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Structural Adjustment and Poverty in Pakistan

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The Pakistan Institute of Development Economics, established by the Government of Pakistan in 1957, is an autonomous research organisation devoted to carrying out theoretical and empirical research on development economics in general and on Pakistan-related economic issues in particular. Besides providing a firm foundation on which economic policy-making can be based, its research also provides a window through which the outside world can see the direction in which economic research in Pakistan is moving. The Institute also provides in-service training in economic analysis, research methods, and project evaluation.

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I. INTRODUCTION

Until recently, the Bretton Wood institutions as well as a number of economists had assumed that growth trickles down to the poor, and exclusive reliance on growth was sufficient for a reduction in poverty. Therefore, Structural Adjustment and Stabilisation Programmes (SAP) that aimed at improving the efficiency levels and higher growth rates were pursued without worrying about the poverty. The conclusion that growth was sufficient for a reduction in poverty was supported by Dollar and Kraay (2000), who found unitary elasticity of poverty with respect to growth. However, this has been contested and Foster, *et al.* (2001) shows much lower elasticity of poverty reduction to growth; under certain assumptions, the impact of growth on poverty turns out to be negligible. Similarly, Ghura, Leite, and Tsangarides (2002) point out that while growth raises the incomes of the poor, the relationship is less than one-to-one. Kakwani (2001) points out the trade-off between growth and income distribution—growth would help in poverty reduction only if growth over-compensates the effect of rising income inequalities. Pakistan's experience of the 1960s and the 1970s does not support the trickle-down theory. Despite high growth in the 1960s, poverty increased, and the slowing down of growth in the 1970s was accompanied by a sharp reduction in poverty [Amjad and Kemal (1997)].

Over the last 15 years, Pakistan has implemented various Structural Adjustment and Stabilisation Programmes (SAP) of the IMF and the World Bank, with varying degrees of implementation and success. These programmes revolve around reduction in the budgetary and balance-of-payments deficits and pursuance of market-friendly policies, and aim at improving the levels of efficiency and achieving higher levels of output. However, deflationary policies to stabilise the economy, and structural changes in the production processes and financial sectors, can result in a loss of output in the transitional period.

Pakistan's track record in implementing the SAPs has not been very good. Most of the programmes were discontinued because Pakistan failed to implement the agreements fully.[1] However, the SAP signed in 2000 was faithfully implemented and it has met almost all the conditionalities under the PRGF. Both because of successful implementation of recent SAP agreement and because of the 9/11 events, she has been able to achieve economic stability. The foreign exchange reserves have increased to a record level of $9.5 billion, rupee has gained strength, inflation rate is less than 5 percent, balance of payments has turned surplus, fiscal deficit has an underlying declining trend, and growth of both internal and external debt has slowed down. However, the real sector of the economy has suffered badly. The growth performance throughout the 1990s has been poor, it has declined from 6.5 percent to 4.7 percent, and during the last three years the growth rate has slumped to just 3.3 percent. Investment has fallen to just 13.9 percent of GDP, unemployment rate of 7.8 percent in 1999-

[1] In 1998 Pakistan implemented the agreement faithfully but it had to be abandoned because of the international sanctions imposed on the country after nuclear explosions.

2000 may have increased even further, the self-employed do not have sufficient work, real wages have fallen, and poverty has almost doubled over the decade. As during the 1990s Pakistan has implemented various Structural Adjustment and Stabilisation Programmes, the increase in poverty is generally attributed to them.

One of the factors responsible for the increase in poverty has been the slowing down of the growth rate, which depends crucially on the rate of investment. While public investment may have fallen because of the requirements to reduce fiscal deficit, private investment has been badly hit by the lack of consistency and continuity of the economic policies, law and order situation, etc. Since Pakistan has failed to implement various programmes and the private investment has been affected by many other factors, the increase in poverty cannot be attributed entirely to SAP. It cannot be ruled out that a counter-factual of the economy if SAP programmes were not implemented may show poorer performance of the economy than has been witnessed in the 1990s. Nevertheless, a better designed programme could have yielded better performance in terms of growth, employment and poverty.

Incidence of poverty has already assumed critical proportions, and it is feared that it may rise even further unless a pro-poor bias is introduced in the macroeconomic policies and/or social safety nets are put in place. We need to underscore the fact that macroeconomic policies not only impact the growth rate by improving the levels of efficiency but also the distribution of income and thus lead to reduction in poverty levels. Since macroeconomic (financial) fundamentals have gained strength, there is a distinct possibility that investment rate starts increasing. With a view to ensuring that economic growth trickles down, the growth needs to be tilted towards creation of remunerative and productive employment opportunities and investment in the human resource development activities, especially education and health services.

The main objective of the study is to examine the macroeconomic policies as a part of various Structural Adjustment and Stabilisation Programmes, with a view to assessing their impact on growth, employment and poverty. By identifying economic policies that impact poverty alleviation, a coherent strategy can be formulated for reduction in poverty.

The plan of the study is as follows: After this introductory section, a review of macroeconomic policies that are pursued under structural adjustment and stabilisation programmes is presented in Section II. The outcome of these policies on savings, investments, growth, employment, income distribution, and poverty is analysed in Section III. The determinants of poverty over time in Pakistan are explored and pro-poor strategy for poverty reduction is presented in Section IV. The final section summarises the main conclusions of the study.

II. MACRO-ECONOMIC POLICIES AND POVERTY

Macroeconomic policies pursued in Pakistan during the 1990s have been influenced by the various structural adjustment and stabilisation (SAP) programmes:[2] These

[2]Three recent programmes relate to the periods of 1988–91, 1993–96, and 1997–2000, and at present Pakistan is implementing the Poverty Reduction and Growth Facility programme.

programmes include rationalisation of the tariff structure, import liberalisation, exchange rate mechanism, broadening the sales tax net, rationalisation of government expenditures including a reduction in subsidies, deregulation of investments and foreign exchange, financial reforms, restructuring of public utilities, divestiture of public assets, etc. While such programmes are expected to improve levels of efficiency, their impact on growth rates of output, employment, and poverty is uncertain in the short run. A number of studies, including Khan and Nadeem-ul-Haq (1990); Cooper (1992); Corbo and Suh (1992); Jain and Bongartz (1994); Sachs and Warner (1995); Banuri, Khan, and Mahmood (1997); FitzGerald and Mavzotas (1997), FitzGerald and Perosino (1999); Pasha, Stubbs, and Clarke (1995); and IEA volume edited by Mahmud (2001) have examined the impact of these programmes and provide conflicting evidence on the impact of such programmes on poverty.

By changing the profitability of various economic activities, macroeconomic policies affect the investment level, allocation of investible funds to various activities and growth rate of output. By influencing the choice of technology, they affect functional and size distribution of income. Through changes in incidence of taxes and expenditure, changes in the administered prices which include utilities, petroleum and wheat, inflation rates, etc. they significantly influence the poverty levels.

That the rising income levels and equitable distribution of income are the basic ingredients of poverty reduction and both of these are affected through production relationship is quite well-known. The output of a country at a point of time is determined through the production function:

$$Y = Ae^{gt}F(K,L)$$

where

Y = output levels
g = growth rate of productivity
t = time
K = capital
L = labour

Entrepreneurs play a key role as they employ capital and labour to maximise the value of output. Their decisions determine the efficiency levels, which in turn are affected by a large number of factors including the market structure, protection levels, technological choices, the degree of distortions in factor markets, etc.

Capital stock in a particular year depends on the existing capital stock and the investment flow during the year:

$$K_t = (1-\delta)K_{t-1} + I_t$$

where

δ is depreciation rate
I is investment level.

Obviously capital stock increases only if I_t exceeds δK and when investment rate is rather low, capital stock may even fall. The investment levels besides a large number of factors including consistency and continuity of policies also depend on the fiscal deficit, corporate tax rates, import duties, sales taxes and excise duties. The protection structure and fiscal incentives play a crucial role in the allocation and utilisation of investment.

Labour employed and its quality also play an important role in the growth process. Whereas labour employed depends on investment levels, technological choices and industrial mix, the human resource development improves the quality of labour. The growth of productivity depends on the changes in allocation of resources towards more efficient activities, human resource development, learning by doing, possibilities of catching up, and technology embodied in new machines.

Value added in any activity and in the economy is distributed between capital and labour. According to Euler theorem, if there are constant returns to scale[3] the output will be exhausted if the production factors are paid in accordance with marginal productivity, i.e.

$$\frac{\partial Y}{\partial L} = w$$

$$\frac{\partial Y}{\partial K} = r$$

The functional income distribution depends on the relative use of inputs and the remuneration to production factors, i.e.

$$s_L = \frac{L_t w_t}{Y_t}$$

$$s_k = \frac{K_t r_t}{Y_t}$$

where

s_L = share of labour
s_k = share of capital
w_t = wage
r_t = rental of capital.

Obviously, adoption of labour intensive technologies implies higher level of employment, and if the demand for labour exceeds the supplies wage rates tend to rise leading to improvement in functional distribution. Markets, and wage rate and income policies determine the household incomes. Therefore, employment oriented growth strategy can result in improved distribution of income and decline in poverty levels.

In the following, we review the following macroeconomic policies:

(i) Fiscal policy;
(ii) Monetary policy;

[3]In case of decreasing returns to scale, there will be excessive profits. When returns to scale are increasing, competitive market structure does not exist.

(iii) Trade policy;
(iv) Exchange Rate policy;
(v) Investment policy; and
(vi) Privatisation policy.

(i) Fiscal Policy

Fiscal policy impacts poverty through four avenues. Firstly, the high fiscal deficit may result in higher increases in money supply thereby generating inflationary tendencies in the economy. Second, by providing fiscal incentives and protection structures it promotes growth in specific economic activities. Third, changes in tax structure and incidence have significant implications for poverty. Fourth, public expenditure, both, development and non-development, also impacts poverty levels.

Fiscal policy since 1987-88 has been governed by three major considerations. Firstly, the fiscal deficit had grown to an unsustainable level of 8.5 percent of GDP by 1987-88 resulting in a rapid growth rate of public debt. The deficit had to be reduced to a sustainable level. Second, distortions in the tax structure and the maladministration were constraining the tax revenues and as such a need to bring about structural changes in the tax system and improvement in tax administration. Third, a conscious decision to reduce the role of the government in the economy by leaving the investments in commercial activities to private sector and thus necessitating rationalisation of the public expenditure. In the following we examine the extent to which these objectives have been realised and have impacted poverty levels.

Fiscal Deficit

The 1987-88 SAP aimed at reduction in fiscal deficit from 8.5 percent of the GDP to 4.0 percent of GDP over a period of three years. While fiscal deficit did decline to 6.5 percent of GDP in 1989-90, it increased subsequently to 8.7 percent by 1990-91. (See Table 1.) The public expenditure gradually declined from 26.7 to 25.7 percent,[4] but fluctuations in revenue were responsible for changes in the fiscal deficit. The primary deficit increased sharply from 1.6 to 4.1 percent of GDP[5] clearly indicating that it was not the debt-servicing but the failure of government to mobilise sufficient revenues that led to increase in fiscal deficit.

Because of an increase in total revenues the fiscal deficit declined to 7.7 percent in 1991-92 despite an increase in public expenditure. In the subsequent years government failed to mobilise resources and resultantly fiscal deficit increased despite a reduction in the public expenditure. While development expenditure declined from 5.7 to 3.9 percent of GDP and the defence expenditure from 6.6 to 5.1 percent, interest payments increased from 5.9 to 7.6 percent of GDP. Accordingly, even though overall fiscal deficit had increased to 7.7 percent of GDP by 1997-98, primary deficit had turned marginally surplus.

[4]The non-development expenditure declined from 19.8 to 19.3 percent of GDP and development expenditure declined from 6.9 to 6.4 percent of GDP over the 1988-91 period.

[5]The primary surplus was 0.4 percent in 1989-90.

Table 1

Budgetary Deficit in Pakistan

(as Percentage of GDP)

Year	Total Revenues	Tax Revenues	Surplus of Autonomous	Public Expenditures				Budgetary Deficits	Primary Surplus
				Total	Non-Development	Interest Payments	Development		
1987-88	17.3	13.8	0.9	26.7	19.8	6.9	6.9	8.5	–1.6
1988-89	18.0	14.3	0.7	26.1	19.9	5.0	6.2	7.4	–2.4
1989-90	18.6	14.0	0.8	25.7	19.3	6.9	6.5	6.5	+0.4
1990-91	16.9	12.7	0.8	25.7	19.3	4.6	6.4	8.7	–4.1
1991-92	19.2	13.7	1.2	26.7	19.1	5.2	6.4	7.7	–2.5
1992-93	18.0	13.3	0.1	26.0	20.3	5.9	5.7	8.0	–2.1
1994-95	17.3	13.8	0.3	22.9	18.5	5.2	4.4	5.6	–0.4
1996-97	15.6	13.4	–	22.3	18.8	6.6	3.5	6.4	+0.2
1997-98	16.0	13.2	–	23.7	19.8	7.6	3.9	7.7	–0.1
1998-99	15.9	13.2	–	22.0	18.6	7.5	3.4	6.1	+1.4
1999-00	17.1	12.9	–	23.6	20.3	8.2	3.3	6.6	+2.2
2000-01	16.0	13.0	–	21.3	19.0	7.3	2.4	5.3	+2.0
2001-02	17.1	12.9	–	23.7*	19.5	6.5	3.4	6.6	+0.1
								(4.6)	

Source: Economic Survey 2001-02 and previous issues.

