Chapter 2

An Analysis of the Military Coup d'etat in 1999

— Economic Conditions Leading to the Coup —

Introduction

A bloodless military coup d'etat by General Musharraf broke out on October 12, 1999. This has placed Pakistan under military control for the fourth time since its independence[1]. The direct cause of the coup is attributed to the deterioration in rapport between the military ruler and Nawaz Sharif, the then Prime Minister, but the reason why the people supported the coup lay in continued economic downturns under the Bhutto and Nawaz democratic regimes since 1988. And the fact that Nawaz came from the business community led people to put particularly high expectations on him to revive the economy and put it back on the road to prosperity[2]. Unfortunately these expectations were not fulfilled and public sentiment for change mounted, making room for the military to take extreme action.

Nawaz Sharif became prime minister for the second time when his party won the general election of February 1997. Immediately after his inauguration, Nawaz set himself to work on restoration of the economy and announced a series of economic reform plans to prevent the economy from deteriorating further. Unfortunately, however, Nawaz's tenure was hit by several external shocks: the East Asian economic crisis, Indian's nuclear detonation, and skirmishes at Kargil in Kashmir. These events caused a delay in implementing the plans and put the prime minister in a difficult situation. With per capita GDP growth in 1998/99 edging past that for the previous year by a mere 0.8 percent[3], he barely managed to keep the status quo of the already deteriorated economy.

In this chapter, we overview economic conditions under the civilian rulers since 1988, especially focusing on the second Nawaz regime from 1997 to 1999, and try to analyze the coup from an economic point of view. We also briefly discuss the economic prospects of General Musharraf's military government.

2.1 An Overview of Economic Performance

2.1.1 From Independence to the Zia Military Regime

During the first ten years after independence in 1947, economic growth in the new nation with little industry and no infrastructure was slow, averaging 2.9 percent per annum (see Table 1). Momentum picked up, however, when Ayub Khan, the first military ruler, presided over the nation from 1958 to 1968. Real GDP growth accelerated to 6.77 percent during the 1960s. Industrialization started and the Green revolution resulted in improved productivity in the agriculture sector. Although economic stagnation was observed in the 1970s during Zulfikar Ali Bhutto's government (1971-1977), overall the economy grew 5.65 percent per annum on average during the 30 years from the beginning of the Ayub Khan regime to

Table 1 Economic Growth under Different Political Regimes (average annual growth rates in %)

	Competitive Parliament Democracy 1947-1958	1st and 2nd Military Dictatorships (Ayub and Yahya) 1958-1971	Civilian Dictatorship (Bhutto) 1971-1977	3rd Military Dictatorship (Zia) 1977-1988	Return of Parliamentary Democracy 1988-1999	2nd Nawaz Regime 97/98	2nd Nawaz Regime 98/99
GDP Growth	2.9	5.3	5.4	6.7	4.1	4.3	3.1
Population Growth	2.5*	2.2	3.2	2.8	2.5	2.4	2.3
Per capita GDP growth	0.4	3.1	2.2	3.9	1.6	1.9	0.8

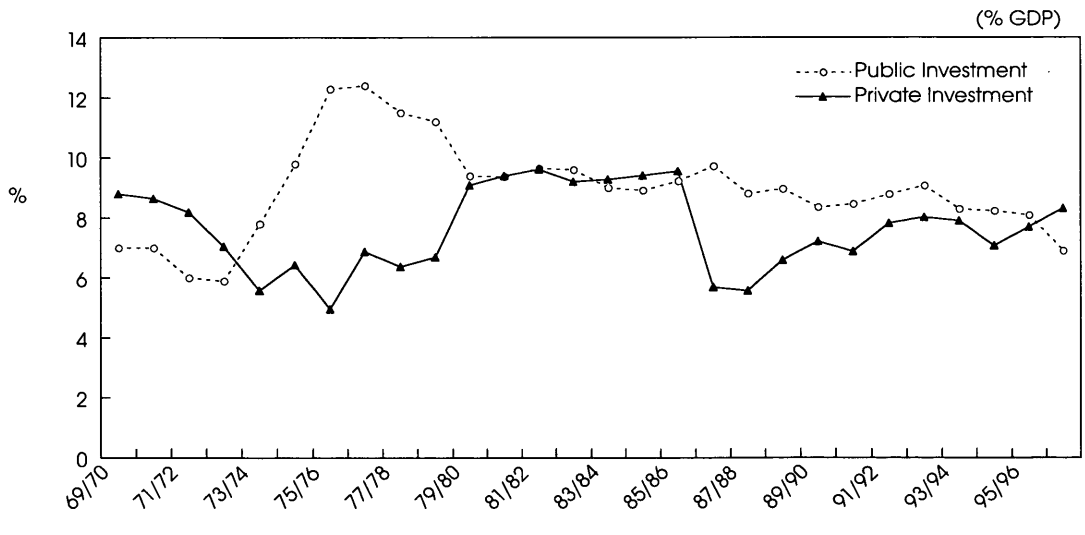
Source: Burki (1999) *Pakistan: Fifty Years of Nationhood*, p103, table 3.4, and the Government of Pakistan, *Economic Survey*, various issues.

Note: * Figure for the period 1950 to 1958.

the end of Zia ul-Haq's military government (1977-1988). As is well known, Pakistan achieved the highest average annual growth rate under the Zia military regime.

The economy at the time Zia ousted Bhutto in 1977 had been on a downward trend due mainly to Bhutto's nationalization policy under the name of "Islamic Socialism"[4]. To revive the economy, Zia started denationalizing the industries frozen by Bhutto, encouraging private sector investment (see Figure 1). But the main engine of economic growth heavily relied on external resources[5]: economic assistance from the U.S., along with the Soviet invasion of Afghanistan and worker remittances from overseas Pakistanis, mainly those working in Middle East countries[6].

Figure 1 Investment Ratio



Source: Data from *Macro Time Series: Global Development Network Growth Database* by William Easterly and Hairong Yu posted on http://www.worldbank.org/html/prdmg/grthweb/GDNdata.htm.

