egy Dev.			160.0				160.0
Pvt. Sec. Egy II				200.0			200.0
Energy Cons (S)					100.0		100.0
Gas Project					50.0		50.0
Small Scale Hydro					100.0		100.0
Energy Sector Ln. III					200.0		200.0
Thermal Power (S)						100.0	100.0
Sub-Total	250.0	420.0	160.0	200.0	450.0	100.0	1420.0
	(1)	(3)	(1)	(1)	(4)	(1)	(10)
Industry							
FSAL	150.0						150.0
Ind. Inv. Credit III	150.0						150.0
Ind. & Trade Policy			150.0				150.0
Micro Enterprises			80.0				80.0
FSAL II/IIC IV				200.0			200.0
Fertilizer V					60.0		60.0
Engineering Industry					100.0		100.0
Sub-Total	300.0	0.0	230.0	200.0	160.0	0.0	890.0
	2	0	2	1	2	0	7
GRAND TOTAL	949.4	1028.0	710.0	800.0	1135.0	100.0	4562.4
	(3)	(8)	(4)	(5)	(10)	(1)	(30)

Note: Numbers in parenthesis are total number of projects.

1/ The FY94 lending program has not yet been approved.

6/21

1) ~~MH~~
2) ~~BBC~~
3) CP/MF - f
PAKistan

DATE: June 20, 1989

TO: EMENA Files

FROM: H. Eberhard Köpp, Director, EM1

EXTENSION: 33000

SUBJECT: Meeting with Prime Minister Benazir Bhutto on June 6, 1989

1. Mr. Conable met Prime Minister Bhutto on Tuesday, June 6, 1989, for about 30 minutes at the Blair House. The meeting was also attended by Mr. Minwala, Ambassador at Large, Mr. Izharul Haq, Secretary of Economic Affairs (EAD), Ambassador Marker, Ambassador Designate Zulfikar Ali Khan, Mr. Mueen Afzal, Economic Minister, Embassy of Pakistan, and by Messrs. Qureshi, Thalwitz and Köpp as well as Messrs. Al-Sultan and Faruqi.

2. In his opening remarks, the Prime Minister emphasized that her Government had tried to balance the books through the new budget as much as it could. This had been a difficult task for a new democratically elected government after so many years of dictatorship. She expressed her gratitude to the Bank and the Fund for relaxing the overall fiscal deficit target for 1989/90 under the adjustment program from 5.5 percent of GDP to 6 percent. She added that her Government was emphasizing in particular expenditure restraint. Mr. Conable responded by emphasizing the importance of fiscal deficit control not only for the assistance program from the World Bank but equally importantly for establishing credibility with other donors to enlist their support. Mr. Conable said he was aware of the difficulty of balancing fiscal restraint with the need to meet social concerns. He congratulated the Prime Minister for her Government's strong efforts in this respect and for the fact that the new budget permitted continuation of a strong development program despite the austerity nature of the budget.

3. The Prime Minister mentioned that the Government had hired tax consultants to get advice on improvements in tax administration. As to new taxes, she stated that the Constitution did not permit the federal government to tax agriculture. Therefore, she had indicated to the provinces that the central government would not cover the provinces' deficit; the latter would therefore have every incentive to mobilize additional resources on their own, e.g., in agriculture. Mr. Conable confirmed that raising additional resources on both federal and provincial levels was extremely important in order to have a realistic chance to meet the fiscal deficit reduction target of 6 percent next fiscal year. He added that a Fund/Bank Mission would visit Pakistan in August to review the budget in detail, including expenditure control and revenue enhancement measures. In this context, he stressed the excellent cooperation between the Bank and the Fund. Mr. Qureshi added that he very

much welcomed the incentives given to the provinces to mobilize additional resources; he felt, however, that the provinces should also be given commensurate responsibilities for implementation of social programs. Mr. Conable expressed his hope that the dialogue with the new Government would continue to be excellent. He indicated that he had full confidence in the Bank staff working on Pakistan and encouraged the Government to talk in a frank manner to them. They would ensure that the Government's messages and concerns would reach the top management of the Bank.

5. In response to Mr. Conable's question regarding the Afghanistan refugees situation, Mr. Minwala pointed out that the Government had been disappointed with the low level of pledges for the Afghan refugees at the Paris Consortium Meeting and the fact that no further pledges had been received yet, contrary to expectations. He suggested that the Bank might call a special meeting of the Consortium for Afghanistan refugees to perhaps work out an "emergency plan". Mr. Thalwitz responded that in Paris some donors had not been in a position yet to make formal pledges but had given positive indications of support. Mr. Thalwitz renewed the Bank's promise to write to the Consortium members some time in July to inform them of the results of further consultations between the Pakistan Government and the Fund/Bank. He felt that it would be more practical to include in this letter to the Consortium members also a plea for pledges for the Afghanistan refugees. It was agreed that this matter be discussed further with Mr. Minwala.

6. In response to the Prime Minister's request for some feed-back from the World Bank on the budget (which had been submitted to the National Assembly on June 3), Mr. Thalwitz said that the Bank and Fund had had only limited information on the budget and only 24 hours to review it. He indicated that obviously the Government had made a serious effort to reach the target of 6 percent of GDP in the coming fiscal year. He also thought the Government had gone very far in successfully coping with the political constraints and based the budget on a realistic balance between expenditures reduction and revenue increases. At this stage, the Prime Minister interjected that the Government was trying to increase the financing of development from savings. She also mentioned that the interest rate for the domestic debt of the Government had been reduced from 15 percent to 12.5 percent. Mr. Qureshi emphasized that it was most important to deal directly with the domestic debt problem. Mr. Conable added that this was also important as a measure to avoid the crowding out of the private sector. Mr. Thalwitz finally added that the Bank also had some reservations and concerns with regard to the budget (time did not permit to specify these).

7. The Prime Minister then turned to the Lending Program of the Bank for Pakistan and expressed the hope that the recent decision of the Bank to allocate funds to the Brady Plan debt reduction scheme would not divert funds from those countries which had performed well, such as Pakistan. Mr. Conable assured her that only a modest amount had been allocated for this purpose and that this would have no impact on the resources available for those countries. He added that the Bank intended to stabilize its Bank/IDA lending program at a level of $800 million. In this respect Mr. Minwala asked the Bank to consider increasing the IDA share from currently about 20 percent to about 50 percent in view of the Government's intentions to increase substantially the support to the social sector. Mr. Conable reminded the Prime Minister and Mr. Minwala of the serious IDA resources constraints and indicated that therefore he could

not make any promises. He mentioned, however, that most social sector projects currently envisaged for Bank financing in Pakistan would be financed with IDA funds. Mr. Qureshi added that the FY89 IDA contribution had included an additional emergency credit of $40 million for flood rehabilitation. He stressed that a way must be found to base social sector programs on domestically mobilized resources. He added that the Bank shared the high priority given by the Government to social subsectors such as education, health and rural electrification.

8. The Prime Minister then emphasized the need to improve the role of women. She felt it was not enough to have programs for enhancing literacy and family planning. It was important to give women better economic opportunities. Her Government was therefore considering to establish "work houses for women", e.g., to produce radio and TV sets, which would also have day-care centers to take care of children and at the same time educate them. Mr. Qureshi responded that the Bank and especially the President shared the Government's concern and would in general be delighted to support programs focussing on women.

9. In closing, the Prime Minister stated that in the absence of the Bank's and Fund's strong support, the Government might have been much less determined to initiate and continue the needed adjustment process and more inclined to increase spending. She added that she was grateful for the support and was looking foreward to a continued excellent cooperation with both institutions.

