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Bleeding Pakistan Army Economically

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Key Points

- Informed media persons and analysts in Pakistan have raised growing concerns of Pakistan's economy sliding into free fall.
- Despite the abysmal state of the economy, Pakistan continues to spend 'disproportionately' large sums on its defence.
- While the Pakistan Army continues to get the lion's share of the allocations, the cut in US aid has had visible impact on its war fighting capabilities forcing Pakistan to turn to China.
- Big ticket purchases, salaries, new raisings, production of Pakistan ordinance factories and security of CPEC are likely to be impacted in future.
- Causing a 'binary stretch', keeping the Pak Army out of their cantonments, increasing the maritime threat to the Makran coast and a more aggressive LC response strategy would raise the economic costs for Pakistan.
- It is time to adopt a policy of 'Bleeding the Pakistan Army Economically' as a quid pro quo to Pakistan's policy of 'Bleeding India by a thousand cuts'.

State of the Pakistan Economy

In a hard-hitting piece in the Pakistani magazine, *Newsline* (June 2019) titled 'The Economic Tsunami', Amir Zia shares his growing despondency over the economic situation in Pakistan. The entire issue carries some very frank and forthright comments by eminent economists, former federal ministers and government officials of Pakistan on the 'out-of-control' free fall of the economy with doomsday predictions for the Pakistani people. According to Rehana Hakim, the Editor:

> "They (the people) are reeling from the economic tsunami that has hit all across the board and impoverished thousands. Their dream of a 'Naya Pakistan' has dissipated and there is enough reason for them to take to the streets."

Imran Khan's (IKs) dream of a 'Naya Pakistan', at least economically, is in tatters. Let me reinforce this reality with a few metrics.

- Pakistan's annual rate of inflation rose to 10.34 percent in July 2019 while it was 3.8 percent in April 2018 during the then PML(N) government.[1]

[1] Pakistan's Inflation Rate, Trading Economics, August 2019.

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- Pakistani rupee has devalued by 42 percent since the IK government came to power.[2] Natural gas prices are set to rise by 25 percent even as companies impose job cuts and cost-cutting measures. Amir Zia believes as many as 5 million (M) jobs will be cut in the next five years.
- Unemployment is likely to rise to 6.27 percent by 2021 from 5.9 percent in 2018. The overall unemployment rates amongst the graduates rose to 16.3 percent in 2018 from 5.3 percent in 2007.[3] 5 M people are likely to go below the poverty line (BPL) instead of 10 M jobs promised by IK in his election manifesto.[4] Electricity 'circular debt' is around US $10.6 billion (bn) and increasing at US $6.4 M per day. This is despite the fact that the PML (N) government was successful in meeting its promises of providing electricity by encouraging coal-fired plants (dirty energy).[5]
- Interest rates have risen to 12.25 percent prompting Ashfaque Hassan Khan, a former member of the Economic Advisory Council to remark—"Do you think the private sector will borrow from banks when the discount rate is at more than 12 percent?" The interest rates currently stand at 13.25 percent.[6] With barely 300 companies paying 85 percent of the tax and 2 M (0.6 M are salaried) out of 210 M people paying tax, Pakistan's tax to gross domestic product (GDP) ratio at 11 percent is the worst in the region.[7]
- Only recently, Pakistan has been given US $1 bn as part of US $6 bn International Monetary Fund (IMF) bailout package covering a 3-year period at 3.2 percent interest.[8] The fears are not unfounded. With the sacking of Asad Umar and the nomination of a clutch of western-educated economists led by Dr. Hafeez Sheikh, desperation seems to have set in the establishment. As Amir Zia remarks, "the PM seems to be surrounded by a small group of smooth-talking bankers and new faces who are leading government policies."[9] Dr. Hafiz A. Pasha, a former Federal Minister, does not rule out the imposition of Article 235 of the Constitution, should Pakistan default on the condition imposed by the IMF loan. Article 235 of the Constitution stipulates that a financial emergency can be declared if the President thinks that "a situation has arisen whereby the economic life, financial stability or credit of Pakistan, or any part thereof, is threatened."

