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Pakistan Economy Today and Tomorrow – Surviving The Crisis

PROFESSIONAL ACCOUNTANTS IN BUSINESS (PAIB) COMMITTEE



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This paper is an extract from the ICAP Webinar Series ‘Pakistan Economy Today and Tomorrow – Surviving the Crisis’ held on April 17, 2020, from 9PM to 10:30PM PST. The panel discussion included industry leaders;



Mr. Muhammad Ali Tabbu, CEO, Lucky Cement; and



Mr. Shazad Dada, President, OICCI & CEO, Standard Chartered Bank Pakistan



Mr. Asad Ali Shah, CEO at Asad Ali Shah Associates, Chairman Pakistan Refinery Limited and Member Policy Board of SECP;

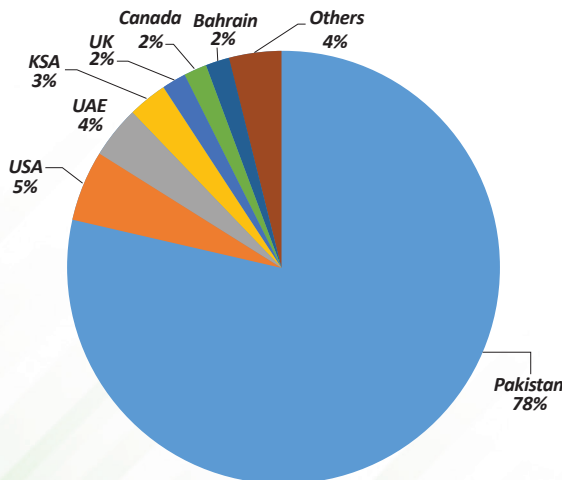


Mr. Ali Khizer, Economist & Head of Research, Business Recorder



'The webinar was moderated by' Mr. Veqar Ul Islam, Director and Chief Executive at Jaffer Business Systems.

*The webinar was viewed by **12,575** participants locally as well as internationally, a quick snap shot of the reach is as follows:*



Statistical realities of the COVID-19 Crisis

Mr. Veqar Ul Islam opened the session by sharing the perspective of the prevailing situation. Following statistics were shared by him to kick start the panel discussion,

- US in the last 4 weeks have lost 22 million jobs, this is more than the job created by US in the last 10 years. Negative 2 million in unemployment.
- COVID is expected to bring half a billion people below poverty line.
- The loss to global economy is expected to be \$9 trillion during the crisis, it is greater than the economies of Japan and Germany combined together.
- The global recession of 2008 shrunk the economy by 0.1 per cent, however, COVID-19 is going to shrink the economy by 3%.
- The vaccine or cure is 12-18 months away so by then we have to live with it.

The biggest challenge at hand is to achieve a balance in fighting the virus and dealing with the economy.

— Veqar Ul Islam

Panel Discussion Summary

Following is a brief of the panel discussion and views shared:

How do you see the economy shaping up in this country and how do you see the financial industry dealing with this crisis?

This is a huge global crisis and its impact is going to be deep and long lasting, however it will also create huge opportunities. Fine balance between human and economy is extremely important. This crisis is a supply side as well as demand side shock. On the supply side, the lockdown has disrupted the production with some of the production completely gone. On the demand side, the business model and the client journeys have been disrupted.

As for the economic recovery, although it is uncertain at the moment, initially it was speculated that it will be a V-shaped recovery or U shaped but I think it will be a W shaped or worst case, L shaped recovery.

All the projections are changing on a weekly basis and sometimes on a daily basis. Right now it is negative 1.5% growth for Pakistan. The interest rates reduction is saving the country 1.3 trillion. This is the first time that the informal economy is getting hit the most compared to formal economy.

Individuals and business leaders need to understand the change in behavior; changes in discretionary spending, savings will become more important specially in the lower income side, loyalty shock, general trust deficit between service provider and the user, value disruption and value creation in different companies of the same sector, high debt low margin companies will get penalized that's where liquidity will become a key question.

On the government side, securing the IMF, RFF multilateral funding is crucial. Moreover, decisiveness and agility shall be the key required attributes.

