1. **Balance-of-Payments Situation and Level of Monetary Reserves**

Beginning in the second half of 1956 Pakistan's balance of payments was under serious pressure and in the third quarter of 1958 reserves touched the low at £54.47 million. At this level the ratio of reserves to total annual payments out of the country's own resources in the preceding year worked out to about one third, which could hardly be considered adequate keeping in view the requirement of currency backing and seasonal fluctuations in exchange receipts.

The balance of payments started to recover in the last quarter of 1958 in the wake of active Government measures. During that period a surplus of £4.32 million was recorded which was the first surplus since January-March 1956 and compared with a deficit of roughly £2.49 million in the corresponding quarter of the preceding year and of £2.7 million in October-December 1956. The improvement was the combined result of an increase in export earnings, a reduction in Government expenditure abroad, lower invisible payments and foreign exchange surrenders.

As the policy measures had time to work and with a gradual recovery in the world economy, the improvement in the balance of payments became more visible in the year 1959 when a current account surplus of £18.78 million (excluding aid) was registered as against a deficit of £20.04 million in 1958. As there were substantial capital receipts in addition to the current account surplus the gold, dollar and sterling reserves rose from £57.45 million at the end of December 1958 to £92.06 million at the end of December 1959 or by £34.61 million over the year.

The improvement in the balance of payments was well maintained in the first quarter of 1960. It may be observed in conclusion that the improvement in the balance of payments has been notwithstanding a further deterioration in the terms of trade. Quarterly indices of the terms of trade declined to 50.9 (1948-49 = 100) in 1959 as against 53.9 in the preceding year. This was attributable to a decline in export prices only partly offset by a smaller decline in import prices reflecting in part reduced ocean freight.

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1. This statement has been drawn up along the lines of Parts I and II of the relevant Plan for Consultations.
2. Balance-of-Payments Prospects and expected Movement in Reserves

The rise in the country's foreign exchange reserves which was substantial during 1959 and the first quarter of 1960 has been halted. There has in fact been a decline in reserves in the second quarter of 1960 due largely to the payment of the gold subscription relating to the increased Fund quota and relaxation in exchange restrictions. Government are now planning to stabilize them approximately at the end 1959 level by licensing imports and other payments to the full extent of projected foreign exchange receipts during the second half of 1960. The improved availability of imported raw materials and spare following Government's policy of liberalizing imports of these items and the additional fiscal concessions to industry announced in the last Budget are expected to increase output of manufactured items, in turn making possible larger exports.

3. Special Considerations Affecting the Availability of or the Need for Monetary Reserves

Apart from currency backing provisions, the country requires a fairly substantial level of reserves in relation to its foreign trade because of marked seasonality in movement of exports, cyclical fluctuations in world commodity prices, the threat of harvest failures due to unpredictable natural calamities which may suddenly raise the import requirements (e.g. foodgrains) or cut into the exportable surplus of (e.g. jute, cotton and tea). The growing dependence on foreign aid in recent years has imparted another element of uncertainty as appropriations are made in most cases on an annual basis, even though the commitments relate to programmes of economic development which must be planned for and executed over longer periods of time. Moreover, changes in administrative procedures relating to the timing of negotiation of aid agreements, the issue of purchase authorizations, the commodity-mix of aid programmes and the sources of supply prescribed might generate dislocation in the smooth flow of imports which require correcting through the use of the country's own reserves. Despite the need for adequate reserves, a steady decline had reduced them to Rs.72.5 crores in September 1958. Thereafter, the new Government decided to build them up through a policy of budgeting for surpluses out of the country's own resources. By the end of 1959, the reserves had touched a level of Rs.122.7 crores, at which it was decided to stabilize them.

4. Factors, either External or Internal, Affecting the Various Elements of the Balance of Payments, such as Exports and Imports

A large part of the strain on balance of payments during 1956-58 was attributable to the difficult food situation necessitating substantial imports of foodgrains from our foreign exchange resources. The total amount of foreign exchange spent on food imports during 1956 amounted to Rs.13.68 crores. It rose sharply to Rs.21.26 crores in 1957. Though the value of food imports during 1958 declined to Rs.13.09 crores, it was still high in view of the meagre foreign exchange resources. Foreign exchange outlays on food imports during these years would have been in fact larger but for Rs.0.75 crores worth of foodgrains received as aid from friendly countries. Government have launched an all-out effort to improve the food situation which has brought about a perceptible improvement since October 1958.
A "crash programme" for agriculture has been launched by the Government covering a number of districts in East Pakistan and West Pakistan. The programme aims at increasing per acre yields in selected districts through the introduction of improved methods of cultivation.

5. Effects of the Restrictions on the Balance of Payments and the Expected Duration of the Restrictions

Restrictions imposed in the past years have been designed to apply scarce foreign exchange earnings to the most essential needs of economic development and mandatory consumption. Given the size of development outlays projected for the next five years, it will not be possible to eliminate or even substantially reduce the restrictions on non-essentials. Within this general framework of policy, the maximum liberalization will be attempted in the light of the evolution of the country's foreign exchange earnings.

6. Prospects of Relaxation or Elimination and Likely Effect of such Action on the Balance of Payments

In view of the substantial improvement in reserves, Government have gradually moved towards import liberalization. The licensing policy for the second half of 1960 has placed several essential consumer and industrial requirements, such as drugs and medicines, iron and steel etc., on virtual Open General Licence. This factor is likely to increase the payments liability. However, the pressure on the balance of payments due to food imports may be lessened due to larger wheat and rice crops during 1959-60 which may increase domestic availabilities during the coming year.

II. ALTERNATIVE MEASURES TO RESTORE EQUILIBRIUM

7. Internal Monetary and Fiscal Situation and Other Relevant Matters which may Affect the Balance of Payments

Excess demand was generated in Pakistan economy prior to October 1958 solely through the large-scale deficit financing operations of the Government. This was responsible for an increase of Rs.71.61 crores in money supply during the 27-month period ending September 1958 during which the payments position of the country steadily deteriorated. In the budget for the year 1959-60 an overall balance was attained. In order to reduce inflationary pressures a tight money policy was inaugurated by raising the bank rate from 3 to 4 per cent in the middle of January 1959. The higher bank rate was followed by certain selective credit control measures in March 1960 with a view to checking excessive credit expansion in certain sectors.
8. **Internal Action to Preserve or Restore Equilibrium including Long-term Measures such as those designed to raise Productivity and Export Capacity or to Reduce Structural Disequilibrium or Rigidities**

In its efforts to strengthen the payments situation Government has laid special emphasis on increased industrial and agricultural production so as to expand the export potential and promote import substitution. The short-term plan of industrial development announced in March 1959 lays emphasis on the balancing and modernization of existing industries so as to make them work at full capacity, reduce the unit cost of production and thus promote exports.

The Government has set up an Investment Promotion Bureau for furnishing necessary information to foreign and local investors on all aspects of Government's financial and industrial policy and for assisting industrialists in securing facilities for the establishment of new industries.

9. **Other Measures which may Help to Restore the Country's Balance of Payments**

Recognizing the need for stimulating the inflow of foreign capital into the country as a step likely to strengthen the payments position, Government announced new terms for foreign investment specially welcoming foreign capital in industries such as: (1) heavy engineering, (2) heavy chemicals, (3) production of synthetic distillation of coal and gas, (4) pharmaceuticals, (5) antibiotics, (6) mining, refining and processing of all minerals including oil, and (7) manufacture of producers' goods and spare parts. Formerly foreign investors were not permitted to start an industrial enterprise in the country without the participation of local capital. This condition has been relaxed. Foreign capital in approved industries established after 1 September 1954 may be repatriated at any time to the extent of original investment, an appreciation of capital investment and profits ploughed back into approved industrial undertakings may also be treated as investment for the purpose of repatriation. The Government has made it abundantly clear that it has no intention of nationalizing industries involving foreign capital. Should circumstances or an emergency necessitate nationalization, fair and appropriate compensation will be paid in the currency of the country from which the foreign investment originated. Relief from double taxation is available to foreign investors by virtue of Pakistan's agreement with the United States, the United Kingdom, the Federal Republic of Germany, Japan and India. At the same time, foreign technicians employed in industrial undertakings under a contract approved by the Government continue to be entitled to income tax relief.