Growth in large-scale manufacturing

BY DR FAISAL BARI

The Economic Survey 2002-3 reveals that large-scale manufacturing grew at the impressive rate of 8.7 percent. This contrasts very well with 4 percent growth the previous year, and compares well with the impressive performance of the 1980s as well. Large-scale manufacturing has been considered the 'engine of growth' in most growth theories, and its role has been found to be significant in the empirical literature as well. So, if large-scale manufacturing growth is going back to its rate of the 1980s, does that mean we are going to have higher growth as well? That question has been taxing many an economist in Pakistan.

The government's answer is clear. They are not only arguing that the revival of large-scale has happened, but that this revival is going to set us on the path of high and sustainable growth, and this revival, coupled with investment trends, implies we are set for a 'take-off'. But I think another interpretation of the performance of the large-scale industry is also possible. One that possibly paints a more realistic picture than the one that government officials are inclined to do.

If one looks behind the aggregates, the revival of large-scale manufacturing is based on very strong growth in the automobile sector (49 percent), metal products machinery and equipment (18.4 percent), mineral products including cement (20 percent), tyres and tubes (16.2 percent), paper and board (15.7 percent), and sugar (13.6 percent). The industries that did not do well in the last year

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competition for local producers, and massive profits for them at the cost of consumer pauperisation. Since large local and foreign companies are involved, no government has had the courage to stand up to this exploitation.

Growth in this industry is a mixed signal. It does tell us that local demand for automobiles must have increased significantly in the last year or so for production to have increased this much, but also tells us that we are expanding an industry that has little or no chance of becoming an export sector, that will have difficulties in competing internationally whenever we decide to open it up, that is dependent on consumer-fleecing, and is likely to remain so for the foreseeable future.

to get a credit card, lease a vehicle or borrow for it, and to acquire consumer durables like TVs, refrigerators and ACs, on credit. This too has helped increase the demand for automobiles.

The demand will not remain very strong for long. Once the class that has money has bought new cars, and increased the number per household to a certain level, and is not willing to change cars very often, the demand will stabilise. This will be especially true if we continue to see increasing inequality and high poverty levels. So unless the car industry is planning to export, of which there is not much chance, it is unlikely that the expansion will last over two or three years.

The same is true of expansion in the sugar industry. The sugar sector too is protected, and even though there is little evidence suggesting we should have such a large industry when sugar is available in the world market at cheaper rates usually, the sector has expanded due to protection. The sugar industry does create rural employment as mills tend to be in sugar-growing areas, but this employment creation is expensive. The consumer ends up paying for both creating this employment and the manufacturers' profits through higher local prices. Thus expansion in the sector, even more than the auto sector, does not really give us much confidence in economic revival.

Questions about cartels in the cement industry make growth in it also suspect. But if construction is picking up, and without any government help, and cement production is reflecting the increased demand from the construction industry rather than cartel machinations, this increase signals a desirable direction. The construction industry is not very capital intensive and has the potential to create a large number of jobs, and not just in skilled categocent), and sugar (13.6 percent). The industries that did not do well in the last year, and there were quite a few of those as well, were textile (5.2 percent), leather products (-6.6 percent), chemicals (3.9 percent), and petroleum products (2.2 percent).

Even a cursory glance at these numbers reveals interesting patterns. Historically textiles have been our biggest industrial sector, and it has contributed the most to employment creation in the industrial sector, and to our export earnings as well. But the textile sector has not picked up significantly in the last year. Another important export sector for Pakistan is leather products, and there too the performance over the last year has been pretty poor. On the other hand petroleum products have always been a very large import item. The slow growth in petroleum products industry should be of concern to us since it means that we are still spending a lot of foreign exchange on importing these products, and have not been able to introduce enough investments in the sector. This is all the more surprising given that most foreign direct investment we have attracted in the last few years has been in this area, and the government has been touting this as one of its successes.

Automobiles were the fastest growing sector last year. The auto sector, which includes the production of jeeps and cars, tractors, light vehicles, buses, trucks and motorcycles, is mainly geared towards fulfilling local demand, does not export much, depends on import of engines, and in some sub-sectors does little more than assemble locally. But in other areas, auto industry has led to the development of a fairly large parts manufacturing light-engineering industry. But auto industry is very heavily protected. Import of second-hand and reconditioned automobiles is not allowed, and there is a 200 percent duty on importing new cars. This heavy protection has meant little the foreseeable future.

Further, the automobile industry is very capital intensive. This means it relies heavily on capital equipment investments for expansion, and thus has limited scope for employment generation. Our concerns about employment, job creation and poverty cannot really be addressed through expansion in this sector. In fact, expansion of an industry under heavy protections, when we know that there is little chance of it becoming an export sector, is likely to be counterproductive as it can lock us into sectors where we do not have competitive advantage, and that we should not be in, even from the long-run point of view.

The expansion also tells us there is a class in Pakistan that has the purchasing power for new cars. This might be for replacing older cars, new demand for additional cars in households, or new people entering the market. The same is true of motorcycles. This ties in well with the increasing inequality that is also becoming clear about our economy. Where poverty has either been increasing or remaining stagnant, increasing national income must imply, by definition, increasing inequality. Rapid expansion in automobile demand points out this trend starkly.

Finally, the increased demand also reflects the changes in the money markets. There are inflows of capital due to remittances coming through official channels, money coming in through aid, loans and other payments, through Afghanistan, and so on, while there are few good investment opportunities. Investors are currently not willing to invest in industry, despite interest rates on industrial loans coming down to around 8 percent only. Banks are thus flushed with liquidity. The State Bank, with the help of the financial sector, has facilitated the entry of banks into consumer credit. Now it is much easier

ries only. Hence a significant number of these jobs are likely to help the poorer, unskilled, sections of our society.

There has also been impressive growth in paper and board, and metal products, machinery and equipment. This is not surprising since one would expect these industries to perform well when demand for consumer durables, inclusive of automobiles, goes up. Demand for packaging material, parts, and smaller products goes up as soon as the mainstream industries pick up. These industries do have higher employment potential, and growth in these can create new jobs if the owners in these sectors believe the increased demand will be sustained for some period at least. If demand for consumer products remains high for a year or so more, we will see job creation in these vendor and other upstream and downstream industries.

It seems pretty clear that though some industrial sectors have performed well, this does not give us a huge amount to cheer about. Most of the expansion has taken place in sectors that are heavily protected, do not have much export potential, and do not create significant employment. There are some linkages to other sectors that will benefit the economy in the medium run, but these are fairly weak. Expansion in cement and other local non-protected industries is a good sign, but this will need to be sustained for a couple of years before we see its impact on employment generation and exports. The sectors that are supposed to give us exports are still not performing as well as they should if we hope to stay on course for sustained 6-8 percent GDP growth. For this, the textile sector in particular, must perform much better than it has in the last few years.

E-mail queries and comments to: faisal@nation.com.pk