Unlocking the chains of debt

A call for debt relief for Pakistan

Foreword

"If the debtor is in a difficulty, grant him till it is easy for him to repay. But if ye remit it by way of charity, that is best for you if ye only knew."
The Qur'an, chapter 2, verse 280

For over 20 years, Islamic Relief has been working in Pakistan to reduce suffering and poverty in the country's most vulnerable communities.

As a country, Pakistan emits low levels of carbon, yet its poorest communities are paying the price of the high global levels of carbon emission. Climatic changes in the region have increased the frequency of natural disasters. When disasters hit Pakistan, Islamic Relief is consistently one of the first agencies to provide emergency aid, including in the wake of the Kashmir earthquake and the catastrophic floods of 2010. In the wake of these crises, we remain in the country, working with local people to help them rebuild their lives and transform their communities.

In a country where more than 50 million live below the poverty line – that's more than double the population of Australia – the need for sustainable development and real solutions to poverty is clear and compelling. However, development is being crippled by Pakistan's staggering debt burden, which has also suffocated public spending.

With the government struggling to spend 3% of GDP on healthcare and education, it is no surprise that the country's poorest people rely on aid and development organisations to provide vital services.

Pressure to make debt repayments – which are set to rise sharply – now sees the country on the brink of an economic crisis, with Pakistan's involvement in the 'war on terror' further depleting already over-stretched resources.

In providing 'bail-out loans', foreign lenders attach economic conditions that inflict greater suffering on the poorest in society – like the IMF's insistence that Pakistan eliminate oil and electricity subsidies – and the government is unable to refuse.

For these reasons, Islamic Relief is calling for a full and transparent audit of Pakistan's external debt, and the cancellation of unjust debt. This intervention – which has been successful in other indebted countries – would allow Pakistan the fiscal space required to build resilience and invest in infrastructure, and other development designed to eradicate poverty. In this scenario, the government of Pakistan would have no excuse for any failure to protect and improve the lives of millions of poor people.

Islamic Relief will continue to support Pakistan's vulnerable communities for as long as we are needed. But the power to achieve profound and permanent change does not lie with us, or any other humanitarian organisation. It is for foreign lenders and the government of Pakistan to accept their duty towards the country's poor people, and to take action – now. Both lenders and the government have prolonged the suffering of poor communities. We urge them to reconsider and overhaul their current policies.

Implementation of our recommendations, alongside a review of Pakistan's debt and spending, could set the country on track to achieving vital Millennium Development Goals. Only then will we see positive steps forward in reducing poverty throughout the country.

Dr Fayaz Ahmad
Country Director, Islamic Relief Pakistan

Executive summary

"Pakistan's people are now suffering from a fourth decade of debt crisis. The system of IMF bailout loans and structural adjustment conditions has not worked. The people of Pakistan need debt to be cancelled, and to gain a greater control over their economic future."
Tim Jones, Policy Officer, Jubilee Debt Campaign

Pakistan is trapped in a debt crisis, and – as ever – this is hitting vulnerable communities the hardest. For four decades, much-needed development in Pakistan has been hampered as the country struggles with its large external debt. The response to the debt crisis has relied upon continual bailout loans from the International Monetary Fund (IMF). Pakistan has received bailout loans for 29 years – one of the longest periods of lending to any country in the world.

The loans have seen the debt passed down through generations. Lending and grants have also been historically used by the western world to prop-up various military governments in Pakistan. Furthermore, the economic conditions imposed by the IMF have given the organisation major sway over the country's development – making it even harder for the country to build a more stable economic future.

In recent years, Pakistan has suffered in the wake of the worst floods in living memory and the global financial crisis. The country's debt burden has increased yet again. In only seven years, the government's foreign owed debt almost doubled from the $30 billion owed in 2006. Today, Pakistan's debt stands at $58 billion – including $8 billion in IMF loans made over just two years.