* Includes net lending of 0.9 to PSEs. The figure in parenthesis is adjusted deficit.

It is generally argued and rightly so that the sequencing of reforms was not proper. It is believed that fiscal deficit should have been reduced prior to the financial reforms so that the government did not have to borrow at very high rates of interest. However, because most of the credit was made available by the nationalised commercial banks, the government believed that higher interest payments would be compensated by the increase in bank profits. However both because the nationalised banks made losses due to number of factors including non-performing loans, and government also borrowed from the private banks, it did not happen. Moreover, it is not very clear if the government would have made any serious efforts to reduce deficit if financial reforms were not undertaken.

Sanctions were imposed on Pakistan after nuclear blasts in 1998. Over 1998-01 period, the fiscal deficit has declined from 7.7 to 5.3 percent of GDP despite the fact that total revenues have declined further to 16.0 percent of GDP by 2000-01. The decline in fiscal deficit has been entirely due to reduction in the public expenditure; non-development expenditure declined from 19.8 to 19.0 percent of GDP and the development expenditure from 3.9 to 2.4 percent of GDP. The expenditure on both defence and interest payments declined during this period, former declining from 5.1 to 4.5 percent and latter from 7.6 to 6.5 percent of GDP. However, the cut in crucial non-development expenditures and public sector development programme had adverse implications for productivity, growth, social infrastructures and poverty. Fiscal deficit declined from 6.1 percent to 5.3 percent of GDP and primary surplus increased from 1.4 and 2.0 percent of GDP over the 1999-01 period.

In the post 9/11 period, fiscal deficit has once again increased to 6.6 percent in 2001-02 but if grants to CBR, increase in defence expenditure and grants to KESC and

WAPDA are excluded, fiscal deficit falls to 4.6 percent of GDP. Moreover, most of the fiscal deficit has been financed by grants. The most worrying aspect of the fiscal system during 2001-02 is almost disappearance of the primary surplus.

Fiscal deficit may either be reduced by mobilising additional resources or by restricting the public expenditures. Preceding discussion shows quite clearly that there is no underlying trend in the revenues; fluctuations have been around 17 percent of GDP. We may underscore that increase in resource mobilisation does not necessarily lead to higher savings unless additional resources are invested, or fiscal deficit is reduced and mobilisation of resources does not reduce the private savings. Obviously, if the decline in fiscal deficit is a result of decline in development expenditure, it retards the growth process.

Taxation Policy

While taxes are generally imposed to generate revenues, they have significant implications for the production structure and income distribution. Pakistan's tax structure has a narrow and distorted base, proportion of indirect taxes has been high making the tax structure inelastic, and it lacks progressivity. Moreover, tax administration has been rather weak leading to heavy tax avoidance and tax evasion.

The four main taxes in Pakistan include: tariffs, sale taxes, excise duties and income taxes.[6] Whereas tariffs were the major source of revenue up to 1980s, its share in revenue has gone down from 41 to 10 percent. This is being used only for protection purposes at present. The share of excise duties has also fallen from 19 to 10 percent, because they are no longer being used for revenue purposes. They are being used only to control the consumption expenditures on specified commodities. However, share of sales taxes has increased almost four-fold from 9 to 35 percent and this is going to be the major sources of tax revenue. The income tax is the only progressive tax in the entire tax structure. While its share has increased from 13.3 to 30.6 percent, most of the growth is due to withholding income taxes that are indirect taxes in nature.

Pakistan's manufacturing industries were raised behind protection provided through quotas, outright bans, and tariffs. However, by the end of 1980s almost all the quota restrictions were removed, and the items on negative list were gradually reduced during 1990s. At present it contains only those products which are prohibited because of health, religious, safety and security reasons. Obviously, if the tariff rates are prohibitive, they are no different from the bans.

High rates of protection breed inefficiency and/or excessive profits. The import duties have been reduced and rationalised; from a maximum import duty rate of around 125 percent in 1987-88 it has been brought down to a maximum of 25 percent in 2002-03 budget. At present protection is being provided only through tariffs, and the reduction in protection has lead to the closure of a large number of firms. Had the investment rates increased, the increase of output from new investment could have compensated for the loss of output as a result of the closure of firms. Over longer run, however, production would accord with comparative advantage resulting in efficient and higher growth rates.

[6]The wealth tax has been abolished recently.

Besides protection, various economic activities have been provided fiscal incentives in the form of tax holidays, accelerated depreciation, tax credit, etc. While in the first half of 1990s these incentives were increased, in the second half most of these were withdrawn. The 1997 Investment Policy allows only accelerated depreciation allowances and concessions in import duties on machinery. The net result of all these measures has been the decline in the post-tax profitability over the 1990s.

Reduction in tariffs though necessary for efficient growth processes, also involves revenue losses. The losses were to be compensated by the increase in sales tax revenue by widening the tax net. While tax net has been extended up to production stage including the food products, consumed by the poor, it could not be extended to wholesale and retail trade. Though in the 2001-02 budget sales tax has been extended to all traders above the threshold level of Rs 5 million.

The share of direct taxes has increased from 13.3 percent in 1987-88 to 16.6 percent in 1990-91, and further to 30.6 percent by 2001-02. (See Table 2.) The sharp increase in the share of direct taxes, however, has come from the mushrooming net of withholding taxes on import, export, contractors' income, etc.[7] It has been estimated by the IMF (2001) that withholding taxes account for around 70 percent of net income tax collections and for almost the entire revenue augmentation over the 1990s. The extensive reliance on withholding tax has been a key factor behind the failure of the tax administration to adopt the modern income tax system. The current system is based largely on manual procedures that allow the tax authorities to use their discretionary powers. Government is deprived of the massive tax revenues. However, 2003 budget has introduced a voluntary compliance, self-assessment scheme supported by an effective, trusted, and well-targeted audit which hopefully would help in the augmentation of the revenues.

Table 2

Tax Structure of Pakistan

(Percentage Share of Tax Revenues)

Year	Direct Taxes	Indirect Taxes			
		Total	Tariffs	Sales	Excise Duties
1987-88	13.3	86.7	40.7	9.3	18.8
1989-90	13.2	86.8	42.4	13.0	19.5
1990-91	16.0	84.0	39.0	13.0	19.3
1992-93	21.0	79.0	35.1	13.0	19.8
1996-97	26.8	73.2	26.5	17.1	17.3
1997-98	29.6	70.4	21.0	15.2	17.7
1998-99	27.0	73.0	20.1	17.6	16.0
1999-00	30.9	72.3	15.7	28.8	14.2
2000-01	30.0	75.8	14.5	34.3	11.3
2001-02	30.6	69.4	10.4	35.0	10.2

Source: Economic Survey, Statistical Supplement, 2000-01 and previous issues.

[7]The 24 kinds of payments/transactions subject to withholding taxes are essentially indirect taxes and are misclassified as direct taxes.

The tax-whitener and immunity schemes have been a moral hazard leading to tax evasion. The same is true of treating the agricultural incomes separately for income tax purposes. While there still exist loopholes, the policy of taxing the perks and incomes of National Saving Scheme, rationalising of personal income and corporate tax rates, annual 3 percent reduction of corporate tax for banking companies, and one percent for the private limited companies over the next five years, are steps towards better compliance.

Changes in the tax structure have significantly impacted the tax incidence. Because of smuggling most of the import duties on the consumer goods were redundant, and as such tariff rationalisation involving a decline in import duties on inputs benefited only the producers.[8] Broadening of sales tax base even to the products used by poor also leads to increase in poverty. The reduction in personal income taxes also helps richer sections of the society. Therefore, incidence of taxes increased sharply for the poor and declined for the higher income groups over the 1988-2002 period. (See Table 3.)

Table 3

Incidence of Direct and Indirect Taxes

Groups	1987-88	1992-93	1997-98	1999-2000
GI	7.94	8.97	8.60	8.24
GII	8.11	9.13	8.67	8.18
GIII	8.63	9.42	8.63	8.18
GIV	8.18	8.89	8.20	7.81
GV	8.18	8.89	8.10	7.65
GVI	8.24	8.95	8.00	7.54
GVII	8.10	8.64	7.67	7.29
GVIII	8.29	8.69	7.68	7.33
GIX	8.03	8.49	7.43	7.13
GX	8.87	9.42	8.14	7.69
GXI	8.70	8.92	7.65	7.33
GXII	10.17	10.14	8.59	8.14

Source: Pakistan Institute of Development Economics, Islamabad.
Note: GI is the poorest and GXII is the richest income group.

Public Expenditures

The public expenditure affects the poverty levels in at least four major ways:

- employment creation;
- provision of physical infrastructure;
- provision of education, basic health care, safe water and sanitation; and
- subsidies.

Public sector development expenditure (PSDP) plays an important role in the provision of physical and social infrastructure. Whereas over 1988–93 the decline in

[8]The households may indirectly benefit through the increase in employment.

PSDP was relatively small from 6.9 percent to 6.4 percent of GDP, in subsequent years it has declined sharply; by 1997-98 it fell to 3.9 percent. It was only 2.8 percent by 2000-01, however, in the year 2001-02, it increased to 3.4 percent of GDP but is stagnant at 3.4 percent for the year 2002-03 Non-development expenditures have also affected the growth as the necessary operation and maintenance expenditure was not provided.

While to some extent the reduction in PSDP was expected because the government had decided not to invest in commercial activities, a steep fall in the development expenditure has serious repercussions for the provision of human capital, physical infrastructure, growth of GDP, employment, and on poverty levels. Obviously, if the physical infrastructure is inadequate, the profitability of industrial activity goes down with serious implications for growth. Similarly, low allocations to the social sectors result in low levels of human capital and productivity.

Public expenditures affect employment levels in at least two ways. Firstly, the increase in non-development expenditures generates direct employment. During the 1977–88 period, an increase in the public sector employment was mainly responsible for the low levels of unemployment. However, creation of unproductive employment is wasteful and reduces the potential for employment growth. On the other hand, employment creation through public works programme may generate productive employment as it would help in improving the availability of infrastructures. Second, basic infrastructure needed by poor farmers, micro entrepreneurs, and labour-intensive manufacturers helps in generating medium and long run employment opportunities.

Whereas almost all successive governments have allocated money for public works programmes under different names, the Khushhal programme of the previous government is meant specifically for creation of employment opportunities and provision of infrastructures. Obviously, if the economic activities and technologies chosen are labour-intensive, more employment would be generated.

The human development indicators of Pakistan are rather poor and public expenditures can go a long way in improving them. Such expenditures would help in raising productivity, improving quality of life, and creating a virtuous cycle for intergenerational economic and social mobility and poverty eradication. The Social Action Programme (SAP) initiated in 1993, failed in improving the primary education, primary health, population welfare, and water supply situation. Primary school gross enrolment rate declined from 73 percent to 71 percent, and net primary school enrolment from 46 to 42 percent. The gross middle school enrolment rate declined for boys—from 58 to 48 percent, and increased marginally for girls from 31 to 32 percent in the 1990–99 period. Whereas in the subsequent period up to 2001-02, gross and net enrolment at primary level has remained almost the same, it has gone down from 80 to 73 percent at middle, and from 84 to 78 percent at matric level.

In the health sector the indicators show some improvement. The infant mortality rate (IMR) declined from 122 to 89 over 1991–99 period and to 82 by 2001-02. The percentage of population immunised has gone up from 37 percent to 49 percent over the 1991–99 period, and to 53 percent by 2001-02. Although some progress has been made to control infectious diseases like tuberculosis, enteric fever, and diarrhea, they continue to

be the major causes of death in Pakistan. Majority of the diseases are preventable at relatively low cost but because of the emphasis on curative health in preference to preventive health it has not been possible.

Though the fertility rate has fallen from 6.2 in 1989-91 to 5.0 percent in 1998-00, it is still higher compared to the desired fertility level. The contraceptive prevalence rate has marginally improved from 17 percent in 1998-99 to 19 percent in 2001-02. While population growth rate over 1981–98 census has declined to 2.6 percent and at present it may be around 2.1 percent, the impact of family planning programme on fertility control leaves much to be desired.

