

*Presidential Remarks*

## **Economic Development: Pakistan's Policy Choices for the 21st Century**

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It is an honour for me as President of the Pakistan Society of Development Economists to welcome you to the 14th Annual General Meeting and Conference of the Society.

As we prepare to enter the new millennium, we find ourselves at a crucial moment in history. It is time to take stock of our past achievements and to assess the new challenges. To deal with the future would require not only thorough knowledge of the evolving nature of development thinking but also a good sense of the policy choices available to a country in its national, international and regional position. What are the main challenges that require our urgent attention?

A few words are in order at the very outset about Pakistan's current difficult economic situation. The slow-down in export expansion, capital inflows and foreign direct investment was an expected consequence of the imposition of sanctions. The pessimistic assessment of Pakistan's prospects is based largely on the recent negative trends of these economic parameters. The optimists are of the view that Pakistan has survived the imposition of sanctions rather well. Economic growth has remained positive and inflation has been kept under reasonable control. The optimists further maintain that Pakistan's current economic situation is no worse than that of the East Asian countries when they started their economic climb and engineered major institutional and policy changes. Lessons from the initial years of the East Asian miracle clearly show that development is decidedly possible no matter what adverse initial conditions obtain in any developing country. Sustained, rapid and equitable growth is possible through the implementation of wide-ranging social and economic reforms. Lessons from the recent East Asian Crises are also before us—guiding us on what not to do and how best to protect ourselves in these rapidly changing times.

The four East Asian countries, China, Malaysia, Indonesia, and Thailand, increased per capita incomes from 18 percent of the industrial country level in 1965 to

66 percent in 1996. In simplest terms economic growth flowed from the accumulation of physical and human capital, labour and advances in production technology reflected in increased total factor productivity. Recent cross-country analyses show the strong overall correlation between policies and income growth performance: countries with open trade positions, a stable economy and a relatively small size of government tended to show significantly better growth outcomes than countries that were less open, less stable and had larger governments. This analysis also shows that good performance in one category alone does not guarantee high growth outcomes. The three sets of desirable policies must operate together. Minor exceptions to this can result from the presence or absence of, for example, social and institutional factors and resource endowments. However, the results are generally robust.

The experience of the recent Asian crises also teaches us some important lessons. In a globalised world economy, market discipline against policy weaknesses can be large and swift and the size and mobility of international capital flows does exert a heightened degree of discipline on the conduct and effectiveness of national macroeconomic policies.

I believe Mr Ahsan Iqbal's Keynote Address will present the details of a reform agenda for Pakistan. While other sessions and presentations in this conference will offer detailed analyses, I take this opportunity to highlight some of the major areas for which we need fresh thinking and approaches. In the process, I shall point out a few specific priority tasks that need the attention of the policy-makers to meet the needs of this new journey ahead.

## **I. THE DEVELOPMENT RECORD**

### **1. Trends in Growth**

Let us take first the growth performance since 1947. An overview of the extent and quality of growth indicates a few problem areas that may constrain continued growth in the next half-century unless corrective policy action is taken now.

Pakistan has experienced a growth rate in GDP of over 5 percent, and in per capita income of about 2 percent per year, over the fifty years since independence. The sharp acceleration from the pre-independence growth performance has been a truly remarkable achievement for a country which was thought by some to be non-viable in economic terms. Pakistan's economy has also performed better than all other countries in the Subcontinent. However, if a comparison is made with the East Asian Tigers, we notice that Pakistan has been left behind in the economic race.

### **2. Equity Outcome of Growth**

At the heart of the endeavours to increase growth is the need to attack poverty. Poverty is a multi-dimensional phenomenon, arising out of the complex interaction of

assets, markets, and institutions. Increasingly the development community is proposing a three-pronged attack on poverty through (i) *ensuring empowerment* of the poor by increasing their participation in decision-making and managing the growth of inequalities; (ii) through *providing security* against shocks at the individual and national levels, particularly for those left behind by rapid change, and (iii) through *creating opportunities* by putting in place the conditions for sustainable economic expansion to provide the material basis for poverty reduction.

The relatively rapid economic growth since independence, which had provided an increase in per capita income of 160 percent, has resulted in a substantial decline in the incidence of poverty. The rising living standards resulted in sharp decline in poverty from about 60 percent in 1947 to 22 percent in 1992/93.

However, on aspects of human capability, other than consumption poverty, Pakistan has not performed very well. Pakistan has always ranked quite low on the basis of the Human Development Index.