Although Zia's tenure is often characterized as one of economic prosperity, the fiscal position of the country had deteriorated, and was later labeled "bankrupt" by Mahbub ul Haq, Finance Minister during the late Zia period. Fiscal deficits reached 7 to 8 percent of GDP every year and overall debt, including domestic and external debt, increased to around 80 percent of GDP. In particular, defense expenditure rose 9.2 percent annually and interest payments on debt increased by 15.2 percent every year[7]. On the other hand, public spending on social development and infrastructure increased by just 3.2 percent per annum, limiting the nation's economic and social developments in the future to low levels.

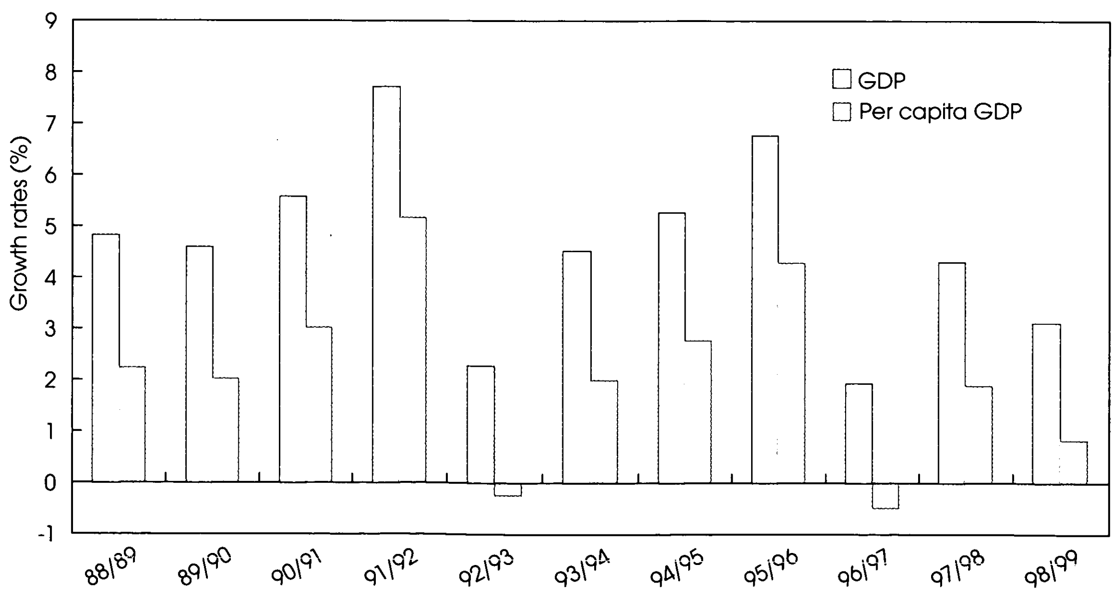
2.1.2 Revival of Democracy and a Decade of Low Economic Growth

Zia died in a mysterious airplane crash in August 1988. After a transitional period under acting president Ghulam Ishaq Khan, general elections were held in November 1988 and Benazir Bhutto of the Pakistan People's Party (PPP) took office as prime minister. The death of Zia ushered in Pakistan democracy once again, but the period after Zia was marked by political instability, low economic growth due to structural problems (see Figure 2), and the start of the IMF's structural adjustment program.

Democratic rule was preserved until October 1999 when General Musharraf took military action against Nawaz. During the 10 years of democracy, Benazir Bhutto of the Pakistan People's Party (PPP) and Nawaz Sharif of the Pakistan Muslim League (PML) became prime minister twice in turn.

Saddled with the many negative debts of the past, the economy was not in good shape when Benazir became prime minister. In order to rescue the country, the democratic governments since 1988 launched economic liberalization poli-

Figure 2 Economic Growth under the Democratic Governments



Source: Government of Pakistan, *Statistical Supplement Economic Survey 98/99.*

cies. The first Bhutto government set up the Board of Investment (BOI) and implemented an active policy of inviting foreign investment. The first Nawaz government that succeeded followed more or less the same policies and carried out privatization of nationalized enterprises. Under the second Bhutto regime, the private sector's involvement in infrastructure building was encouraged. In the area of electric power production, the government adopted the Independent Power Producer (IPP) scheme, a scheme whose benefits had been recognized in other Asian countries, and succeeded in attracting private investment in this area by offering easy contracts. Later these contracts signed under the IPP scheme were harshly criticized by the second Nawaz government, which aimed at undermining Benazir Bhutto's political influence. Nawaz charged that the contracts were concluded by bribing Benazir and her husband Asif Ali Zardari and caused huge losses to the nation. He announced the abrogation of these contracts and ordered IPP producers and the authority to renegotiate terms. The IPP issues have yet to be resolved, causing considerable detrimental effects on foreign investment in Pakistan (see more on this in chapter 3).

The second Nawaz government continued economic liberalization, but despite the efforts made since 1988, the economy did not show steady signs of recovery. Structural macro-problems, poor governance, and political instability negated the positive effects of economic liberalization. The average real GDP growth rate for the period between 1988/89 and 1998/99 ended up at just 4.1 percent per annum. Over the same period, the growth rate exceeded 6.0 percent only two times. Taking into account of a 2.5 percent population growth for this period, the annual per capita GDP growth rate dropped to a disappointing 1.6 percent, which is way below the rate achieved during the Zia regime.

Low growth rates after the revival of democracy might be explained by the political instability reflected in eight changes of regime, including four caretaker governments. It is important to note that none of these regimes completed its five-year tenure. These frequent changes of regime resulted in frequent changes of policy and framework, leading to a lack of long-term policy implementation. Also relevant was the impossibility of tackling and solving structural problems under short-lived regimes.