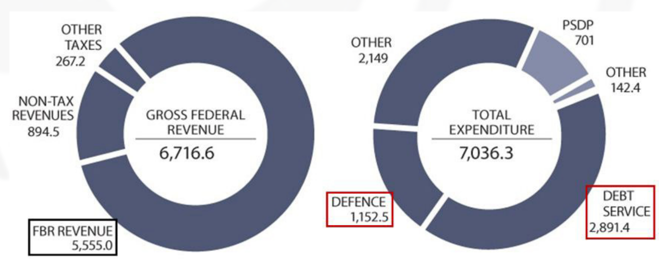
Pakistan's Budget: 2019/20

Salient Features

Some of the salient features are as follows :

- **Net Revenue Receipts:** The total federal revenues are estimated at PKR 6.717 trillion (tn) with the collection of revenues by the Federal Board of Revenue (FBR) estimated at PKR 5.555 tr (Figure 1).

Figure 1: Budget at a Glance[10]



Source: Khaleeq Kiani, 'Tax Heavy Budget Fails to Arrest Growing Fiscal Deficit', *Dawn*, 12 June 2019

- **Expenditure:** Out of the total revenue collections, an amount of PKR 2.892 tn, which is well over 40 percent, has been earmarked for Debt Servicing while PKR 1.153 tr, which is nearly 17 percent of its budget, has been earmarked for defence.

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2 Amir Zia, 'The Economic Tsunami', *Newsline*, June 2019, p. 18.

3 Abrar Hamza, 'Unemployment Among Graduates Rising at an Alarming Rate', *Daily Times*, 23 April 2019.

4 Akbar Zaidi, a leading economist quoted by Amir Zia in Abrar Hamza, 'Unemployment Among Graduates Rising at an Alarming Rate', *Daily Times*, 23 April 2019.

5 Asad Hashmi, 'Lights Out: Greater Circular Debt Cripples Pakistani Power Sector', *Al Jazeera Business & Economy*, 12 May 2019.

6 Reuters, 'Pakistan Raises Key Interest Rates to 13.25%', *Gulf News, Reuters*, 16 July 2019.

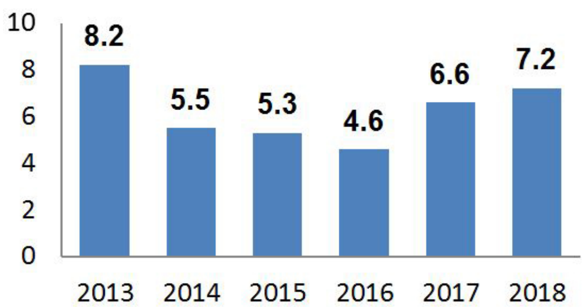
7 Amir Zia, op. cit (2).

8 Kunwar K Shahis, 'The IMF Takeover of Pakistan', *The Diplomat*, 18 July 2019.

9 Amir Zia, op cit (2), p. 20.

10 Khaleeq Kiani, 'Tax Heavy Budget Fails to Arrest Growing Fiscal Deficit', *Dawn*, 12 June 2019.

Figure 2: Annual Budget Deficit (in percentage of GDP)



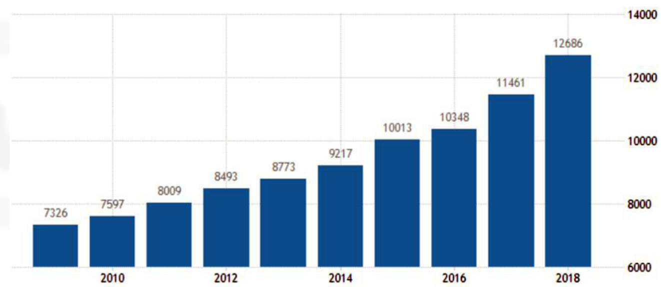
Date Source: www.ceicdata.com
Figure Annotated by Author

- **Budget Deficit:** The consolidated fiscal deficit has been estimated at PKR 3.137 tn or 7.1 percent of the GDP which is to the higher side when compared with the previous years (Figure 2).