Pakistan also reduced both development and non-development subsidies under the SAP. Elimination of development subsidies resulted in an increase in the prices of fertiliser, tubewells, pesticides etc., thus increasing the cost of production leading to reduction in the profitability of the agriculture sector. No doubt, the farmers were compensated through an increase in the prices of agricultural products but only large farmers benefited from this increase in prices because the small farmers had very little marketable surplus. Moreover, the small farmers have not been able to use the requisite amount of agricultural inputs because of the non-availability of credit leading to decline in production. The current subsidies are meant to keep down the prices of wheat, vegetable ghee, etc. for the consumers and their elimination hurt the poor most.

Though subsidies in nominal terms have increased but most of these have been provided to loss making public enterprises. As a matter of fact, the poverty related subsidies have declined from Rs 5257 in 1990-91 million to just Rs 284 million by 2000-01, i.e. from 0.52 to 0.01 percent of GDP. (See Table 4.)

Table 4

Federal Subsidies at Current Prices

(Million Rupees)

Year	Total Subsidies	Poverty Related Subsidies	As % of Total Subsidies	Wheat for FATA/NA	Imported Wheat	Wheat for Afghan-istan	Edible Oil	Sugar
1990-91	8150.9	5256.6	64	148.6	788.3	1156.1	2140.9	312.0
1991-92	8205.9	5259.7	64	128.4	3671.4	250.0	187.9	32.0
1992-93	5177.3	3235.7	62	126.4	2324.9	100.0	–	–
1993-94	5138.2	2999.4	58	142.3	483.2	175.0	–	–
1994-95	3691.1	3331.3	90	521.6	443.9	44.0	–	–
1995-96	10435.4	9181.5	88	537.7	7014.0	107.8	–	–
1996-97	7588.2	6798.1	90	473.8	5864.7	–	–	–
1997-98	6554.8	4897.6	75	464.1	4221.5	10.0	–	–
1998-99	3992.5	3623.8	91	501.0	2072.9	60.0	–	–
1999-00	14427.0	1555.9	11	474.0	1045.9	5.0	–	–
2000-01	27706.1	671.5	3	638.5	0.0	20.0	–	–
2001-02	25,580.0	659.0	3	638.5	–	20.8		–
2002-03	20,794.0	790.0	4	649.0	–	20.0	–	–

Source: Niazi (2001).

The preceding discussion shows quite clearly that the burden of reduction in fiscal deficit for stabilising economy has been placed squarely on the poor. The tax incidence on poor has increased, consumption subsidies for the poor have fallen, and even though expenditure on education and health did increase, it hardly benefited them.

(ii) Monetary Policy

The stabilisation programmes call for demand management and though the contractionary monetary policy. Since Pakistan's fiscal deficit has been large until recently, necessitating borrowings from the banking sector, the central bank had to perform a rather difficult balancing act between growth and stability. While an increase in credit beyond safe limits generates inflation and slowing down, the growth of money supply with a view to bringing stability in the economy has serious repercussions for the growth. Reduction in the fiscal deficit and reprofiling of the debt in recent years, however, has eased the situation considerably.

The growth rate of money supply accelerated from 12.2 to 17.8 percent over the 1988–93 period mainly due to increased demand for credit for the budgetary support.[9] The monetary growth in the 1993–98 period slowed down, though it still remained in the double digit. However, in this period the credit to private sector grew at a more rapid rate than the credit to the government sector. The growth of money supply decelerated during 1999-01 period to single digit, but increased very rapidly during 2001-02. It increased at a rapid rate of 14.8 percent mainly due to sharp increase in the foreign assets which grew by Rs 206 billion due to the sharp increase in foreign exchange reserves.[10] The decline in debt servicing and the sharp fall, or even retirement of public sector loans to private sector has created more space for the private sector credit. Despite excess liquidity with the banks both because of the reluctance of the banks to take risk and the lack of demand on the part of private investors, credit to private sector has been constrained [see Table 5]. Private investment especially in the manufacturing sector and credit availability are significantly related [see Khan (1996) and Kemal (1989)].

The liquidity in the system instead of financing real investment has flowed to stock exchange and the real estate. There is a grave danger that the bubble may burst with far-reaching implications for both the real and financial sectors.

While at present there is enough liquidity in the system, the credit to private sector continues to be low. In a bid to reduce infected portfolio of the banks, NAB action has eroded the confidence of investors as well as bankers, and resultantly the credit to private sector has fallen. The rates of interest continue to be high, though nominal interest rates have fallen. Any reduction in the discount rate is not passed on to the borrowers because of high dispersion between the deposit and lending rates. Since infected portfolio is the main reason for dispersion, it is high time that this problem is resolved on an urgent basis. Since banks are owned by the government, they will eventually have to bear the cost of

[9]While the credit to private sector also increased, it was almost one-half of that of the public sector borrowing.

[10]The domestic credit increased by just Rs 20 billion, i.e., 1.3 percent.

Table 5

Growth Rate of Money Supply

(Percent)

Year	Public Sector Borrowing	Budgetary Support	Private Sector	Money Supply (M2)
1987-88	17.3	13.3	13.4	12.2
1988-89	5.7	5.6	8.3	4.6
1989-90	8.8	–2.2	11.4	12.6
1990-91	24.7	33.2	9.0	17.4
1991-92	34.3	32.2	12.0	26.2
1992-93	27.8	25.6	20.7	17.8
1993-94	8.2	7.2	10.1	18.1
1994-95	14.2	10.5	17.7	17.2
1995-96	16.0	13.5	13.7	13.8
1996-97	16.3	16.7	11.7	12.2
1997-98	8.4	9.5	13.8	14.5
1998-99	–11.8	–13.6	17.1	6.2
1999-00	13.3	7.9	3.2	9.4
2000-01	–7.1	–6.0	8.2	9.0
2001-02	2.4	2.4	2.1	14.8

Source: State Bank of Pakistan, *Annual Report 2001-02,* Karachi.

write-offs. Earlier they do the better it is. Nevertheless, effective implementation of prudential regulations such as Per Party Exposure, maximum lending to a single 'person', and avoidance of political intervention must be ensured.

While credit availability even to large producers is constrained, small farmers, businessmen and industrialists have been the worst sufferers. Various schemes instituted in the past to provide credit to small producers at concessional rates have not been successful because the small enterprises could not meet the collateral requirements. The establishment of SME Banks, Poverty Alleviation Fund, Khushhal Bank, and micro banks in private sector are expected to help in disbursing credit to these enterprises.

There have been structural weaknesses in the financial sector including the control of credit through administrative measures, the restrictions on maximum and minimum interest rates, and extension of credit to the government sector at a fixed rate. Structural Adjustment Programme called for removing these weaknesses. Major reforms in the financial sector include autonomy of the State Bank of Pakistan, use of market based instruments to control the money supply, auctioning of the government securities through the bids, development of the secondary securities market, withdrawing restrictions on the maximum and minimum rates of return on the deposits, and improvements in the State Bank's regulatory and surveillance capacity. Reforms in the early 1990s replaced the system of administrative controls on credit with market-based instruments. Financial institutions have neither any credit limit nor are obliged to provide credit to the government at a specified low rate of interest any longer.

The nominal lending rates have gradually fallen from 14.8 percent in June 1999 to 13.2[11] percent in June 2002, but the real interest rate over the same period has increased from 9.1 to 9.7 percent. The high interest rates are essentially because of the large spread (7.9 percent) between lending and deposit rates. (See Table 6.) The interest rates are extremely high and may have been the major contributory factor in the low demand for credit by the private sector.

Table 6

Lending and Deposit Rates

Year	Lending and Deposit Rate		Weighted Average Deposit Rate		Difference between Lending and Deposit Rate	
	Nominal	Real	Nominal	Real	Nominal	Real
June-1995	13.7	0.7	8.2	–4.8	5.5	5.5
June-1996	14.4	3.6	8.2	–2.6	6.2	6.2
June-1997	14.6	2.8	8.5	–3.3	6.1	6.1
June-1998	15.6	7.8	8.4	0.6	7.2	7.2
June-1999	14.8	8.9	8.0	2.3	6.6	6.6
June-2000	12.9	9.3	7.4	3.8	5.5	5.5
June-2001	14.2	9.3	6.4	1.5	7.8	7.8
June-2002	13.2	8.4	6.4	1.6	6.8	6.8

Source: Economic Survey (various issues).

Pakistan introduced prudential regulations in 1993 with a view to keeping the infected portfolio to a minimum. However, the non-performing loans (NPLs) amounted to PRs279 billion, (see Table 7) i.e., 8.2 percent of GDP, 18.6 percent of domestic assets, and 32.5 percent of total credit made available to private sector and public enterprises by June 30, 2001. Non-performing loans of the banking sector were PRs221 billion, i.e. 6.5 percent of GDP and 22.1 percent of total deposits. However, by June 2001, the magnitude of both non-performing and defaulted loans has fallen. Nevertheless, the infected portfolio is large and is one of the main factors for high spread between the lending and deposit rates.

Table 7

Non-performing and Defaulted Loans

(Rs Billion)

Year	Non-Performing Loans	Defaulted Loans
June-1998	207.9	146.1
June-1999	212.1	143.1
June-2000	239.5	148.1
June-2001	279.1	172.4
June-2002	259.3	166.1

Source: Unpublished data.

[11]By September 2002, the rate fell to 11.9 percent.

It is generally believed that defaulted loans are a result of loans advanced on political grounds. While this is true, the infected portfolios may have also arisen because of the four other factors. First, the producer is inefficient and makes losses and therefore, is unable to pay back the loan. That there are bankruptcies all over the world is testimony to that. Second, changes in the tariff rates and removal of export duties especially on raw cotton made the firms uncompetitive in Pakistan and even those units which earlier made profits, suffered losses. Third, smuggling also reduced profitability, forcing some of the firms to go out of business. Fourth, when prior approval of the government was essential before setting up of any industry the projects were appraised by Investment Promotion Bureau. Since the bank had little capacity to appraise projects properly, non-viable projects were also funded. The infected portfolio has also been inflated by the penal interest rates.

The defaulted loans can only be recovered to the extent of the present value of the firms, remaining balance has to be written off. However, it needs to be ensured that the write-off does not encourage further defaults. Government has taken a number of legal and administrative measures for recovery of these loans but has met with limited success. These include the Banking Council Bill of 1997 aimed at addressing the problem relating to foreclosure of property and the efforts to recover the loans through National Accountability Bureau that arrested a number of persons. However, both have not been successful. Nevertheless, CRIC is making significant efforts to convert sick units into operative ones. These efforts would hopefully clear the infected portfolio and pave the way for reduction in interest rates and higher investment levels.

(iii) Debt Overhang

Because of high fiscal deficits, public debt has accumulated to Rs 3060 billion (97.8 percent of GDP) by 1998-99. Since then the growth of debt has decelerated and by 2001-02, it increased to Rs. 3761 billion (98.4 percent of GDP). The internal debt has increased from Rs 1376 billion (45.1 percent of GDP) to Rs 1696 billion (45.1 percent of GDP), external debt from Rs 1614 billion (52.8 percent of GDP) to Rs 2006 billion (53.3 percent of GDP) over 1999-02 period. However, during 2001-02, the debt actually declined. (See Table 8.)

Pakistan has been suffering from debt overhang for over a decade and when the debt is high, it discourages investment. This is because the investors expect that the government for financing the debt servicing, may have to increase taxes resulting in lower investment levels. If the taxes are imposed on the goods consumed by the poor, it reduces the real income of the poor. On the other hand, if the public expenditures are reduced, especially the development and the social sector expenditure, the poor are impacted adversely. All the three ways imply an increase in poverty.

The $12.5 billion rescheduling of bilateral debt implies that the short run problem has been resolved. The surplus in current account balance of payments would help further in the resolution of external debt problems. One hopes that with the resolution of debt problems and strong financial indicators, investors' confidence shall be restored.

Table 8

Profile of Domestic and External Debt

(Rs Billion)

	1998-99	1999-2000	2000-01	2001-02
Total Debt	3060.4	3318.0	3866.0	3760.5
Domestic Debt	1375.9	1559.9	1712.5	1695.5
	(45.0)	(47.0)	(44.3)	(45.1)
External Debt	1614.4	1682.7	2059.5	2005.6
	(52.8)	(50.7)	(53.5)	(53.3)
Total Debt Servicing	343.1	353.9	340.3	412.5
Total Interest Payment	220.1	256.8	254.4	245.4
Domestic	178.9	206.3	195.4	179.1
Foreign	38.0	44.9	51.2	60.8
Explicit Liabilities	3.2	5.6	7.8	5.6
Repayment of Principal (including Repayment of Foreign Debt)	123.0	97.1	85.9	167.1
Ratio of External Debt Servicing to				
Export Earnings	35.3	36.5	37.3	44.1
Foreign Exchange Earnings	23.6	23.4	23.3	26.1
Ratio of Total Debt Servicing to				
Tax Revenue	87.8	87.2	76.5	86.5
Total Revenue	73.2	65.9	62.3	65.4
Total Expenditure	53.0	47.6	46.8	47.2
Current Expenditure	62.7	55.0	52.3	57.5

Source: Economic Survey (various issues) and *Annual Report* of the State Bank of Pakistan, 2001-02.

(iv) Trade Policy

When in 1983-84 Pakistan switched to negative list of imports there were 724 products on the list but the number fell to just 100 by the mid 90s and now there are only a handful of products placed on the list for security, health and religious reasons. With the abolition of bans and quotas, it is the tariff policy and not the trade policy that determines the level and structure of protection. Tariff structure has been rationalised: maximum tariff has been reduced to 25 percent, trade weighted average tariffs to only 11 percent and a number of SROs have been withdrawn. Similarly, all types of restrictions on exports except a few primary goods have been removed, export financing is provided to small, medium and large enterprises engaged in exports of manufacturing products and to the indirect exporters.[12] Despite duty drawbacks, export processing unit scheme, no-duty-no-draw-back scheme and bonded warehousing scheme, exporters still do not have duty free access to the imported inputs. Delays in the receipt of duty drawback, liquidity problems, and cumbersome procedures are stumbling blocs in accessing the duty free inputs. It needs to be underscored that with the globalisation challenge, the provision of inputs at competitive prices, especially the duty free imports, has assumed great significance. Though Pakistan's trade policy still has a distinct anti-export bias, the bias

[12]Small and medium enterprises and indirect exporters point out various difficulties in accessing credit for exports.

has declined over time. Export duties and other restrictions on exports have been withdrawn and exporters are also provided concessional credit and income tax rebates.

Globalisation provides both challenges and opportunities. The removal of quota provides an opportunity to raise the export of textile products on textiles by the developed world by 2004. However, the benefits would accrue only if Pakistan is able to improve production efficiency, improvement in quality and standardised goods in accordance with demand and moving towards high value added goods. This may result in an increase in exports of Textiles and clothing at a rate of 13.2 percent [see Kemal and Haider (1997)]. Pakistan is also committed to reduce the import duties further so that the domestic producers are exposed to competition and become efficient. Nevertheless the producers must be given sufficient time to adjust otherwise there will be closure of industries at a massive scale. Since protection results in lower demand for the factor in which the country is abundant, reduction of anti-export bias will result in higher level of employment. However, aggressive marketing would be essential.

Because of liberalisation policies, degree of openness increased in 1988–93 period, contributed by the rising share of both the exports as well as imports, but since then openness has declined. (See Table 9.) The exports ratio to GDP has increased in the pre-sanctions period but stagnated in the post-sanction period, while the import-GDP ratio has declined over 1992-93 period. It declined subsequently as the imports fell rather sharply because of various factors including sluggish demand in the economy as well as declining commodity prices in the world market.

Table 9

Degree of Openness in Pakistan's Economy

(% of GDP)

	1987-88	1992-93	1997-98	1999-2001
Exports	11.6	13.2	14.1	15.5
Imports	16.7	19.3	16.3	18.4
Degree of Openness	28.3	32.5	31.4	34.9

(v) Exchange Rate Policy

Because of the increase in the balance of payments deficit as well as increase in the rate of inflation, which remained double digit in most of the years, rupee depreciated. Whereas until 1998 Pakistan had frequently devalued its currency, it hardly compensated the increase in inflationary tendencies. The real exchange rate by 1997-98 had in fact appreciated by 5.5 percent. Over the 1999-01 period, there has been real devaluation of around 12.1 percent and exports have increased by 25 percent. Because of sharp increase in remittances and capital inflows in the recent months, however, rupee has appreciated. At present Pakistani rupee is floating and the State Bank of Pakistan intervenes in the market for stabilising the exchange rate.

(vi) Investment Policies

The investment policies of Pakistan have not been all that consistent. Over the 1988-97 period various schemes including special industrial zones, the industrial estates, rural industrialisation etc. provided incentives which were later withdrawn. A comprehensive investment policy was announced in 1997, which with certain modifications continues to be the policy. While the hi-tech and export oriented industries and those having 40 percent value addition are provided maximum incentives, the incentives for other industries have also been clearly specified. These incentives are in the form of initial depreciation allowances and concessions in the import duties on machinery and equipment.

Whereas until the late 1980s Pakistan had an ambivalent attitude towards foreign private investment government took a number of important initiatives to attract private investment. First, a Negative List of industrial activities for private investment was issued.[13] Second, restriction on maximum holding of equity by foreigners has been removed. Third, remittances of dividends and disinvestment proceeds no longer require the State Bank's permission. Fourth, restriction on raising of loans from domestic market have been removed. Fifth, foreign firms are allowed to raise equity capital from the domestic market. Sixth, on repatriable basis, investment in stock exchange has been allowed. Seventh, restrictions on royalties and technical fees have been removed. Eighth, the foreign investors have been provided guarantees relating to remittances of profit, capital, and appreciation of capital investment. And, ninth, the foreign private investment shall not be subject to more burden of taxes on income than those applicable to investment made in similar circumstances by citizens of Pakistan. Foreign investors have also been provided relief from double taxation in cases of those countries with which Pakistan has agreement for avoidance of Double Taxation. In order to encourage assembly-cum-manufacturing, government provides incentives to assembly through lower import duties on components if the producers agree to a programme of indigenisation.

(vii) Privatisation Policy

So far, 104 units, five financial institutions, three energy sector enterprises, one telecommunication, three tourism enterprises and 92 manufacturing units have been partially or completely divested. Government intends to privatise 10 financial institutions including Habib Bank Ltd., 9 oil and gas units, 2 power and electricity units, 23 manufacturing enterprises, telecommunication corporation and three other units. The experience with privatisation, however, has been mixed. While in the banking sector the efficiency has improved, in the manufacturing sector efficiency has improved only where there was competitive market structure.

Privatisation has significant implications for employment. Besides low level of employment due to capital-intensive techniques, there are three main issues relating to

[13]Industries on the negative list are the ones set up for security and social reasons, such as arms and ammunition, security printing, currency and mint, high explosives, and radioactive substances.

employment in the divested units. First, private sector generally does not hire professional workers and as such the problem of unemployment amongst educated and trained labour force may become even more severe. Second, even when more workers are required in the private sector, they shall be hired on contract with a view to avoiding labour legislation. For example, employers of the privatised units in Pakistan are encouraging workers to opt for golden hand-shake and get rehired on contract. Third, if the producer is a monopolist, he/she would restrict output and as such employment shall be curtailed.

Because of inefficiencies in public enterprises, privatisation may be imminent. Yet it needs to be ensured that the competitive market structure accompanies the divestiture. For the traded goods, the import policy and tariff policy need to be judiciously employed, and for the utilities an effective regulatory framework must be established.

III. THE IMPACT OF STRUCTURAL ADJUSTMENT PROGRAMMES ON STRATEGIC ECONOMIC VARIABLES

(a) Savings and Investments

Investment in Pakistan has been constrained by investible resources though in recent years demand factors have also impacted adversely the investment. The investible resources comprise national savings, as well as foreign capital inflows. Despite an increase in per capita incomes, savings rates continue to be low; domestic and national savings are around 13–15 percent of GDP and GNP respectively. Even though dissaving of government sector has declined, the household and corporate savings rates have fallen in recent years and, resultantly, aggregate savings rate has failed to increase. Nevertheless a reduction in the wasteful public expenditure, privatisation of loss making public enterprises and taxing the conspicuous consumption may result in higher level of aggregate savings.

Reduction in private consumption is essentially a decision of the household. It depends on a number of things including sustained levels of higher growth of GDP, high interest rates, inflation rates, profitable investment opportunities, dependency ratios, and the good banking practices. No doubt, household savings are affected by the behaviour of the households, by taxing the conspicuous consumption the government can create a conducive atmosphere for savings.[14]

Savings in Pakistan are not only low they also depict wide fluctuation. The national savings show rising trend in the 1988–92 period when they increased to 17.1 percent of GDP. However, in 1992-93, it declined to 13.6 percent both because government savings turned negative due to large fiscal deficit and the household savings declined because of fall in the growth rate. Savings did increase in the next year but since then have fallen

[14]It is important to note that high import duties and countervailing duties on domestic outputs will be futile if government's resolve to control smuggling is not that strong.

once again. From 1995-96 onwards, because of negative net factor income from abroad, national savings have fallen short of the domestic savings. Whereas by 1997-98, domestic savings had increased to 15.7 percent from 12.8 percent in 1992-93, the national savings increased from 13.6 to only 14.3 percent over the same period. By 2000-01, national and domestic savings were 15.0 and 16.6 percent, respectively. However, in 2001-02, because of sharp increase in the remittances, national savings increased to 15.4 percent though domestic savings were constrained to 14.7 percent. (See Table 10.)

The fluctuations in savings rate are mainly a result of changes in terms of trade. For example, terms of trade improved from 101.6 in 1996-97 to 123.5 in 1997-98 and since then have deteriorated to 94.3 by 2000-01. The computed savings rates may also reflect the massive capital flight after the nuclear blast.[15]

Table 10

Trends in Savings

(as Percentage of GDP)

Year	National Savings	Domestic Savings
1987-88	13.6	10.6
1988-89	14.1	11.8
1989-90	14.2	11.7
1990-91	14.1	11.8
1991-92	17.1	16.0
1992-93	13.6	12.8
1993-94	15.6	15.4
1994-95	14.3	13.6
1995-96	11.6	12.0
1996-97	11.6	12.8
1997-98	14.3	15.7
1998-99	11.7	12.9
1999-00	14.1	15.6
2000-01	15.0	16.6
2001-02	15.4	14.7

Source: Economic Survey, 2001-02.

(b) Investment Trends

Because of divergent trends, the investment since 1987-88 has been divided into four sub-periods. Firstly, 1988–93 period, when the country pursued consistent policies and the programmes were implemented with reasonable degree of conviction, the country experienced increase in investment. Second, 1993–98 period, when neither the programmes were seriously implemented, nor there was any continuity of policies. The private sector investment fell because of political uncertainty, lack of continuity in economic policies, and the ongoing process of structural adjustment. Third, the post-sanction period, when the

[15]The savings in Pakistan are estimated as residual; because such foreign investments are not recorded in the total investment, saving as a residual falls.

country faced major problems relating to servicing of debt and there was a further decline in foreign and domestic investment. Fourth, period subsequent to 9/11 events the prospects of foreign private investment have brightened because of strong economic fundamentals.

During the 1988-93 period, public investment slightly increased from 8.5 to 9.0 percent of GDP but private investment rose sharply from 7.4 percent to 10.0 percent of GDP. The private investment increased because the government pursued market friendly and privatisation policies. Despite changes in the governments, the policy continuity was ensured. Total investment consequently increased from 17.3 to 20.6 percent of GDP. Over the 1993-98 period political uncertainty, lack of continuity in economic policies, and the stop go policies relating to SAP led to a fall in private investment from 10.0 to 9.6 percent of GDP. Public investment fell drastically from 9.0 to just 4.9 percent of GDP because of inadequate resource mobilisation efforts. Total and fixed investment declined from 20.6 to 17.1 percent of GDP and from 19.0 to 14.5 percent of GDP.

The problems compounded further by the sanctions imposed following the nuclear blasts in 1998. Consequently total investment during the 1998–01 period declined from 17.3 to just 15.9 percent of GDP in 2000-01. (See Table 11.) The decline has been entirely due to fall in the private investment, which declined from 9.6 to 8.0 percent and public investment increased from 5.2 to 4.7 percent. However, because of strong (financial) macroeconomic fundamentals the prospects of indigenous and foreign private investment have brightened. However, in 2001-02, total investment has declined to just 13.9 percent of GDP and fixed private investment to 12.3 percent of GDP. The decline has been due to fall in both the private and public investment, private investment declined from 8.0 to 7.4 percent and public investment from 6.3 to 4.7 percent.

Table 11

Trends in Investment

(Percentage of GDP)

Year	Total Investment	Fixed Investment	Public Investment	Private Investment	Share of Private Sector in Fixed Factor
1987-88	17.3	15.8	8.5	7.4	46.5
1988-89	18.3	16.7	8.7	8.0	48.2
1989-90	18.2	16.6	8.0	8.6	51.7
1990-91	18.5	17.0	8.3	8.7	51.3
1991-92	19.9	18.4	8.7	9.7	52.7
1992-93	20.6	19.0	9.0	10.0	52.5
1993-94	19.4	17.8	8.3	9.5	53.6
1994-95	18.3	16.8	8.2	8.6	51.3
1995-96	18.7	17.1	8.1	9.0	52.5
1996-97	17.7	16.2	6.8	9.4	58.0
1997-98	17.3	14.7	5.2	9.6	65.3
1998-99	15.6	13.9	6.1	7.9	56.8
1999-00	16.0	14.4	6.0	8.4	58.3
2000-01	15.9	14.2	6.3	8.0	55.9
2001-02	13.9	12.3	4.7	7.6	61.8

Source: Based on *Economic Survey* (various issues).

Preceding discussion brings out quite clearly that decline in private investment has nothing to do with structural adjustment. It is either due to the inconsistency of the government policies or due to external factor.[16] However, it is the public investment which has been constrained by the SAP.

Until the early 1990s, Pakistan had an ambivalent attitude towards foreign private investment. All foreign investment had to go through an approval process and investment decisions were delayed sometimes for years. But as pointed out in Section II, Pakistan has actively pursued foreign investment during the 1990s. Foreign private investment increased from $177 million in the 1987-88 to $443 million in 1992-93 and further to $1532 million in 1994-95 out of which $1090 million was portfolio investment that mainly flowed as a result of the divestiture of 12 percent shares of Telecommunication Corporation. The direct investment was the maximum in 1995-96 when it was $1102 million, but financed mainly the power units. Since then, however, due to sanctions and inconsistent policies, foreign investment has declined to $182 million by 2000-01, though in 2001-02, FDI has increased to $485 million. (See Table 12.)

Table 12

Foreign Investment

Year	Direct	Portfolio	Total
1987-88	–	–	177.0
1988-89	–	–	200.0
1989-90	216.2	–4.7	211.5
1990-91	246.0	–9.0	237.0
1991-92	335.1	218.5	553.6
1992-93	306.4	1368	443.2
1993-94	354.1	288.8	642.7
1994-95	442.4	1089.9	1532.3
1995-96	1101.7	205.0	1306.7
1996-97	682.1	267.7	949.8
1997-98	601.3	221.3	822.6
1998-99	376.0	27.3	403.3
1999-00	469.9	73.5	543.4
2000-01	322.4	–140.4	182.0
2001-02	484.7	–10.1	474.6

Source: Economic Survey, Statistical Supplement, 2000-01 and previous issues.

(c) Growth of GDP

Investments plays a crucial role for sustained economic growth. Obviously with declining investment levels, GDP is bound to slow down. At the same time, inadequate infrastructure, load shedding of power on the one hand, and a reduction in demand due to deflationary policies on the other adversely affect the growth process.

The GDP grew by 5 percent over the 1988-93 period. The manufacturing sector grew at a rate of 5 percent and agriculture at a rate of 3.7 percent. Growth rate of GDP

[16]To the extent that the private sector investment has a positive association with public investment, the decline in public investment may have also been responsible for the declining level of private investment.

declined further in the 1993-98 period to 4.1 percent; growth rate of manufacturing sector fell to just 3.5 percent but growth of agriculture increased to 5.6 percent. The measures taken by the government installed in the early 1997 relating to reduction in the rates of income, corporate and sales taxes and import duties, investment policy that clearly spelt out incentives to various economic activities, and agreement with IMF on Structural Adjustment and Stabilisation Programme created euphoria of rapid economic growth and stabilisation in the economy. The growth rate in 1997-98 increased to 4.3 percent compared to 1.9 percent in the previous year. The growth rates of agriculture and large scale manufacturing surged from 0.1 and –2.14 percent to 3.8 and 7.6 percent respectively, and the inflation rate declined from 11.8 to 7.8 percent in 1997-98. However, the nuclear blasts in May 1998 changed the scenario completely. The freezing of foreign currency accounts, declining remittances, and imposition of sanctions with meagre foreign exchange reserves of $1.6 billion necessitated major reversals in the liberalisation process. The dual system of foreign exchange was introduced, cash margin requirements on imports were imposed, repatriation of profits was suspended, further reduction in tariff rates was postponed, and the IMF programme was held in abeyance. The country started accumulating arrears on the repayment of debt and by the end of 1998 it was quite clear that Pakistan would default on the debt repayments unless its debt was rescheduled. The debt rescheduling for three years did take place with a strong IMF programme in the late 1998. While the new IMF programme was still under implementation, the government was dismissed, adding to the uncertainty. These developments together with ineffective governance, weak implementation of the policies, law and order situation, and poor physical infrastructure and human resource development led to further erosion of investors' confidence, and the investment rate plummeted to the lowest level since the 1950s. The falling levels of investment took a heavy toll of the growth rate of output which has averaged to 3.3 percent over the last three years. However, the real per capita income has increased at a rate of 2.0 percent mainly because of a sharp increase in net factor income from abroad. (See Table 13.)

Table 13

Compound Growth Rates at Constant Factor Cost of 1980-81

	1987-88 to 1992-93	1992-93 to 1997-98	1998-99 to 2000-02
GDP	5.0	4.1	3.3
Manufacturing	5.0	3.5	4.5
Agriculture	3.7	5.6	1.6
Investment	5.7	1.6	1.1
Per Capita Income	1.5	0.6	2.0

Source: Economic Survey, 2001-02.

Agriculture

The agriculture sector is beset with many problems including water availability, seeds, fertiliser and pesticides, credit facilities and R&D. The extreme drought over the last three years has brought home the point that the agricultural production would be

badly affected unless more water reservoirs were created. Accordingly, in 2002-03 budget allocation to water sector has been enhanced to Rs 16.2 billion. These may not be enough and allocation to water sector will have to be enhanced considerably after the feasibility reports are completed. Since agriculture is labour-intensive and water is a crucial variable, it has to be accorded top priority.

Agriculture has grown the fastest when there has been technological improvement. For sustaining the high growth rate through productivity research development and extension will play a dominant role. It needs to be underscored that growth has been higher during the periods when there were technological improvements. While more priority should be accorded to research and development, extension services need to be improved to ensure that most of the farmers are on frontiers of technology. While more resources to R&D will help in discovering new high yield varieties, Pakistan has suffered from the problems in breeding, multiplication and distribution of improved certified seed to the end users. The private sector has been inducted in development, multiplication and sale of seeds but because they are expensive, majority of farmers are left out. Probably, if the seed developed by public sector are multiplied and sold by private sector as well, the problem would be easily resolved. It would not only promote growth but would also generate more employment.

Poor marketing facilities, inadequate farm to market roads, warehouses, cold storage, grading and processing facilities have been responsible for low income levels. No doubt the government has been fixing the prices of various agricultural commodities, lack of effective intervention in the market when the crops was surplus have not helped the farmers especially the poor. Moreover, the government has not been very consistent in announcing the support prices. Frequent and haphazard changes in the support prices have resulted in wild swings in the output levels of various crops, while output of others suffered. While the price support mechanism should continue, it must also be strictly enforced.

Manufacturing

The liberal industrial and trade policies have been the major factor in high growth rate and improvement in the industrial efficiency during the 80s. Even though there was an increase in investment in the manufacturing sector in 1988-93 period the growth momentum could not be sustained, and the growth rate fell from around 10 percent in the 1980s to 5.8 percent in 1988–93 period. Severe law and order problem especially in Karachi where almost one-half of the industry is located, inadequate infrastructure, load shedding and low demand have been the major problems affecting the manufacturing sector during this period.

The growth rate fell sharply in the 1993-98 period and in fact it turned negative in 1996-97. Both because of the fall in domestic and foreign demand, load shedding, continued smuggling, and the low levels of investment have been responsible for the decline in the manufacturing output during this period. In the post-sanctions period the performance has been mixed. While in 2000-01 the large scale production increased by 8.6 percent, in 2001-02 the growth rate slipped to 4.0 percent.

Reduction in the growth rate is the result of a number of factors including slackness of demand, low level of investment in the manufacturing sector, lack of diversification, tariff rationalisation culminating into lower levels of protection, smuggling, and deflationary policies. Another significant element in the slow growth rate of manufacturing has been closure of a large number of industrial units. These units have become sick because of various reasons including over-capacity in the industry, over capitalisation of different industrial units, inappropriate site selection, poor technology, poor management and lack of working capital. Government has appointed various committees but so far only a few units have been revived. In any case, the firms with poor technology and/or improper sites have to be liquidated, while those suffering from poor management need to be declared bankrupt so that new management can run it efficiently. It needs to be underscored that in 1980s, high growth has essentially been due to improvement in technology.

Because of the stabilisation programme, domestic demand for a number of industries slackened. Since the productive capacity released by a decline in demand was not compensated by increase in exports, the deflationary policies have resulted in under-utilisation of capacity in various sectors especially in cement and other construction related activities. Accordingly a public sector programme with maximum stimulant for domestic output would go a long way in generating high growth rate of the manufacturing sector. Similarly reduction in import duties on inputs for smuggling prone industries would also help in raising the manufacturing output.

The low level of investment implies very little growth in productive capacity. The low levels of investments also result in obsolescence. While investments under balancing, modernisation, and replacement (BMR), and upgradation of technology in the textiles sector would make it competitive in the world market, in the other sectors there has been little investment.

The manufacturing industries continue to face the major structural problems. The foremost challenge faced by the sector is restructuring towards those industries in which the country has dynamic comparative advantage. Diversification of output is necessary for long run sustainable growth but there has been very little diversification and new investments continue to flow to traditional industries. Availability of imported raw materials at low rates of import duties is essential for industrial diversification. Industries such as engineering, electronics and chemicals essentially depend on imported raw materials and intermediate inputs. The reduction in import duties on inputs would go a long way in promotion of these activities. Moreover, they require skilled workers and at present skill acquisition is limited and not in accordance with the markets needs. In the absence of skilled workers, producers make stopgap arrangements leading to sub-optimal decisions, low levels of productivity and the loss of output.

Augmenting science and technology apparatus of private sector, bringing research institutions upto international standards, streamlining of technology creation, and absorption and diffusion systems are essential for diversification of the industrial base. With a view to improving the standardisation and quality of products and to transferring technology, Pakistan has been encouraging foreign private investment. Technology transfer is

effected through indigenisation programmes that create incentives for the firms to develop vendors but under Trade Related Investment Measures (TRIM), the indigenisation programmes may have to be abandoned. This will have serious implications for vendors and a strategy needs to be devised for promotion of vendors through tariff measures.

Small-scale enterprises are labour intensive and through sub-contracting with the large enterprises can help in improvements in the competitiveness of the manufacturing sector as a whole. However, they suffer from poor quality, and lack of standardisation and this problem can be over come through their linkages with large scale firms, improvements in skills and the sharing of common facilities. Already there has been development of the vendors and they are being considered indirect exporters and are being provided the necessary facilities.

The growth of small scale industries has been below their potential because of a number of factors including relatively higher import duties on input compared to the concessional import duties levied on large producers, limited availability of credit, unavailability of the common services, poor quality lack of demand, and lack of grading, and inadequate training. While as a part of tariff rationalisation and withdrawal of SROs, the difference between commercial and industrial importers has disappeared or narrowed for a large number of industries, the differential does exist in some of the industries. The sooner the differential is removed, better for growth and employment.

Cluster approach, i.e., an agglomeration of key industries, supporting sectors, infrastructures, and institutions that are inter-linked and inter-dependent because of some shared technological or skill base would be quite helpful in the development of vendors. The cluster funds provided by government can be used to carry contract research which would enhance the technological landscape. As a result, entrepreneurs would use the imported technology in a better way. They would also be able to implement ancillary system such as quality control, material handling and distribution system. The industries such as electronic or auto parts would benefit from these clusters in product design, automation and inventory control.

(d) Inflation Rates

Since wages fail to rise instantaneously, the inflation rates are the major factor in declining real wages and an increase in poverty. The inflation rate has declined essentially due to the prudent monetary policy shows the success of stabilisation policies. The inflation rate has fallen from double digit up to 1996-97 to less than 5 percent over the last three years. (See Table 14.)

Poverty may have also have increased because the poor has to spend more on fuel and lighting, especially the electricity, which leave little amount for purchasing the necessary food. While fuel and gas prices in the first half of 1990s moved slowly compared to the general inflation rate, in the second half CPI for fuel and lighting has increased rather sharply; the index increased by 79.6 percent and relative to CPI by 17.7 percent. Over the 1990s, fuel and electricity prices have increased by 255.6 percent and 9.6 percent relative to general CPI.