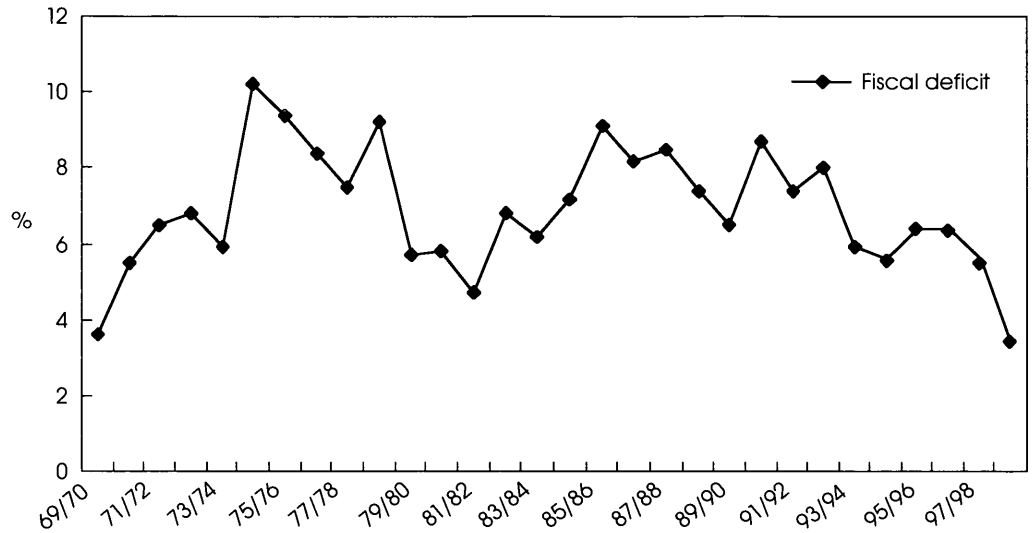
2.2 Structural Macro-Problems

2.2.1 Fiscal Deficits

One of the major structural problems facing Pakistan is a chronic fiscal deficit over more than 30 years caused by low tax revenue and growing non-development expenditure (see Figure 3). On the revenue side, although substantial tax reforms have been carried out, they have yielded only marginal improvements in tax collection due to the inelastic tax structure. Numerous tax exemptions and concessions abound as a result of political pressure, severely narrowing the tax base. For example, agricultural income tax was not imposed until quite recently because the majority of politicians are of the landed classes[8]. The tax-to-GDP ratio has improved from 9 percent in the 1960s and 1970s to around 13 to 14 percent in the 1980s and 1990s, but it is still too low to cover expenditure. In addition, tax evasion and corruption of revenue officers are epidemic and have further reduced tax revenue.

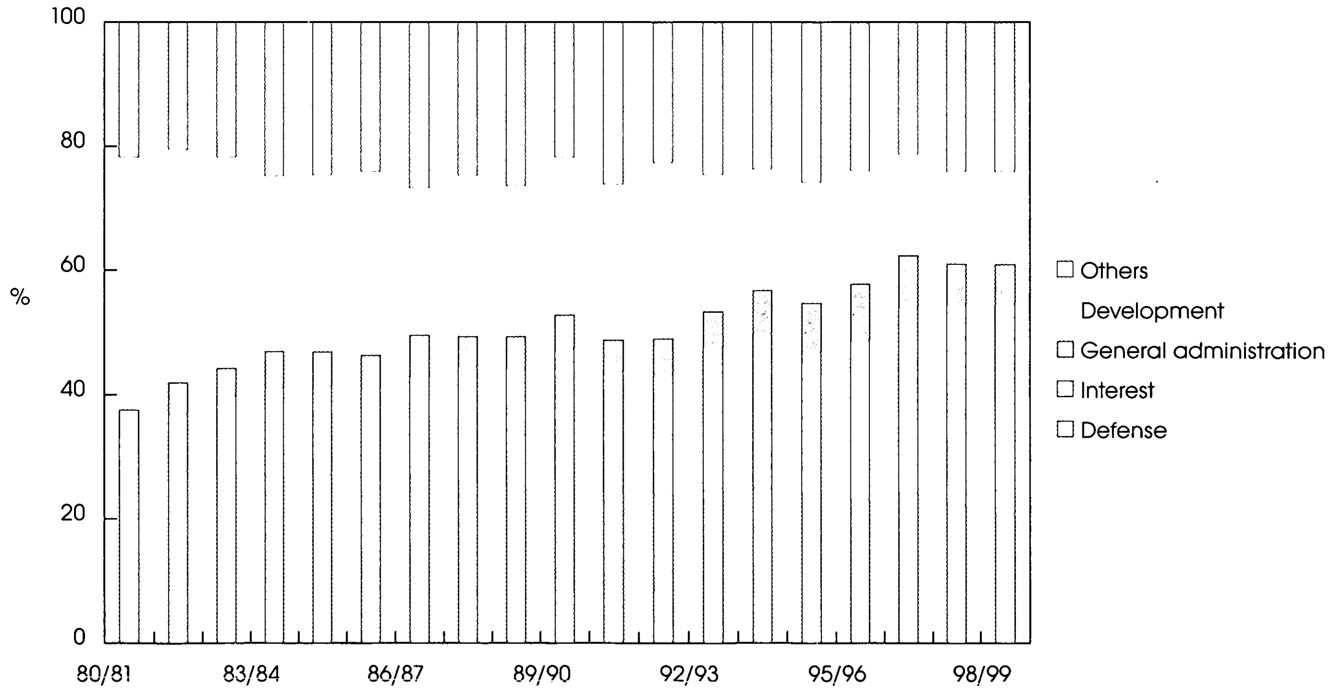
On the expenditure side, increasing interest payments and defense expenditures have eaten more than 50 percent of the federal budget every year, leaving little room for adjustment (see Figure 4). Furthermore, inefficiently managed public sector enterprises have been operating at a loss, incurring a burden of debt. Tax and expenditure

Figure 3 The Ratio of Fiscal Deficits to GDP



Source: Government of Pakistan, *Economic Survey*, various issues

Figure 4 Trends in Government Expenditure



Source: Government of Pakistan, *Statistical Supplement Economic Survey 98/99.*

policy reforms have been proposed under the IMF's structural adjustment programs, but the pace of implementation is slow due to rent-seeking activities from the landed aristocrats and business community.