Pakistan's Defence Budget

- A week before the Budget was announced, Pakistan's Army Chief General Qamar Bajwa announced that the armed forces would be foregoing their routine increase in the annual defence budget. On the face of it, the projected expenditure of PKR 1.15 tn (PKR 1,150 bn) for 2019/20 stands at near parity with the previous year's budget allocation of PKR 1.10 tn (PKR 1,100 bn). While the increase is a nominal 4.5 percent, one needs to understand the complexities of Pakistan's Defence Budget in more details.
- The projected Defence Budget for 2018/19 was PKR 1.1 tn (PKR 1,100 bn) but the final expenditure stood at PKR 1.26 tn (Figure 3). A similar comparison with the previous year shows that traditionally the Pakistan Army has overshot its laid down budget every year since 2009.[11] Thus, projected estimates can at best be considered as a broad planning figure which can easily be increased as per the needs of the all-powerful military. Since it's a tradition for the last 10 years, there is no reason to believe that the same will be discontinued this year—more so with the increased level of alertness at the borders post abrogation of Article 370 by India.

Figure 3: Pakistan Annual Defence Expenditure[12]



Source: Stockholm International Peace Research Institute 2018-19, available at www.sipri.org

- While Pakistan's Defence Budget has been increasing progressively over the years, the 2019/20 budgetary allocation is unique. This is primarily because the Pakistani Rupee has depreciated more than 30 percent from the preceding year. Hence, the overall availability of funds will impact the budget allocation by as much as 30 percent, i.e. PKR 1.15 tn which would effectively mean PKR 0.8 tn (PKR 800 bn). Moreover, given the increase of 10 percent in the salaries of troops in the budget, the revenue expenditure bill of the Pakistan Army is set to increase.

How the Pakistan Army Conceals its Expenditure

- **Pensions:** The Defence allocation does not include PKR 327 bn earmarked for pensions of retired soldiers which is paid out of the civilian budget. For the fiscal year 2018/19, PKR 342 bn was allocated for military and civil pensions. The pension bill for troops is set to increase by nearly 25 percent in the coming year over the previous year due to declared increase in salaries[13, 14] (Figure 4).

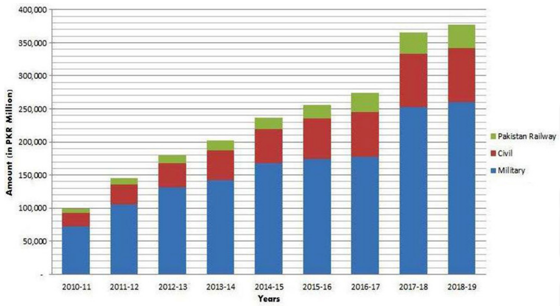
[11] Shane Mason, 'Military Budgets in India & Pakistan', Stimson Center, 2016.

[12] Stockholm International Peace Research Institute 2018-19, available at www.sipri.org

[13] Baqir Sajjad Syed, 'Budget 2019-20: Defense Budget to Grow Nominally Next Year', *The Dawn*, 12 June 2019.

[14] Ammar Habib Khan, 'Pensions the Next Big Crisis', *Daily Pakistan Global*, 17 December 2018.

Figure 4: Pension Allocated in Federal Budget



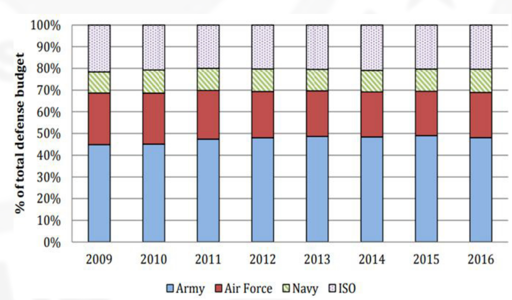
Source: https://en.dailypakistan.com.pk/17-Dec-2018/pensions-the-next-big-crisis

- **Weapon and Equipment Procurement:** Allocations for major procurements/strategic programmes are never made public and at times are over and above the allocated budget.
- **Humanitarian Aid and Disaster Relief (HADR):** Payments / reimbursements on account of internal security and HADR activities in support of the civil authorities are borne by the government so that there is no depletion in the allotted budget and the government alone bears the expenditure of any such contingencies.
- **Off-budget Financing:** There is some amount of off-budget financing also done (estimated at US $1.5 bn) by the assets created by the Pakistan military over decades. Most of this is in the form of welfare activities with prominent players being the Fauji Foundation, Shaheen Foundation, Bahria Foundation, Army Welfare Trust, etc. The total assets of these 'welfare' organisations which includes almost 50 business enterprises are about US $100 bn.[15]
- **Additional Allocation:** Allocations to organisations such as the Inter-Services Intelligence (ISI) are over and above as admitted by the former Finance Secretary Salman Siddiqui to the Public Accounts Committee of the National Assembly or the Lower House of Parliament in 2008. Such allocations are supplementary and are not included in the annual budget.[16]

Defence Budget: Allocation to Services

Traditionally the Pakistan Army has been allocated the lion's share of the Budget due to its large size and its preeminence (Figure 5)[17]. The distribution also shows an allocation to the ISI which is more than the budget of the Pakistan Navy (PN) and almost equivalent of the Pakistan Air Force (PAF). The Army outspent its estimated budget each year from 2009 to 2016. Its revised budgets were, on average 5 percent higher than what was allocated. While the other services do the same, the Pakistan Army routinely overspends the allocated budget which indicates that the overall spending is more than the allocated budget. This year the allocation for the Army would remain static at PKR 523 bn which accounts for 45.4 percent of the total defence allocation. The budget of the PAF would increase by 9.64 percent to over 22 percent of the defence allocation while the PN share would expand by 9.6 percent which is 11.3 percent of the defence pie. The defence establishment/ inter-services organisation/institutions (ISO) will get an 8.78 percent hike which accounts for the balance 21 percent.[18] Dawn reported that freeze on defence budget would affect the 'civil works' head the most as it has received a 12.77 percent cut while the 'Operating Expenses' head which covers transport, fuel, ration, medical treatment, training, etc., would increase by 4.4 percent only.[19]

Figure 5: Pakistan Annual Defence Expenditure



Source: Shane Mason, Military Budgets in Indiaand Pakistan – Trajectories, Priorties and Risks, Page 28, Stimson Center, Oct 2016

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[15] FM Shakil, 'Pakistan Army Moves Into the Oil Business', *Asia Times*, 8 March 2019.

[16] Baqir Sajjad Syed, 'Budget 2019-20: Defence Budget to Grow Nominally Next Year', *Dawn*, 12 June 2019.

[17] Shane Mason, op. cit. (11).

[18] 'Pakistan Govt Says No Change in Defence Budget; Documents Show 4.5 percent Increase', PTI, *Business Standard*, 12 June 2019.

[19] Khawar Ghumman, 'Pakistan Denied Information About Rs 5.5 billion Paid to ISI', *Dawn*, 22 September 2010.

Table 1: Direct Overt US Aid Appropriations for and Military Reimbursement to Pakistan, FY 2002 to FY 2020

(Rounded to the nearest millions of dollars)

Program or Account	*FY 2002 – FY 2013*	*FY 2014*	*FY 2015*	*FY 2016*	*FY 2017*	*FY 2018*	*Program or Account Total*	*FY 2019 (req.)*	*FY 2020 (req.)*
CN	273	18	23	12	15		341		
FMF	3,031	280	265	255	241	–	4,075		–
IMET	32	5	5	5	5	–	52		–
INCLE	774	57	40	40	38	12	970		21
NADR	146	11	10	10	5	2	184		1
PCF/PCCF	2,352	–	–	–	–	–	2,352	–	–
Total Security-Related	6,920	371	343	322	305	23	8,284		22
CSH/GHCS/GHP	249	–	–	23	23	–	283		–
ESF/ESDF	7,351	477	468	200	200	48	8,744		48
Food Aid	590	30	–	23	–	–	643	–	–
IDA	724	101	93	85	62	36	1,101	–	–
MRA	257	–	–	–	–	–	257	–	–
Total Economic-Related	9,457	608	561	331	285	84	11,326		48
CSF Reimbursements	12,125	1,198	700	550			14,573		
Grand Total	28,502	2,177	1,604	1,203	590	108	34,183		70

