

Inaugural Address

GHULAM ISHAQ KHAN*

Syed Nawab Haider Naqvi,
Dr A. R. Kemal,
Distinguished Guests,
Ladies and Gentlemen,

It is my privilege to inaugurate the Sixth Annual General Meeting of the Pakistan Society of Development Economists.

During the past seven years, the Society has become an institution in its own right, devoted to the creation of scientific knowledge in the general area of development economics. It has provided an effective forum for the exchange of views on problems and challenges faced by development economics in general, and by Pakistan's economy in particular. The massive outpouring of knowledge in the shape of Papers and Proceedings published by the Society each year sheds ample light on complex academic issues and also constitutes an invaluable source of information for policy formulation. I am happy to note that the Society has been pursuing its objectives with determination, and has sought to cultivate its intellectual pursuits unhindered by any extra-academic considerations. This is as it should be. For, when it comes to academic excellence, the limits should only be those of the imagination.

We are meeting today at a time when the world is changing – and changing at an unprecedented pace. The scary chapter of cold war, replete with memories sending cold waves down one's spine, seems to be drawing to a close. And a new happy chapter in international relations has begun to unfold itself, bringing relief and hope for weary humanity. Conflict is changing to detente and detente to co-operation. Walls cutting nations apart – all kinds of them from mental to concrete – are crumbling. A new pattern of global relations is emerging with more togetherness and greater openness as its distinctive features. The post-World War ideological divide is losing its sharper edges. In the welfare state and its general shift to the left, Capitalism has assumed a "kinder and gentler" face and an egalitarian stance while, by attempting to become more like market economies, Socialism has acquired a

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more humane posture. The battle-cry of Communism still is "Workers of the world, unite"; but this time – at least in Eastern Europe – against Communism itself. While Eastern Europe is seething with a democratic upsurge, European democracies are merging into one single market. In some other parts of the world, also, causes of tension and friction are fading out, giving way to prospects of a relaxed harmony. Today's man is thus more hopeful about the future than yesterday's.

These are developments of tremendous import. We welcome them. We wish that they turn out to be a prelude to the creation of a safer, happier world order. But we also have to be mindful of their impact which will be felt globally in all walks of life, including the economy. Reduction in the areas of conflict and the growing trend towards general disarmament will, it is expected, release vast technological, financial and manpower resources for more productive investment. But these, like fat on the body, may accumulate at the wrong places and may not always find their way to where they are most needed. New friendships may render old alliances irrelevant. Political re-alignments may lead to fresh economic partnerships. A democratised East Europe may attract greater assistance and collaboration from the free world, leaving a smaller portion of the pie for the developing countries to share. Apprehensive of the marauding economies of the Pacific Rim, the Land of the Rising Yen, and the powerful North American free trade area, the European Community is feared to convert itself into a "fortress trading bloc" after 1992. More inward-looking trade groups may emerge elsewhere too and strengthen regional protectionist tendencies. We hope and pray that these apprehensions never come true. But what if they do? Will then the exuberance of the First and the Second World over their newly-entered courtship result in a cold indifference towards the needs and aspirations of the Third World? This is the question the decade of the 80s has left for us as a legacy for the 90s – a question which has to be taken as a new factor in determining our development strategy, a question which has accentuated more than ever before the need for self-reliance and self-dependence.

As you know, the international economic environment we faced in the Eighties was characterized by moderate economic growth, high rates of unemployment and balance-of-payments problems compounded by the resurgence of protectionism in the developed countries. Also, the engine of growth moving from North to South had slowed down visibly. This, combined with a slower growth of world trade and a worsening of the terms of trade, widened current account deficits of developing countries. The situation was further aggravated by the decline in the net resource transfers from the developed to the developing countries.

In such an international economic environment, Pakistan has done reasonably well. During the Eighties, the Pakistani economy experienced an average annual growth rate of 6.3 percent with inflation, on average, at a reasonable single-digit level. This indeed was a notable achievement. However, due to a somewhat ineffec-

tive population programme, Pakistan's population increased at a rate of over 3 percent, with the result that per capita GNP improved only moderately. According to studies carried out by the Pakistan Institute of Development Economics, another important feature of growth during this period was that employment increased at an average rate of 2.4 percent per annum, while the "open" unemployment rate declined from 3.9 percent in 1982-83 to 3.05 percent in 1986-87.