Along with challenges, opportunities are also emerging under the current situation. Reforming under crisis is better for companies as well as governments. Systematic resistance of change will be reduced. There will be new business models, new value chains, new operating models will be the need of the hour. Digital is the biggest opportunity right now therefore, it is important to construct a digital world that blends well with the physical world. Change in the way we look at cost; fixed costs should be reduced, digital spending budgets shall have to be increased. There has been 15-20% increase in data usage but to increase this further, we need to build an ecosystem, only 35% of cell phone subscribers have smartphones. Some of the examples we can follow to introduce and implement technology in Pakistan can be taken from Korea and China where Artificial Intelligence is being used effectively.

In terms of trade, supply diversification is in the agenda of global suppliers. Companies and governments should restrict non-essential imports. Retail stores that are providing safety and online stores will be the need of the hour.

Qualities of leadership during pandemic

- Have a sense of urgency and agility in decision making
- Launch the plan ahead looking at the timeframe
- Less dependency on projections instead focus on customer confidence signals and own instincts
- Communicate regularly with all stakeholders; clients, regulators etc.
- Collaborate with private sector, public sector, regulators and even competitors

Shazad Dada

Give an account of the life of an entrepreneur and businessmen these days? Country leaders are dealing with human life on one hand and economy on the other; how things have changed over the past month, what could be done better etc.?

The biggest challenge today is for the industries catering to export orders. Pakistan's export market is primarily Europe and USA and since they have stopped orders, the biggest hit is on the apparel industry. Consequently, there are two challenges arising from this situation,

- a. Securing jobs
- b. Liquidity crunch

Whereas, opportunity arising from the current situation is local demand which can be fulfilled by local industries thus helping to recover economy. For instance, since the

government has announced relief for the construction industry, the cement demand from North has returned to 80% however, demand recovery is slow in South. Hopefully by next month, we might start recovery in cement exports.

The relief to the construction industry is a good decision on part of the government as this initiative will help with employment since the 24 allied industries related to the construction sector will also boost.

Another important sector is the agriculture sector where government should ensure support price wherever required. To reduce imports and ensure food security, farmers should be given incentive to grow crops that they don't usually grow.

Opportunity arising from the current situation is local demand which can be fulfilled by local industries thus helping to recover economy. The relief to the construction industry by the government will help with employment in the 24 allied industries associated with the construction sector.

Muhammad Ali Tabba

How do you see Pakistan dealing with the economy and coming out stronger and which are the areas the country needs to focus from a futuristic viewpoint?

This is the third largest pandemic humanity has seen in the last thousand years; black death, Spanish flu and COVID-19. The crisis will likely stay for months or maybe years. It is causing a total pervasive change in businesses, the way we do business and interact with each other. The biggest opportunity is for those people who will adapt to the change as rightly said by Darwin, "It is not the strongest of species that survive, nor the most intelligent that survives, it is the one that is most adaptable to change".

Certain businesses will never be the same in the foreseeable future such as airlines, hotels, travel, tourism, public transport, sport, musical festivals, conferences, manufacturing, retail, service industry, educational institutes; all need to modify.

Pakistan economy was already shrinking, we repeatedly went to IMF to get balance of payment support, government was virtually constrained – the opportunity of the crisis is that because of the crisis IMF/G-20 countries have become very supportive so government has huge space to address the issues such as unemployment, relief to poor, support businesses etc. Along with World Bank and Asian Development Bank support, government will have a fiscal space of about Rs 4 trillion. Central bank has reduced interest rates due to which government cost of borrowing will also reduce that will provide additional space of Rs 1.3 trillion.

The State Bank of Pakistan should reduce 300-400 bps more because with 9% policy rate businesses cannot survive with interest rate of 11-12% which they should bring down to 5-6%.

Government should announce bold steps together with facilities in health, smart lockdowns, providing protection to healthcare professionals etc., invest in reviving the businesses and provide incentives for innovative businesses.

