

Rethinking Growth Model: From Hardware to Software

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The Need for Rethinking Pakistan’s Growth Model

To absorb Pakistan’s youth bulge, into gainful employment, and to sustain the country’s high level of debt, PIDE’s estimates suggest that the country’s GDP should grow at a rate of 7-9 percent per annum for a fairly long period running into decades.

What is Software of the Economy and the Society

Laws, rules and processes that and impact economic activity.

Growth-conductive software will facilitate economic activity (i.e. transactions) in lesser time, at low monetary cost to the stakeholders, will encourage competition and provide a level playing field to

Pakistan’s present growth rate is not only low the long term trend of growth is declining as well. Productivity and investment the two key drivers of growth are also on a declining course (see Figures 1 and 2). Breaking away from this low growth trajectory calls for deep-rooted structural reforms. Realising this, the PIDE with active consultation of renowned economists and development practitioners from all over the country has developed the PIDE Reform Agenda for Accelerated and Sustained growth (2021).

Fig. 1.

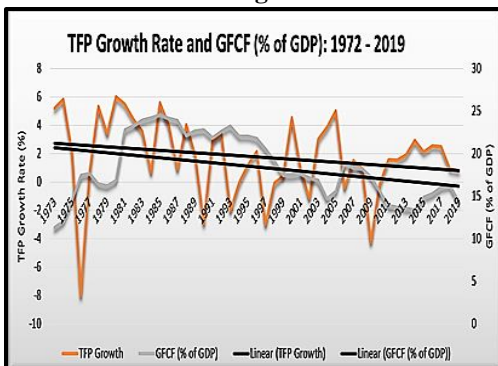
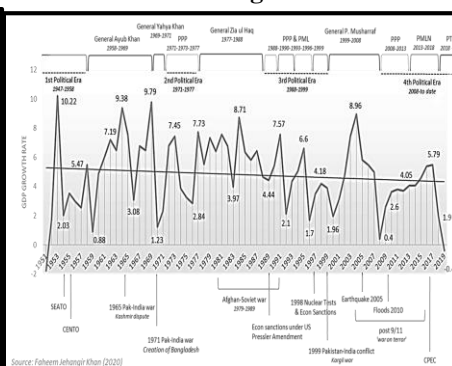


Fig. 2.



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Author’s Note: This policy viewpoint heavily draws upon PIDE Reform Agenda for Accelerated and Sustained Growth prepared by PIDE Growth Commission and Growth Reform Agenda Secretariat at PIDE (GRASP).

The development model which Pakistan has followed since the sixties emphasises investment in hardware—roads, dams and buildings etc. This model developed by Dr. Mahbub Ul Haq and the Harvard Advisory Group did serve the immediate needs of the economy at that time. However the recent thinking in economic literature North (1990); Acemoglu & Robinson (2013) and inadequate returns from the growth model being followed at home calls for a paradigm shift – from hardware to software – the software of the economy and the society.

From Hardware to Software

The PIDE Reform Agenda for Accelerated and Sustained Growth (2021) takes the view that bad laws and cumbersome procedures keep productivity and investment low in Pakistan. Therefore the development model needs to undergo a paradigm shift. The country should now focus more on developing growth-conducive software, which is; laws, rules and processes that influence economic activity.

The constraining laws, rules and processes lead to situations like where; forty-five steps are needed to lay a n optic fibre for internet connectivity. Firms on average spend 577 hours and wade through 47 procedures to pay all the taxes for the year. Nine procedures are needed for a construction permit and this can cost up to nine per cent of the construction value. Land developers must obtain 22 NOCs from different agencies in order to proceed. Some laws also provide an unfair advantage to one or few players in the economy thus killing the competitive environment.

The kind of constraining laws and rules operating in situations like the ones referred above are typically developed by the government, at times, in good faith to check unwanted and unfair practices. In practice these constraining laws and rules go beyond the intended objective, to the extent of hurting the much-needed fair economic activity. The lengthy and obsolete processes too are practiced mostly at public entities. Therefore, it is the government which has to be reformed. We take this up after the next section on transaction costs.