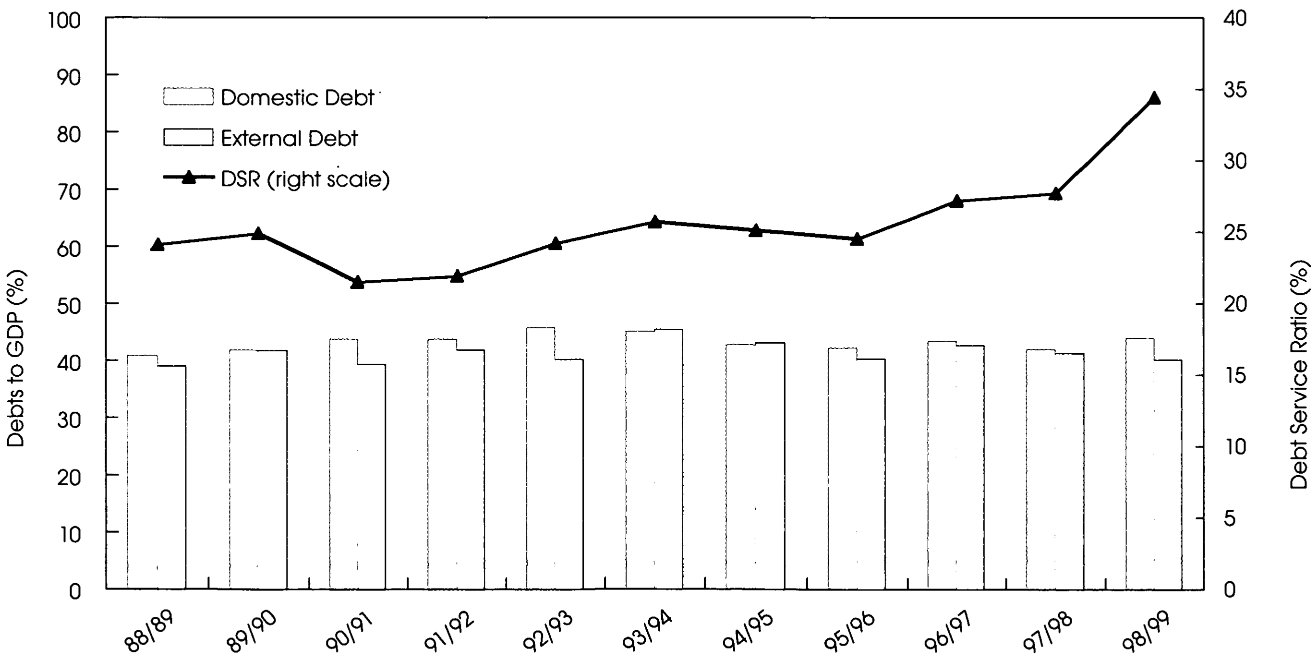
Besides the problems above, Pakistan's tax system has created an unfavorable environment to domestic manufacturing industries. Under Pakistan's tax system, tax revenue has been heavily dependent on indirect tax, especially on import duties[9]. Import duties, however, have provided incentives to smuggle goods into Pakistan and deter the development of domestic manufacturing industries.

2.2.2 Domestic and External Debt

The external and domestic debt position of Pakistan has been at an alarming level because of continued fiscal and balance of payments deficits over the years. In 1980/81 the debt-to-GDP ratio was 54.4 percent, but it increased to 84.3 percent in 1998/99. This rapid increase in debt accumulation is owing to borrowing from the non-banking sector during the1980s[10] and decreasing a portion of grant out of economic assistance. Consequently interest payments have swollen as well. In 1980/81 the size of interest payments was 2.1 percent of GDP and 9.2 percent of the government budget, increasing to 6.9 percent and 34 percent, respectively, in 1998/99. The debt-service ratio (DSR), a measurement to gauge the ability of paying off external debt, has been constantly above 20%, a level considered to be unsustainable (see Figure 5)[11].

Foreign exchange earnings have been stagnant, making debt service payments even more difficult, especially after 1992. A poor cotton harvest due to virus attacks and bad weather, and a consequently low level of cotton production,

Figure 5 Public Domestic and External Debts



Source: Government of Pakistan, *Economic Survey 98/99*.

coupled with increasingly tough competition in the international market, contributed to poor performance of cotton-based exports, which comprise a major part of total exports. Another major source of foreign exchange earnings is overseas Pakistani workers' remittances. These workers' remittances peaked in 1982/83 at US$2.88 billion, but due to the Gulf war, economic recession in the Middle East, and several other factors, the amount has been declining, reaching US$1 billion in 1998/99.

In order to ease external payments difficulties, the first Nawaz government allowed domestic residents to hold foreign currency accounts in domestic banks with a view to luring foreign currency to Pakistan. This scheme was successful in terms of obtaining foreign exchange but it had a negative effect on the fiscal side. Since the exchange risk associated with foreign currency accounts was covered by the State Bank of Pakistan, continued depreciation of the rupee created huge annual losses to the Bank[12].

2.3 Economic Situation under the Second Nawaz Government

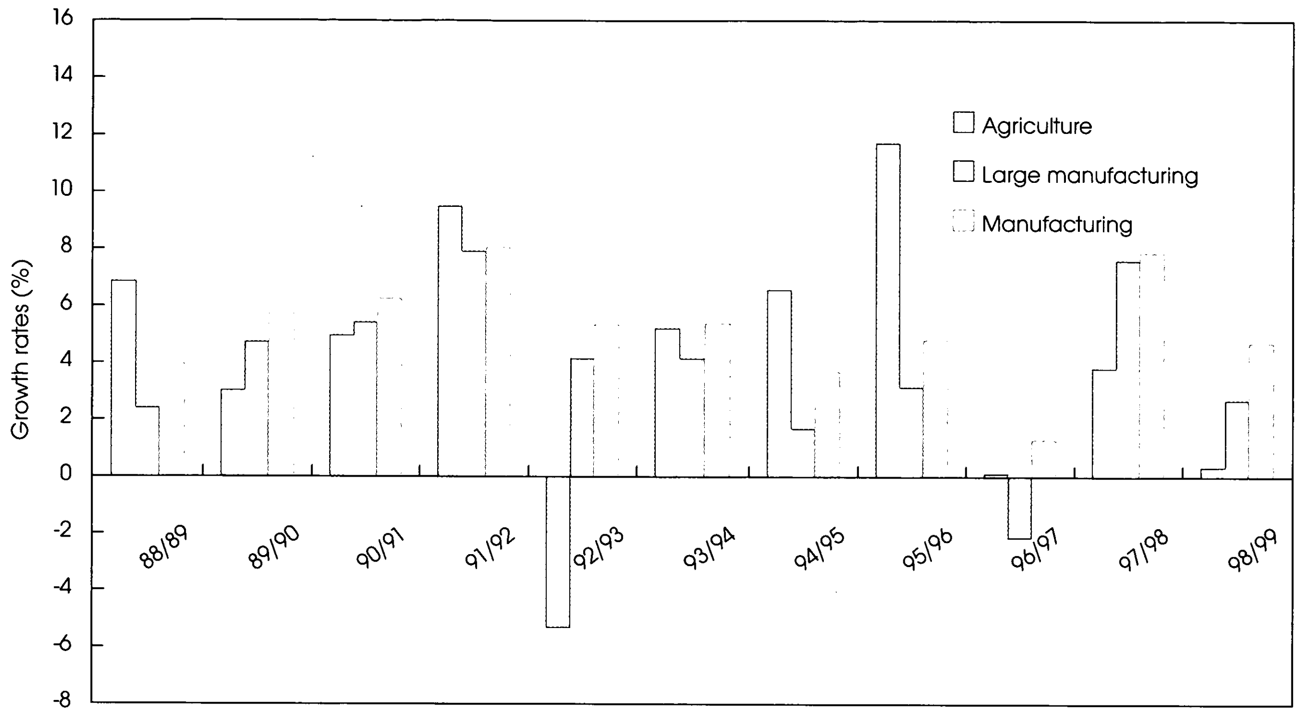
2.3.1 Economic Revival Plan

Benazir Bhutto was sacked in November 1996 by Leghari Farooq, the then President. In February 1997, general elections were held and the Pakistan Muslim League won a majority in the National Assembly as well as in the provincial assemblies, leading Nawaz Sharif to be prime minister for the second time. When he took power, the Pakistani economy was in such a state of crisis that it was even having difficulty keeping afloat. Business confidence was shattered and domestic and foreign investors had lost interest in Pakistan because of its political instability, inefficiency and corruption in the public sector, and deterioration of law and order. Structural problems such as fiscal deficits and mountainous debts contributed to the difficulties. The overall performance of the economy in 1996/97 illustrated all too well the state of health of the economy (see Figure 2). Agricultural production did not show any growth, and the manufacturing sector could make no significant progress with the large-manufacturing sector registering negative growth (see Figure 6). The economy registered a mere 1.93% real GDP growth, the third worst figure in the last 40 years. Even worse, the real per capita GDP growth rate was a minus 0.8 percent, contracted from the previous year.

A top priority of the Nawaz government was the recovery of the economy. Immediately after taking office, Nawaz announced a series of economic revival plans. Focusing on regaining investors' confidence in Pakistan and macroeconomic stability as well as structural reforms, these plans included: 1) tax and tariff reforms, 2) debt restructuring program, 3) banking and financial sector reforms, 4) capital market development, 5) export promotion, 6) agriculture incentive package, and 7) improvement in public institutions. The overall package was well received by the IMF and the World Bank, and the IMF resumed a structural adjustment loan program of US$1.6 billion for a three-year period in October 1997.

The immediate effects of the economic revival plans appeared in the industrial sector. By November 1997 industrial production had not show any sign of recovery, but it increased by 10 percent in December 1997 over the same month of the previous year and grew further in February 1998, registering 22 percent growth. The overall growth rate of the manufacturing sector in 1997/98 showed a higher growth, 7.88 percent, than the 3.1 percent growth in 1996/97. Other positive signs of recovery were found in the areas of fiscal deficits and inflation rates. With the introduction

Figure 6 Economic Growth by Sector since 1988/89



Source: Government of Pakistan, *Statistical Supplement Economic Survey 98/99.*

of the IMF's structural adjustment program, the ratio of fiscal deficits to GDP was curtailed from 6.4 percent in 1996/97 to 5.6 percent in 1997/98 and the inflation rate, from 11.8 percent to 7.8 percent. Despite the East Asian financial crisis and prolonged economic recession in Japan, which is one of Pakistan's main export destinations, exports in 1997/98 increased by 4.2 percent. The agriculture sector had recorded low growth in the preceding year, but it picked up in 1997/98 to 3.82 percent growth. In the end, real GDP grew by 4.3 percent, showing some signs of recovery. However, the structural problems still remained and the speed of policy implementation was slower than originally envisaged. In addition, the law and order situation, especially in the Karachi area, deteriorated further. The IPP-related problems and contagion effects from the Asian economic crisis discouraged foreign capital inflows to Pakistan.

2.3.2 Crisis Management

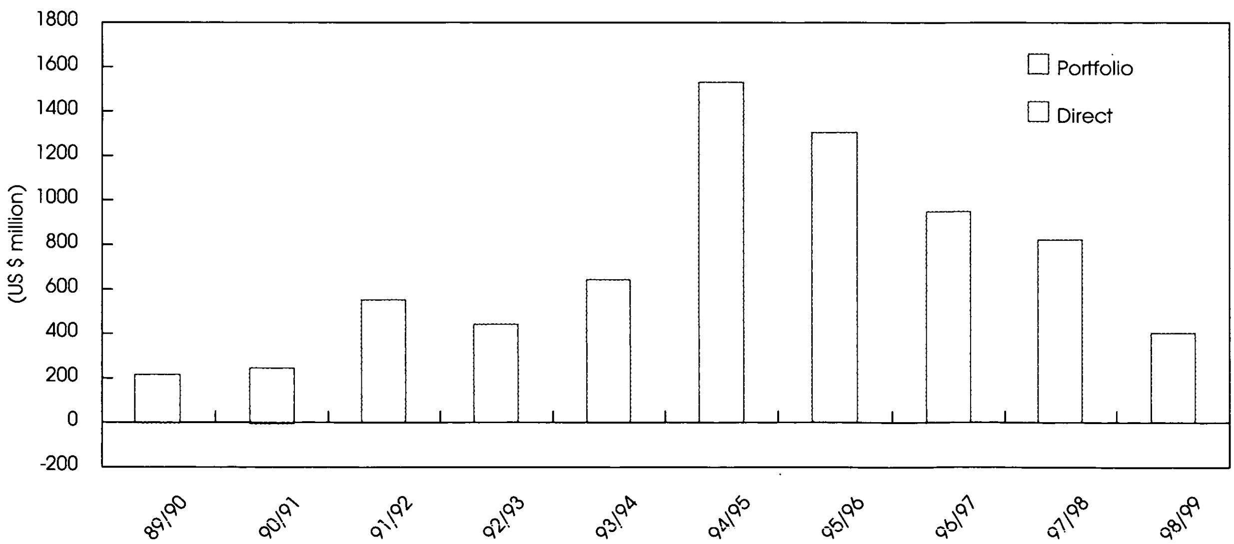
Although the figures had shown a little hope for economic recovery, the Nawaz government was forced to shift from the implementation of economic revival plans to crisis management due to an unexpected external shock, namely, India's detonation of a nuclear device. As in the past, the fate of Pakistan was once again shaken by external factors.

On May 28, 1998, Pakistan responded to India's nuclear testing by conducting its own series of nuclear tests. Immediately after the two countries' nuclear tests, the US and Japan imposed economic sanctions on Pakistan and India, and international organizations such as the IMF and the World Bank suspended their loans. These sanctions immediately put Pakistan on the verge of defaulting on its debt service payments but took only a small toll on India, which had a sufficiently large pool of foreign exchange and was less indebted to foreign sources. Pakistan had US$1.3 billion worth of foreign reserves prior to the nuclear detonation, but in November 1998 this dropped to US$400 million, which just covered values of imports for two weeks.

The freezing of foreign currency accounts announced on the day after the nuclear testing and restrictive measures on foreign remittance applied later, coupled with the IPP problem, were enough to make domestic and foreign investors shy away from investing in Pakistan. As a result, foreign direct investment dropped by 37 percent to US$376.6 million in 1998/99 from US$601 million in 1997/98. Portfolio investments, in particular, plunged 88 percent from US$221.3 million in 1997/98 to US$27.3 million in 1998/99 (see Figure 7). And also the freezing of foreign currency accounts and subsequent exchange controls by the State Bank of Pakistan, resulting in wider open market exchange rate premiums, had the effect on Pakistanis, especially overseas Pakistanis, of making them shift from formal to informal channels of remittance. Part of the decline in workers remittances from US$1.5 billion in 1997/98 to US$1 billion in 1998/99 can be attributed to this cause (see Figure 8).

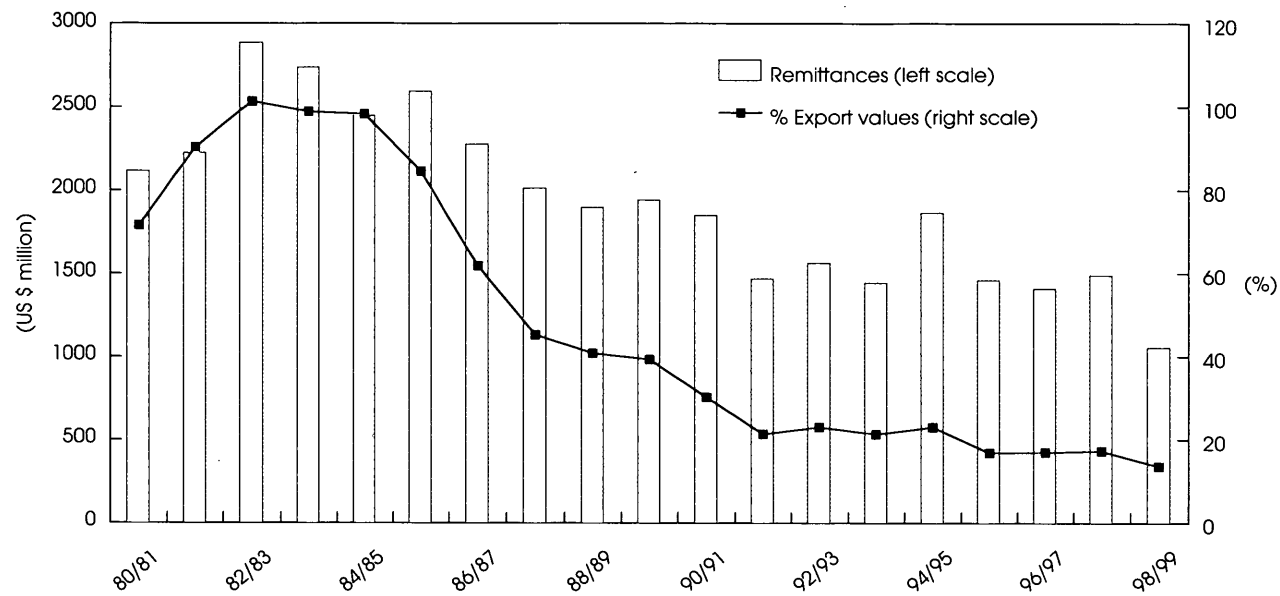
Several measures to prevent foreign capital outflow such as the imposition of cash margins in opening L/Cs[13] and introduction of composite rates[14] immediately affected imports. The values of imports decreased by 9.3 percent to US$9.43 billion from the previous year. Lack of imported raw materials, however, lowered the level of production in the large-scale manufacturing sector, with a growth rate of only 2.7 percent, down by about 5.0 percentage points from the figure in 1997/98. Exports also shrunk by 10.2 percent in 1998/99 compared to the figure in the previous year. The positive effects of depreciation of the rupee were negated by the worldwide recession, low

Figure 7 Trends in Foreign Investment



Source: Government of Pakistan, *Statistical Supplement Economic Survey 98/99.*

Figure 8 Trends in Worker Remittances



Source: Government of Pakistan, *Statistical Supplement Economic Survey 98/99*

cotton production, and stagnated manufacturing production due to the above reasons. The real GDP growth rate of 1998/99 decreased to 3.1 percent, down from the 4.3 percent of the previous year, and far from the target of 6.0 percent.