Government should initiate a 5-point strategy

1. Increase the stimulus package from 1.2 trillion to at least 4 trillion
2. Digitize and embrace e-government, communicate and be productive so the services are available
3. Incentivize export based goods and services industry
4. Promote technology related businesses
5. Promote agro based manufacturing that can use local raw material

Asad Ali Shah

R&D perspective

- IMF foresees that Pakistan economy will undergo contraction of 1.5% GDP which means this quarter Pakistan will have shrinkage of about 15% which is the quantum minimum expected.
- External debt over the next few years will be low. This crisis is affecting the informal and formal economy the same way and formal more because it is affecting more on the retail side than the wholesale side which is as big as our agricultural sector.
- When we go digital, the kind of workforce we have (aged 40-60) will lose, however we have a huge influx of youth that can bring change.
- Restructuring mortgage market and retail market is another opportunity to grasp in the current circumstances.
- This is the time to work on the fundamental weaknesses of the economy; energy, consistent fiscal deficit and external vulnerabilities.
- Trade will fall drastically over the period of 3 months or more but remittances will stay.

This is the time to work on the fundamental weaknesses of the economy; energy, consistent fiscal deficit and external vulnerabilities.

Ali Khizer

Audience Questions Answered

It has been a debate whether this crisis can be compared with 2008 crisis or not?

‘Covid19 pandemic has had far more adverse economic impact as compared to 2008 economic crisis.’

Is fiscal stimulus more important or fiscal austerity?

‘We need fiscal stimulus more than fiscal austerity. Lenders and multilateral have been very generous in giving funds to Pakistan and they have been very flexible in announcing the stimulus package of Rs 1.2 trillion. However, stimulus should not only be limited to economy, but should also support small businesses and daily wagers etc.’

How can we protect export related jobs given the issues with the export sector?

‘Export jobs are vulnerable across all segments. Demand will start to pick up later and therefore, it is time to be considerate about employees and protect jobs; maybe do pay cuts rather than laying off people.’

Back to Basics – Is it a myth or reality? In this digital age, can we continue with having a ‘necessities-only’ lifestyle and if yes, then for how long?

‘The biggest thing that will happen in this crisis is that it is going to push the entire world into becoming digital. The nation and people who move in this direction smarter and faster, getting involved in data, exponential technologies and e-commerce will become even a bigger reality.’

Is digitalization over-rated?

‘No, it is under-rated.’

What more initiatives should be taken by the government in addition to providing stimulus to the business and relief to people and will that support the economy?

‘The stimulus packages being offered by the government are not a solution but to relief the liquidity issues for the moment. Government should expand Ehsaas Program because Rs. 12,000 per family for four months makes Rs 3000 per month which is clearly not sufficient because the food expense for an average household for one month is around Rs 11,000. The vulnerable population is about 43 million which needs a bigger support program than this.’

On the fiscal side, we need to give more to the SMEs which are not bankable. Bankable companies and SMEs are being supported by State Bank of Pakistan through deferment of loans and giving fresh cheaper loans for salary expense etc. Moreover, non-bankable SMEs need to have a guarantee mechanism as well.’

Considering the crisis clears up in 6 to 8 months, what opportunities do you see for Pakistan which, if capitalized on time, can give Pakistan’s economy an edge over regional economy?

‘One of the visible internal opportunity is to manufacture domestically while reducing dependence on imports. Since Pakistan has around 220 million people as consumers, businesses can sell to them and save on the very scarce foreign exchange that is hurting the economy from a deficit point of view. From export point of view, demand will be a bit weaker due to changes in buying behavior. At the same time, demand exists; for instance, US has decided not to export meat so Pakistan can export to middle east

because there is a realization in the middle east that being too dependent on certain markets is causing food insecurity.

Businesses and government should use this downtime to address opportunities, get laws and regulations in place, fix cost structure and be geared up for opportunities.'

How can government handle the data for all departments? Should it be centralized?

'All governments have been fast in announcing stimulus packages and lockdowns. However, Pakistan is lacking in using the data and technology such as tracking data points etc. to manage the crisis by use of data analytics. Hence there is an opportunity for the government to employ data analysts, data scientists in Federal Board of Revenue and other social services to take decisions on the basis of data.

Having said that, for data analytics, cyber security is of utmost importance to avoid getting confidential data leaked. Ensuring cyber security will give people confidence in technology.'