Cleared with and cc: Mr. Thalwitz

cc: Mr. Conable
Mr. Qureshi
Mr. P. Hasan
EM1 Management Team

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

WH / BBC

DATE: March 8 1989

TO: Wilfried Thalwitz SF

FROM: Stanley Fischer

PHONE: 33774

SUBJECT: Back-to-Office from Pakistan.

1. I was in Pakistan for three days, from March 2-4 as the guest of the State Bank, mainly to deliver on March 2 the annual Zahid Husain Memorial Lecture, a copy of which is attached. March 3 the State Bank took me to Moendejaro to see the sights. We had lunch in the provincial town of Larkana, which was very interesting, and after lunch went to visit the Bhutto family village and tombs. On Saturday March 4 I was in Islamabad, under the care of Luis de Azcarate.

2. Although I was formally the guest of the State Bank, I did not get much information about the economy from them (but they were very attentive hosts). The Governor was out of the country and the Deputy not very self-confident about the economy. Janjua, the Economic Adviser, who seemed to be on top of things, is concerned about the external accounts and the budget -- which is heading for a deficit of about 7% of GNP -- and is pleased with the conditionality in the FSAL.

3. Luis de Azcarate held an interesting lunch, where we talked about the population problem and heard the confident view that there was no religious or societal objection to mounting a birth control campaign, provided it was sensitively done.

4. I had brief chats with Jafarey (in the VIP lounge in the Karachi airport) and with Kazi, who chaired the lecture I gave in Islamabad. They and other officials to whom I spoke professed not to worry about missing Fund targets on the budget, but to be more worried about the external situation. Although my Islamabad lecture (the attached, on the economics of the government budget constraint) went down well, I don't think they take the macro threat very seriously. They did seem worried about inflation but weren't sure why it was there (this is a standard stage in an inflationary process). No-one believed they could raise more taxes, nor could they cut spending (another standard stage). You may have to be a real nag when you are there.

5. At lunch at Luis de Azcarate's, I met Mr. Mohibullah Shah, who is Assistant Secretary in the PM's Secretariat, and in charge of economic and financial matters referred to the PM from elsewhere in the government. He pushed me quite hard on the possibility of stepping up

annual lending to $1 billion. He claims to have looked at some numbers and concluded that Pakistan isn't getting its fair share. I expect you will have to deal with this issue during your visit.

6. Attached is a draft letter I will send him, saying you have been informed of our discussion and that I expect you will deal with the issue when you are there. Please let me know if you have any objections or whether I should go ahead.

7. One important point that emerged from talking to Luis de Azcarate and to some of your people before I left is that they all think the PFP process for Pakistan was highly successful. They said that it had taken a lot of work with the Fund, which had put far more resources (five trips) into this document than into their usual agreements with countries. I think it is a good document, which is far more realistic in the pace at which it proposes attacking the budget problem than the normal Fund approach would be. It might be useful to think of PFPs in other countries as giving us an opportunity to influence the Fund's program in a constructive and pro-development way.

8. The impression given by reading the newspapers is that the politicians don't understand how to operate in a democracy. The LBJ precept "Don't spit into the soup because we all drink from the same bowl" appears not to be part of their code of behavior. This may all be understandable given recent history, but is still very bothersome. I was also surprised during my visit to Sind to discover that the roads are unsafe after dark (and also before dark sometimes), and that everyone knows which leading figures are engaged in dacoitry but that nothing can be done about it.

cc: M/M Conable, Hopper, Qureshi, Husain, Kopp, Haug, Linn, de Azcarate, Cohen.

(cc.s w/o att.)

Name of Country: PAKISTAN   Date: September 2, 1988

Meeting with: Dr. Mahbub ul-Haq, Federal Minister of Finance

Population: 101 m January 1987 Estimated Growth Rate 3.1% (1965-86)
GNP per capita: $360 (1987)

	($million)
Total Commitments to date:	5,913.2
Bank (no. of operations and value) 65,	2,855.6
IDA (no. of operations and value) 105,	3,057.6
Total Undisbursed:	2,363.1
Lending Program: FY89-90	1,658.0

	($million)
FY88 Commitments:	466.9
Disbursements:	364.0
Amortization:	51.4
Net Disbursements:	312.6

Summary Data	Average FY83-87	FY88
GDP growth (%)	6.8	5.3
Export Growth	8.6	12.3
Import Growth	5.1	4.9
Current Acc. Deficit % GDP	3.3	2.7
Gross Debt Service Ratio	21.2	27.0
Annual Inflation Rate	5.5	6.5

: Aid Group Meeting: Consortium
: Last Meeting: April 21/22, 1988
: Last Article IV Consultation:
: August 1987
: Next IMF Visit: September 1988

Background: Bank/Fund/Government have made progress in the negotiation of a draft PFP. The Government's June budget message contained measures which would reduce the budget deficit from 8.5% of GDP in 1988 to 6.5% of GDP in 1989. Other measures pertinent to a satisfactory medium-term economic framework also were announced. Unfolding political developments in the wake of President Zia's death will reveal the likelihood of adoption of the full FY89 budget and other economic measures.

Issues Likely to be Raised by Delegation

The delegation is likely to press for two sector loans in the FY89 lending program and is likely to ask that they be increased in size.

Issues to be Raised by Bank Management

1. Outstanding issues, if any, which would adversely affect processing of the Bank lending program.

2. The Government should provide adequate funding for development projects.

3. How does the Government anticipate that the transition between Governments will take place?

Attachments:
Five-Year Lending Program: FY88-92 (FY88 actual)
Biographical Information

2828I pp.14-15

Typewritten Character Must Fall Completely in Box!

PAGE 1 OF 1

OFFICIAL DEPT/DIV ABBREVIATION: SVPOP

MESSAGE NUMBER

TEST NUMBER (FOR CASHIER'S USE ONLY)

START HERE

HIS EXCELLENCY MAHBUB UL HAQ

Country File

MINISTER OF FINANCE, PLANNING AND COMMERCE

ISLAMABAD, PAKISTAN

I HAVE SENT THE FOLLOWING TELEX TO PRESIDENT ZIA-UL-HAQ.

QUOTE I AM VERY PLEASED TO INFORM YOU THAT IN VIEW OF THE MEASURES THAT YOUR GOVERNMENT HAS RECENTLY ADOPTED TO REDUCE THE OVERALL BUDGETARY DEFICIT AND TO REFORM TRADE POLICIES, I AM RECOMMENDING TO THE BOARD OF DIRECTORS OF THE WORLD BANK THAT WE PROCEED WITH A QUICK-DISBURSING LOAN OF DOLLARS TWO HUNDRED MILLION IN SUPPORT OF THE AGRICULTURAL SECTOR. I EXPECT THIS MATTER TO BE CONSIDERED BY THE BOARD ON AUGUST 2. THESE GOVERNMENT ACTIONS OPEN THE WAY FOR FURTHER COLLABORATION ON A MEDIUM TERM FRAMEWORK FOR PAKISTAN'S DEVELOPMENT WHICH I HAD THE PLEASURE OF DISCUSSING WITH YOU DURING MY VISIT TO YOUR COUNTRY UNQUOTE

I WISH YOU SUCCESS IN THE IMPLEMENTATION OF THE MEASURES OF FINANCIAL AND TRADE POLICY REFORMS THAT HAVE BEEN INTRODUCED.