Prepared by the Congressional Research Service for distribution to multiple congressional offices, March 12, 2019

Note: Final obligation and disbursement totals may be lower than program account appropriations

Sources: U.S. Departments of State, Defense, and Agriculture; U.S. Agency for International Development

Impact of Withdrawal of the United States Funds

The withdrawal of US funds has hit the Pakistan defence budget significantly. The US gave nearly $33 bn to Pakistan from 2002 to 2017 (Figure 6). From 2002 to 2015, these funds constituted nearly a fifth (20 percent) of the total defence budget which was reduced to 11 percent in 2016/17 before being stopped in 2018. Even the economic-related funds have reduced considerably from US $608 M in FY 2014 to barely US $84 M in FY 2018 leaving Pakistan with little option but to turn to its 'all-weather friend' China (Table 1). With the reduction in US support, Pakistan has fostered a deeper economic and military relationship with China. Under the China–Pakistan Economic Corridor (CPEC), Pakistan has already raised one Special Security Division in 2016 ostensibly for the protection of CPEC while the second is to be raised soon.[20] The funding for the same is being done by the Pakistani companies who are paying one percent of the project cost for security and passing on the expenditure to the Pakistani consumers in the form of high tariff.[21]

Figure 6: Allocation of US Funds

Source: US Department of State, Defence, and Agriculture; US Agency for International Development

Implications for the Pakistan Army

Speaking at the National Defence University (NDU) Seminar, Pakistan Army Chief Qamar Javed Bajwa

[20] PTI, 'Pakistan Army Plans New Unit to Protect CPEC Projects', *Gulf News*, 19 May 2019.

[21] Shabaz Rana, 'Power Consumers to Pay for CPEC Security', *The Express Tribune*, 24 September 2016.

pontificated on the need to show prudence in financial management, declaring how the Pakistan Army was setting the tone for the nation to follow, by making a huge 'sacrifice' by foregoing any increase in the defence budget.

"There cannot be any sovereignty in the absence of economic sovereignty. Armed Forces played their part by voluntarily foregoing annual increase in the defence budget and this is not the only step we are taking for improvement of the economy", says a DG ISPR press release.[22]

If indeed, the Pakistan Army is serious about playing a positive role in the nation's economy, it would come with some hard options. The possible implications on the Pakistan Army are likely to be as follows:

- **Big Ticket Defence Purchase:** It is unlikely that 'big ticket' purchases will fructify till the IMF loans are paid, especially from the western countries. This excludes those commitments made by China on 'friendship rates' or honouring 'previous commitments'.
- **Training:** One can expect the annual training calendar of the Pakistan defence forces to be somewhat truncated. Major exercises and field commitments involving large-scale manoeuvres may have to be compromised. Squeeze and cuts on the expenditure of training ammunition are axiomatic.
- **Salaries:** The Pakistan Chief of Army Staff (COAS) has already announced that Pakistan Army officers will forego any raise in salaries voluntarily while the salary of JCOs and ORs would be unaffected. While this does not adversely affect the officer cadre (especially the senior officers) in any manner given the perks and privileges which the officer cadre enjoy; however, this decision will adversely impact the soldiers who are already grappling with the fallout of the grave economic situation that confronts Pakistan (high prices and inflation). High expenditure on account of high prices of items of daily requirements such as vegetables (tomatoes in particular), sugar, wheat, medicine, and electricity has been in the news for a considerable period. This is likely to deepen officer-man divide which the officer corps is conscious not to aggravate or inflame.
- **New Raisings.** New raisings and conversions may be delayed with this being particularly true for mechanisation and induction of new equipment. In 2016, Pakistan Army planned to raise two (34 and 44) Special Security Divisions (SSDs) for the protection of CPEC with over PKR 23 bn spent on raising the first one. However, four years down the line the second SSD is yet to materialise.
- **Commitment to CPEC:** The commitment of raising 15,000 troops in two division-size forces for the protection of CPEC may face delays. The raising of the second SSD will impact the security of CPEC even as the Baloch Liberation Army's (BLA) attacks on Chinese personnel gets bolder in execution and is frequent in numbers.
- **Production in Pakistan Ordnance Factories and Collaborative Projects:** The continuing revision of costs in the production of JF-17 aircraft and Al-Khalid tanks are likely to be exacerbated by cost overruns and credit squeeze. Resultantly, one can expect Pakistan Ordnance Factories (POF) outputs to be sluggish and sub-optimal.
- **De-Mob of Para Militaries:** To cut costs, the Pakistan Army is likely to demobilise para-militaries. Raising or embodiment of Mujahids in case of operational exigencies would require deeper thought. In effect, the operational readiness levels are likely to be impacted.