Is there a need to restructure institutions such as PIDC, PICIC, IDBP for long term financing?

'These institutions were formed with the idea of providing long term financing that commercial banks which are focused on short to medium term businesses aren't capable of. It is crucial to compare and align long term assets with long term liabilities. With high interest rates, short term liability windows were available and these organizations were moving away from their purpose and what they were formed for so it would be a great opportunity to reform that.'

Interest rate reduction is a short term solution or should it be reduced further to provide support to the economy?

'Prospective inflation number will be lower so the State Bank of Pakistan will have more space to reduce interest rate. To kick start our economy, the best way is to invest and investment will only be possible if investors feel that the interest rate is at a lower level for them to be comfortable to go for short term and midterm funding.'

Global supply chain is declining; what restructuring is needed for sustainability?

'Supply chain is declining and global buyers are looking at markets to understand and be ready.

On the other hand, since Pakistan has never been an integral part of supply chain and its export basket is very small therefore it is going to get least affected in this area.'

Comments on construction sector package from the government.

'Government realized that we need to revive the economy as construction is the sector that will drive growth and bring jobs back. They need to go a little easy on the informal economy as it will stimulate the demand side and we need demand so industry can operate at maximum capacity.

At the same time, we need buyers, so they should give room to buyers as well. In Karachi, there are 30%-40% houses that are empty which is evident of the fact that there are less buyers in the market.

The mortgage market has been really under-penetrated; with interest rates coming down this is a huge opportunity for banks to provide capital to the consumers.'

At policy level, the priorities will change after the crisis or will they go back to the bureaucratic style?

‘Before the crisis started, economy was already shrinking, but now with fiscal space available, government has an opportunity to come up with innovative policies, better package to save livelihood, revive the existing businesses and reward innovation.’

‘Anyone who lives within his means, seriously lacks imagination’

Is there a risk of rupee sliding further?

‘Today, the rupee is appreciated; closed at 163 and it’s a reflection of some of the bilateral relief that we got such as RFF funding which has boarded really well for us. Exports and remittances will be in for a challenging quarter. Although there is uncertainty, there is still opportunity that rupee will be stable.

If Pakistan holds up key exports and remittances coupled with being more disciplined on imports, then the country will be able to bring currency back to normal.’

What has changed in the last 4 weeks?

- ‘ 1. Started working from home
- 2. Bureaucracy is having virtual meetings
- 3. Online stores sales have gone up
- 4. The informal sector is connecting with consumers via SMS’

Which industries are expected to grow and which ones will shrink post COVID-19?

‘Health, hygiene, food and packaging industries will grow while auto, retail and export industries will shrink post COVID-19.’

What is your view on opportunities for construction sector (in terms of government relief) textile sector (in terms of declining exports), manufacturing sector (in terms of low oil prices will it help the sector), banking sector (in terms of supporting SMEs) and automotive industry?

‘I believe construction sector will flourish after the lockdown. It will have support from private sector as well as Government PSDP to develop infrastructure projects. Textile sector particularly export sector will have a major challenge because of decline in demand from retailers. If Government is sensible they should pass the impact of low oil & gas prices by reducing the gas/electricity tariff which will help to reduce the cost of doing business. This is applicable for all industries.

Automotive industry will also see a decline in demand due to Economic Contraction. Banking should support small businesses in this difficult time and Government should also help small & medium businesses to survive in these difficult time.’

Shouldn’t zero rating of export sector be reinstated to ease liquidity crunch?

‘Absolutely, they should reinstate zero rating for only 5 export sectors.’

The moderator concluded the session with the thoughts;

What fundamental structural changes you expect on three fronts, 1) On the organization of economy (how much and which sectors to leave to market forces and which should be directly dealt with by the state). Or in other words any re-balancing

between state and private ownership; 2) How to build safety net for labor and workers; and lastly 3) how this will effect 4th industrial revolution adoption. If west accelerates it then what options, we have who are basically dependent on cheap availability of labor. Their automation of processes will take back the industry (for example apparel) back to European centers.