Table 14

Inflation Rate (FY 1996-97 to 2000-01)

Period	Consumer Price Index	Wholesale Price Index	GDP Deflator
1987-88	6.3	10.0	9.61
1988-89	10.4	9.7	8.59
1989-90	6.0	7.3	6.45
1990-91	12.7	11.7	13.07
1991-92	10.6	9.8	10.07
1992-93	9.8	7.4	8.67
1993-94	11.3	16.4	13.08
1994-95	13.0	16.0	14.8
1995-96	10.8	11.1	8.0
1996-97	11.8	13.0	13.3
1997-98	7.8	6.6	7.7
1998-99	5.7	6.3	5.5
1999-00	3.6	1.8	3.9
2000-01	4.4	6.2	5.6
2001-02	3.5	2.1	4.6

Source: Economic Survey *(various issues).*

(e) Balance of Payments

Removal of non-tariff barriers, tariff rationalisation, and the exchange rates have implications for exports and imports. During the 1988–93 period (except for the 1992-93), the trade balance has been around $2.5 billion and the balance of payments deficit around $2 billion. However, because of massive increase in the imports of transport equipment, trade deficit rose sharply to $3.3 billion and the balance of payments deficit to $3.7 billion in 1992-93. Whereas in 1993-94 both the trade balance and balance of payments deficit fell to around $2 billion it increased in the next three years and in 1995-96 trade deficit had risen to $3.7 billion and the balance of payments deficit to a record high of $4.6 billion. During these years, there were heavy imports of power machinery. Through demand management and devaluation of the currency trade balance was reduced to $1.87 billion and balance of payments deficit to $1.92 billion in 1997-98. During 1998-99 exports slumped from $8.4 billion to just $7.5 billion and though imports also fell from $10.3 billion to $9.6 billion both the trade deficit and balance of payments deficit increased. However in the next two years there has been an increase in exports and the unrequited transfers and resultantly by the year 2000-01, trade deficit declined to $1.3 billion and the balance of payments deficit to just $508 million. As a matter of fact if the official transfers are also included then it turns into a surplus of $331 million. (See Table 15.)

Because of the 9/11 event, Pakistan's exports suffered badly as the confirmed orders were cancelled. However, because of the access to European markets in the second half of the fiscal year, exports picked up and the year ended with a modest export growth of 2.2 percent. Due to a further decline in the investment levels and low levels of manufacturing activity, imports fell by 9.9 percent resulting in a sharp reduction in trade deficit to $360 million. However, because of a sharp increase in remittances, increase in the FE-25 accounts and the government's purchases from the open market the balance of payments deficit has turned surplus of about $1428 million.

Table 15

Trends in Balance of Payments

(Million $)

Year	Exports	Imports	Trade Balance	Remittances	Current Account Deficit
1987-88	4362	6919	2557	2013	1682
1988-89	4634	7207	2573	1897	1934
1989-90	4926	7411	2485	1942	1891
1990-91	5902	8385	2483	1848	2171
1991-92	6762	8998	2236	1468	1346
1992-93	6782	10049	3267	1562	3688
1993-94	6685	8685	2000	1446	1965
1994-95	7759	10296	2537	1866	2484
1995-96	8311	12015	3704	1461	4575
1996-97	8096	11241	3145	1409	3846
1997-98	8434	10301	1867	1490	1921
1998-99	7528	9613	2085	1060	2429
1999-00	8190	9602	1412	983	1143
2000-01	8933	10202	1269	1087	–513
2001-02	9133	9493	–360	2389	–1428

Source: State Bank of Pakistan, *Annual Report 2001-02,* Karachi.

(f) Employment

Growth of employment is a function of the growth rate of output, composition of output and employment elasticity. The growth rate of GDP fell; the major decline has been in the manufacturing sector, which has both significant backward and forward linkages. Therefore, employment generation in other activities have also gone down. Because of the low growth rate, the open unemployment rate has increased from 5.9 percent in 1997-98 to 7.8 percent[17] in 2001-02. The unemployment rises to 13 percent if under-employment is also included. (See Table 16.)

Table 16

Labour Force and Employment in Pakistan

(in Millions)

	1987088	1992-93	1997-98	1999-00
Labour Force	29.9	32.4	38.2	41.0
Employment	28.9	30.9	35.9	37.5
Unemployment Rate (%)	3.3	4.7	5.9	7.8
Under-employment Rate (%)	10.6	12.8	12.0	13.1

Source: Labour Force Survey (various issues).

[17]There is no Labour Force Survey for 1998-99, nor any after 1999-00.

Employment generation in the 1990s has been inadequate to provide jobs for the growing work force, resulting in an increase in unemployment and under-employment rates over time. About 10 percent of the employed had insufficient work, i.e., fewer than 35 hours per week. Unemployment rates are highest among youth and women. Moreover, a quarter of employed persons earn incomes that fall short of the subsistence level, while another quarter is on the borderline of the subsistence level.

As investigation of poverty and labour market interlinkage through disaggregation of household population and workers by poverty status show an association between inactivity and poverty, particularly in rural areas (see Table 17). The labour force that belongs to poor households exhibits a higher level of unemployment and under-employment than its counterparts in the nonpoor households. Controlling for the poverty status of the households, the association between employment structure and poverty suggests that workers from poor households are disproportionately absorbed into the informal and farm sectors, whereas the reverse holds for relatively rich households, which are employed in the formal sector.

Table 17

Percentage Distribution of Workers by Establishment

Establishment	Poor			Non-poor		
	Pakistan	Urban	Rural	Pakistan	Urban	Rural
Farm	43.62	4.45	50.26	37.69	5.09	60.75
NFE <10	37.96	68.42	34.38	25.11	43.37	24.58
NFE ≥ 10	5.78	7.69	4.93	17.44	24.88	3.56
Govt.	4.30	6.75	3.14	12.10	16.14	5.47
Other	8.34	12.69	7.30	7.66	10.52	5.64

Source: Nasir (2001).

NFE < 10 = nonfarm enterprises with less than 10 employees.

NFE ≥ 10 = nonfarm enterprises with more than or equal to 10 employees.

Wages reported by Federal Bureau of Statistics for certain categories of workers such as construction workers or agricultural labour is the only information that is available. The limited evidence suggest that there has been only 8.4 percent increase in nominal wages whereas prices increased by 13.5 percent, indicating a decline in real wages. The declining and stagnant wage rates of unskilled and skilled blue-collar workers led these workers to transact in the informal markets where wages are rather low.

Since 1989-90 public enterprises have been divested, compounding the problem even further. With a view to protecting the workers against job loss, the government and the representatives of the workers have reached an agreement whereby the new owners will keep them at least for one year. Nevertheless, the new owners are getting rid of the workers by encouraging/forcing them to opt for the golden hand-shake. Since the job becomes insecure after one year, many workers prefer the golden hand-shake option. Almost one-half of the workers have opted for golden hand shake [see Naqvi and Kemal (1994)]. It is quite well known that the monopolist tries to maximise profits by restricting the output and increasing the prices and as such privatisation can even lead to lower levels of efficiency.

(g) Trends in Poverty Levels

Pakistan does not have an official poverty line though recently Planning Commission has announced that it shall be based on calorific requirements of 2350 per adult equivalent. Every researcher in Pakistan has adopted its own poverty line and used various methods to estimate poverty levels which make inter-temporal comparison rather difficult. The three most common measures of poverty suggested by Foster, Greger and Thorbeck (FGT) indices are:

- The proportion of the population whose incomes fall below a specified poverty line, generally known as head count;
- The income gap, i.e., the income required to bring all the poor above the poverty line; and
- Income inequality among the poor, the severity index.

The consumption levels that are essential for meeting the basic needs of common people are basic to the assessment of basic needs of the poor. Ahmad (1993) estimates the basic needs on the basis of educated guesses by knowledgeable persons. The linear expenditure systems approach may be used to determine the basic needs of the poor and to reflect the norm of society as it relates to the basic needs of people in a particular year [Ali (1995)]. Malik (1988) defined a poverty line with reference to a calorie requirement of 2,550 for an adult,[18] and the revealed expenditure pattern of the poor between food and nonfood expenditures. The poverty line for different years is adjusted by changes in the Consumer Price Index to ensure that the same poverty line in terms of real incomes is used to estimate the poor in each year. Similar methodology is used by the FBS (1995), which defines basic needs as 2,550 calories for adults, and the average coefficient of nonfood expenditures of the poor is regressed against the food goods. The poverty estimates presented in Qureshi and Arif (2001) are based on food energy intake and the cost of basic needs.[19] The requisite food expenditure corresponding to the required calorie intake has been obtained by regressing an equivalent of the daily calorie-intake per adult against an equivalent of the monthly food expenditure per adult for both rural and urban areas. The cost of nonfood elements of the basket was determined by assuming that those households whose food expenditures were equal to the food poverty line would also satisfy their other basic needs. They also examine the sensitivity of poverty to increases in nonfood expenditure.

It may be argued that poverty is not just income (consumption) deprivation but is a multidimensional concept. The "poverty of opportunity" index, a composite of deprivation in three vital dimensions (health, education, and income) captures more appropriately the real causes of human suffering [MHDC (1999)]. Almost one half of the population of

[18] Malik (1988) used adult equivalence scales to adjust for gender and age considerations.

[19] Poverty lines have been determined on the basis of estimated cost of food, consistent with a calorie intake of 2,550 per adult equivalent per day in rural areas. A daily intake of 2,295 calories per adult equivalent is considered adequate for urban areas of the country.

Pakistan suffers from serious deprivation of the most basic opportunities of life, compared to the proportion of the population below the poverty line per the head-count definition [Syed (1999)].

(h) Incidence of Poverty

Even though poverty estimates vary depending on the choice of poverty line, all the studies show an increase in poverty in the 1987-88 to 1998-99 period except the World Bank study which shows a decline in the consumption poverty up to 1996-97 but an increase in poverty in 1998-99. (See Table 18.) The preliminary estimates for later years suggest a further increase in poverty. Even though the poverty has increased in both the rural and urban areas the poverty in urban areas is higher.[20]

Table 18

Trends in the Incidence of Poverty (Head-count Ratios, % Poor Population)

Year	Total	Rural	Urban
1963-64	40.24	38.94	44.53
1966-67	44.50	45.62	40.96
1969-70	46.53	49.11	38.76
1979	30.68	32.51	25.94
1984-85	24.47	25.87	21.17
1987-88	17.32	18.32	14.99
1990-91	22.10	23.59	18.64
1992-93	22.40	23.35	15.50
1996-97	31.00	32.00	27.00
1998-99	32.60	34.80	25.90

Source: Amjad and Kemal (1997); Jamal and Ghaus-Pasha (2000) and Qureshi and Arif (2001).

Arif, Nazli, and Haq (2000) provide estimates of P_0, P_1, and P_2 using the same poverty line in real terms for three different years. Their estimates show a much sharper increase in the poverty gap (P_1) than do the World Bank estimates: from 5.3 percent in 1993-94 to 7.6 percent in 1998-99. (See Tables 19 and 20.) Their estimates indicate that the severity of poverty has also increased, while estimates by the World Bank show a decline.

[20]Because of differences in the methodologies that estimate poverty lines, it is difficult to ascertain the trends in poverty. Even so, studies that are based on different methodologies (or poverty lines) are commonly used to investigate changes in the incidence of poverty. In an effort to mitigate the effects of these different "yardsticks" of poverty, Amjad and Kemal (1997); Jafri and Younis (1999) and the World Bank (2000) have developed a consistent time series on rural, urban, and total poverty.

Table 19

Poverty Trends in the 1990s by Rural and Urban Areas

Year	Rural-Urban Areas	Poverty Incidence (P_0)	Poverty Gap (P_1)	Poverty Severity (P_2)
1993-94	Total	27.4	5.31	1.6
	Urban	29.9	6.67	1.8
	Rural	23.1	4.82	1.4
1996-97	Total	29.6	5.80	1.7
	Urban	31.6	6.00	2.1
	Rural	27.4	5.90	1.1
1998-99	Total	35.2	7.58	2.5
	Urban	39.8	8.39	2.6
	Rural	31.7	9.67	3.5

Source: Arif, Nazli and Haq (2000).

Table 20

World Bank: Poverty Indicator 1984-85 to 1996-97

Year	P_0	P_1	P_2
1984-85	46	11.1	3.8
1987-88	37	7.7	2.3
1990-91	34	7.1	2.2
1992-93	25	5.1	1.4
1993–94	28	5.4	1.6
1996–97	24	4.2	1.4
1998-99	32.6	7.0	2.2

Source: World Bank (1995) and (2002).

(i) Income Distribution

Income distribution, measured in terms of Gini coefficient and household income share of the lowest and highest 20 percent for rural and urban areas, is presented in Table 8. Since the 1960s, the level of inequality in Pakistan has tended to be moderate, with the Gini coefficient of household income around 0.35 or below. The Gini coefficient reached 0.407 in 1990-91 and declined slightly to 0.400 in 1996-97.

In 1990-91, the income share of the bottom 20 percent of households fell to just 5.7 percent, after being in the range of 7.5 to 8.0 percent during the 1970s and 1980s. With the share of the upper quintile rising, the ratio of the share of the top quintile to that of the bottom quintile rose to an unprecedented 8.6 percent in 1990-91. The increase in income share of the bottom 20 percent of households increased from 5.7 percent in 1990-91 to 7.0 percent in 1996-97 and consequently the ratio declined to 7.1 in 1996-97. (See Table 21.) Separate data for rural and urban areas, presented in Table 22, indicates that the increase in inequality around 1990 occurred in both rural and urban areas. In the former, however, the jump from 1987-88 was dramatic, while in the latter it was more the continuation of a trend that began in the mid-1980s.

