How donors control our development policy

Pak. Eco.
Dawn 24-5-03

By Aqil Shah

DONORS concluded last week's Pakistan Development Forum (PDF) meeting on a note of cautious optimism. Their customary kudos for the government's economic reforms aside, many were also visibly concerned about the growing incidence of poverty despite the apparent gains in macroeconomic stability.

IMF representative Klaus Enders reportedly reminded the government of the "intolerable levels" of poverty which in his view reflected, among other things, low public expenditures on human development. The World Bank remained sceptical of the government's ambitious poverty reduction targets since "the absolute levels of spending foreseen did not match the outcomes sought".

At the root of these apprehensions is the pervasive fear in the development community that the newly elected government will squander the macro stabilization achieved under the military-led regime. Donors need not worry though. Not only has our hapless prime minister repeatedly assured them of the "continuity of reforms," economic policy planning in Pakistan remains largely outside the purview of elected authorities. Imported Citibank and World Bank officials, backed personally by the country's powerful military ruler, continue to call the shots on the economic front.

No matter who is in power, the sad truth is that the socially disruptive levels of poverty and unemployment in Pakistan are not merely the result of 'slippages in reform implementation.'

find these extra resources? Are donors willing to match their holier-than-thou rhetoric with additional financing?

Dwindling aid commitments and the deteriorating terms of external assistance suggest otherwise. For instance, the share of grants as a proportion of overall aid shrunk drastically from around 80 per cent in the 1950s and early 1960s to 12-15 per cent during the 1990s. This is not all. The average rate of interest on external loans and credits too has skyrocketed while average maturity periods have declined sharply.

With stagnant export earnings and domestic revenues, the only way for Pakistan to repay loans is to borrow more, thus driving itself deeper into the debt trap. The net value of foreign aid transfers turned negative in 1996-97, and again in 1999-2000/2000-01 as debt repay-

> As long as the interests of the donor country governments and commercial firms are not threatened, recipient countries can count on business as usual. Thus politically correct buzzwords like "good governance" and "democracy" are not to be taken too seriously since they are often meant to help donors gloss over their own failures and pass the buck on to recipient countries. External aid agencies have simply used them to bypass existing institutions in project planning, management and implementation.

with Mr. John Wall, the World Bank country director for Pakistan and Afghanistan, when he says that "good governance takes eternal vigilance — it has to be earned every day." But why is it that those who preach the virtues of vigilance and integrity rarely seem to practise them.

In early 1998, relations between Pakistan and the IFIs soared when the Nawaz Sharif government initiated investigations into allegations of kickbacks and overpricing in power purchase agreements signed by the previous PPP government with mostly western independent power producers (IPPs). Many of them were backed by World Bank financing and guarantees.

After the Sharif government cancelled as many as half the contracts on charges of corruption in May 1998, it soon discovered how aid could be used as an arm-twister. The Bank issued a stern warning to the government of Pakistan to keep its legal actions separate from "the commercial and contractual issues involving IPPs."

The government's political motives notwithstanding, the IMF and several other PDF members, including the United States, Canada and Japan, instead of encouraging the government in its anti-corruption efforts, withheld aid and investment on the grounds that the IPP issue be resolved first.

In October 1998, an IMF mission to Pakistan was indefinitely postponed because of the lingering dispute. Similarly, in early 2001, the auditor-general of Pakistan reported embezzlement of $400 million in the World Bank-led multi-donor Social Action Programme. While the Bank swiftly dispatched an "integrity assurance mission" to Pakistan, press reports indicated that a $700 mil-
lion credit line was simultane-

At the root of these apprehensions is the pervasive fear in the development community that the newly elected government will squander the macro stabilization achieved under the military-led regime. Donors need not worry though. Not only has our hapless prime minister repeatedly assured them of the "continuity of reforms," economic policy planning in Pakistan remains largely outside the purview of elected authorities. Imported Citibank and World Bank officials, backed personally by the country's powerful military ruler, continue to call the shots on the economic front.

No matter who is in power, the sad truth is that the socially disruptive levels of poverty and unemployment in Pakistan are not merely the result of 'slippages in reform implementation.' What donors conveniently forgot to mention during PDF 2003 — and no one from the government side dared point out — was the sharp and sustained contraction in development expenditures since the early 1980s when Pakistan first signed structural adjustment loan (SAL) agreements with the IFIs.