‘These are complex questions, but here is my response to each of the three questions:

1. On the organization of the economy, minimize the government at all levels. We have highly inefficient and very large governments. For instance, in the federal government, the cabinet, in addition to the Prime Minister, comprises of 50 ministers, ministers of state, advisors and special assistants to the Prime Minister. Additionally, there would be equal number of secretaries who head the ministries / divisions. Compared to this, in the US, the largest economy in the world, there are only 15 secretaries who are part of the cabinet of the President. Similarly, at state level, California, which is the largest state equal to fifth largest economy in the world, has only 10 secretaries, in addition to the Governor. In Pakistan, Punjab has over 50 cabinet members and Sindh has 44 members with similar number of secretaries. Also, positions of President and Governors are totally redundant. There is a large army of unproductive staff. Even KPK and Baluchistan have bigger cabinets than California. The businesses run in public sector, are similarly overstaffed and can never compete with private sector, and it is virtually a waste of tax payer’s money. The annual losses of PSCs have now crossed over a trillion, and this is going on since decades. So, all businesses need to be privatized and size of all governments need to be drastically cut.
2. BISP, now expanded into Ehsaas, has done good work in providing some minimum payments to the population below poverty line. They have also done good work in distributing Rs. 12,000 to over 6 million households, planning to expand to 12 million. Another 4 million unemployed people are planned to be covered. Important thing is to enhance further data about these families and evaluate how to make them as productive as possible, rather than providing only charity. Following objectives should be pursued to make this more productive:
 - Identify at least one member in each family who can do some simple work (if not doing already) to enhance his / her skill so that in a period of one year, the family’s dependence on BISP / Ehsaas is reduced, and the members of the family start to earn.
 - Develop a program to identify unemployed youth, for some minimum education / skill development in consideration of some minimum stipend.
 - Major effort needs to be made to enhance usefulness / productivity and knowledge of this segment by Ehsaas leadership. It should not be just the distribution of doles.
3. Unfortunately, cheap labor is no longer any advantage, in the age of robotics and Internet of Things and other technological advancements. There is no shortcut to prosperity, and unless we invest in our human resources to enhance their basic education and skills, simultaneously developing a strategy to transform Pakistan into an idea economy, where entrepreneurship and risk taking is rewarded and rent seeking is discouraged, we will continue to lag behind, remaining at the bottom of the world. The risk / concern highlighted in the question that even apparel making / textile industry may become uncompetitive is valid. As a nation, we are fast

becoming irrelevant to the world, unless we make major and serious changes in our ecosystem.'

How can we channelize our local demand to compensate the biggest exports hit area i.e. textile, to save jobs?

'Increase the consumption and productivity. For this, we need to gradually open up our economy with some minimum protocols / SOPs. We have to learn to live with new norms and cannot stop living. Good thing is that CV's impact, based on last two months' experience, in terms of fatalities and health crisis is relatively very low when we compare ourselves with western economies of Europe and the US. If we are able to restart the economy with a smart approach to operate, not only we can start production, consumption, but we may also be able start export and regain some of the markets.'

Do you think that, post-COVID, the federal government must establish sector-wise technical committees that includes top industry people to define roadmaps for growth and the bureaucracy be given the role to implement decisions?

'Not post-Covid, but immediately, Federal government should set up some task force to advise on reset of the economy, which may have sub-groups / experts on different sectors of the economy. Such groups should be used for consultation to face current crisis as well as develop future strategy. Consultation with the stakeholders is continuous process, always helpful, but obviously, it is desperately needed during a major crisis. Even for implementation, GoP should not just rely on bureaucracy, rather a robust monitory and evaluation mechanism needs to be built using teams inducted from the private sector.'

The moderator concluded the session with the thoughts;

There is a strong case for policy intervention to construct a digital world.

The Paper is reviewed by Members of the ICAP Professional Accountants in Business Committee; Syed Khalid Noor, Director, Novartis Pharma Pakistan Limited and Mr. Usama Rashid, CEO, V2F Solutions Pvt. Ltd.

Polls conducted during the webinar

During the webinar, polls were conducted with respect to the prevailing situation, recovery from this situation and related questions. Following is a summary of the answers received:

