Pakistan: The return of poverty — II

Pak. Eco. Daily Times 7.7.03

OP-ED

SHAHID KARDAR

The government's economic policy is today narrowly focused on a one-item agenda, the control of the budget deficit. This dogmatic adherence to macroeconomic stabilisation will not automatically translate into economic growth

The structural features of Pakistan's economy — the structures that influence the functioning of markets and the access to resources, the pattern of ownership of productive assets, the role of state institutions that affects access to scarce public goods and services and policies embedded in the adjustment lending by the multilateral agencies have impeded the potential of the growth process to reduce high levels of poverty.

The inequitable distribution of assets (especially land in rural areas where close to 70 per cent of the population resides) essentially explains why rural poverty has increased. Although agriculture grew at 4.5 per cent in the 1990s, rural poverty increased sharply, since 81 per cent of the farms measure less than 12.5 acres and make up 39 per cent of cultivated area while two per cent of farms, each more than 40 acres, cover 44 per cent of area.

A survey conducted for the National Human Development Report (NHRD) revealed that poor farmers/tenants lose almost one-third of their income from poor access to markets for agricultural inputs and outputs as the balance of power at the local level was unfavourable for them. They face an asymmetric market for inputs and outputs, since land is not just a material asset but also a political and social arbitrator — rural power is traditionally associated with land ownership.

Public expenditure can address poverty through provision of social services, subsidies, provision of physical infrastructure and creation of jobs. In particular, effective expenditure on social services can compensate for the limited capability of the poor to acquire these services from the market. Amartya San argues that markets succeed only when the government takes concomitant measures to expand social opportunities. In other words, market outcomes depend upon the ability of public policy to create efficient non-market institutions. Since the impact of such spending is not captured by conventional measures of income poverty, progress in these areas is better reflected in the measurement of outcomes.

Pakistan, with a 45 per cent literate population has fared rather poorly on this front. Its social indicators continue to be significantly lower than those of other countries similarly placed economically. This is largely because of poor budgetary allocations for social services, with defence expenditure exceeding social sector spending and endemic issues of governance affecting the quality of service provision.

The low quality of education and skill mismatch, has lowered the return on human capital, thereby reducing the role of education in poverty reduction. About 26 per cent children of school-going age remain out of the school system, 44 per cent of the population has no access to basic health services while 50 per cent has no access to sanitation. According to the NHRD study, mentioned earlier, poor health and malnutrition are major factors that push people into poverty.

Moreover, essentially because of the expenditure squeeze between 1990 and 1999 the net enrolment rates for the primary stage of education declined to 42 per cent from 46 per cent, with the gross enrolment rates for boys for the middle level grades declining from 58 per cent to 48 per cent over the same period.

The poor outcomes in the social sectors has been seriously impacted by inappropriately selected sites, poor maintenance of installed infrastructure, inadequate number and skill mix of staff at the service delivery sites, somewhat indiscriminate compression of expenditures to adjust for resource shortfalls, lack of timely provision of complementary non-salary inputs, equipment and consumables critical to service delivery (with audit related issues hindering timely disbursements) and continued weaknesses in mechanisms for holding service providers, like teachers, paramedical staff and doctors accountable for even failing to turn up for duty let alone get them to provide good quality services..

The government's economic policy is today narrowly focused on a one-item agenda, the control of the budget deficit. This dogmatic adherence to macroeconomic stabilisation will not automatically translate into economic growth in future years. The single-minded pursuit of the objective of fiscal austerity, which appears to be driven more by ideological purity considerations, has stifled economic growth.

The financial solvency of government cannot be an objective *per se*. Nor can the government simply continue to argue that criticism of its economic strategy that is contributing to the increase in poverty is being made by misguided do-gooders. And the government cannot insist that addressing the worst manifestations of poverty through micro-credit and Zakat programmes with their limited outreach is an adequate response.

Poverty alleviation has to be an integral part of an overall strategy for economic development. Similarly, poverty reduction cannot be achieved from just additional allocations for social services, as is envisaged in the IMF's Poverty Growth Reduction Facility, especially if provinces, responsible for improving the efficiency of social services, continue to be starved of funds through a patently unjust NFC Award and the harsh and ridiculous budget deficit ceilings imposed by the IMF. The provinces are seemingly bearing almost the entire cost of structural adjustment.

The economy is like a machine and not a house. And this is not a machine that can be switched on and off whenever we like. If sluggish demand (domestic or external) or rapid reduction of import tariffs results in closure of some enterprises, and/or loss of production capacities and markets and lowers the trajectory of growth it is not possible to quickly return to the earlier path and from there push the economy onto a higher durable growth trend.

Since industrial production (and particularly that of small and medium manufacturing enterprises) has strong forward and backward linkages it can stimulate growth all round. Growth in natural resources generally cannot create this momentum. Investment in industry brings in capital and new technologies, enhances the human capital base and creates new markets.

With a large amount of slack or underutilised industrial capacity and a low rate of inflation a moderate increase in the deficit to finance public sector investments should be affordable as it is not likely to unduly disturb the inflation rate and macroeconomic stability. This stimulus is urgently required. However, one is not advocating fiscal recklessness, since large injections will, in the medium- to long-term, have to come from expenditure reprioritization and a major shift of scarce resources from defence that has been crowding out productive investments.

Much of the fiscal space for poverty reduction expenditures in education, health and nutrition and development-related spending in public works and infrastructure which augment the supply side of private investment would have to come from the recent rescheduling and re-profiling of debt, the reduction that has taken place in the interest rates on domestic public debt, privatisation or closure of public sector enterprises that continue to soak up at least Rs. 50 billion a year of hard earned tax payers' money and cuts in defence expenditures

Development surcharges and excise duties that raise the cost of production and affect competitiveness of domestic industry should be quickly phased out and replaced by GST. GST should be withdrawn on subsistence level consumption of utilities like electricity, gas and water.

The private sector's cost of doing business should be reduced through policy and rule application consistency, predictability and transparency, further deregulation to create a more comprehensive environment and a revamping of the regulatory environment.

A policy package that stimulates investment in urban housing and related construction should be developed. In view of its high employment elasticity and large forward and backward economic linkages this sector can stimulate economic activity.

Poor maintenance of the irrigation system has affected agricultural growth through the loss of almost 35 per cent of water from the canal head to the field (25 million acre feet of water), reducing its availability at the farm gate. Since the potential for bringing additional land into cultivation has largely been exhausted, sustaining higher levels of agricultural growth will require a major rehabilitation of the system to improve irrigation efficiencies. Hence, the need for the development and maintenance of irrigation and drainage systems, lining of watercourses and storage of water for irrigation.

The development of the livestock sector can improve milk yields, which can then be exported to potential markets in Central and South East Asia. Similarly, huge potential exists for developing marine fisheries.

There is a need to rectify dysfunctional land administration and judicial processes and reduce conflicts over ownership of land (false records and forcible occupation of land). Provision of secure property rights will help convert assets of the poor into viable collateral, by making them fungible.

Good governance through better management and improved delivery systems in areas affecting civil society (police, judiciary and administration) and institutional reforms are important for creating a favourable investment climate and critical for the effective delivery of basic social services, like education and health, to the poor.

Shahid Kardar is an economist. This is the second of a two-part series. The first part was published on Sunday, July 5, 2003