Table 21

Household Income Distribution in Pakistan

Year	Household Gini Co-efficient	Household Lowest 20%	Income Middle 60%	Share Highest 20%	Ratio of Highest 20% to Lowest 20%	GDP Growth Rates
1979	0.369	7.4	47.6	45.0	6.1	5.5
1984-85	0.335	7.3	47.7	45.0	6.2	8.7
1985-86	0.346	7.6	48.4	44.0	5.8	6.4
1986-87	0.348	7.9	48.5	43.6	5.5	5.8
1987-88	0.407	8.0	45.3	43.7	5.5	6.4
1990-91	0.410	5.7	45.0	49.3	8.6	5.6
1992-93	0.400	6.2	45.6	48.2	7.8	2.3
1993-94	0.400	6.5	46.3	47.2	7.3	4.5
1996-97	0.373	7.0	43.6	49.4	7.1	1.9
1998-99	0.410	6.2	44.1	49.7	8.0	4.2

Source: Economic Survey (various issues).

Table 22

Household Income Distribution by Rural-Urban Areas

Year	Rural Share		Gini Coefficient	Urban Share		Gini Coefficient
	Lowest 20%	Highest 20%		Lowest 20%	Highest 20%	
1979	8.3	41.3	0.32	6.9	48.0	0.40
1984-85	7.9	42.8	0.34	7.0	47.7	0.38
1985-86	7.9	40.0	0.33	7.5	45.0	0.35
1986-87	8.0	39.0	0.32	7.9	44.0	0.36
1987-88	8.8	40.0	0.31	6.4	48.1	0.37
1990-91	6.0	47.4	0.41	5.7	50.5	0.39
1992-93	7.0	44.8	0.37	6.1	48.9	0.42
1993-94	7.4	43.1	0.40	6.7	47.1	0.35
1996-97	7.3	49.3	0.41	7.6	47.0	0.38

Source: Economic Survey (various issues).

During the more recent period, 1992-93–1996-97, income distribution has worsened in both rural and urban areas, although there was a slight improvement in income distribution for urban areas between 1992-93 and 1993-94. The data on income distribution, particularly for the 1990s, give cause for serious concern about distribution of the fruits of growth in Pakistan. It seems that in Pakistan, growth is weakly associated with distribution of income.

Household income distribution appears to have worsened more in rural areas than in urban areas. The Gini coefficient in rural areas increased from 0.31 to 0.41. While the share of the lowest 20 percent of households has declined, those at the top experienced gains, which resulted in an increase in the highest to lowest income ratio.

(j) Nutritional Status

Three common indicators of nutritional status for preschool children are stunting (height-for-age), being underweight (weight-for-age), and wasted (weight-for-height) [Kemal, *et al.* (2002)].[21] As much as 38.0 percent of children in 2001-02 were underweight, 36.8 percent were stunted, and 13.1 percent were wasted. (See Table 23.) This indicates that a substantial proportion of children are living in poor socioeconomic conditions at high risk of exposure to disease. While there has been a decline in underweight children from 52 percent in 1985–87 to 38.8 percent in 1998-99, stunting (height-for-age) increased to 50 percent in 1990-91 and further to 60.1 percent in 1998-99. This indicator is associated with poor socioeconomic conditions and increased risk of frequent exposure to illness. The high incidence of malnutrition can partly be explained by the increasing trend of poverty in the 1990s. The increased level of food poverty coupled with unfavourable socioeconomic conditions and inappropriate feeding practices, has resulted in an increase in the incidence of chronic malnutrition.

Table 23

Trends in the Prevalence of Malnutrition

(%)

Data Year	Height-for-Age (Stunted)	Weight-for-Height (Wasted)	Weight-for-Age (Underweight)
1976-77	42.9	8.6	–
1985-87	41.8	10.8	51.5
1990-91	50.2	9.2	40.4
1998-99	60.1	9.5	38.8
2001-02	38.0	13.1	36.8

Source: Micronutrient Survey (1978), *National Nutrition Survey* (1988), *Pakistan Demographic and Health Survey* (1990-91), PIDE (1998-99) and Kemal, *et al.* (2002).

– Implies not available.

Socioeconomic factors affect significantly the growth pattern of children less than five years of age. Using a regression framework, Kemal, *et al.* (2002) show that mother's education, breast feeding, and modernisation were negatively associated with malnutrition.

IV. DETERMINANTS OF POVERTY AND PRO-POOR GROWTH STRATEGY

A large number of factors, significantly impact the poverty levels. Ghura, Leite and Tsangarides (2002) identifies four pro-poor conditions besides growth that are influenced by policies. These include inflation, government size, educational achievement and financial development. Amjad and Kemal (1997) examine four broad categories of factors that impact the levels and trends of poverty: structural characteristics of the economy, per capita output, foreign flows, and safety nets.

[21] In order to examine the status of child malnutrition, a comparison with a reference child of the same age and sex may be made. Z-score is calculated by using the median value and standard deviation (SD) of the reference population. The percentage of children whose Z-score falls below a defined cutoff point, i.e., –2SD from the median of the international reference population, is identified as malnourished children.

(i) *Structural characteristics of the economy* include structure of output, sectoral distribution of the labour force, and pattern of ownership of the means of production.
(ii) *Output Levels.* Especially important here is the availability of food at stable prices, given the nutritional norms underlying the specification of the poverty line. Levels of per capita income (alternatively GDP or its growth) are expected to be associated with a lower level of poverty; a higher level of inflation is expected to adversely impact poverty levels.
(iii) *Foreign Remittances.* These flows can impact poverty levels by directly supplementing incomes and consumption levels, increasing the capital stock, and resulting in higher levels of output growth and employment generation in the economy.
(iv) *Subsidies* are provided by the Government to keep prices low for essential commodities and to subsidise key inputs, which would result in increasing the output of key commodities, especially in the agricultural sector.

With respect to the major correlates of poverty, economic indicators are identified that could best capture these characteristics.[22]

(i) Real per capita GNP (YPEP). Alternatively GDP and its growth rates (GGDP);
(ii) Income distribution measured by Gini coefficient (Gini);
(iii) Per capita availability of food grains (CPC);
(iv) Inflation rate as percentage change over the previous year (CPI); and
(v) Unemployment rate (UNEMP).

In terms of available output for current consumption we would expect:

(i) the higher the per capita income, the lower would be the level of poverty;
(ii) the higher the per capita availability of food grains, the lower would be the level of poverty;
(iii) the lower the level of inflation, the lower would be the level of poverty;
(iv) the higher the level of remittances per capita, the lower would be the level of poverty;
(v) the higher the level of available subsidies, the lower would be the level of poverty; and
(vi) the lower the unemployment rate, the lower would be the level of poverty.

Would the increase in growth rate of GDP or an increase in per capita income help in reducing poverty has been analysed through multivariate analysis. Three variables have alternately been used to capture the impact of growth on poverty: level of GDP, growth rate of GDP, and per capita income. When all other variables besides growth are introduced in the equation, growth turns out to be an insignificant variable (Equations 1, 6, and 11 of

[22]The impact of subsidies and real wages could not be examined as data were not available for some of the years.

Table 24). This is because the series is short and a number of variables form a collinear set. The impact of each variable, therefore, is difficult to ascertain. The Gini coefficient has the right sign, but it is insignificant. Cereal production is significant, but it has the wrong sign: an increase in cereal production causes an increase in poverty. Remittances and unemployment are two variables that are significant and have the right sign. Inflation rates also turn out to be insignificant. Cereal production, inflation, and the Gini coefficient are excluded from this specification. Per capita income, employment, and remittances are all significant in explaining poverty. The three factors explain 93 percent of the variations in poverty (see Table 24).[23] It shows quite clearly that rapid growth rate with employment orientation would help in eradicating poverty.

Investment is the basic determinant of growth. The level of employment depends on the growth rate of output, composition of output, technology employed and the scale of production. With low levels of investment, it is imperative that the economic activities, which are labour-intensive, are encouraged. This will not only increase employment opportunities but also higher output levels. Four labour-intensive sectors are: agriculture, small-scale manufacturing, construction, and general services. The government has identified agriculture, small-scale industries, IT and oil and gas as priority sectors.

Agriculture absorbs almost half the labour force but it is feared that a large proportion of them are only partially employed. The ability of the sector depends on a number of factors including the compositional change within the agriculture, technology employed and the pricing structure. The sectors such as livestock, forestry, fisheries and other high value added crops are the ones which are more labour-intensive. However, these sub-sectors have never been accorded priority.

The industrial policy of Pakistan provides maximum incentives to Hi-tech and export-oriented industries. High tech industries include electronics, information technology and chemical sectors while textiles is the major export product. Chemical industries are rather capital intensive while electronics and engineering industries are skill intensive. The information technology, one of the priority sectors of previous government, has helped in the integration of world economy and is expected to result in higher levels of productivity. However, it can result in digital divide with serious implications for the workers. The unskilled or semi-skilled workers will be replaced with skilled workers on the computers and the total demand of the workers may shrink. Moreover, the divide between the haves and have-nots may increase further. The skilled

[23]The results regarding the other variables need to be interpreted with extreme caution. The fact that the level of inflation is not significant may have far more to do with the way it has been defined and used in this analysis. The analysis is picking up only the level of inflation in that year and poverty levels are based on observations with widely different time intervals; hence they reflect changes over that time period as well as economic developments in that particular year, and it would be difficult to isolate the impact of inflation in that year unless it were dramatically high. The same is true of changes in the Gini coefficient.

Table 24

Multivariate Regression of Poverty

	Constant	GDP	GGDP	YPER	REMT	GINI	UNEMP	CPC	CPI	R^2	R^{-2}	F
1	5.65	0.053			–0.234	0.612	0.616	0.281	–0.58	0.95	0.92	26.4
	(1.65)	(0.15)			(4.61)	(0.97)	(2.66)	(1.85)	(0.30)			
2	5.083	–0.20			–0.228	0.537	0.611	0.290		0.95	0.92	35.3
	(2.70)	(0.85)			(5.17)	(0.98)	(2.79)	(2.06)				
3	4.500	0.301			–0.221	–0.193			–1.554	0.83	0.76	11.9
	(1.15)	(0.56)			(2.84)	(0.19)			(0.48)			
4	8.700	–0.377			–0.178	–0.042	0.837			0.92	0.90	32.5
	(3.69)	(2.04)			(4.20)	(0.08)	(3.84)					
5	8.77	0.379			–0.180		0.859			0.93	0.91	52.07
	(5.56)	(2.61)			(5.25)		(4.77)					
6	6.643		0.047		–0.242	0.689	0.762	0.243	–0.72	0.95	0.92	27.74
	(1.86)		(0.63)		(6.87)	(1.14)	(2.68)	(1.68)	(0.50)			
7	4.897		0.033		–0.243	0.691	0.664	0.295		0.95	0.93	36.28
	(9.23)		(0.60)		(7.25)	(1.08)	(3.38)	(3.12)				
8	10.64		0.086		–0.244	0.507	0.997		–2.508	0.94	0.90	27.19
	(3.66)		(1.12)		(6.33)	(0.77)	(3.67)		(2.30)			
9	4.08		0.046		–0.260	–0.508	0.649			0.91	0.86	22.9
	(6.44)		(0.52)		(5.73)	(0.87)	(2.41)					
10	4.62		0.055		–0.264		0.591			0.89	0.87	33.43
	(33.47)		(0.75)		(7.69)		(3.17)					
11	5.880			–0.029	–0.225	0.571	0.638	0.269	–0.340	0.95	0.92	26.36
	(1.33)			(0.05)	(3.12)	(0.91	(2.80)	(1.73)	(0.22)			
12	5.533			–0.094	–0.221	0.522	0.623	0.281		0.95	0.92	35.4
	(1.43)			(0.17)	(3.37)	(0.94)	(3.02)	(2.04)				
13	10.79			–0.876	–0.137	–0.148	0.818			0.92	0.90	32.70
	(3.2)			(2.06)	(2.33)	(0.29)	(3.88)					
14	11.260			–0.501	–0.167	0.147	0.842		–1.299	0.93	0.90	25.38
	(3.28)			(–0.79)	(–2.37)	(0.23)	(3.89)		(–0.81)			
15	11.32			–0.927	–0.131		0.824			0.93	0.91	52.35
	(4.46)			(2.63)	(2.64)		(4.86)					

Source: Estimates of present study.

workers will not be working in a common place and the concept of union workers going on strike if fair demands are not met would be diluted.

