Integrated framework of economic policies crucial for sustained developm

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Pakistan's economy is currently confronted with macro-economic imbalances and structural weaknesses of significant proportions which unless effectively tackled on the basis of a well designed and properly integrated package of economic and social policies could pose serious threat to socio-political stability aside from having an adverse impact on country's growth.

The principal areas of concern are well known and have been frequently highlighted by domestic and international experts. These are: rapid population growth, growing unemployment and under-employment, low savings and investment rates, vulnerable balance of payments position, huge fiscal deficits, unsustainable external and domestic debt service ratios, worsening inequalities of income and wealth, disconcerting increase in poverty, regional development disparities, infrastructural bottlenecks, rapid unplanned expansion of urban areas, environmental degradation, uncomfortable inflationary pressures, poorly developed human resources, unsatisfactory industrial relations, soft and corrupt public services, sub-optimal investment and production decisions, inefficient public sector enterprises, large infected portfolios of banks and development finance institutions, extensive proportions of the under-ground or parallel economy and our disappointing rating in terms of the physical quality of life index (PQLI).

To a large extent, our economic and development failures can be attributed to the absence of an effective mechanism for designing a timely and well coordinated response, that could take maximum advantage of Pakistan's potential in a rapidly changing international economic environment and initiate vigorous measures for repairing our deficiencies.

Again, our planners and economic managers have not always succeeded in convincing political/military leadership that the consequences of ignoring economic problems and of making major economic mistakes could be serious.

In the last three decades, mismanagement of the economy has been responsible for the downfall of many governments across the globe.

Generally, our economic and financial policies are marked with adhocism. More specifically, there has never been a sound evaluation of major policy changes in terms of their effectiveness to achieve the intended goals. Absence of such appraisal allows the development of vested interests which often work for the perpetration of policies which are contrary to the national interest. This highlights the need to establish some mechanism for an objective review of major polices and projects on periodic basis.

Unfortunately, so far we have not been able to establish an effective mechanism for devising and implementing an integrated macro economic policy framework consisting of fiscal, monetary, exchange and trade policies for achieving our growth and equity objectives in a milieu of relative price stability and sustainable external account. The conduct of monetary and fiscal policy is generally regarded as being the respective responsibility of the central bank and the government, but both of these, alongwith trade and exchange policy, form the essential ingredients of economic policy and they are not to be viewed in isolation but as part of an overall package of policies aimed at sub-serving the objectives of growth, stability and equity.

Price and exchange stability the traditional concerns of monetary authorities far from being regarded as being incompatible with other objectives of economic policy like the furtherance of growth and maintenance of high and stable level of employment are basic to successful achievement of these objectives. Actually, sustained growth is not possible without some degree of price stability.

In determining the role of monetary policy in the development context, it should be kept in view that it is not money but real resources that determine the rate of growth. It is only the increase in real resources, the success with which these are mobilised and the efficiency with which they are invested that help to enhance the rate of economic growth. As I.H. Adler very appropriately observed: "If growth of real output could be purchased by money alone, the central bank could easily solve the problem and solve it in a hurry."

In a properly integrated framework of macro-economic policy, monetary and fiscal policies have complementary roles. When structural changes in the economy are being attempted, fiscal policy commends itself as the most appropriate instrument while the impersonality, flexibility and ability to respond quickly to situations are factors to be taken into account in deciding on deployment of monetary policy to manage short-term or conjunctural situations, though obviously monetary policy is not without relevance even to the pursuit of longer term objective of growth.

In Pakistan despite the existence of a National Credit Consultative Council and the device of the Annual Credit Plan (which inter-alia, makes recommendations for ensuring a coordinated approach to fiscal and monetary policies), experience has shown that in a large number of years during the 1980s and 1990s the ex-ante arithmetic of the needed volume of credit to the government could not be faithfully adhered to; the ex-post reality in this behalf often revealed a large excess leading to a measure of imbalance in the domestic economy.

