

Growth engine and distribution

BY DR FAISAL BARI

The Economic Survey 2002-2003 is out and, according to the government, it shows that Pakistan has had a remarkably good year. Mr. Shaukat Aziz and his team had, of course, been giving us the good news all along, but we had not paid much heed to it. Now the Survey has put the entire issue to rest. Or so it would appear.



We have foreign currency reserves of \$ 10.5 billion, current account is in surplus, exchange rate is stable, inflation is low, interest rates are low, direct foreign investment has grown remarkably, and the capital markets are going through a boom, debt has stabilized and is slowly coming down, fiscal deficit has been brought down to below 5 percent of GDP, tax collections are up, and exports and imports are showing some buoyancy.

The successes are reflected in sector-level performance as well. Large-scale manufacturing has shown remarkable recovery, especially in some sectors like automobile production, major crops, especially wheat, have shown good growth as well, and even the services sector growth has picked up. Hence, in a time of turmoil and upheaval around the world, the ship of Pakistani economy is seeing relatively smooth sailing. The Survey even lists some of the countries, from the region and across the development spectrum, who are not doing as well as Pakistan has been doing.

The Survey also points out some of the areas and sectors that still pose a challenge for the policy-makers. Poverty levels are very high, and despite the best

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*Pak-Eco-
The Nation
9.6.03*

macroeconomic numbers, and the jugglery done in Islamabad, what is conveniently overlooked is the misery that the economic setup, despite the upswing, is imposing on the more vulnerable sections of the society. And this misery is of the scale that no Rs. 10 billion odd increase in the development expenditure or expenditure for poverty alleviation can address adequately. When one reads of self-immolations and suicides in the papers, the \$ 10 billion of reserve appears either insignificant, or criminal to keep in the face of people being forced to kill themselves.

The Minister of Finance, his coterie of bureaucrats, the bureaucrats at the State Bank of Pakistan and most members of the government keep their focus on the bright side and only refer to the misery as a side concern: as something that needs to be addressed, but will take care of itself in due course if we keep staring at the bright side long enough. To them all people who stare at the dark side of things directly are poor intellects, traitors or leftists (same as traitors to these bureaucrats). But what else can one expect from people whose job depends on making even the miserable appear rosy!

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intensive, as most durable goods industries tend to be, then the increase in employment is not going to be significant. Furthermore, if currency markets are fairly free, and profits can be repatriated, then there is no necessity that the profits that these industries make will even stay in the country and get invested or consumed here.

What is missing in the above picture, if we wanted to ensure that the profits and growth permeates the entire spectrum, are the institutions that ensure proper distribution. The progressive tax system, the high employment generation potential and ratio, the skilled labour, fairly decent markets for education and vocational skills are some of the transmission mechanisms that would ensure a wider sharing of good fortune. But few of these are present in Pakistan. Our tax system does not have the ability to tax most of the corporate sector, we have very relaxed rules for foreign investors, most of the informal sector is outside the tax net and those who are in the net are overtaxed so that they have every incentive to hide information from the tax department.

Similarly there are significant market failures in the labor market and the education and vocational training markets. These failures imply that the benefits of expansion in one market, even if they were going to travel to other parts of the economy, would take that much longer. Capital market imperfections also exacerbate the situation. There are people who sometimes have the skills, and more often the gumption to become an entrepreneur and benefit from the possibilities that are available in an area. But due to lack of credit and other financial services, they are unable to do so.

Then there are larger issues that create problems. Law and order situation, lack of democracy and rule of law, deficiencies in establishing property rights,

sectors that still pose a challenge for the policy-makers. Poverty levels are very high, and despite the best efforts of the government to massage the data, do not show any significant change from last year. This is especially interesting given the fact that the government is claiming that national income and per capita income have gone up significantly. If poverty levels have not altered significantly, it must automatically mean that inequality has become worse in Pakistan in the last few years. If total income goes up, but the level of poverty is more or less the same, then the only explanation can be that the additional income is going to the non-poor. That is exactly what a worsening income distribution is all about.

Unemployment levels also remain very high. This is not only true of the unskilled, it is also true of the skilled and even the educated. To give one example, sometime back the State Bank of Pakistan had advertised for officer level openings, they got some 9000 applications, of which some 6000 odd were actually eligible for the job, and fulfilled the basic criteria of masters in the relevant subject and all that. That the quality of the candidates was quite poor in general is another matter all together. But the sheer numbers applying for jobs with advanced higher education requirements tells us about the job situation in the country, even for the very educated.

At another level, go to almost any market center in the city, even at midday, and you see a large number of labourers sitting by the roadside, waiting for work and the possibility of getting a decent meal for themselves and their families. In the glitter of the

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So how can these two very contradictory pictures of the economy co-exist? And more importantly, is the government right in arguing that the rosy picture of the economy will eventually, if we are patient enough to wait that long, overwhelm the dark picture, and the benefits of the recently acquired macroeconomic stability will trickle down to the masses, and turn into a flood at the same time. Maybe. But the evidence available thus far does not suggest this. And one can very easily show that there is no necessity involved here. To ensure the spread of benefits one needs some very basic reforms at the institutional level, which, if one goes by the history of institutional reform, is beyond the capacity of this government.

Think of the following scenario. With more income coming from abroad, and more relief from various countries and agencies on our debt (the post 9/11 world), it can be very possible that demand for certain goods, like durables and consumer items, favoured more by the well-off, goes up significantly. If this is the case, we will see large scale manufacturing, in certain industries, responding positively to the increase in demand. But if the companies in these sectors are multinationals or if their ownership is concentrated over a few individuals, there is no reason to believe that this possibly significant increase in incomes and national output will have a large impact on the much more numerous but poorer sections of our society. One route would of course be the possible increases in employment triggered by the increases in demand for production, but if these sectors are capital

Then there are larger issues that create problems. Law and order situation, lack of democracy and rule of law, deficiencies in establishing property rights, and problems with contract enforcement all reinforce the fragmentation of markets and sectors.

All of the factors given above ensure that progress, if there is any in an area, does not get translated into a broader prosperity. Sadly a lot of the above have to do with the state directly. In most areas the state was supposed to go through a reform process, a structural adjustment, a liberalization, and a corporatization effort that was going to get incentives aligned and remove the imperfections as such. But this, most significantly, has been the most prominent failure of the current and previous government (the General Musharraf / Shaukat Aziz era). In fact, if WAPDA and CBR efforts are to go by, they could not have done worse. In the case of the CBR in particular, the regime failed completely, and after years of effort the very people who have been opposing reforms all along are now in-charge of 'reforms'.

No doubt the Economic Survey 2002-2003 brings some glad tidings. But it also shows where the problems are. And it also highlights the roots of the problem as well. These lie in lack of institutional reforms. Unless and until the state addresses these seriously, the glad tidings will not last very long. But does the state have the gumption to take the task of institutional and organizational reform on seriously. That probably is the weakest link in the entire 'good news' reading of the economy.

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