2.3.3 Structural Reform by the IMF

The suspension of loans from international financial institutions had driven Pakistan into the corner of default, but the IMF reached an agreement with the government of Pakistan on conditionalities to resume lending in late November 1998. In January 1999, the board of the IMF formally approved the release of loans and resumed lending to Pakistan. In addition to the loans from the IMF as well as financial support from the World Bank and the Asian Development Bank, approvals were given for public debt rescheduling worth US $3.3 billion by the Paris Club and for private debt rescheduling of US $900 million by the London Club. The size of the overall debt rescheduling came to around US $7.7 billion. The rescue package saved Pakistan temporarily from a debt service payments crisis, but at the same time shackled the country with the conditionalities imposed by the IMF.

The main aim of the IMF program is to reduce fiscal deficit, which had been the major item of the past structural adjustment programs. Setting the level of fiscal deficits at 4.3 percent of GDP in 1998/99 and 3.3 percent in 1999/2000, the conditionalities focusing on tax revenue collection include: 1) raising the GST (general sales tax) rate from 12.5 percent to 15.0 percent, 2) abolishing sales tax exemptions on oil, gas and electricity, 3) extending the GST to the service sector, and 4) reinforcement of taxation on agriculture income. Other conditions include tariff reduction, privatization of public enterprises, and the settlement of IPP problems.

In 1998/99 Pakistan almost cleared the fiscal deficit target set with the IMF. The ratio came down to 4.5 percent of GDP, but the tight budget was not able to jump-start the recession-hit economy. Development expenditure was cut in order to achieve the fiscal deficit target[15]. It should be carefully noted that the declining trend in development expenditure since 1988/89 would be obstacles to the Pakistani economy's long-run prosperity.

From late August to September 1999, nationwide general strikes were organized against the introduction of retail GST. Traders ostensibly opposed to it because: 1) GST might discourage consumer demand for goods, 2) the documentation process was complicated, and 3) it could lead tax officials to solicit bribes. However, the real reason they opposed to the GST was because they feared that its introduction would mean documentation and exposure of their business activities, leaving little room for tax evasion. But whatever the reason, the strikes against the imposition of retail GST spread throughout the nation. The opposition parties jumped on the anti-GST bandwagon to gain as much political mileage as possible. With this issue as a turning point — coupled with Nawaz's decision to withdraw freedom fighters from Kargil, Kashmir, a step much criticized by the public — anti-Nawaz feeling mounted and calls for him to step down snowballed.

2.4 Economic Management by the Musharraf Regime

The military coup of October 1999 took place amid shouts of dissent against the Nawaz government. The timing was perfect for General Musharraf to legitimate the military action.

General Musharraf pledged as a top priority to restore the economy, impoverished under the Bhutto and Nawaz governments. He formed a National Security Council (NSC), with himself as chair, and appointed Dr. Muhammad Yaqub, the governor of the State Bank of Pakistan, as the NSC member dealing with economic issues. He also appointed Mr. Shaukat Aziz of the Citi-Group finance minister, and Dr. Ishrat Hussain of the World Bank to replace Dr. Yaqub at the State Bank.

Soon after General Musharraf took office, he started a loan recovery drive. A list of bank loan defaulters was released and they were warned to repay outstanding debt arrears within one month. By the due date, Rs 8 billion out of a total of Rs 211 billion in non-performing loans (NPL) were recovered. Since this is only 4 percent of total NPL, some criticized the loan recovery drive as just creating noise in the credit market, resulting in fewer credit advances to the private sector. Nonetheless, the operation achieved its goal of restoring public confidence in the government. And considering the fact that there is not sufficient liquidity to make full payment of Rs 211 billion in cash, and the fact that the Rs 211 billion rupee is somewhat overstated, including as it does not only principles but arrears of interest payments, it can be said that the loan recovery drive was rather successful.

Debt rescheduling agreements with member countries of the Paris Club are almost concluded. By the end of March, 2000, Pakistan reached an agreement with the 17 out of 18 member countries. The Pakistani government also successfully avoided being the first to default on eurobond by offering an attractive eurobond exchange scheme to bond holders and mitigated possible damages in the international capital market.

On December 15 1999, General Musharraf announced an economic recovery plan. In an appeal to restore investors' confidence and establish accountability in the public sector, he named the following four areas as keys to economic revival: 1) upgrading of the agriculture sector, 2) vitalization of small and medium industry, 3) encouragement of oil and gas exploration, 4) development of the IT industry. He also stressed that measures to alleviate poverty would be introduced and tax reforms such as the GST imposition across the board and agriculture income tax collection would be implemented. The plan was well received and Karachi's stock market index rose by 20.81 points, 1.5 percent up from the previous day. The IMF and the World Bank also welcomed the recovery plan.

General Musharraf's economic management looks promising, but the crucial moment lies ahead. There are at least three critical issues to be settled in the short-run. First on the agenda is the resumption of the IMF loan, which has been held up since July 1999 due to delay in implementing conditionalities. To this end, it is imperative to introduce the unpopular retail GST, but the business community has already hinted that they would call a nationwide general strike like the one last year. In addition to introducing the GST, the IMF has asked the government to revise the price scheme currently governing oil products to reflect the recent surge in the international crude oil prices. The loans from the IMF are much needed, but the implementation of conditionalities has been controversial and unpopular. From the experience of previous governments, one cannot discount the possibility that implementation might even deal General Musharraf a fatal blow, so the decision on this issue will be extremely tough for the government.