The people of Pakistan have also suffered in the 'war on terror'. Reports put the total cost to the Pakistan government at between $68 billion[1] and $80 billion.[2] In addition, data compiled by the Pakistan Institute of Peace Studies (PIPS) indicate that over 24,000 people - mostly civilians - have been killed in terror attacks, Pakistan security force operations and drone attacks by the USA. Official Pakistani Government sources give estimates of deaths which are as high as 38,000.[3]

In addition, Pakistan faces huge development challenges. Despite being classed as 'middle income' since 2010, the national income per person is just $1,372. Many Millennium Development Goals will not be met, and this will be of concern to the international community as part of the response to regional instability. High levels of poverty and deprivation provide a conducive environment for recruitment by regional and global extremist groups. At present, Pakistan's creditors have failed to achieve one of the criteria under Millennium Development Goal 8 – the requirement to "deal comprehensively with the debt problems of developing countries".

The most recent IMF loans must be repaid between 2012 and 2015. To meet this obligation, Pakistan's debt payments are rising dramatically to over $6 billion a year (which is over 20% of export revenues).

Repaying the debt may trigger an economic and social crisis. It will certainly increase inequality, injustice and instability both in the country and the wider region. However, there is an alternative that could create a more stable, just and equal country.

WE RECOMMEND THE FOLLOWING MEASURES BE TAKEN NOW

- **Debt payments are suspended until a public audit into Pakistan's debt has been carried out**
- **Following the public audit, unjust debts are cancelled**
- **Progressive taxation reforms are introduced, so the government has the revenue it needs to tackle poverty and increase equality**
- **Public spending is rebalanced towards tackling poverty and investment in infrastructure**
- **Inflows of foreign capital and aid are regulated to secure useful investment, ensure that domestic saving is not crowded out, and speculation does not create unsustainable financial bubbles.**

Pakistan's debt crisis

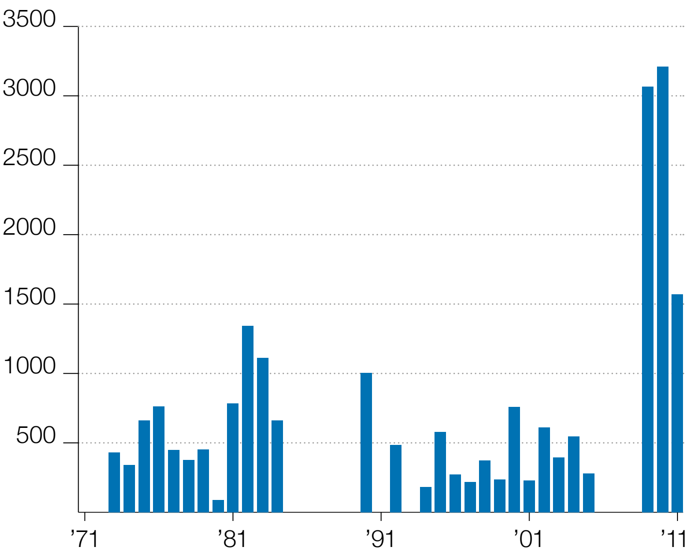
"If Pakistan's debt issues are not resolved, the weight of the current debt has the potential to cause economic turmoil and widespread instability in the country. Every Pakistani will feel the brunt of this."
Atallah Fitzgibbon, Head of Policy, Islamic Relief Worldwide

Pakistan has a history of significant government foreign-owed debts. Successive governments of Pakistan have tried to tackle the high debt burden by taking bailout loans from the IMF, which come with economic conditions attached. The country has borrowed from the IMF for 29 out of the 40 years between 1971 and 2010.[4]

For over 40 years the high debt has remained, taking away resources that could have been used to reduce poverty and increase economic development. In the midst of this, the power of external creditors to impose economic conditions has been maintained.

The IMF lends money so debt payments can be made. It bails out the original lenders at the cost of the future generations which inherit the debt. Pakistan's history is just one of many examples of how this strategy is failing the world's poorest communities.

IMF loans to Pakistan 1971–2011 ($ million, 2007 prices)[5]



Millennium Development Goals that Pakistan will not meet include

- Halving the proportion of people going hungry
- Ensuring all children are able to complete a full course of primary schooling
- Eliminating gender disparity at all levels of education
- Reducing by two-thirds the child mortality rate
- Reducing by three-quarters the maternal mortality rate
- Halving the proportion of people without access to basic sanitation

Debt payments have averaged above 15% of exports for most years in the past four decades.[6] The IMF and World Bank regard government debt payments of more than 15–25% of exports as unsustainable for low income countries. However, this only considers whether a government is able to make debt payments – not the impact they have in reducing expenditure on public services and undermining the domestic economy.

In 1953, Germany – now one of Europe's strongest economies – had half its foreign-owed debt cancelled. Interest rates were cut on the remainder, which reduced debt payments to 3% of exports and less. The countries that cancelled Germany's debt included Pakistan.

The average debt repayments for the 35 countries that qualified for debt relief through the Heavily Indebted Poor Countries (HIPC) initiative are now 3% of exports.[7] That is below the current payments for Pakistan. In HIPC countries, following debt cancellation, expenditure on activities defined by the IMF and World Bank as 'poverty reducing' has increased from 7% of national income in 2000 to 9% in 2009.[8]

Pakistan also took extensive development loans from institutions such as the Asian Development Bank and World Bank. Foreign government creditors include Japan, France, China, Germany and the USA. External borrowing can reduce poverty when invested in useful projects which create the revenue for the government to repay the debt – with surplus to be used in improving the lives of Pakistani people. However, foreign lending may be wasted on failed projects, consumption rather than investment, or used to buy assets which already exist.

Large amounts of foreign lending can also undermine the domestic economy. Capital inflows, or exports of particularly high value goods, can push up the exchange rate and damage other industries. Known as 'Dutch Disease',[9] in this situation certain sections of society – usually the elite – benefit from the income and wealth, while workers in other industries are at a disadvantage.

Pakistan and the Heavily Indebted Poor Countries (HIPC) initiative

In 1996, the IMF and World Bank created the HIPC initiative, which was designed to reduce the unpayable debts of low-income countries. Following calls for debt cancellation or repudiation by millions of people across the world, the scheme was expanded to increase the amount of debt relief available. However, to qualify countries were forced to implement IMF and World Bank economic conditions. This saw water services in Tanzania privatised, and a grain reserve sold off before a food crisis in Malawi.

The HIPC initiative has led to the debts of 35 countries being substantially reduced, with $130 billion of debt cancelled in total. Eligibility was based on two criteria: being a 'poor' country, and being heavily in debt. Both criteria applied to Pakistan, which had a debt of more than 200% of exports during most of the 2000s.

However, Pakistan was judged ineligible because it was able to borrow from the part of the World Bank which lends to middle-income countries. The arbitrary criteria was introduced to exclude heavily indebted large countries – such as Pakistan and Nigeria – because the absolute size of their debt was larger[10] and therefore seen as more costly to cancel. However, in 2005, Nigeria had $18 billion of debt cancelled by the Paris Club group of rich countries, after it paid a lump sum of $12.4 billion. The countries include Japan, France, Germany and USA who together own a substantial proportion of Pakistan's debt.

Damaging debt
The National Drainage Program

Between 1998 and 2005, Pakistan borrowed $273 million from the World Bank, $140 million from the Asian Development Bank, and a further $100 million from Japan's Overseas Economic Cooperation Fund.

The funds were invested in a scheme to improve drainage in Pakistan's irrigation system to combat salinisation and waterlogging. However – following complaints by local people in the Sindh region – a World Bank inspection panel found that the project had caused widespread environmental harm and suffering among local communities. It had violated six of the World Bank's safeguarding policies, including failures to consult with and disclose information to local people.[11]

The panel found that technical mistakes were made during the design of the drainage canals, discovering that their alignment was "technically and environmentally risky". This created failures in the drainage system, which increased salinity in agricultural lands and led to major harm to ecosystems. In 2003, increased flooding - partially caused by the project – claimed more than 300 lives.[12]

The affected communities and NGOs Action Aid Pakistan and International Rivers Network called for the World Bank to make restitution. This has not been forthcoming. In addition, the loans pushed Pakistan even further into debt.

The country has already started making repayments on this loan. So far, $42 million has been paid to the World Bank, with $34 million in interest, charges and fees ($76 million in total).[13] $231 million is still owed to the World Bank, with an estimated $200 million still owed to the failed scheme's two other creditors.

In addition, other parts of the domestic economy shrink, leaving the whole country more vulnerable when the capital inflows stop, the prices fall, or the goods run out.

Research commissioned by Islamic Relief[14] suggests that Pakistan suffered from the Dutch Disease during 2002–08. During this time, net capital inflows increased rapidly –increasing from less than $5 billion at the start of the period to top $20 billion in 2007. The exchange rate appreciated by a staggering 33%. In 2008, following a huge increase in imports, which soared by 270%, Pakistan's current account plunged into deficit of 8.5% – having previously been in surplus in the early 2000s.

Moreover, borrowing from foreigners can 'crowd-out' domestic saving, leading to no net increase in investment and more foreign-owed debt. Payments leave the country rather than being reinvested into Pakistan. The research by Islamic Relief shows that in Pakistan, foreign borrowing and even aid grants have had a negative impact on domestic saving. It found that a 1% point of GDP increase in foreign loans and grants decreases domestic savings by 0.8 % of GDP.[15]

Lending and grants have been used in the past to prop-up military governments in Pakistan, including those of General Musharraf (2000-2008), Zia-ul-Haq (1978-1988) and Ayub and Yahya Khan (1960-1971). Assistance, especially from the USA and the Western world, has been in return for military government general support during the Cold War, Pakistan support for Afghan fighters against Soviet occupation, and during the 'war on terror'.

Military governments have received at least as much foreign lending and grants as elected governments. For instance, the annual inflow of loans and grants under General Musharraf was 1.4% of GDP. Since the election of Raza Gillani in 2009 it has fallen to 0.9%. Moreover, a greater proportion of assistance to military governments has been in the form of grants. Since 1960, grants have averaged 30% of assistance to military governments, but 15% to elected governments.[16]

Disaster increases debt

"Pakistan urgently needs more aid to tackle the unmet needs that remain following the floods and to bolster its people against the next major bout of monsoon flooding – a challenge that climate trends suggest is just around the corner."
Jehangir Malik, UK Director, Islamic Relief

At around $30 billion Pakistan's government foreign-owed debt was stable in the lead-up to the global financial crisis, and even falling as a percentage of national income. However, it increased rapidly from 2007 with the global financial crisis, and in particular the increase in the cost of fuel imports.[17]

Pakistan was also hit by a succession of disasters, devastating large areas of the country. In 2007, cyclone Yemyin affected almost two million people. Three years later, devastating floods left approximately one-fifth of the country submerged and wrecked the livelihoods of 18 million people. These were followed by further large floods in 2011. The cyclone and floods are estimated to have caused $11.1 billion of damage, in a country still reeling from the Kashmir earthquake of 2005 – which caused $5.3 billion of damage.

Climate change is hitting poorest communities hardest, with more intense and frequent disasters diverting already limited financial resources away from vital public expenditure. Countries which have a greater responsibility for greenhouse gas emissions, have a moral imperative to provide compensation for the impacts of climate change in Pakistan.

Indeed, extra resources could reduce the extent of future damage. For example, the former chair of Pakistan's Natural Disaster Management Authority (NDMA) estimated that an investment of $40 million in flood protection measures could have reduced economic losses from the 2010 floods by 90%.

Post-catastrophe debt relief

In 2010, the people of Haiti suffered from a horrendous earthquake. Global calls for the country to have its debt completely cancelled led to the IMF creating a 'post-catastrophe debt relief fund'. This enabled Haiti's debt to the IMF to be cancelled, whilst creating a fund which would compensate the IMF for doing the same for other low income countries, if they suffered from disasters which:

- Affected more than one-third of the population
- Destroyed a quarter of a country's productive capacity, or the equivalent of 100% of a country's annual national income.

Whilst this was an acknowledgment of the need for debt relief in the wake of a crisis, the stringent conditions mean that only gigantic catastrophes affecting small countries would lead to any debt relief. No other country apart from Haiti has qualified. Pakistan was excluded both because it is a 'middle-income' country, and because the 2010 floods were not deemed catastrophic.

IMF loan conditions

One of the conditions of the most recent IMF loan programme was to increase Value Added Tax (VAT) – a pattern of the organisation's loans to the heavily-indebted country. Throughout the 1980s and '90s, Pakistan increased VAT as demanded, whilst reducing taxes on imports. As a percentage of tax revenue, sales taxes increased from 7% in 1980 to almost 30% by 2000. Shahid Hassan Siddiqui from the Research Institute of Islamic Banking said in 2010 that IMF tax conditions would "hurt the poor".[23] The changes imposed by the IMF in the 1980s and 1990s increased taxes by 7% for the poorest households and reduced them by 15% for the richest.[24]

Another condition was to allow fuel prices to increase. This led to the near-collapse of Pakistan's government, as the second largest party in the coalition threatened to leave the government in opposition to rising fuel prices. The planned price rises were subsequently reversed, but as a result the IMF closed the door to future loans. Although discussions between the two have continued, Pakistan has not taken further loans from the organisation.

War on terror

"Young, unemployed and deprived Pakistanis are the ones that are most vulnerable to extremism. If poverty and inequality continue, we could see the 'terror' situation escalate."
Muhtari-Aminu-Kano, Senior Policy Advisor, Islamic Relief

The Pakistani people have also suffered significantly in the 'war on terror'. Reports put the economic cost of the 'war on terror' to the Pakistan government at between $68 billion[18] and $80 billion.[19] As of 2008, the USA has provided grants amounting to $12 billion to cover some of these costs, but estimates show that it has cost Pakistan three times more than the value of these grants.[20]

By 2012, in addition to the continuing costs of the 'war on terror', Pakistan's external debt had increased to $58 billion.[21] This included $8.1 billion of loans from the IMF.

HOW TERRORISM HAS AFFECTED THE PAKISTANI PEOPLE[22]

- **During 2005 and 2010, terrorists killed 21,000 people and injured more than 35,000**
- **Operations by Pakistan's government forces have led to 2,007 deaths – mostly civilians**
- **US drones are estimated to have killed over 900 civilians in 2010 alone.**

Development challenges

"Widespread poverty in Pakistan forces ordinary Pakistanis to also burden their own personal debt. The inability and pressures of repaying such debt are so overwhelming, that death is seen as the only solution for hundreds of Pakistanis."
Adnan bin Junaid, Head of Programmes, Islamic Relief Pakistan

Pakistan faces huge development challenges. Four years ago, it was classed as a low-income country. Today, it is regarded as middle-income, despite its national income per person being only $1,372.

A number of crucial Millennium Development Goals will be missed. For instance, one goal is to halve the number of people who are undernourished by the year 2015. However, this has fallen by only 6% in 22 years, with 35 million people still classed as undernourished by the UN.[25] Even if improvements continue uninterrupted at this pace, the goal will not be met until 2038, and undernourishment will not be eradicated until 2086.

In Pakistan, the proportion of people struggling to survive on less than $1 a day fell from 65% in 1991 to 29% at the end of the decade, thus apparently meeting the goal to halve the proportion of people living in extreme poverty. However, there has been little subsequent progress. According to the latest figures, published in 2008, 21% of the population still live on less than $1 a day.[26]

Whilst the Millennium Development Goals aim for all children to complete primary school, in Pakistan today, only two-thirds of children achieve this. There is also a huge disparity between the opportunities available to girls and boys: 74% of boys complete primary school, while only 59% of girls are able to.[27]

Child mortality has only fallen by 40%, rather than two-thirds. This means that 72 of every one-thousand children die before their fifth birthday.[28] Pakistan is almost four decades away from achieving this vital Millennium Development Goal.

Today in Pakistan, 260 out of every 100,000 births will bring about the mother's death.[29] This will need to be halved in just two years in order to achieve the Millennium Development Goal. Pakistan is also a long way away from achieving the goal on access to basic sanitation: in 1990, 73% lacked access, and ten years later, the figure only dropped to 52%.[30]

To ensure that the Millennium Development Goals were achievable, the international community made a commitment in MDG 8 to "deal comprehensively with the debt problems of developing countries". With this promise still unfulfilled, Pakistan is failing to achieve vital development goals and the country's poorest communities continue to suffer as a result.

Widespread poverty

The horrendous poverty in Pakistan forces many people into debt themselves. In 2010, the BBC's Orla Guerin reported that Akbar Beenish, a rickshaw driver in Lahore, killed himself and two of his daughters with poison. Akbar was driven to despair by owing 60,000 rupees ($700). Akbar's wife Muzammil survived after spitting out the poison, but still had to be treated in hospital. Professor Javed Akram, the doctor who treated Muzammil, said that he sees ten cases of poisoning a day, when it used to be four or five. According to Professor Akram, most of those who kill themselves are in poverty.[31]

Debt burden set to spiral out of control?

Pakistan's external debt is currently thought to be around $58 billion[32] – about 24% of GDP and 200% of exports. The IMF and World Bank argue that debts for low-income countries usually become impossible to repay when they are between 30-50% of GDP or 100–200% of exports.[33] This is based on countries forced to default when they can no longer afford to pay. It does not consider the impact the repayments have in reducing money available for public services, or the undermining of the domestic economy.

Debts vs exports

Revenues from exports are needed to pay foreign debts. Pakistan's external debts are owed in foreign currencies, such as the dollar and yen. As a result, the country must earn foreign currencies to pay the debts. The only way it can earn foreign revenues is by exporting goods and services.

The burden is the annual cost

Over the last five years, Pakistan's foreign debt payments have averaged $2.3 billion. That's the equivalent of 10% of exports, and 10% of government revenue, and is half the amount spent on health and education combined.[34]

Disturbingly, over the next three years, debt payments are expected to be much higher as IMF loans from 2008–10 are due to be repaid. This year, Pakistan is to pay $3 billion, with a further $3.4 billion next year and $1.3 billion by 2015. On top of this, the country needs to make other debt payments. Islamic Relief has estimated[35] that this year, debt payments will reach $5.6 billion and will hit $6.2 billion in 2013–14 – an estimated 21-23% of export revenues.[36]

To meet the repayments, the government has resorted to using its foreign currency reserves. In one year, these reserves halved to just $7.4 billion in 2012/13.[37] With reserves down to the equivalent of only two months of import revenue, Pakistan is now exceptionally vulnerable.

The next two years are critical

To make its debt payments the government will be forced into actions which will only exacerbate Pakistan's debt and economic crises:

- Take out new loans, which will prolong the debt burden into a fifth decade
- Create large cuts in government spending or increases in taxes. Even progressive reforms will depress the economy, as proceeds are spent on debt payments
- Utilise the last of the country's foreign currency reserves, leaving the country highly vulnerable to crisis.

Each of these will move the country even further away from meeting the Millennium Development Goals.

Most of Pakistan's debt is owed to multilateral creditors – particularly the Asian Development Bank, World Bank and IMF. It also owes a significant amount to foreign governments, primarily Japan, but also France, China, Germany and the United States. Only a small proportion is owed to private creditors.

Pakistan's creditors and debt in 2011[38]

Creditor	$ debt	% of total
Multilateral	**$34.8 billion**	**61.7%**
World Bank	$12.8 billion	22.7%
Asian Development Bank	$12.3 billion	21.8%
IMF	$8.9 billion	15.8%
Other	$0.8 billion	1.4%
Bilateral	**$18.1 billion**	**32.0%**
Japan	$7.9 billion	14.0%
France	$2.3 billion	4.1%
China	$2.0 billion	3.5%
Germany	$1.9 billion	3.4%
USA	$1.5 billion	2.7%
Others	$2.5 billion	4.4%
Private	**$3.5 billion**	**6.2%**
Total	**$56.4 billion**	

Solutions are needed immediately

Debt tops $56.4 billion

Spend on foreign debt repayments = $2.3 billion

Spend on health and education = $5.7 billion

Who is the debt owed to?