Consistent with the neo-classical dogma that the state roll back its productive activities, government after government was forced to curtail public spending ostensibly to reduce fiscal deficits.

While deficits continued to be around the high seven per cent mark throughout the 1990s, expenditure cuts severely restricted the ability of governments to deliver social services or spend on human development.

Evidence shows that this most intensive period of structural adjustment also coincided with increased poverty and worsened income distribution as real wages and household incomes declined as a result of wage and employment freezes, public sector retrenchments and subsidy withdrawals.

Besides, real GDP growth and investment fell, inflation remained high, saving and investment rates stagnated while imports and government consumption surged. In addition, debt in absolute terms, the debt/GDP and debt service/export ratios also increased.

With such a disastrous track record, it must take some nerve on the part of the IFIs to blame the government for not doing enough to reduce poverty. No one in our officialdom — not even the most ardent advocates of the IMF-Bank variety of economic reforms — disputes the need for increased allocations for human development priority areas.

But forced to cut corners, exactly where will the government

donor country governments and commercial firms are not threatened, recipient countries can count on business as usual. Thus politically correct buzzwords like "good governance" and "democracy" are not to be taken too seriously since they are often meant to help donors gloss over their own failures and pass the buck on to recipient countries. External aid agencies have simply used them to bypass existing institutions in project planning, management and implementation.

ments registered a steep rise.

Put simply, we paid back more forex for debt retirement than we received as aid. Besides, a lion's share of aid is tied to specific projects and purchase of donor country goods and services.

Tied aid not only increases procurement costs but also undermines local production, investment and employment structures since donors typically use aid to finance their investments, hire their own nationals as "consultants" or create markets for subsidized imports.

Worse still, geo-political considerations rather than the nature of the political regime or the policy performance of governments still determine who gets how much donor money. For instance, the European Union admits rather frankly in its Pakistan Country Strategy 2002-2006: "...there has been a major re-orientation by the donor community towards Pakistan in view of its support to the coalition against terrorism."

It is no surprise that successive governments in Pakistan have hedged their bets on the country's geo-strategic importance to side-step politically difficult reforms.

While donor decisions are typically shrouded in secrecy, press reports suggest that endorsement by the United States has been key to IMF bailouts of Pakistan. In early 1999, for instance, new IMF lending worth $1.56 billion was approved only after Washington decided to ease non-military sanctions in light of a deepening economic crisis triggered by Islamabad's nuclear testing.

The post 9/11 circumstance under which Pakistan's bilateral creditors offered a unique $12.5 billion 'debt reprofiling' agreement on almost the entire stock of bilateral debt too was highly special.

One could not agree more

ment of Pakistan to keep its legal actions separate from "the commercial and contractual issues involving IPPs."

The government's political motives notwithstanding, the IMF and several other PDF members, including the United States, Canada and Japan, instead of encouraging the government in its anti-corruption efforts, withheld aid and investment on the grounds that the IPP issue be resolved first.

In October 1998, an IMF mission to Pakistan was indefinitely postponed because of the lingering dispute. Similarly, in early 2001, the auditor-general of Pakistan reported embezzlement of $400 million in the World Bank-led multi-donor Social Action Programme. While the Bank swiftly dispatched an "integrity assurance mission" to Pakistan, press reports indicated that a $700 million credit line was simultaneously extended.

The bottom line is this: as long as the interests of the donor country governments and commercial firms are not threatened, recipient countries can count on business as usual. Thus politically correct buzzwords like "good governance" and "democracy" are not to be taken too seriously since they are often meant to help donors gloss over their own failures and pass the buck on to recipient countries.

There is no doubt about the need for improvements in the quality of governance in Pakistan. Rampant corruption, poor planning and implementation, low quality of public investments, inefficient resource allocation, to name a few, are serious problems. But instead of addressing these issues, external aid agencies have simply used them to bypass existing institutions in project planning, management and implementation. By taking over the critical policy functions traditionally performed by governments, they have further undermined the already weak state capacity.

Since donors now virtually control the entire development policy process in Pakistan, as elsewhere in other aid-dependent countries, the onus of bridging the gap between the good governance (less corrupt, economically sound and more democratic governments) and prescription and practice rests squarely with them.

The complex nature of Pakistan's developmental deficits means there can be no quick fixes. Sustainable development and poverty reduction will require long-term aid commitments delivered on favourable terms and tailored specifically to the development needs of Pakistan. In other words, donors should put their money where the mouths are.