Transaction Costs

GDP, as we know, is the sum of transactions between two parties to an exchange. Some costs have to be incurred to execute a transaction—lower the transaction costs greater the number and magnitude of transactions. The volume of transactions will be facilitated and hence GDP will increase if transaction costs can be reduced. Following are the different types of transaction costs:

- Search and information cost: the cost incurred to know the attributes of a product, its availability, and sellers.
- Bargaining cost: costs incurred to arrive at a price and terms of sale.
- Settlement cost: Terms of payment and flow of proceeds.
- Enforcement & policing cost: Enforcement of the terms of sale/exchange.

Haque, 2017

Enhancing Productivity

Productivity will improve by amending our laws and procedures to cut down frictions involved in undertaking an activity or executing a transaction.

We recommend;

- (1) Reviewing all laws, rules, and processes from the very scratch, to identify frictions.
- (2) Work towards creating a suitable environment for amending frictions causing laws, rules and processes.

The increase in productivity will also improve the return on investment leading to increase in investment and hence growth.

It is not difficult to see that the transaction costs are higher in Pakistan (especially due to the constraining laws referred above). The government, through its legislative and regulatory authority can mandate or facilitate mechanisms that would reduce transaction costs. For example the availability of prevailing exchange rates on the website of State Bank and Forex Association of Pakistan reduces the Search and Information costs as well as the bargaining costs for those aiming to buy or sell one or the other currency. Following this pattern, the search and information costs, for example, in the land market can be reduced if the buyers, sellers, realtors or the government were to declare the price on which a transactions has been executed—declaration of prices can be mandated by law or the realtors association can license realtors and one of the condition of the membership could be the declaration of prices. All this is bound to increase the volume of trading in real estate. Similar mechanisms The use of technology helps reduce the settlement costs – the government, the SBP and the internet service providers together can facilitate technology led electronic settlement mechanisms. Finally the government has a responsibility to ensure secure property rights and that the contracts signed are enforced—sound regulatory and judicial performance will ensure this.

It can be easily seen that all the interventions discussed above are soft in nature and boil down to improving governance which does not involve huge investment in monetary terms. Therefore too wade on a high growth trajectory the government will have to be transformed into a well-functioning state. The entire public service including civil service Judiciary, regulatory bodies, and local governments, etc. will have to be reformed to serve as an ‘enabler’ in the economy. Systems will have to be designed to make public servants work harder, better and faster. Host of NOCs and permissions required to engage in entrepreneurship will have to be cut. To augment efficiency of the government, technology and e-governance will have to be used.

Reforming the Government

Making the public servants work harder, better and faster is easier said than done – an extensive set of reforms will be required to make this happen. Key reforms are required are listed in Box 1.

Box 1: Pre-requisite for an Efficient Civil

- (1) Make it easier to lay-off non-performing employees.
- (2) Offer market based monetised salaries to all employees.
- (3) Hire specialists rather than generalists in civil service.
- (4) Allow lateral entry at senior levels (Grade 19 and above) in civil service.
- (5) Restrict transfers and in no case post a person outside his/her area of expertise.
- (6) Do away with the dominance of a single group in civil service.
- (7) Continuously train civil servant for upcoming assignments. Conduct training of civil servants at universities.

Enforcement and Policing Contracts

Violations of contract between two entities or individuals do happen—a buyer may not be satisfied with performance of a product that he bought or a seller might face difficulties in recovering money for the goods that he sold on credit. It is not difficult to see that entrepreneurial activity will be encouraged only if the disputes be resolved quickly at little cost to the aggrieved. With cases pending in courts and the average shelf-life of a court-cases being 37 months, it is clear that cases are not being disposed of quickly at present.

Box 2: Reforming Judiciary

Appoint judges strictly on merit-based on performance in courts and in academic life.

- Train judges, especially in commercial matters.
- Extensively use the option of expert testimony
- Limit adjournments.
- Observe the stay order limit defined in the law.
- Use sophisticated softwares for allocation of cases to judges.
- Increase the number of judges where required.