International Monetary Fund
World Bank
Asian Development Bank

The governments of: Japan, France, China, Germany, USA

Last summer, Pakistan's National Assembly formed a committee to investigate the country's debt. Both the government and opposition agreed to a bipartisan inquiry into the benefits and costs of external and domestic borrowing and debt payments, since 1985. This move shows a political willingness to seek real solutions to Pakistan's debt problem, rather than further short term fixes that will only fuel the debt crisis for many years to come.

Following the devastating floods of 2010, the Pakistani parliament requested a means of debt relief. In November of that year, the Pakistani Senate, Minister of the Interior and President Zardari all called for debt cancellation or relief.[39] None of Pakistan's creditors heeded the call.

Attempts to tackle Pakistan's debt crisis have been failing for 40 years, with loans piled on top of loans. The national economy has been undermined. Effective development has been hampered. Poverty and inequality continues.

Today, the country sits on the brink of a preventable crisis. Creditors and Pakistani authorities must act now to implement a sustainable solution.

Who else is looking at debt?

Auditing Pakistan's debt can cast a fresh light on the issue. For example, the Ecuadorian government held a public debt audit in 2008, which concluded that the majority of that county's debts were 'thoroughly illegitimate'. Following the audit, Ecuador's debt to the rest of the world fell to 23% of national income, saving $2 billion immediately and a further $7 billion of future interest. This money was invested in social provision. Norway is currently looking at the loans that it has provided, and Tunisia is planning an audit into debts inherited from the Ben Ali government.

Recommendations

Audit the debt

To uncover who has benefited and determine how loans should be used in the future

Around the world, civic society has backed debt audits. These public investigations look at the benefits and costs of borrowing, and also increase public oversight and accountability over debt and economic policies.

Debt audits may also investigate the legality and legitimacy of loans. For example, where lenders failed to exercise responsibility over loans, the people of Pakistan should not be forced to repay debts that have caused damage. An audit will also allow a strategy to be developed to ensure any future lending and borrowing is beneficial and does not create another crisis.

- **The Pakistani parliament should initiate a public debt audit, by creating an independent debt audit commission, which includes relevant experts and representatives of civil society.**
- **Foreign lenders should release all information and evaluations concerning their loans, and take part in the debt audit process.**

Cancel unjust debts

For four decades, Pakistan's debt has been huge. The enormous revenue spent on debt payments has greatly reduced the country's ability to tackle crippling poverty. In addition, debt payments due over the next two years could tip Pakistan back into an economic crisis.

An immediate moratorium on debt payments to creditors is needed. Following a comprehensive debt audit, any illegal or illegitimate debts should be cancelled. All creditors should make further debt cancellation as needed to remove the historic debt burden, in line with a national, participatory strategy for preventing debt crises in the future.

In 1953, Germany's debt cancellation led to its debt payments being the equivalent of around 3% of exports. Debt relief for HIPC countries has also reduced their payments to an average of 3% of exports. Reducing Pakistan's debt to at least this level would allow the country a new financial start, and release significant resources for much-needed poverty reduction and economic development.

- **The Pakistani parliament should call for the cancellation of unjust debts following a debt audit.**
- **Foreign lenders should agree an immediate moratorium on debt payments, cancel unjust debts following a debt audit and cancel remaining debts to enable repayments to fall to at least 3% of exports.**

Implement progressive tax reforms

To give the government the revenue it needs to tackle poverty and increase equality

Pakistan's government currently collects between just 12–14% of national income as revenue. This is well below the 20% average for developing countries in Asia. Government revenue in sub-Saharan Africa is on average 25% of national income, and in Latin America it is 30%.[40]

Government revenue must increase so the coverage and quality of public services can be improved, social protection can be provided, and investment in infrastructure enabled – without creating large foreign debt burdens.