Rationalisation of tariff structure results in major changes in the production structures; industries in which the country does not have comparative advantage close down leading to immediate loss of employment in these activities. However, employment opportunities are created in the new industries where investments flow but in general they may not be sufficient to offset the loss of employment opportunities in the short run though over medium and long run it is expected to do so.

The export industries, textiles, leather, sports goods, surgical instruments, etc. are labour intensive industries. These are high value added goods and are expected to generate more employment. Globalisation would help in an increase the production of these products. Whereas assembly in automobiles and engineering goods industries is quite capital intensive, the components industry is labour intensive. Through sub-contracting arrangements, the large enterprises can be instrumental in promotion of small-scale industries. Small-scale enterprises can create more jobs at much lower capital cost. For example, capital-labour ratio in the small-scale industries on average has been one fourth of large-scale industries and if land and buildings were excluded then the cost may be just 5 percent of that in the large scale [Kemal and Mahmood (1993)]. The four major macro-economic policies of great consequence for small-scale industries are tax structure, demand for the goods produced by the small-scale enterprises, credit and technology. The removal of these impediments would go a long way in improving the profitability of small farms.

Construction sector is labour intensive and employment elasticity is relatively much larger. Output of this sector depends on the investment levels and private sector investment is not expected to grow in any significant way in the near future. Therefore, growth of the construction sector requires public sector intervention to generate employment through programmes including farm to market roads, water supply improvements and renewal of small rural towns. Construction and widening, and repair of farm-to-market roads are very labour intensive activities and provide the necessary infrastructure at the lowest cost. Similarly remodeling, rehabilitation, and improvement of canals and water channels, lining of canals where feasible, improvement of karezes, construction of check dams, tubewells and small dams which at present are in bad shape due to insufficient allocation of operation and maintenance expenditure is a labour intensive activity. Similarly repair and desilting of the canal system would not only enhance agricultural productivity but would also generate sufficient employment. Renewal of small towns is another labour intensive and useful scheme involving upgradation of services such as sewage and solid waste disposal, repair of roads and pavement within towns. The provision of basic infrastructure would induce private sector to invest in these towns.

Services sector can result into higher employment levels. While in general they are determined by the demand from other sectors and households, their improvement results in higher level of output. With globalisation, there is an urgent need to revamp the services sector.

V. SUMMARY AND CONCLUSIONS

Major conclusions of the study are summarised below.

(a) The macroeconomic policies pursued since 1987-88 aimed at stabilisation of the economy and to bring about structural changes in the various sectors of the economy. Both were necessary because by 1987-88 the fiscal deficit had reached to an unsustainable level and the distortions in various sectors of the economy were impeding growth rate. Pakistan has been successful in achieving economic stability by successfully implementing SAP in recent years and 9/11 events. However, investment and growth rates have fallen and unemployment and poverty levels have increased.

(b) Reduction in the fiscal deficit has been due to a reduction in public expenditures, especially the development expenditure with serious repercussions for growth and poverty. Accordingly, there is a need to increase the public expenditures; non-development expenditures for efficient use of productive capacity, and the development expenditures for increasing productive capacity. However, it needs to be ensured that it is not at the cost of instability. The increase in public expenditures should be financed through higher resource mobilisation.

(c) Even though there has hardly been any increase in the tax-GDP ratio, the major structural changes in the taxes hold promise for higher growth of revenues. However, tax burden on the poor has increased and tax structure has become regressive. The public expenditure has gone down, especially that which had helped the poor; subsidies have been removed and the social facilities for poor show hardly any improvement.

(d) There have been major reforms in the financial sector including autonomy of the State Bank of Pakistan, use of market-based instruments to control the money supply, auctioning of the government securities through bids, prudential regulations and improvement in the regulatory and surveillance capacity of the State Bank of Pakistan. Even though there has been some decline in nominal interest rate, the real rate of interest has increased. The high interest specifically is due to the high spread between lending and deposit rates, which in turn is due to a very large infected portfolio of the banking sector. Despite various efforts of the government, the growth of non-performing and defaulted loans could not be stopped.

(e) Pakistan is no longer using non-tariff barriers to restrict imports and tariffs are being used only for protection purposes. The exchange rate has been floated to bring about equilibrium in the balance of payments. Even though there have been fluctuations in the growth rates of exports and imports, there has been an increase in the degree of openness of the economy.

(f) The savings rates in Pakistan have not only been low but have shown fluctuations. These fluctuations arise because of the two factors, viz., changes in the current account budget and changes in the terms of trade. In the recent

years because of negative net factor income, national savings fall short of the domestic savings. Reduction in fiscal deficit has led to an increase in government savings (less dissaving) but the public savings and the aggregate savings continue to be at rather low levels.

(g) The investment rate has fallen to the lowest level of 13.9 percent of GDP since the 1950s. Unless the investment level is raised, and the investment flows to the sectors with high employment intensities, unemployment and poverty would rise.

(h) Investments show divergent trends over time. During 1988–1993, when consistent policies were pursued and structural adjustment and stabilisation programmes were implemented, the investment did increase rapidly. However, when there was no continuity of policies in the period 1993–98, the private sector investment fell. Moreover, because of the lack of resource mobilisation, public sector investment has fallen drastically. During the post-sanction period the problems were aggravated further. However, subsequent to 9/11 events because of the improvement in the economic fundamentals, the prospects of investment have brightened.

(i) Pakistan has so far divested 103 units and Rs 60.5 billion proceeds have been realised. The government intends to privatise 10 financial institutions, 9 oil and gas enterprises, two power and electricity enterprises, 23 manufacturing enterprises and telecommunication corporations and three other units. So far, the performance of privatised units has been a mix. In the banking sector there has been an improvement in the efficiency. However, in the manufacturing sectors where cartels were formed, the performance seems to have deteriorated. Therefore, prior to divestiture, competitive market structure needs to be ensured.

(j) Due to various factors including falling levels of investment, the GDP growth rate over time shows persistent decline. Whereas it was more than 8 percent in the 1980s, it declined to 5 percent in 1988–93 period, to 4.1 in 1993–98 period and further to 3.3 percent in 1999-2002 period.

(k) The agriculture sector that had performed reasonably well earlier, could not do so over the last two years (1998–01) due to drought conditions. The agriculture sector has grown at a rate of 4 percent over the period though there have been fluctuations in the growth rate. However, for sustainability of the agriculture growth rates, marketing facilities, support prices, allocation for water, and adequate availability of credit to the poor would have to be ensured.

(l) The large scale manufacturing output has grown at a rate of around four percent which is less than half of that achieved in the 1980s. Since investment levels have been low the construction activity with highest employment elasticity and lowest capital intensity has been sluggish. Similarly the growth rate of services sector, another labour intensive activity has also gone down.

(m) Employment has gone down as a result of lower growth rate of output. Unemployment increased from 4.7 percent in 1992-93 to 6.4 percent in 1998-99 and further to 8.4 percent in

1999-2000. It is much higher in urban areas, where it increased from 5.8 percent to 8.9 percent; in rural areas it increased from 4.3 percent to 5.0 percent during the period from 1992-93 to 1998-99. Teenagers, youth and females suffer the highest levels of unemployment. Underemployment has also increased: from 11.5 percent to 18.4 percent over the same period.

(n) The incidence of poverty has increased from 17.8 percent in 1987-88 to 32.6 percent in 1998-99. The incidence of poverty in rural areas is more widespread than in urban areas. Per capita income, remittances, and employment are the major variables that affect poverty. The export-oriented strategy that favour the generation of employment would be instrumental in reducing poverty.

(o) About 38.0 percent of children are underweight, a number very similar to the proportion of poor persons. That as many as 36.8 percent of children are stunted and that 13 percent were wasted is rather worrisome. These figures indicate that a substantial proportion of children live in poor socioeconomic conditions and at a higher risk of exposure to disease. A decline in the mean weight of children aged less than six months is another cause for concern. It not only indicates a high incidence of malnutrition among children of this age group, but also among their mothers. Education and modernisation of women has a positive effect on the overall level of nutrition.

That Pakistan has been able to achieve stability is a good omen. One only hopes that stability would result in higher levels of investment, output, employment, and exports. However, in order to reach that stage, a number of measures will have to be taken. This calls for a substantial increase in public sector investment, restoring the private sector's confidence, and promotion of small-scale industries and the agriculture sector, to name a few of these.

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STRUCTURAL ADJUSTMENT AND POVERTY IN PAKISTAN

By A. R. Kemal

SUMMARY

On the assumption that growth trickles down to poor, Structural Adjustment and Stabilisation Programmes (SAPs) that aimed at improving the efficiency levels and higher growth rates were pursued without worrying about poverty. However, various studies particularly on Pakistan show that growth does not necessarily lower poverty.

The SAPs aim to reduce budgetary and balance of payments deficits, pursuance of market friendly policies, improving the levels of efficiency and higher levels of output. Over the last 15 years Pakistan has implemented various SAPs of the IMF and the World Bank with varying degree of success and implementation. Although, Pakistan has implemented SAP signed in 2000 faithfully and has achieved stability, the growth performance has not been all that good. The poverty has almost doubled over the decade. This increase in poverty is generally attributed to SAPs, but in view of the fact that Pakistan has failed to implement various SAPs and investment has been hit by factors other than SAP, the increase in poverty cannot be attributed entirely to SAP. Nevertheless, a better designed programme could have worked better to increase growth and employment and to reduce poverty.

Macroeconomic policies affect poverty through various channels. By influencing the choice of technology, they affect functional and size distribution of income; through changes in incidence of tax rates etc., they significantly influence the poverty levels. Therefore, employment oriented growth strategy can result in improved distribution of income and decline in poverty levels. Macroeconomic policies in Pakistan have been influenced by SAPs.

The decline in fiscal deficit in Pakistan has been entirely due to reduction in public expenditure, both development and non-development. This reduction has had adverse implications for productivity, growth, social infrastructure, and poverty. Moreover, incidence of taxes increased sharply for the poor and declined for the higher income groups over the 1998-2002 period. These have led to an increase in poverty.

Despite major reforms in the financial sector including autonomy of the State Bank of Pakistan, use of market-based instruments to control the money supply, auctioning of the government securities through bids, prudential regulations and improvement in the regulatory and surveillance capacity of the State Bank of Pakistan, the spread between lending and deposit rates continues to be high, and the growth of non-performing and defaulted loans has continued to rise. The inflation rate has fallen to less than 5% over the last three years. This decline is essentially due to prudent monetary policy, which shows the success of stabilisation policies.

Pakistan is no longer using non-tariff barriers to restrict imports and tariffs are being used only for protection purposes. Tariff has been rationalised and maximum

import duty is only 25%. The exchange rate has been floated to bring about equilibrium in balance of payments and there has been an increase in the degree of openness of the economy. Whereas until 1997 investment policies of Pakistan were not consistently pursued, a comprehensive investment policy was launched in 1997 giving incentives to hi-tech and export oriented industries. The regime for foreign investors has been liberalised. The experience with privatisation has been mixed; in banking it resulted in improved levels of efficiency but in manufacturing results are mixed. However, one-third of the workers of public enterprises after privatisation lost jobs.

During 1988-93 investment increased due to consistent policies and serious implementation of the programmes, but investment declined in subsequent periods due to non-implementation of programmes and discontinuity of policies. In post 9/11 period, foreign private investment is likely to rise because of strong economic fundamentals. Falling investment has slowed down the production. Growth of employment is a function of the growth rate of output, composition of output, and employment elasticity. The growth rate of GDP has fallen and therefore employment generation has also gone down. Employment generation in 1990s has been inadequate to provide jobs for the growing work force, resulting in an increase in unemployment and underemployment rates over time.

Poverty shows an increase in poverty over the 1987-88 to 1998-99 period in Pakistan. Per capita income, employment, and remittances are important factors in explaining poverty. The implication that emerges from this analysis is that rapid growth rate with employment orientation would help in eradicating poverty. Four labour intensive sectors are agriculture, small-scale manufacturing, construction, and general services.

Income distribution has also worsened during 1992/93 – 1996/97 period in rural as well as urban areas. As regards the nutritional status, in 2001-02, 38% of children were underweight, 36.8% were stunted, and 13.1% were wasted. This indicates that a high number of children are living in poor socio-economic conditions.

The study concludes that the macroeconomic policies pursued since 1987-88 aimed at stabilisation of the economy and to bring about structural changes in the various sectors of the economy. Pakistan has been successful in achieving economic stability by successfully implementing SAP in recent years and 9/11 events. However, investment and growth rates have fallen and unemployment and poverty levels have increased. One hopes that stability would result in higher levels of investment, output, employment, and exports as time would pass. However, in order to achieve this, a number of measures have to be taken, which include substantial increase in public sector investment, restoring the private sector's confidence, promotion of small scale industries, and the agriculture sector.