BEST REGARDS, BARBER CONABLE, PRESIDENT, WORLD BANK

DATE: JULY 14, 1988

EXTENSION: 73665

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...ble / Barber Conable

USE OF CABLE SECTION

THE WORLD BANK

July 14, 1988

Mr. Conable:

The Government has taken a whole series of measures along the lines we had recommended. I think it would be a good gesture of support if a message could be sent along the lines I have drafted for you.

Moeen

MOEEN A. QURESHI
Senior Vice President, Operations

11:45

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: April 14, 1988

TO: Mr. Barber Conable, President

FROM: Wilfried P. Thalwitz, Vice President, EMENA

EXTENSION: 3-2676

SUBJECT: PAKISTAN - Briefing Note for Your Meeting with Dr. Mahbub ul-Haq, Minister of Commerce and Planning on April 18, 1988, at 11:45 a.m.

As I told you today, we have prepared a preliminary assessment of the Government of Pakistan's medium-term program as presented in their submission for the Pakistan Consortium. The attached assessment may be useful background for your meeting with Mahbub ul-Haq.

Attachment

cc: Mr. Köpp (EM1)

OFFICE MEMORANDUM

DATE: April 13, 1988

TO: Wilfried P. Thalwitz, EMNVP

THROUGH: Hans-Eberhard Köpp, EM1DR

FROM: Michael A. Cohen, Chief, EM1CO

EXTENSION: 32756

SUBJECT: Pakistan: Assessment of Proposed Medium-Term Program

Summary

1. The Government's new proposals, as contained in its Development Policy Agenda, 1988-89/1990-91, represent a major step forward in the Bank-GOP dialogue. The fact that the GOP has prepared the document is itself a positive indication of the GOP's interest in working out an agreement. In addition, the major policy initiatives and important components of the macro-economic framework which are presented in the document are in line with the Bank's recommendations.

2. It should be noted that the Government's formal endorsement of the policy agenda cannot be made before June, with the approval of the Seventh Plan and the FY89 Budget. Therefore, the document does not contain the details of the GOP's programs, including the sequencing, timing, and specific content of the individual policies. Nonetheless, it presents the authorities' intent to change the macro-policy stance for the better and embark on major structural reforms. At this point, it is the maximum that we can expect.

Assessment

3. The Government's new proposal calls for a similar magnitude and pace of fiscal deficit reduction as that of the Bank:

Fiscal Deficit as % of GDP	FY89	FY90	FY91
Original GOP	6.9%	6.0%	5.6%
Revised GOP	6.3%	5.3%	4.9%
Bank	6.2%	5.5%	4.8%

- The new GOP proposals rely on larger current expenditure cuts to achieve the larger deficit reduction. In addition, the GOP has kept its original intention to reduce development expenditures (ADP) as a percent of GDP (from 7.0% to 6.7% in FY91). The revenue effort--a modest one to begin with--remains essentially unchanged.

- For FY89, the GOP is now proposing to freeze non-development expenditures, including defense, at their FY88 nominal levels. (In subsequent years, defense and general administration would grow less than social and economic services in real terms.)

- This is an acceptable way to proceed. However,

  (a) While an expenditure freeze is inevitable in the first year, an effort should be made in subsequent years to prioritize programs and projects in a manner which will not materially damage development prospects.

  (b) We would prefer to place more emphasis on revenue generation, and less on cuts in ADP and in non-defense currrent expenditures, to protect the development-related part of the program.

4. For the period FY89-91, the GOP's <u>current account deficit</u>, relative to GDP, is similar to that projected by the Bank.

	FY89	FY90	FY91
GOP (est.)	2.6	2.7	2.5
Bank	2.6	2.5	2.4

GOP's projected buildup of gross reserves is substantially lower than that envisaged by the Bank.

	FY89	FY91
GOP (weeks of imports)	2.7	5.3
Bank	4.7	6.2

With reserves of only about $500 million, or just over 3 weeks of imports, at the end of FY88, the GOP's reserve estimate for FY89 leaves insufficient flexibility for Pakistan to respond to unforeseen external shocks.

- While we agree with the Government's current account deficit level, we are concerned about its over optimistic export projections (10.4% annual average real growth for FY89-91 vs. the Bank's 6.6%). Should export growth be lower than projected, it would still be possible to contain the current account deficit, but only with lower import growth than the Government is now projecting (5.2% annual average for the GOP vs. 2.9% for the Bank).

- The GOP's financing requirements appear insufficient to ensure an adequate buildup of reserves, especially in FY89. While their financing projections are similar to those of the Bank, Bank projections assume the availability of SAF and standby resources from the IMF. In the absence of these, other sources of fast-disbursing assistance would be needed.

5. The GOP's real GDP growth rate for FY89-91 is higher than the Bank's recommendation--6.5% vs. 5.5%. For FY89, a 6.5% growth rate is reasonable, because of the anticipated recovery following the crop failures of FY88. While we would not object to such rapid growth in subsequent years, provided that appropriate policy changes are made, it is our conservative judgment that such a high growth rate in later years would not be compatible with the needed policy adjustment--notably the fiscal deficit reduction effort and the necessary expansion in capital-intensive investments to renovate and expand public infrastructure systems and social services. Such high GDP growth also requires rapid import growth, which is only possible if exports grow as fast as present GOP projections.

6. The proposed sectoral policy reforms (trade, regulatory and financial, as well as agricultural, irrigation, energy, urban, and transportation sectors) are substantially the same as the program recommended in the Policy Framework Paper. The stated stance on trade policy reforms clearly reflects the post-PFP discussion with the authorities.

Issues to be Raised in Further Discussions with GOP

7. Achieving the Fiscal Deficit Targets. Historically, deficit targets have not been met because of expenditure overruns and revenue shortfalls. While an initial freeze on expenditures is appropriate, in order to control expenditures, the Government will need to give more attention to monitoring. Expenditures are also subject to the risk of military spending overruns. With defense taking up such a large share of current expenditures (35%), unexpected defense demands could seriously disrupt the Government's expenditure program. In light of these problems, it may be optimistic for the Government to rely so much on expenditure control relative to revenue mobilization unless accompanied by a stronger expenditure control system. The new revenue measures now being proposed by the Government are similar to those of the Bank. We believe that, if implemented fully, they would generate more revenues than the Government is now projecting equivalent to an additional 0.9% of GDP over three years). Therefore, the Government should concentrate on both getting the political support for its revenue program and its early and effective implementation.

8. External Financing. For the Government's program to work, it would require more fast-disbursing funds than is now presently projected. The GOP is now assuming one fast-disbursing loan apiece from the ADB and the Bank every year. We estimate that about $500 million more is needed over the next three years, starting in FY89, to build up reserves to an acceptable level. This could come from the IMF or from other donors, or from a second fast-disbursing loan from the Bank.

9. Political Uncertainty. While this proposal represents considerable progress at the technical level, its political feasibility still very much depends on legislative debate on the budget in June. This debate could significantly change the basic framework of the proposal, including the prospects for revenue generation, expenditure control, and key sectoral policy initiatives. In addition, the laudable effort to reduce defense expenditures remains dependent on exogenous factors. The ability of the Government to resist requests for additional defense spending is unknown.

10. In view of the political risks, we return to the need for a cushion in order to achieve the budgetary targets.

Proposed Stance at the Consortium

11. The GOP proposal, while a major step forward, is still a proposal which needs the formal endorsement of the Government. Therefore, the Bank should stand firm in waiting for an approved budget in June which contains the above elements, before deciding on the level and composition of Bank lending. At the consortium, we should offer constructive appreciation of the Government's new proposals which respond favorably to the Bank's concerns for the need for a medium-term framework. At the same time, you should note that the success of the Government's program is dependent on a set of accompanying policies and measures at both the macro- and sectoral levels. Our summary assessment should therefore be hedged, because the Government's ability (1) to put the program in place and (2) to implement it are both subject to considerable uncertainties.

cc: Mr. P. Hasan; EM1CO Staff

11:~~00~~
4/18 @ _pm

PAKISTAN

1. In view of Mr. Thalwitz's report, what is the proposed Bank position at next week's Pakistan Consortium meeting:

   - What did we tell the co-financiers;

   - On what basis will we negotiate ~~as noted by Mr. Thalwitz's para.~~ with the Pakistani

2. Lending level for FY88 - Will we proceed with the Agriculture Sector Adjustment Loan?

Update to Country Strategy Paper on Pakistan

Macroeconomic Update

1. As agreed at the 1987 Annual Meetings, Mr. Thalwitz and EM1 staff visited Pakistan from February 28 to March 4 to meet Government to review: 1) the status of the FY88 budget, 2) the progress in preparation of tax reform, and 3) the proposed medium-term program for policy reform. This visit followed intensive discussions between the Bank and the IMF on a Policy Framework Paper and review of the Pakistan Country Strategy Paper (CSP) by the Operations Committee on February 17, 1988 (minutes attached). The same adjustment scenario had been proposed in the PFP, CEM, and CSP and therefore provided a consensus against which GOP performance and proposals could be assessed. This assessment was intended to provide the basis for discussions on the level and composition of Bank lending to Pakistan.

2. Prior to the mission's arrival, the IMF mission had concluded that, in view of its strong FY87 and FY88 balance of payments position, Pakistan did not qualify for a SAF. The requirements for a SAF included "protracted" problems--past as well as present--on the external account. The IMF and Government did agree, however, that an IMF mission would return to Pakistan in late April 1988, following the Consortium, to consider a proposed Standby Agreement.

3. The mission met the Prime Minister, Muhammad Khan Junejo, the Minister of Finance, Mian Mohammad Yasin Khan Wattoo, the Minister of Commerce and Planning, Mahbub ul-Haq, the Deputy Chairman of the Planning Commission, Mr. A.G.N. Kazi, the Governor of the Central Bank, Vasim Jafery, and the Secretaries of Finance, Economic Affairs, Planning and Commerce and thus was provided authoritative views on the present situation and prospects for reform.

4. The Government made the following points to Mr. Thalwitz with respect to the <u>current year</u>:

A. GOP has been unable to maintain its FY88 budget deficit target of 7.6% of GDP, allowing expenditures to increase, resulting in a projected end-year deficit of about 8.3% of GDP compared to 8.9% in FY87. Nevertheless, the projected current account deficit, at 2.5% of GDP, is better than originally expected because of growth in cotton-based exports.

B. Preparations are underway for tax reform, although reform proposals, while in the right directions, are not projected by GOP to lead to major revenue improvements.

C. A medium-term program had not been prepared (despite written and verbal assurances to Mr. Conable).

The Government's presentation for the Seventh Plan period FY89-FY93 consisted of the following:

A. The GOP proposed deficit reduction at a slower pace than the Bank/IMF scenario, beginning with a deficit target of 6.9% of GDP for FY89 and arriving at 4.8% by FY93.

B. A gradual restructuring of the revenue base would occur, introducing a value-added tax and possibly an agricultural land tax, while reducing taxes on trade. This would not, however, lead to a substantial increase in domestic resource mobilization. According to GOP projections, the tax/GDP ratio would increase from 13.1% to 13.8% from FY89 to FY93. Government, particularly the Prime Minister, expressed caution about the likelihood of substantial new revenue measures receiving parliamentary approval.

C. Even with a planned increase in the domestic savings effort, GOP proposed greater reliance on foreign financing. This is reflected in a current account deficit of 3.3% of GDP for FY89-FY91, declining to 2.5% in FY93, as compared with the Bank's recommendation of 2.4-2.6% for the period. The GOP's proposal implies a very large increase in net public disbursements ($1.34 billion on average for FY89-FY93 versus $0.780 billion for FY85-FY88). The external position would further require additional commercial or short-term borrowing of about $200 million per year if reserves were to be increased to $2 billion (10 weeks of imports) by FY93. With such a scenario, the debt service ratio would be over 25% and rising by FY93.

5. These conclusions are of great concern, because they clearly affect creditworthiness. Although the Government's deficit reduction strategy is in the right direction, the feasibility of achieving the deficit targets is questionable. For the past two years, the actual deficits have been almost 1% higher than targeted. In addition, more expenditure control exceeding present Government plans is likely to be needed. The Government's balance of payments projections reflect unrealistic expectations concerning the disbursement rate from new commitments. The rapid growth of imports incorporated in the current account projections also may not be realized because of optimistic manufacturing export growth assumptions.

6. Bank concerns on both the fiscal deficit and current account deficit, including their unrealistic underlying assumptions, were expressed to the Prime Minister, the Ministers of Finance and Planning, and the Secretaries. Emphasis was placed on the need for "cushions" in planning to achieve budgetary targets, particularly in light of historical performance and uncertainties in both the external environment and the domestic economy. The pitfalls of relying on reducing tax evasion rather than broadening the revenue base through introduction of new taxes were discussed. Alternatives, such as holding defense expenditure constant in nominal or even real terms, were

explicitly raised. While GOP officials clearly understood and appreciated the need for cushions, they indicated limited room for maneuver in the face of expected parliamentary opposition. The Prime Minister, however, indicated that the Government would give "serious consideration" to limiting defense expenditure, which accounts for about 35% of current expenditure, as part of budgetary control.

7. In view of the above findings, Mr. Thalwitz indicated to GOP that the Bank would have to wait until the FY89 Budget was approved in June 1988 to evaluate whether GOP had managed to formulate and gain political support for a sustainable medium-term program. Presentation of the $200 million Agricultural Sector Loan to the Board in FY88 would be contingent on receiving a satisfactory FY89 Budget. In the interim, the Pakistan Consortium would be held in Paris on April 21-22, 1988, and, for the Bank to adopt a constructive stance, it would be helpful for the Bank to receive the proposed program by early April, understanding that it would not have parliamentary approval. The Minister of Planning, Mahbub ul-Haq, promised to send the program to the Bank at that time.

8. Prospects. While the FY88 fiscal situation is somewhat worse than at the writing of the CSP and the Government's Seventh Plan strategy disappointing, it is premature to make a judgment about the final outcome. The Bank's message was clearly received. The visit seems to have generated renewed debate in Islamabad and more clearly defined the stakes involved, particularly in fiscal policy. We believe that negotiation is still possible. Informal reports suggest that revised assumptions for the Seventh Plan are being developed using a current account deficit of about 2.8% of GDP for FY89-91. A current account deficit of this magnitude, coupled with a fiscal deficit reduction target below 6.9% of GDP for FY89 and further subsequent reductions, would bring the country closer to Scenario B than to Scenario A. This would be a positive, if less than optimal, outcome. The Consortium meeting will provide the next occasion for negotiation.

9. The Government essentially has until June 1988, when the FY89 budget is presented and approved, to delineate its program in concrete terms. The National Economic Council also is scheduled to review the Seventh Plan for approval in June. Meanwhile, the Government is soliciting broad-based support for the Plan. In addition to submitting the draft Plan to a parliamentary committee, the GOP is undertaking high-level discussions with the provincial governments.

10. Consequently, it is recommended that the Bank's lending posture be determined only after the FY89 Budget is approved. The Government's receptivity to an IMF Standby during an IMF visit in late April would provide an earlier indication of the prospects for reform. However, agreement with either the IMF or the Bank would depend on actions contained in the FY89 budget.

Exposure Indicators

11. As noted in the minutes of the Operations Committee of February 17, 1988, the Region and the Risk Management and Financial Policy Department (FRS) have agreed on the exposure indicators and financing plan for FY88-95. The revised exposure indicators are presented in the attached Table 4. Table 3, on external capital requirements, remains unchanged.

12. The exposure indicators (Table 4) have been modified in the following ways:

(a) The IBRD share in total public MLT debt outstanding and disbursed (DOD) has increased. This is because the FY87 IBRD debt stock, from the Financial Data Base, reflects the current market value, rather than the historical book value. In addition, total public DOD has been redefined, to exclude short-term debt as well as private non-guaranteed debt.

(b) The IBRD share in total debt service and IBRD debt service as a percentage of current account receipts have fallen substantially. The IBRD interest rate originally used by the Region exceeded the FRS interest rate projections plus commitment fee.

(c) The share of public and publicly-guaranteed MLT debt to preferred creditors remains above 33% until FY93, although the estimates have fallen slightly.

13. As a result of the upward adjustment to the IBRD and multilateral debt stock from exchange rate changes, a revised debt table (Annex Table 4) is also attached.

Revised Table 4: IBRD EXPOSURE RATIOS, FY88-95

	FY88	FY89	FY90	FY91	FY92	FY93	FY94	FY95
DOD: IBRD/Total Public MLT /a	8.1	10.0	12.6	15.1	16.6	17.6	17.9	17.9
Debt Service: IBRD/Total Public /a	8.7	9.6	11.1	14.1	18.8	19.8	22.2	24.1
Preferred Creditors DOD/MLT DOD /a	31.7	33.3	34.0	34.2	33.5	32.5	31.9	31.3
IBRD Debt Service/Current Account Receipts	2.1	2.3	2.5	2.9	3.7	3.9	4.2	4.3

/a Includes IMF.

March 25, 1988

2825I p. 21

Revised Annex Table 4: Pakistan -- Summary of External Debt Outstanding and Disbursed (Base Case)

(US$, Million)

	Est.	Projected								
	FY86	FY87	FY88	FY89	FY90	FY91	FY92	FY93	FY94	FY95
Official Conces. Debt	9382	9713	10010	10322	10631	10914	11264	11642	12016	12386
Of which: IDA	1491	1650	1879	2146	2382	2604	2808	2999	3180	3349
Official Non-Conces. Debt	1164	1211	1495	1840	2273	2741	3237	3800	4428	5117
Of which: IBRD	506	739	1019	1340	1782	2259	2601	2867	3064	3273
Other Non-Concs. Debt	757	636	492	399	267	208	243	299	376	500
Total Public MLT Debt \a	11439	11742	12087	12595	13232	13926	14760	15647	16571	17822
IMF DOD	1168	875	550	817	957	1015	883	671	529	468
Private MLT Debt	132	132	132	215	213	234	316	420	541	634
Total MLT Debt (Incl. IMF) \a	12739	12749	12769	13627	14402	15175	15959	16738	17641	18924
Short-Term Debt	1651	2064	2296	2268	2280	2292	2304	2316	2328	2340
Total External Debt \a	14390	14813	15065	15895	16682	17467	18263	19054	19969	21264

\a Adjusted for exchange rate changes.

March 25, 1988

10/14
4:30

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: October 13, 1987

TO: Mr. Barber B. Conable, President

THROUGH: Moeen A. Qureshi, SVPOP

FROM: H. Eberhard Köpp, Director, CDI, EMENA Region

EXTENSION: 33001

SUBJECT: PAKISTAN: Visit by Dr. Mahbub ul Haq

1. Dr. Mahbub ul Haq, Minister for Commerce and Planning and Development, Government of Pakistan, is visiting Washington October 12-15, and has requested to meet with you to discuss the Prime Minister's national programme for the shelterless and the Seventh Plan Strategy.

Macro-Economic Policy

2. As you know, during the Annual Meeting the GOP responded to your July 1987 letter through a letter from the Ministry of Finance. The letter and the GOP delegation reiterated the commitments made to Mr. Qureshi during his September visit to Pakistan. These commitments included: a serious effort to maintain the FY88 budget deficit no higher than 7.5% of GDP, vigorous preparation of tax reform, a decision to develop a two- to three-year, medium-term plan within the context of the Seventh Five-Year Plan to be initiated in July 1988, and continued progress on de-regulation and trade liberalization. It was agreed that the Bank and GOP would jointly review progress in these areas in February 1988, with the outcome of the review determining the level of Bank lending for FY88, including whether to present the Agricultural Sector Loan to the Board. Even though Dr. Haq did not attend the Annual Meeting, he participated in discussions with Mr. Qureshi in September and is therefore aware of these commitments. All of the above measures have direct impact on the objectives and resources available for the Seventh Plan, for which Dr. Haq is responsible.

3. In Mr. Thalwitz's meeting today with Dr. Haq, the Minister elaborated on the above commitments of the Government. He outlined the major features of the two- to three-year plan, including increased domestic resource mobilization, shifting public sector agencies off the public budget,

deregulation of the financial sector, development of sectoral reform plans, and a financial strategy for social sector programs. The proposed plan would be reviewed by the National Economic Council in early January 1988, and would be presented to the Bank in February. Dr. Haq invited the Bank to participate in a "brainstorming" session on the Seventh Plan at that time. While we welcomed the opportunity to participate in such informal, technical discussions, Mr. Thalwitz reiterated the importance the Bank would attach to the assessment of FY88 budgetary performance and progress in definition of the medium-term program at that time. Dr. Haq agreed on the difference between assessment and "brainstorming".

4. During a working session with the staff of the Country Department, Dr. Haq was briefed on the findings of sector studies on trade policy, industrial regulation, and financial deregulation. He invited the Bank to participate in a December 1987 GOP meeting with representatives of the Government of Turkey to discuss the Turkish experience with trade liberalization. At that time a seminar would also be held on Bank sector studies.

Support for Shelter

Context:

5. Pakistan is rapidly urbanizing, but has been unable to provide adequate shelter. Twenty-five percent of an estimated 31 million urban population live in informally organized, badly serviced and untenured "katchi abadis", or slum areas. There are, in addition, some 2.2 million landless rural families. In December 1985, the Prime Minister announced a Five-Point Programme (1986-90) to address the needs of the poor through improved education, health, water supply, rural infrastructure, and housing. About US$200 million was committed to housing through two programs: urban "katchi abadis" improvement, including infrastructure and land tenure, and "seven marla scheme" comprising 1,575 square feet plot land allocation and housing for the landless rural poor. Although the Five-Point Program has been well-launched in education, it has been less successful in housing, where there has been: (a) lack of a clear strategic framework for implementation; (b) insufficient previous experience in low-cost shelter; and (c) insufficient financial resources.

Previous Bank Support to the Shelter and Infrastructure Sector:

6. The Bank has supported the urban shelter and infrastructure sector through (a) three earlier water supply and sewerage credits (Lahore and Karachi), and one under preparation for Karachi; and (b) two urban projects currently under implementation in Lahore and Karachi. A proposed Punjab Urban Project (FY88) has recently been appraised and includes slum upgrading in four Punjab cities. A rural water and sanitation sector mission is currently in Pakistan to lay the basis for a proposed lending operation in FY90. Within our urban sector strategy for Pakistan, two further operations are planned for Sind and Punjab up to FY92.

7. Since the mid-1970s, the Bank has been urging the GOP to adopt an affordable approach to land tenure and infrastructure standards. The issue of cost recovery for urban services has remained a stumbling block. Recently, GOP has begun to accept more affordable standards, which has led to modest housing components in our urban operations. The Punjab Project originally included "katchi abadi" upgrading, but GOPunjab advised us that Bank involvement was not required. In the ongoing Karachi Special Development Project, the upgrading component has experienced implementation difficulties.

8. Dr. Haq formally requested Bank support of a new initiative by the Prime Minister to create a "One Million Homes" program to address the needs of the shelterless. This initiative is modeled on the very ambitious program in Sri Lanka, which has been supported by five external donors, including the U.S. The Pakistan proposal involves 1) sites and services schemes in rural and urban areas, 2) establishment of a National Housing Authority and provincial authorities, 3) creation of a system of savings and loan associations, and 4) formulation of a shelter strategy for the Seventh Plan. At first glance, however, the proposal does not seem to have a realistic approach to subsidies, infrastructure standards and implementation arrangements.

9. Dr. Haq was aware that extensive Bank experience in this sector would be very helpful on all components of the initiative. Technical staff met with Dr. Haq and will hold a working session with him on Thursday, October 15. We will try to send a mission to Pakistan before the end of the calendar year to determine how we can be helpful to the Government. (Regional urban staff are presently completing the appraisal report for the Punjab Urban Project and plan to hold negotiations in late November.) Until then, we will formulate an agenda of issues which such an initiative would have to address.

cc: Mr. W. Thalwitz, Vice President, EMENA

The World Bank
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

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(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

July 30, 1987

Mr. Muhammad Khan Junejo
Prime Minister
Government of Pakistan
Prime Minister's Secretariat
Rawalpindi

Dear Mr. Prime Minister:

As you are aware, there has been a very close association and cooperation between Pakistan and the World Bank, almost since the country's inception. We in the Bank feel privileged to have provided support for your country's efforts towards economic development, and I share with my staff the view that Pakistan's growth record has been impressive. Progress has been made on many fronts and it is our hope, as I am sure it is yours, that this trend is maintained in the future.

I write to you at this time because I have become increasingly concerned about recent trends in economic management and wish to share these concerns with you. Over the past few years, we have observed an overall decline in investment in the country's future. The impressive returns which have been realized from private sector investment in the recent past result in part from the large public investments that were made in infrastructure and other capital stock in previous years. We now see Pakistan facing a deteriorating infrastructure which threatens to deprive the country of the benefits from its agricultural and industrial potential.

Future growth in Pakistan requires a new cycle of investment. This necessarily demands an increased effort to generate new resources through public savings. The government must seek ways to reverse the recent declining trends in savings. The shortage of funds appears most critical just at the time when you have initiated important new programs, particularly your Five Point Program, with its welcome emphasis on the social sectors. We believe, however, that success in these initiatives ultimately depends on sound macro-economic management as well as realistic sectoral policies.

Looking at Pakistan's external sector, it is apparent that a vulnerable balance of payments structure, with a narrow export base and heavy reliance on remittances, endangers the country's ability to meet its external obligations. In this context, past budgetary deficits have placed additional burdens on the country's debt and debt-servicing obligations, which have potentially serious repercussions on overall financial stability. Pakistan's external sector ultimately depends on the active promotion of exports and significant improvement in export performance.

ITT 440098 RCA 248423 WUI 64145

As you know, the country's ability to compete effectively in world markets has been hindered in the past both by its trade regime and industrial structure. Efforts to liberalize trade while at the same time improving the efficiency of industrial production and capacity utilization deserve urgent consideration. The Bank is aware of important policy changes achieved during the Sixth Plan; indeed, your Government's efforts to date in the deregulation of business activities represent significant first steps. But, to sustain Pakistan's growth and development, the problems we see call for substantial adjustment and structural policy reforms before it is too late. Simply put, the Bank's concern is that Pakistan may - without timely reforms - end up heavily mortgaging its otherwise bright future.

In view of our shared recognition of these problems, we had hoped to see the emergence of a medium-term economic strategy which would lead the country back to a sustainable path of economic growth. It is in this regard that the events surrounding the FY87-88 budget are most disappointing. Based on our continuing dialogue with the Government in Islamabad, at the Pakistan Consortium, and in Washington, we had hoped that the Government would develop a politically acceptable formula for strengthening its resource mobilization effort while devoting scarce resources to priority sectors. Effective management of the exchange rate could have been accompanied by a tariff policy with reforms on the import side to complement the proposed export promotion measures. Most importantly, we had hoped to see a well articulated development strategy for the next few years as the economy continued its adjustment process. Instead, in place of a medium-term strategy, we appear to have a set of short-term rescue plans.

This situation gives us serious concerns about Pakistan's medium-term creditworthiness. As you know, the World Bank and IDA have been increasing their financial assistance to Pakistan, with lending nearly doubling from about \$300 million in 1984 to more than \$600 million in 1986. We had hoped to provide about \$700 million in 1987, as we indicated at the Consortium in April 1987. I am afraid that unless there is a clear willingness on the part of the Government to come to grips with some of the urgent issues to which I have drawn your attention and a distinct improvement in economic management, we would not be in a position to recommend these high lending levels to our Board. Regrettably, we would have to face the possibility of reverting to the 1984 lending levels. This process would also necessarily involve a reduction in quick disbursing sector lending, which is itself tied to macro-economic performance.

Such a scenario for Pakistan is definitely not what the Bank wishes to see. To prevent it from becoming a reality, I very much hope that your Government and the Bank can work together, and find some bold and creative solutions to current problems.

To this end, I would like to suggest that we work together to establish a medium-term strategic program to strengthen Pakistan's economic performance. I understand that on the fiscal side, the basis for such a program has recently been formulated by the National Tax Reform Commission. A good starting point also exists here at the Bank in our recent economic work on Pakistan. In the area of trade, I would also like to suggest that we continue our close collaboration in building on the new trade policy regime by rationalizing the tariff structure in an appropriate sequence so as to both replace non-tariff barriers with appropriate tariffs and avoid adverse revenue implications. The Bank remains convinced that an outward-oriented trade regime is a critical building block to Pakistan's economic well-being.

In conclusion, let me say that the Bank expects neither the policy changes nor their full benefits to be realized immediately. We are prepared to assist Pakistan in an appropriate and flexible manner, to develop a medium-term framework for sustained progress toward macro-economic and structural reforms. The Government's commitment to implement such a framework would then be the basis for determining future levels of Bank assistance. To that end, we look forward to a serious and substantive discussion with your Government in the near future to develop feasible targets of economic and budgetary performance. I hope these discussions can be completed by the time of the Annual Bank-Fund Meetings in late September so that I can personally confirm the basis for Bank assistance to Pakistan to your delegation at the Annual Meetings.

I very much look forward to visiting Pakistan in early November and especially to the pleasure of meeting with you.

Sincerely,

Barber Conable

Barber Conable
President

Kopp

THE WORLD BANK INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Date: October 29, 1986

To: Mr. Barber B. Conable, President

Through: Mr. Ernest Stern, Senior Vice President Operations

From: W. David Hopper, Vice President, South Asia Region WDH

Extension: 33000

Subject: Meeting with Mr. Jamsheed K.A. Marker, Pakistan's Ambassador to the U.S.

1. On November 5 you will be meeting with the new Ambassador for Pakistan, Mr. Marker, and Mr. Ihsanul Haq, Economic Minister at the Embassy. We understand this to be a courtesy call.

2. The Bank has a large diversified program in Pakistan which includes a strong component of policy-based lending. Following our Energy Sector Loan, (US$178 million in FY86) we are currently considering an Agricultural Sector Loan (US$150 - FY87) and are anticipating policy-based lending in transportation and industry over the next two years. Bank assistance to Pakistan has grown from $138 million in FY82 to $473 million in FY86. IDA has remained stable at around $160 million. The Region feels strongly that, while supporting the Government's development efforts in agriculture, infrastructure, and now particularly in education, we must give strong signals to the Government concerning the need to improve project and program implementation.

3. Our concern with ongoing operations has been heightened when placed in the context of the current macro-economic situation. The September 1986 economic mission believes that the budget deficit has now reached at least 7 1/2 percent of GDP and may ultimately be as high as 9 percent. This has resulted in excessive domestic borrowing which brings with it other negative consequences for the economy. We have urged the Government to improve resource mobilization and Bank lending to Pakistan at this time is strongly focused on this issue. While we appreciate the accompanying political difficulties, we feel a reduced budget deficit is necessary for stability and development.

THE WORLD BANK
Washington D C 20433
U S A

A W CLAUSEN
President

January 7, 1986

Dr. Mubashir Hasan
4 K Gulberg 2
Lahore, Pakistan

Dear Dr. Mubashir Hasan,

Thank you for your letter of December 14, 1985, concerning the Kalabagh Dam project. We are particularly appreciative of your concern, as a former Governor of the Bank, that the Bank's role as "executing agency" in investment feasibility studies financed by the UNDP continue to retain the highest technical integrity and reputation. This, as you know, has characterized the Bank's supervision of feasibility studies on many projects in many countries over the years. Let me assure you that the Bank has and intends to live up to these standards on the proposed Kalabagh Dam.

Like you, we in the Bank have followed recent press reports on the proposed Kalabagh project. We find some of them relatively misinformed. We believe that an objective review of all the technical reports available to date would show that a careful and systematic study of this project is being made, and that further studies now underway will provide a sound basis for a final assessment and decision on the technical and economic feasibility and the affordability of this huge project. A decision on whether to proceed with the project would be for the Government and people of Pakistan to make. The role of the Bank as "executing agency" for the studies has been to see to it that the best talent (Pakistani and expatriate) is involved to provide a technically objective basis for such decisions. As a matter of fact Kalabagh project happens to be the first project on which an independent panel of experts (comprising world renowned dams experts) has been associated for detailed review of all technical aspects right from the initial stage of project study since 1982 - contributing to several modifications in the project's layout and design concepts. In any event, I can assure you that Pakistani engineers, working for the appropriate government departments and agencies, have had and will continue to have full access to all the available technical material.

The Bank believes that the availability of power will continue to be a binding constraint to Pakistan's development and industrial production. Pakistan has to find cost effective ways of overcoming this constraint. Among options that will need to be carefully examined are investments in hydro power which can take up to 10 years of feasibility and engineering studies. It was against this background that the Bank agreed to supervise the feasibility studies on Kalabagh, continuing the role that we have played in the Indus Basin Treaty, Mangla, and Tarbela. We are proud of our contribution to these earlier efforts.

Again, I appreciate your continued interest in the Bank and its contribution to Pakistan development efforts.

Sincerely,

A.W. Clausen
President

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OFFICE OF THE PRESIDENT

From Dr Mubashir Hasan

OPEN LETTER TO PRESIDENT WORLD BANK

Mr A. W. Clausen
President,
International Bank of Reconstruction and Development,
Washington, D.C.

Subject: Kalabagh Dam, Pakistan.

Dear Mr. Clausen,

As a former Governor of the Bank and as a taxpayer of a country that has contributed to its capital, may I draw your attention to the following:

1. The Bank is the "Executing Agency" for the preparation of the Kalabagh Dam Multipurpose Project in Pakistan.

2. The scheme of the project has not been revealed to the people of Pakistan but some of its details, made known to officials, have given rise to an extremely bitter controversy among the military governments of the provinces of the Punjab, North-west Frontier, Sind, and Baluchistan. Unfortunately for the country, the controversy has become ethnic in character and has assumed frightening political implications for the security and integrity of the country.

3. According to newspaper reports, the governments of the three out of our four provinces, for one reason or another, have taken a position against the dam, as designed.

4. All the major political parties of the country have also expressed their opposition to the construction of the dam as designed. During the course of the next nine years, should any political government come into power into Pakistan, the project, as now planned, runs the danger of being abandoned.

5. From what scanty details have appeared in the press five major faults of the design and the estimates of cost are manifest at this stage:

(a) The design does not take into consideration the compelling necessity of construction of more reservoirs on the Indus river system in the near future which will reduce its cost, substantially increase the cost-benefit ratio and will reduce the number of persons to be displaced as a result of the execution of the project.

(b) In a politically callous and technically unjustifiable manner, the project includes the construction of massive flood protection works in the valley of the River Kabul. These works are totally avoidable if the procedure to regulate the level in the lake behind the dam is correctly devised. Savings, $ 500 million.

(c) The project, as planned, does not take into consideration the totality of benefits from the Indus system for power and irrigation purposes.

(d) The estimates of cost are inflated to the extent of $ 1,500 million.

(e) At a fabulous cost to Pakistan, the project is proposed to be executed by expatriate supervising staff and foreign contractors. Sufficient talent and skills are available in Pakistan at ten to thirty percent of the estimated cost. Construction machinery worth hundereds of millions of dollars is lying unused throughout the country. There should be no problem for Pakistan to convince the most stringent of the lending agencies, including the Bank, of the ability of Pakistanis to do the job. Only what is not available in Pakistan needs to be hired or imported from abroad.

6. Prima-facie, the project as it stands today has no chance of being acceptable to either the people of the three smaller provinces or to the engineering profession of Pakistan. I am sure there is none who is dreaming of implementing it on the strength of physical force.

7. To be frank, the Bank, the consulting engineers and the "Government Coordinating Agency", that is, our Water and Power Development Authority have been less than diligent in the performance of their obligations. Having once assumed the extraordinary role of an Executing Agency in a highly charged political environment of Pakistan, the Bank needed to proceed with greater circumspection. Some aspects of the project appear preposterous earning a bad name for the Bank. At one time the cost of the project was $ 2,000 million. Then a stage came when it is reported to have rocketed to over $ 9,000 million. Now it is reported to be of the order of $ 3,500 million. The estimate of nationalist minded Pakistani engineers is that it should not exceed $ 2,000 million. The saving of $ 1,500 can be

profitably utilised to build another power plant to generate an additional 1500 MW.

8. All the aforementioned has appeared in the Press in Pakistan but it is not likely to have been brought to your notice. The first pre-requisite to salvage the project and to bring down its cost to a reasonable level is that you should direct your engineers to make available to Pakistani engineers the details of the project. This should be followed by technical discussions. Only then perhaps the way may be opened to make the project politically acceptable.

9. May I suggest that at the completion of the present phase of the work the Bank should withdraw as an Executing Agency. It may resume its role as a lender for the project when Pakistani governments of the provinces have made up their mind about the design of the dam after settling their political and technical differences on the question.

Yours sincerely,

Mubashir Hasan

(Dr Mubashir Hasan)
4 K Gulberg 2
Lahore, Pakistan.

December 14, 1985.

Briefing Note for Meeting with Dr. Mahbub ul Haq, on December 12 & 13, 1984

We understand that Dr. Mahbub ul Haq, during his short stopover in Washington, would like to brief Senior Management on a number of recent initiatives which bear on Pakistan's economic prospects. First, GOP has now decided to prepare a three year rolling public investment program in light of the shortfall in development resources envisioned under the Sixth Plan. Secondly, the Cabinet is finalizing its decision on the Kalabagh multi-purpose dam and expects the Bank Group to play a lead role in assisting Pakistan to mobilize required funding. Thirdly, reasonable progess is being made on the proposed sector loans in energy, agriculture and industry to support further structural adjustment in the economy. Finally, last week, President Zia ul Haq announced the date for a Presidential Referendum, the first major step in the political transition that is expected to culminate in the election of National and Provincial assemblies.

Public Investment Program

The Bank review of the Sixth Five Year Development Plan issued in 1983 noted that the Plan's proposed policy framework was right and the size and composition of the public investment program appropriate. At the same time, the review noted that a major effort in domestic resource mobilization would be required to fund the Plan. There has been a shortfall of about 8% in the annual development program in each of the first two years of the Plan. The Government, with our advice, has now decided to prepare a program of priority core investments that should be protected in order to ensure adherence to the Sixth Plan's basic objectives and priorities. The draft rolling plan is expected to be ready sometime in February and Dr. Mahbub ul Haq has indicated that he would welcome a discussion with the Bank before finalization. The consultation would be along the lines of that held at Tarbela during the formulation of the Sixth Plan. We suggest you confirm the Bank's willingness to do so.

Kalabagh Dam

After a period of some indecision as to whether Pakistan was going to ask the Soviet Union or the Pakistan Consortium members to take the lead in financing the large Kalabagh multi-purpose dam (estimated cost US$6 billion over six years), we understand the Cabinet is strongly leaning towards the Consortium. Indeed, Dr. Mahbub ul Haq at a recent news conference indicated that GOP may request the Bank to convene a special meeting of the Consortium on the project. We suggest you ask the Minister when the Cabinet might make its final decision. With regards to a special meeting on Kalabagh, the Bank should underline the importance of adequate advance preparation including studies on the macro-economics of such a large investment including impact on debt servicing, crowding out of other important investments especially in the social sectors, etc.

Sector Loans

Of the three sector loans, energy is the most advanced and should receive GOP priority for this fiscal year. The first of a two phase appraisal of this loan has just been completed and there appears to be a significant convergence of views on most policy issues except gas pricing. On producer pricing the Minister of Finance has raised a number of important questions and has asked for a further paper from the Bank addressing these. On consumer pricing the Minister of Finance feels very strongly that the covenant under SAL I to raise prices to two-thirds of fuel parity by 1988 is the most that can be committed at this time. Dr. Mahbub ul Haq will no doubt want to elaborate on the Finance Minister's views on the gas pricing issues. We recommend you emphasize that agreement on an acceptable producer pricing formula for gas is a prerequisite for approval of the loan. With regards to consumer prices, our proposal was for actions to be taken after 1988 and there will be other opportunities in the next three years to reach an understanding with GOP on this. We therefore recommend that this not be made a sticking issue for the sector loan.

Very good preparation progress has been made in recent months on the agricultural sector loan and we may be able to prepare the initiating memorandum to the Loan Committee on it towards the end of this fiscal year. The industrial sector loan initiating memorandum to the Loan Committee is under preparation. There is therefore the possibility that we could process one of these loans in FY86.

Political Transition

In our recent CPP, we emphasized that the success with which the proposed elections are carried out and the extent to which the Government that emerges is able to continue the policy advances of recent years will significantly affect Pakistan's economic prospects and creditworthiness. Last week, the President of Pakistan announced that an important referendum, under which he is seeking and is likely to be confirmed for a further five year term, will be held December 19, 1984. It is not clear, however, how this referendum will affect the proposed national and provincial elections. Dr. Mahbub ul Haq may be able to clarify this.

بسم اللہ الرحمٰن الرحیم

No.S (5) WB/83
Government of Pakistan
MINISTRY OF FINANCE AND
ECONOMIC AFFAIRS
(ECONOMIC AFFAIRS DIVISION)

Telegram : ECONOMIC
Telex : ECDIV No. 05-634
Secretary General,
Phone:20629.

Islamabad, the 21st January 1

Dear Mr. Clausen,

In response to your request regarding the 7th Replenishment of IDA, the President of Pakistan was pleased address letters to the Presidents of the United States and France, the Prime Ministers of the U.K.,Japan, Canada and th Chancellor of Federal Republic of Germany.

2. The reactions of these Heads of Governments to the President's letter have been received expressing appreciatic of the contribution made by IDA towards world development ar stability. However, no firm commitment is indicated that they would support funding of IDA VII at the proposed level of $ 16 billion.

3. The President of the United States has termed the World Bank's proposal for the Seventh IDA Replenishment of US $ 16 billion as being "unrealistically high". Budgetary constraints and the need for more effective utilization of existing resources have been advanced as the main reason for a lower contribution by the USA. However, in determining the level of US contribution to the IDA VII, he would work hard, in consultation with the Congress, to avoid the funding difficulties experienced during IDA VI.

4. The British Prime Minister has also pleaded public expenditure constraints but has extended the assurance that the United Kingdom would support the next replenishment " within the limits of what donors collectively can afford". Contribution of the United Kingdom would be in line with the relative economic strength of the donor countries which mean: less than the 10.1% level which the United Kingdom contribut to IDA and "was acknowledged by other donors as being very

high". Besides the United Kingdom have a substantial bilate aid programme particularly for the poorest countries. Her country will however, continue to play its part in various European Community programmes to help the developin countries.

5. The Chancellor of the Federal Republic of Germany has stated that his country would cooperate to bring about agreement on the Seventh Replenishment of IDA which should b based on the principles of equal burden sharing among the contributors and consensus among the participants on the tot volume of funds to be provided. He has assured that his Government will participate in the talks with determination and commitment.

6. The Canadian Prime Minister has expressed his disappointment with the progress todate in the IDA VII negotiations and that his Government has urged the United States to modify its position, pointing out that an IDA VII, at least as large as $ 12 billion originally agreed to for IDA VI would be the minimum amount acceptable.

7. The Prime Minister of Japan has stated that the level of IDA VII should not be lower than US $ 12 billion. Accordin to him in view of the urgent financial needs of low income developing countries, it was essential that the negotiations on IDA VII be brought to a conclusion as quickly as possible with a realistic volume of replenishment. His government take a view that unless the ranking of Japan's share in capital subscription in the IBRD and in the IDA is harmonized, it would be impossible for him to secure public support and legislative approval for subscriptions to IDA in the present stringent financial situation. Japan will be prepared to make contributions to IDA-VII corresponding to adjusted ranking of its share in the IBRD.

contd....p/2

8. This brief summary of the replies received from the various Heads of States/Governments is being submitted for your information.

9. Reports appearing in the Press have indicated that the IDA replenishment meeting held on 12th January,±984, th US representative did not consider it possible to change hi Government's decision to limit the US contribution to IDA V to $ 750 million per annum. In the light of this decision of the US Government, which would restrict the IDA VII leve to $ 9 billion, you may wish to suggest the future course o action. The Government of Pakistan, being one of the main beneficiaries of IDA funds would always be ready to offer i cooperation and assistance in this regard.

With best regards,

Yours sincerely,

(EJAZ AHMAD NAIK)

Mr.A.W.Clausen,
President,
world Bank
Washington DC.