Secondly, debt service payments starting from January 2001 must be prepared. Thanks to Paris Club agreements, Pakistan has survived the default crisis of last fall and gotten a breathing space. Nonetheless, debt repayments start again from the beginning of next year. Given Pakistan's poor performance in obtaining foreign exchange, the government has to be fully aware that there might be another default crisis if it does not take appropriate measures. Furthermore, market conditions are not in Pakistan's favor. With declining cotton prices and increasing oil prices[16], Pakistan's current account could get even worse. Higher oil prices weaken Pakistan's export competitiveness and lower cotton prices lead to lower gains from exports without a big jump in export volume of cotton products.

Thirdly but not least, the IPP problem has to be settled. Particularly important, the government must come to terms with HUBCO, which is the biggest producer among the IPPs. Unless the two sides come to terms in a mutually agreeable manner, it will be quite difficult to win back investors' confidence and investment in Pakistan will not pick up.

Conclusion

This chapter has not aimed to link the cause of the coup with economic problems, but rather has tried to examine the coup from an economic point of view. We have shown the grounds for public support of the military action by analyzing recent economic developments, supplementing this with an overview of the economy since independence.

Low economic growth under democratic regimes has not been acceptable to the common people. With the return of democracy, people expected something very positive and drew a rosy picture of the future. Instead, what they saw were rampant corruption in the public sector, deterioration in law and order, increase in violent crimes, and so on. Still, people put their last bit of faith in Nawaz Sharif and expected him to bring the economy back on track. Unfortunately, he was not able to come up to their expectations.

The democratic governments of Benazir and Nawaz are to blame insofar as they failed to do their job, but at the same time we need to recognize that the problems facing this country were not solely caused by the civilian governments in power. They had taken deep root even before Bhutto came to power in 1988. The civilian governments were not able to solve these structural problems under the politically unstable situation that has prevailed since 1988. It also should be mentioned that external shocks such as India's nuclear testing dealt a fatal blow to economic management during the second Nawaz era, leading the nation to an unmanageable level.

The critical question that arises then is what General Musharraf can do. As already argued, it is not possible to solve the structural problems in the short-run. Hence the most important prescription for the country is consistent policy frameworks that can be fully implemented in politically stable environments. However, under pressure to restore democracy from the international community, and with General Musharraf's pledge to do so, the military government might step down in the foreseeable future, leaving many problems unsolved. For the future development of Pakistan, therefore, it is critical that General Musharraf could instill a spirit of reform in the nation, a spirit that must be passed on to successive governments.

Notes:

1. Half of the fifty years after independence were dominated by three military rulers: Ayub Khan (1958-1969), Yahya Khan (1969-1971), and Zia ul-Haq (1977-88).
2. Nawaz's father, Mian Mohammad Sharif, was the founder of the Ittefaq Foundries. The Ittefaq had been nationalized by Zulficar Ali Bhutto (1971-1977), but was returned to the Sharif family by Zia ul-Haq. One of the big industrial conglomerates in Pakistan, it operates textile mills, sugar cane industry, steel mills, and so on.
3. The Pakistani fiscal year runs from July to June. All the figures quoted in this paper are from various issues of *Economic Survey*, the Government of Pakistan, unless specified otherwise.
4. Zulfikar Ali Bhutto is the father of Benazir Bhutto, who presided over the nation twice in the 1990s. The former was arrested on charges of complicity in the murder of his political opponent, and was hanged to death on April 4 1979 despite diplomatic pressure from foreign countries.
5. It is also believed that the narcotics trade greatly contributed to the growth of the service sector of the economy, pushing the overall growth rate even higher.
6. U.S. president Reagan announced US$3.2 billion military and economic assistance for six years in 1981. Additional aid worth US$4 billion was approved in 1986, but it was suspended later when the Soviet Union withdrew from Afghanistan.
7. Figures are taken from Hasan (1999).
8. Political pressure from landed aristocrats succeeded in getting a clause included in the 1973 Constitution, making it legal to exempt agricultural income from taxation.
9. Because of tax reforms, the dependence ratio of custom duties to federal tax revenue has been declining. The figure recorded 46 percent in 1989/90 but decreased to 34.3 percent in 1994/95.
10. Borrowing from a non-banking system has the benefit of avoiding inflation, although it may lead to the crowding out of investment by raising interest rates and accumulation of debt burden. In the 1980s the inflation rates remained at a single digit because the budgetary deficits were financed through borrowing from non-bank sources. On the other hand, in the 1970s and early 1990s, deficits were financed by borrowing from the banking sector, causing inflation rates of more than 10 percent.
11. The debt service ratio is the ratio of annual external debt service payments to annual exports values for a given year. In general, there is a risk of defaulting on loans if DSR exceeds 20 to 25 percent as a rough measure.
12. When commercial banks receive foreign currency deposits, they turn over the foreign currency to the State Bank of Pakistan in exchange for Pakistani rupees. Since the rate used for future conversion from the rupee to the foreign currency was guaranteed by the State Bank at the time of deposit, the depreciation of the rupee in the meantime incurred large losses to the State Bank. Hasan (1999) reports that

the State Bank lost Rs 70-80 billion between 1992/93 and 1996/97.

13. The composite rate was determined by a weighted average of the official rate set by the State Bank and the inter-bank rate. When introduced in June 1998, the weight was 50 to 50, respectively. In March 1999, the weight was modified to 5 to 95. With the introduction of a unified exchange rate (floating rate) in May 1999, the composite rate was abolished.
14. The L/C margin was 30 percent when introduced and was later reduced to 10 percent in January 1999. The margin was abolished in February 1999. However, soon after the coup, the State Bank started re-imposing 10 to 35 percent of L/C margins.
15. The ratio of development expenditure to GDP was 6.9 percent in 1987/88, but it declined to 3.0 percent in 1998/99.
16. The international cotton price declined from US70 cents per pound in September 1998 to US50 cents in November 1999. The international crude oil price increased from around US$10 per barrel in February 1999 to US$25 in November 1999. Refer to ABN Amro Economic Bulletin 5(7) for more details.

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