### **3. Investment and Savings**

Let me turn now to some other worrying aspects of past growth. Pakistan's savings and investment rates were low at the time of independence which is not surprising due to the low per capita income in the initial years. The improvement in the national and/or domestic savings rates and investment has been only marginal in the last 50 years. The rates of investment as well as savings in Pakistan have also been low relative to most low-income countries. The excess of investment over domestic savings in the past was financed mostly by large unrequited transfers and/or low-cost foreign resources. Pakistan's option to finance the foreign exchange gap at low cost seems to have vanished due to a change in the international economic environment.

### **4. Exports and Growth**

Merchandise exports as a percentage of the GDP have increased from 4 percent in the early 1950s to 15 percent in the 1990s. The composition of exports has also changed from the main reliance on primary exports to manufactured exports. However, the point to be stressed is that the export expansion and the changed composition of exports does not imply that Pakistan has successfully exploited its opportunities in the rapidly growing world economy over the last 50 years. Pakistan's exports remain undiversified and consist mostly of lower-end of cotton textile products. The country has also failed to make a mark in the export markets of technologically advanced and labour-intensive commodities.

The summary verdict on the past economic performance is quite clear. Despite reasonably high growth and substantial reduction in absolute poverty, which has declined from 60 percent in 1947 to 22 percent in 1992-93, about a quarter of the population does not have enough food to subsist. Poor performance in human

development, savings and investment and export earnings is a major source of vulnerability and a dire constraint. It should also be noted that the deterioration in income distribution, rise in poverty, and weak employment creation of the last few years are associated with the adoption of market-friendly economic reforms in Pakistan. We do not yet know enough about the exact causal connection.

## II. POLICY CHOICES FOR THE FUTURE

I now briefly turn to the policy priorities in support of renewed and better-shared economic growth. I would touch on seven interrelated areas.

*First*, There is a need to get right the role of the state. That it cannot be the do-all for managing investment and domestic and international trade or for generating employment, is quite obvious. On the other hand, the government needs to play a new role of ensuring macro stability, creating and fostering markets if they are missing or not working properly, and ensuring adequate level of investment in providing public goods.

*Second*, Pakistan's low domestic savings rate of 13.2 percent and low levels of tax collection at 13 percent of the GDP are not sufficient to finance a high GDP growth rate. It is no wonder that job creation has been so sluggish in Pakistan. The issue here is not only a low savings rate. An equally relevant policy issue is: how to increase savings and what sector could be relied on to generate them? In Pakistan, public savings are negative. Corporate savings are also insignificant. Savings may be enhanced by positive real interest rates, efficient financial intermediation, and good investment opportunities. Public savings should lead the way by raising revenue and/or scaling down unproductive public expenditures and downsizing of bureaucracy. Increased taxation requires a government that is not only strong but perceived to be fair as well.

*Third*, the question of the high level of poverty and high inequalities in income in Pakistan needs to be paid urgent attention. Expansion of basic education and a more equitable pattern of land distribution are probably the key to the moderation in the income inequalities. Employment and productivity increases are potent policy instruments for poverty reduction on a sustained basis.

*Fourth*, increasing globalisation has both advantages and disadvantages. The challenges that this process poses for public policies in Pakistan are serious questions that need to be tackled now and in the years ahead.

*Fifth*, export expansion needs to be given a high priority. Regional integration as well as removal of impediments to exports are probably the starting point for evolving a coherent export development strategy in this context.

*Sixth*, the biggest challenge facing the development community as we move closer to the 21st century is the need to develop an integrated multidisciplinary approach that brings together political democracy, social and cultural development, and economic efficiency in such a way as to ensure empowerment of the people, especially the poor. Only that can provide security against national and international shocks and create the

opportunities for participation of all in an economic expansion that remains sustainable.

Last but not the least, there is the important issue of the implementation mechanism of the selected policies and related political decision-making. There is a large gap between the public policies announced and their actual ground-level implementation. The lack of coordination between different levels of government and between different government departments and the civil society is a major lacuna for which corrective measures must be provided.

As we all understand, a conference of this type requires a great deal of effort, public interest, and private support. We have been fortunate with all of these as our friends everywhere have been helpful and generous both with moral and material support. I would like to acknowledge and thank particularly the members of the PIDE community for the countless tasks that they have performed to make this possible. Crucial to the undertaking has been the financial support given by numerous organisations to make the organisational, logistical, and the frequent prandial needs fulfilled. Our banner over there says it so, but let me name them to be sure: it is the World Bank, Islamabad Office; Friedrich Ebert Stiftung, Islamabad; the National Bank of Pakistan; and, the Pakistan Telecom Authority. Last but not the least, the personal active interest of Mr Ahsan Iqbal has been a source of strength.