Good performance in the past, however, does not by itself guarantee that the same trend will continue in the future as well. Measures need to be taken now not only to maintain and strengthen the growth process, but also to neutralize the possible adverse effects of exogenous shocks. As a result of the changes in the international political scene I have referred to earlier, it is likely that the direction of aid, trade and investment flows from the prosperous Western Bloc will change to Eastern Bloc countries, particularly after the latter complete the process of opting out of centrally planned and managed economies to market systems and assuming full membership of such erstwhile reviled organizations as World Bank, IMF and GATT, and get incorporated in the world economy.

Much of Pakistan's economic growth in the Eighties had been financed through excessive borrowing – both domestically and from abroad. Since 1980-81, domestic debt has increased more than fivefold to over Rs 310 billion. We also owe more than US \$ 14 billion to the outside world. At the same time, the inflow of workers' remittances has considerably dropped. Inflation is rising and has already crossed the single-digit threshold. The increasing instability of our trade sector is yet another problem area which should cause considerable anxiety. Our performance in the export sector, in terms of what we earn for our goods, has been far from satisfactory.

Worse still, the level of investment has declined in recent years. The national savings rate is at best moderate. One may also bemoan the severe problems being faced in mobilizing domestic resources through taxation. Total tax revenue remained around 16 percent of the GDP in the Eighties with direct taxes constituting only 2 percent.

The constraint on resources had an adverse impact on other sectors also. While the economy grew at a healthy rate, the development of the social sectors, including education and health, did not show the same dynamism. A literacy rate of 30 percent is nothing less than a national scandal. In addition to the overall low literacy rate and school enrolment ratios, large differentials continue to exist between the urban and the rural areas, and within each area, between males and females. Similarly, a large portion of our population continues to be deprived of basic health facilities. The infant mortality rate is still unacceptably high, and life expectancy at birth considerably low.

Another area which needs serious re-thinking and more devoted effort is the problem of a rapidly expanding population. Since the early Sixties, Pakistan's

population has been increasing at an annual rate of over 3 percent. With the existing rate of employment generation estimated to be 2.4 percent per annum, the present rate of population growth is constantly adding to the pool of the unemployed labour force. At the current rate of growth, we will have 156 million people to take care of by the end of this century.

Again, behind the overall low national unemployment rate, there are considerable regional disparities. Unemployment among the educated workforce is much higher than the national average. The ostensibly low unemployment rates do not also imply that all those who are employed are being utilized to their full potential. What makes the present employment situation even more serious is that the employment generating capacity of the manufacturing sector has declined considerably in recent years.

Talking of the future, the objective of the policy should be to alleviate the constraints I have referred to. The focus should continue to be on maintaining a high GDP growth rate within an environment of stable prices. The objective should be to maintain a growth rate of GDP in the minimum range of 6.5 to 7 percent, with the inflation rate not allowed to exceed 5 percent. To make sure that such a policy is pursued for a reasonably long period, attempts should be made to evolve a national consensus among the political parties within the framework of a development plan to safeguard the growth poles of the economy. To achieve this target, it is of central importance that the performance of the commodity-producing sector, i.e., agriculture plus manufacturing, is improved. It is equally important that the structure of this sector is diversified in favour of higher value-added products, and it is made more efficient, competitive, and responsive to the needs of the domestic and international markets. At the same time, we must revive the dying embers of the private investor's faith in the vitality of the manufacturing sector so that it plays an effective role in the progress of the country.

However, a high growth rate of GDP will be meaningful only if it translates itself into a higher increase in *per capita* GNP. Presently, despite an over 6 percent GDP growth, our GNP *per capita* is growing at the rate of only 2.5 percent. At this rate, it will take us close to fifty years to become a middle-income economy with *per capita* GNP of over US \$ 1000. This is much too long a period to enthrall people to get earnestly involved in the process of growth. If the objective is to be achieved within, say, 25 years, which itself might prove to be an exasperatingly long period for the bulk of the population, the GNP *per capita* will have to increase at an annual rate of 4.3 percent. This may appear difficult but, considering the potential of the country, it is not an impossible target. Many countries in Asia, like South Korea, Malaysia, Taiwan, have shown that it can be achieved. But to do this we must, among other things, control the rapid growth of population. We must take literally the advice of what our good poet has conveyed in humour:

شوق سے محنت جگر، نورِ نظر پیدا کرو
ظالمو! تھوڑی سی گندم بھی مگر پیدا کرو

Under no circumstances should we allow population growth to outpace the rate of growth in *per capita* GNP. Otherwise, it will be harder even to maintain the present quality of life of our people. Furthermore, the rapid growth of population will require that additional resources are committed in order to keep the unemployment rate at the present level. A minimum of Rs 800 billion of investment, at constant prices of 1988-89, which on average constitutes about 18 percent of GDP — over the next five years will be required to maintain the open unemployment rate at the existing level of 3.1 percent. In real terms, this would require investment, which has been stagnating at 17 percent of GNP, to grow at an average rate of 7.4 percent per annum.

We should also work for improvement in the distribution of income by ensuring that real wages rise together with a higher level of employment. If suitable means could be devised for the purpose, groups which somehow do not benefit from the growth process should be compensated by making direct transfers, rather than by compromising the dynamism of economic growth.

Also, it is imperative to establish, as early as possible, a sustainable fiscal balance. This should be done by intensifying resource-mobilization efforts, increasing domestic savings, reducing the rate of growth of government expenditure, eliminating subsidies, and lowering public sector investment. The household sector is already making its due contribution at the rate of 80 percent of total national savings and we should not expect more from it. Besides, to raise the household savings further will call for a still higher return on savings which will certainly adversely affect the level of investment. Hence, to increase domestic savings, greater attention will need to be paid to increasing the savings of the corporate and the public sectors.

The balance-of-payments, position has been a source of perennial concern. Attempts should be made to prevent it from deteriorating any further, which to the extent we succeed in doing so, will also reduce our excessive dependence on external borrowing. To that end, we will have to work more seriously to widen our export base and improve the quality of exports. In particular, we should be exporting increasingly higher value-added items such as engineering goods, enhancing export potential of our agro-industrial products, and exploring new markets, especially for those items where we have a natural advantage. Efforts should also be made to maximize the inflow of remittances and improve their utilization. The possibility of using a part of these remittances for retiring a portion of the outstanding external debt each year may also be explored. We should also devise a more alluring package to attract foreign investment, especially from Asian countries like Japan and South Korea, which have built up substantial investible surpluses in recent years. We have

perfected the art of borrowing and lived on it for too long. It is now time we learnt the techniques of forging partnerships and attracting foreign capital for joint ventures and investments.

For balanced development and to make a perceptible improvement in the standard of living of our people, much more attention should be given to developing our education and health sectors. Efforts should be made to universalize, in the first stage, primary education in the shortest possible time. It is now recognized that the externalities arising from having a high literacy rate far exceed the benefits to individuals from attaining education. Time has come for us to introduce compulsory education up to high school level. Facilities need to be created accordingly and measures adopted to improve the standard and efficiency of the system. Similarly in the health sector, facilities need to be expanded, particularly in the rural areas. Health-cover for all by the year 2000 should be our watchword. Attention should also be paid to removing the urban bias in the present distribution of health facilities.

The aim of economic development is to build a dynamic society which guarantees individual freedom and social justice, without their being detrimental to each other. Countries have their own moral and ethical values and common ideals. Foundations of economic progress will have to be laid on the basis of a shared vision of these values and a voluntary commitment to such ideals. In the context of Pakistan, solutions to the country's problems need to be found within the framework of the Islamic vision of economic relationships. It is our constitutional obligation to do so.

Even otherwise, we have to draw our lesson from humanity's not-altogether-pleasant experimentation with man-made economic systems and the cruelties, imposed in the name of either freedom or social justice. Man's frustration with the exploitative nature of Capitalism had given birth to the god of Communism. But that god has failed. And it is no accident. It had to; for it was unnatural, unjust, unkind and based on premises ultimately proven false. It is now said in retrospect that Stalinism was a morbidly unnatural growth of Socialism, and Fascism a more natural one of Capitalism. We have to find an alternative to these failed systems. In my opinion the only system that can offer panacea for the ills plaguing human society today is the one that ensures individual freedom in an environment of social responsibility, as different from individualistic ego-centrism and self-seeking profit maximization of the capitalist system and voluntary regulation and self-restraint derived from spiritual and ethical considerations, as distinct from the suffocating regimentation of Socialism. The only system that can put an end to exploitation, injustice and misery is the one which makes production welfare-oriented, distribution justice-oriented and consumption balanced-oriented. As Muslims, it is our belief that such a system is offered by Islam.