To decide court cases speedily and at little cost to the aggrieved a through restructuring of the systems surrounding the judiciary is required. Some key requirements for reforming the judiciary are listed in Box 2.

Devising Public Policy using Research-based Inputs

Too often the government takes decisions which are later regretted. The reason is that enough research input has not gone into decision making. To make sound decisions mechanisms will have to be developed to ensure that public policy is always informed by research undertaken at local universities. For this to happen, on one hand construct a public service mindset believing that believes in research based evidence as an essential. On the other hand develop capacity of the universities to undertake research of interest to the government. This would mean

that universities are staffed with competent faculty enjoying sound credentials in undertaking research. The present incentive structure that induces the faculty to produce research has a tilt towards quantity rather than quality and the structure does not encourage policy oriented research. Therefore, revisit the incentive structure that the faculty faces - focus on 'impact' on economy/society rather than the impact factor.¹

Box 3: Policy Decisions based on Research

- (1) Ask for research based evidence while considering policy options and taking decisions.
- (2) Policy makers should ask universities to provide research on a subject of interest to them.
- (3) Staff universities with competent faculty with ability to undertake policy oriented research.
- (4) Devise an incentive structure for university faculty that encourages research which would make an 'impact' upon the economy/society, without worrying about the 'impact factor'.

Rethinking Cities

Presently Pakistani cities are expanding horizontally. The horizontal expansion has led to urban sprawls with several consequent problems including; residential space taking over valuable farming land, ever-widening roads, flyovers and signal free corridors, greater fuel consumption and pressure on energy systems including transmission networks.

Evidence, on the other hand suggests that the cities that allow workplace, residence, leisure, hospital, school, and shopping, etc. near each other encourage economic activity. Such cities are dense, high-rise, and mixed-use. By clustering economic activities, these cities generate knowledge spillovers and reduce transaction costs (Contextualising Pakistani Cities: Writings of Nadeem Ul Haque (Eds. Ali).

Box 4: Measures Required for Developing Cities that Serve as the 'Engine of Economic Growth'

- Vest the management of a city in a single authority.
- Do away with long-term, rigid city master plans – replace these with loose guidelines.
- Zoning should merely differentiate between city centres and suburbs.
- Relax floor area ratio to allow high-rise buildings.
- Develop a rental housing market.
- Develop a Car Policy with salient features like; congestion tolls and paid street parking.
- To allow inclusivity in cities, sell apartment parking separately from the apartments.
- Develop an efficient public transport that serves most parts of the cities, especially its dense areas.
- Look at street vending as a legal activity and establish street vending zones across the city.
- Unlock dead capital: make better use public and private property like; land, stadiums and parking spaces etc. —like; constructing high rise buildings and charging parking fee etc.

¹The impact factor of a journal reflects its relative importance within its field—journals with high impact factor are highly regarded.

A cursory look around the globe tells that in developed countries cities are configured in this manner. To grow economically, at an accelerated pace for a long enough period, we must rethink our cities in the manner discussed. To have such inclusive cities that serve as the engine of economic growth measures listed in Box 4 should be implemented.

Embracing Technology

Technology and artificial intelligence are disrupting almost every field. To be a part of the disruption and to gain from it, one must embrace technology. Embracing technology calls for capacity building and cultural change. To build capacity we must disrupt the education system to foster creativity and problem-solving skills in the graduates. This calls for staffing our universities with competent faculty and offering them an incentive structure, including career progression structure, that makes them put in effort to teach and to undertake meaningful, demand-driven impactful research—the said incentive structure will not only reward performers, regardless of age-bracket and seniority/grade but will also consistently penalise non-performers culminating in parting ways with them.