For monetary policy to be effective, therefore, close coordination with the fiscal authorities is clearly indicated as otherwise fiscal operations in the form of large deficits exert a direct effect on monetary expansion beyond the control of the central bank. The ability of the central bank to contain its credit to the government within prudent limits is an aspect of its status within the government.

In this regard, it is heartening to note that the State Bank of Pakistan as a result of legislation promulgated in 1997 has been given the authority to determine and regulate the money supply and government borrowing from the central bank. Furthermore, any governmental or quasi-governmental body or agency has been debarred from issuing instructions directly or indirectly to any banking company or any other financial institution regulated by the State Bank, which is inconsistent with the polices, regulations and directives issued by the Bank.

Aside from integrating monetary, fiscal and trade policies for sustaining growth with stability, our development experience has also highlighted the importance of setting up a mechanism to fully integrate the current management of the economy with long term social and economic goals. Planning and economic management are not separate but inter-related tasks, one being long-term in nature and the other being short-term.

In the past, even with considerable support provided by external resources, there has been a real hiatus between shorter and longer term economic policies, the former being in nature restrictionist and the latter expansionist, each partially under-cutting the purpose of the other. Actually, at the moment, there is an urgent need of ensuring a measure of harmony between long-term development goals and short-term crisis management. The theme of achieving the goals of economic growth, expansion of employment opportunities, equity and stability has been felt with increasing sharpness in recent years. We must craft an appropriate institutional mechanism to respond to this challenge.

Pakistan's economy, notwithstanding it's macro imbalances and poor social indicators, is basically resilient in as much as it has survived frequent and major political changes in the country. The country achieved an annual average rate of growth 6.3 per cent during the Sixth Five Year Plan (1983-88). During the period of the Seventh

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Five Year Plan (1988-93), the growth rate decelerated to to an annual average of 4.8 per cent and to 4.2 per cent in the Eighth Plan (1993-98) period. During the three year period FY99-FY01, the average annual growth of domestic output fell further to 3.6 per cent. In the current fiscal year (2001-2002), the growth in GDP is expected to be 3.5 per cent as against the target of 4.0 per cent.

The economy will certainly respond to improvements in policy framework and governance as is being currently attempted. It should not be difficult to achieve an annual real growth rate of 5 per cent by 2003-04 and of 6.3% in 2010-11 as projected in the Planning Commission's Ten Year Perspective Development Plan 2001-11.

The case...

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The political forces sustaining financial liberalisation have been identified in a number of studies. Hellineir for example shows that international financial liberalisation has been an explicit political choice of the metropolitan states. He attributes capital account liberalisation by the OECD governments to the growing political influence of international banks in the United States, Germany and Britain.

Under this political pressure advanced country governments, choose not to implement more effective capital controls when they have both the legal right and the technical expertise to do so. Financial liberalisation is a political not a technical imperative States continue to have the technical resources to regulate capital markets but they choose not to do so for political reasons. Governments are not forced to liberalise for technical reasons but choose to do so because the political representatives of international finance dominate them.

In recent years, a large literature has been produced to show that capital controls retain high effectivity in present circumstances. The choice not to use capital controls reflects a political willingness to bear the domestic costs of the international integration of financial markets. In the post Bretton Woods period the financial power of the United States vis-a-vis other states has not declined. It has declined with respect to the international financial markets because the representatives of international finance have captured the US state. As domestic political costs of adjusting to international financial market integration increase international policy co-ordination becomes a matter of imposing a larger proportion of such costs on the weaker open states - such as those of east and south Asia. In this sense, international financial market integration increases the vulnerability of the weak states, which rely on foreign capital (Thailand, Malaysia and Indonesia). Failure on the part of these states to subordinate their fiscal and monetary policies to those of the western powers is heavily punished by the speculators dominating the world financial markets.

— See part-II in next Monday's issue