To put into practice the Islamic economic system, which is independent without being 'separatist', is the challenge we face. I do not wish to go into a detailed inter-systemic comparison, but let it be noted that the Islamic system, based on the Divine principles of *Adl* (i.e., social equilibrium) and *Ihsan* (i.e., compassion), has certain peculiarities which set it apart from other economic systems. Consistent with the principles of *Adl*, Islam seeks a synthesis and emphasises the common rather than competing interests. It avoids extremes and enjoins taking the middle course. Thus, with respect to the basic question of the right to private property, the Islamic viewpoint is to recognize man's right to private property, but to redefine this right as a relative and not an absolute right. In practice, the 'relative' property right may be indistinguishable from 'absolute' property right – according to clear Islamic injunctions, one's private property cannot be willfully taken away by any individual or by the state – and yet there is an important difference between these two types. For instance, while an absolute owner may squander away his (her) resources; Islam, not recognizing absolute ownership, except that of Allah, definitely prohibits waste of resources and their use in manners detrimental to the community's interests or in violation of ethical norms.

Another example of Islam's distinctive middle-of-the road economic philosophy is its view on individual freedom and, specifically, on the role of the individual as opposed to that of the state. In the Islamic view, the basic reference unit is the individual, and the question of freedom relates only to the individual. The state, *per se*, does not enjoy any "fundamental rights" in the same sense as the individual does. Instead, the state, in the Islamic view, is there only to legislate the individual's fundamental rights, which are derived from the purely theological principle that man is born with a free will – i.e., with the basic right to choose between alternative courses of action within set limits, and that this innate freedom of the individual is inviolable. The state must also make sure that freedom for one (say of the rich) is not enjoyed at the expense of the freedom of another (say of the poor). The state, therefore, has to legislate not only about individual freedom *per se*, but also about how this freedom is shared among, and exercised by, different individuals in the society.

There is also in Islam the fundamental issue about the motivation of man's economic pursuits. While the individual's concern about his self-interest is recognized within certain limits, it is not glorified as the central principle that moves the economic universe. Instead, the central principle is that of the individual's commitment to the welfare of the society which implies, in certain cases, the individual's readiness to accept a cut in his own material welfare for the greater good of the society. In general terms, man's economic concern for his own good must be informed with an ethical concern for the betterment of other individuals in the society. The Islamic economic system thus has five basic characteristics which should be

noted:

First, man is seen not as an absolute owner of what he owns, but only as a "trustee". As the real and absolute owner of all wealth is Allah, the needy and the deprived have a known and recognized "right" in the wealth of the rich. It also follows that the act of giving, within the mandatory limits, is not charity. Having acquired wealth through legitimate means, an individual has a definite obligatory social responsibility to discharge. And this social responsibility takes the form, among other things, of helping out the least privileged (*al-musta'afin*) in the society through the institution of *Zakat*.

Second, real resources should be transferred to meet the needs of the society, to reduce the incidence of absolute poverty and to minimize to the extent possible differences in the distribution of income and wealth. A comprehensive social security system is encouraged to be devised to redress the sufferings of the needy and the deprived.

Third, on the question of state versus the individual, the Islamic viewpoint is to recognize the peaceful, and purposeful co-existence of both. While individual freedom to enter or quit legitimate economic activities is guaranteed, the need of the society must also be kept in view. The state must, therefore, ensure that individual freedom is optimally combined with social responsibility.

Fourth, Islam considers interest as exploitative and, therefore, unjust. Accordingly, it prohibits *Riba* in all its forms and prescribes its total elimination from the financial sector. This calls for a re-structuring of the entire financial system by replacing the existing interest-bearing policy instruments with alternative non-interest-bearing ones. Substantial work in this respect has been done already; but for the complete elimination of *Riba*, the process needs to be taken to its logical conclusion. The new instruments, if designed with care and imagination, are likely to lead to greater saving and investment by improving the efficiency of financial intermediation.

Fifth, Islamic reforms must be comprehensive and wide-ranging in scope – to include such elements as universal education, health, and housing. This is because the whole range of problems which tend to promote and perpetuate *Zulm* (i.e., social disequilibrium) in the society – which is the antonym of *Adl* – must be tackled to make the process of Islamization meaningful. As in the financial sector, here too this would call for fresh innovative policy instruments.

I do not wish to go into details. I have only pointed out for your consideration a few facts about Islam's vision of economic processes. This is not out of any proselytizing zeal, but only to remove misunderstandings about the Islamization process – to which we are committed in Pakistan.