'Haemorrhaging' the Pakistan Army Economically

- **Binary Stretch:** The "chickens have come home to roost" seems apt to describe the rebound of terror that has begun to haunt the Pakistan Army. Not only has it raised two divisions of troops to protect the CPEC on China's directions, but there has also been a substantial increase in border troops under the Inspector General Frontier Corps, Balochistan and Khyber Pakhtunkhwa (KPK). Even Pakistan

[22] DG ISPR Press Release Number 125/2019 dated 28 June 2019.

Army regulars, especially infantry units have been pulled out in fair numbers from the Eastern Front against India and deployed along the Afghan border.[23] Additionally, PKR 18.2 bn has been spent to fence 432 kilometre (km) of border fencing along the Durand Line with Afghanistan.[24] The BLA has been active in recent years fighting for the rights of self-determination of the Baloch people. Their attacks on CPEC projects and Chinese diaspora working on these projects have become 'bold and bloody' with one attack on the Chinese Consulate in Karachi in 2018, imposing fear and raising questions on the capability of the Pakistan security forces to ensure their safety and well-being. Peace tenures are shortened even as body bags in 'khakhi' are finding their way to the rural and impoverished interiors of Pakistan, demolishing the myth of Pakistan Army's invincibility. Already committed on both frontiers, the need to use all available diplomatic, political and asymmetric means to widen the binary stretch of the Pakistan Army will facilitate the 'haemorrhage'.

- **Operational Preparedness:** Perhaps the biggest vindication of the Balakot strike was the caution and fear imposed on the PAF forcing the Pakistan government to close the Pakistan air space for 140 days. A conservative estimate of the loss to Pakistan exchequer for this policy decision was PKR 8.5 bn (US $50 M) according to Ghulam Sarwar Khan, the Federal Minister for Civil Aviation.[25] While surgical strikes like the one at Balakot would be the 'new normal', such reactions to every strike would be catastrophic for Pakistan Civil Aviation. More importantly, it will keep the PAF 'on the edge'.

  The Pakistan Army is heavily dependent on Chinese equipments. According to Stockholm International Peace Research Institute (SIPRI), an authoritative think-tank, 63 percent of Pakistan equipment is of Chinese origin, a shift that happened in the last five years as relations with the US continued to downslide. As is the Chinese way of doing business, the Pakistan Army gets 'No free lunches' from their 'all-weather friend'. The continued commitment of forces on both borders and internal security duties creates external dependence. With a proclivity to depend on others for military support ever since independence, the Pakistan Army's increased dependence on China increases the risk of being deprived or denied, should India-China relations improve over a period of time.