To tackle poverty and increase equality, revenue must come from progressive taxation on the income and wealth of richer individuals and companies. In particular, taxes on the wealthy land-owning elites are needed, not regressive increases in taxes such as VAT which have already increased inequality in Pakistan. In addition, measures are required to make sure that multinational companies are paying a fair rate of tax.

- **The Pakistani parliament should improve tax administration, whilst introducing progressive taxes on income and wealth so that the rich pay a fair share of tax.**
- **Foreign lenders should stop demanding regressive economic conditions (sometimes known as structural adjustment) - such as increases in VAT – whilst facilitating payment of taxes by companies. All multinational companies should be required to report on how much tax they pay in every country in which they operate.**

Rebalance public spending

Towards tackling poverty and investment in infrastructure

Pakistan currently spends $5.3 billion - around 3% of national income - on the military. This is over one-fifth of government revenue. Pakistan's high military costs arise from tensions and conflict with India, and the costs of the global 'war on terror', much of which has taken place in Pakistan. Spending on both debt payments and the military must decrease, and greater investment in socially useful schemes must be made instead.

The people of Pakistan are paying a heavy price for the country's participation in the 'war on terror'. The country's involvement so far has killed thousands of people, cost billions of dollars, and has contributed to widespread resentment. In contrast, a strategy that reduces poverty and allows economic development would have profound and positive impact upon Pakistan and the wider region. It would also help to bring people out of the poverty and desperation which can lead to people resorting to violence.

- **The Pakistani parliament should devise innovative strategies to enhance national productivity resulting in a striking reduction of Pakistan's dependence over foreign debt in the near future. The increased national productivity should be specifically and effectively channeled towards poverty reduction initiatives.**
- **Foreign lenders should increase focus and effort on supporting poverty reduction and development in the country, and make sure that the people of Pakistan do not shoulder the costs of the 'global war on terror'. Foreign governments – including that of USA – should also stop counter-productive military action.**

Regulate foreign capital and aid

To secure useful investment, to ensure that domestic saving is not crowded out, and that financial speculation does not create unsustainable economic bubbles

Foreign lending can be beneficial if it funds useful investment and if it does not have a negative impact or prevent the development of domestic industries. Lending should not be wasted, used to invest in damaging projects, or to buy up assets that already exist. Nor should it push up the exchange rate, therefore 'crowding-out' the development of local industries. It can, and has, been used to prop up anti-democratic, military-based governments in previous years.

Before contracts are signed on a new loan, both lender and borrower should clearly set out the benefits and risks. These should be independently evaluated before, during and after the project.

In addition, Pakistan's parliament and media should debate and scrutinise lending proposals.

Comprehensive public consultation must be undertaken, so that local communities are informed of the proposals and have the opportunity to make appropriate representations in support or opposition to the scheme.

At the macro-level, capital account regulations have been adopted by various countries to support investment rather than speculation. Such policies include taxes, reserve requirements and ownership limits – all of which can encourage long-term investment that involves local people and businesses. Crucially, they create a disincentive for short-term financial speculation and asset-stripping.

However, World Trade Organisation and free trade agreement rules have made such policies illegal. The IMF and World Bank have often set conditions to remove capital account regulations and prevent them being reintroduced – although the IMF has now accepted that capital account regulations can be useful in limited circumstances.

- **The Pakistani parliament should, following a debt audit, adopt a strategy that sets out what foreign lending the whole economy needs. It should then introduce regulations to favour such lending over speculation. All loan contracts should be made publicly available prior to being signed, and subject to parliamentary debate and assent.**
- **Foreign lenders should allow such regulations to be introduced by removing bans on them in trade treaties and by not making loans dependent upon economic policy conditions. All future official aid should be given as grants rather than loans, in light of UN commitments, such as the UNFCCC.[41]**

End notes

1 Crawford (2011): 'War Related Death and Injury in Pakistan' (http://weeklypulse.org/details.aspx?contentID=795&storylist=16).
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