Embracing technology also calls for access to high speed uninterrupted internet to all and sundry. The ‘internet for all’ requires facilitating service providers to lay down the infrastructure required, making use of internet affordable - subsidising it where required and maybe providing it for free to the very poor. Having this kind of ambitious public policy will enormously boost economic activity and public welfare like; online education, increase in literacy, ecommerce, telemedicine and several other kinds of service delivery in rural/remote areas. Add to it the increase in benefits by allowing better connectivity to those who currently have access to internet and the payoffs of an ambitious internet access policy increase manifolds.

Box 5: Internet for All

- Make internet widely and cheaply accessible in urban centres during 2021.
- Sell Spectrum to service providers at very low rates—do not eye spectrum as a revenue source.
- Bind service providers to lay down internet specific infrastructure for provision of high speed internet and ensure access in rural/remote areas.
- Offer internet at subsidised rates/free of charge to those who cannot afford to pay for it.
- Reduce taxes on devices used to avail internet access like; mobile phones and laptops etc. to make these affordable.

A question often raised is; given present low growth base and a historical long term declining trend how a high growth rate sustained over decades is possible. This question is answered in Box 6.

Box 6: How Accelerated and Sustained Growth Rate will be Attained?

Productivity and investment are two key drivers of growth. These two are constrained in Pakistan for several reasons. Productivity can be improved by removing what Sunstien (2020) calls, 'Sludge' – excessive frictions that unnecessarily constrain an activity i.e. productivity can be enhanced by changing the way we use to do certain things. For example, if a person can deposit the fee for driving license online instead of queuing up for an hour in a bank this would save time and money which can be put to an alternate use – productivity will improve. Similarly requiring someone to personally collect a driving license, CNIC, and passport etc. if these can be delivered by post this again will save time and money which can be put to alternate use—again productivity will improve. Other examples of frictions include asking a bank account holder to present his ID card for umpteenth time while a copy is available in bank records unnecessarily imposes costs upon the account holder. The host of NOCs/approvals etc. required before a business can be launched or a building can be constructed may not be required at all or in some cases could be duplicative. Removing such frictions will add to productivity considerably.

In sum productivity will improve by amending our laws and procedures to cut down frictions involved in undertaking an activity or executing a transaction. What is needed is a thorough review of all laws, rules and processes to identify excessive frictions. The next task will be to create an environment suitable enough for amending the laws, rules and processes to remove excessive frictions.

The increase in productivity, thus achieved, will improve the return on investment leading to increase in investment and hence growth.

The investment will improve independently as well by amending laws and procedures to allow a level playing field and fostering a competitive environment— those unable to survive in a an environment which gives an advantage to a privileged few by way of e.g. SROs, will invest in a competitive environment. In a certain sectors, e.g. airlines, banking and fertiliser etc. the government is a dominant player, which by default enjoys a privileged position—exit of the government from these sectors will allow the private sector to operate—investment and efficiency would improve.

Yet another question frequently raised is; how the reforms will be implemented? This question is answered in Box 7.

Box 7: How the Reforms will be Implemented?

Reforms can only be implemented if a significant proportion of stakeholders agree that the reforms are worth pursuing i.e. the reforms, if implemented, will yield the intended benefit.

Opposition to reforms will come from two kinds of people: One, who given their belief system and experience, genuinely believe that the suggested reforms will not work. For example if those at the helm believe that centralisation as a system yields superior outcomes relative to decentralisation, then the reforms envisaging a greater role for local governments cannot be immediately implemented.

To implement reforms, first the people will have to become pro-reform. A continuous debate over the need to reform and the kind of reforms required will make people pro-reform. The three important sources of carrying out, debate are the academia (through research and discussion forums), print and electronic media and of course the now very important influencer, the social media, which despite its shortcomings still manages to convey an unfiltered view of the society at large.

Most reforms often produce winners as well losers. The would-be losers resist reform. For example if certain functions, currently being performed at provincial level were to be devolved to the local government those currently performing these functions may resist devolution despite believing in the benefits of devolution.

Historically advocacy has proved instrumental in winning over or at least taming the opposition of the would-be losers of reforms. To create a pro-reform lobby debate over reforms will have to be supplemented with strong advocacy to make a case for reforms.

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