- **Training.** It is no secret that the Pakistan military is extremely cautious of Indian military formation's training and exercising along the western borders in Rajasthan and Punjab. After Operation Parakram, the Pakistan Army has followed a rule of 'mirror-imaging training' to avoid being surprised by way of manoeuvre by the Indian Army (IA). Our training regime must be intensified and the ability to respond aggressively to any Pulwama/Uri or even Pathankot-type incident at a place of our choosing, must be key to a robust and muscular response strategy. Not only will this keep the Pakistan Army out of their cantonments, but it will also impose costs due to wear and tear of the equipment, fatigue to troops and impact morale. For an army that is already self-imposing cuts on its budgets and officer salaries (but not troops), inflation at 9 percent and galloping revenue expenditure, the Pakistan Army will have to take a call between greater borrowings to ensure matching operational readiness and a looming Indian threat along the IB/LC.
- **Maritime Threat:** In a sheer act of desperation the PN, China's closest ally, refused to participate in the International Fleet Review at Qingdao in China in 2019 held to commemorate 70 years of the PLA Navy (PLAN). Surprisingly, the Indian Navy (IN) sent two ships. According to the Press Trust of India (PTI), the "Pakistan Navy reportedly could not send its ships to PLANs most celebrated moment despite the 'all-weather relations' due to the Indo-Pak hostilities after the deadly Pulwama terror attack in February."[26] Clearly, the PN was spooked by the aggressive deployment of the IN.

[23] Faseeh Mangi, 'Pak Will Add 60,000 Troops to Patrol Afghan Border', 9 August 2018.

[24] Waseem Abbasi, 'Rs 18.2 Billion Spent on Afghan-Pakistan Border Fencing', *The News*, 28 April 2018.

[25] 'Airspace Closure Caused Over 8 Billion Loss: Minister', *The Dawn*, 19 July 2019.

[26] KJM Varma, "Chinese Military silent over Pakistan Naval Ships Absence at Chinese Navy Fleet Review", *PTI*, 25 April 2019.

...Economically

Continued patrolling by IN surface and sub-surface combatants can virtually drain all the resources of the PN forcing extended vigil and deployments to safeguard her assets, ports, commercial shipping and oil terminals. Continuous pressure on the Makran coast can also raise insurance premiums and the cost of imports to Pakistan with a cascading impact on its economy.

- **Line of Control Response Strategy:** The IAs subtle shift in it's response to Pakistan Cease Fire Violations (CFVs) has had a salutary effect.

  According to the then COAS General Bipin Rawat on 22 September 2018: "We need to take stern action to avenge the kind of barbarism that terrorists and Pakistan Army have been carrying out against our soldiers. Yes, it is time to give it back to Pakistan in [the] same coin. Not by resorting to similar kind of barbarism but I think the other side must also feel the same pain."[27]

  Resultantly, the intensification of our response in depth and scope including artillery (including use of 155mm Bofors) has upped the ante by inflicting casualties in large numbers both on the terrorists and the Pakistan Army regulars.[28] Additionally, Pakistan has already raised 34 Light Infantry Division (with 15,000 troops) while another (44 Light Infantry Division) is under raising. Although both the divisions are meant for the protection of CPEC, however, they can be trained and employed for operations on/across the LC at a short notice.[29] Aside from the human cost to the exchequer, the Pakistan Army finds itself saddled with huge wages and equipment bills to feed, clothe and arm this force which is normally raised only in times of war. Also, Pakistan has been forced to deploy greater firepower assets in some areas, increase its tiers of obstacle system and improve the survivability of its troops, all of which come at a cost to money that could be better used for improving its abysmal human development index (HDI).

Conclusion

In conclusion, its time to adopt a policy of 'Bleeding the Pakistan Army Economically' as a quid pro quo to Pakistan policy of 'Bleeding India by a Thousand Cuts'. If the Pakistan military is squeezed financially, its ability to pose a viable threat will continue to suffer credibility and over time force Pakistan to turn towards the betterment of its people rather than sacrifice their development and the future of its generations to the lost cause of jihad and proxy war in Jammu and Kashmir. In keeping with our muscular strategy of no compromise on terror, the recommendations to drain the coffers of Pakistan economy in parallel would force the Pakistani establishments to revisit its policy towards India.

27 'Time to Give it Back to Pakistan in Same Coin', *The Economic Times*, 23 September 2018.

28 'Indian Artillery Targets 4 Terror Camps Across Line of Control', *Hindustan Times*, 21 October 2019.

29 Snehesh Alex Philip, 'Pakistan to Raise New Division HQ in Gwadar to Protect $60 Bn Economic Corridor to China', *The Print*, 14 October 2019.

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