Lectures in Development Economics
No. 10

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A CASE STUDY OF PAKISTAN

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First Edition.

ISBN 969-461-090-7

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PREFACE

Large macro imbalances, policy distortions, and weakening of the institutions have emerged as major development constraint to achieving and sustaining a high rate of growth. Pakistani government has negotiated more than a dozen stabilisation and structural adjustment programmes with the international financial institutions since 1980. The high growth momentum achieved during the 1980s faltered during the current decade. The drastic slow-down in the economic activity and the persistence of large current account and fiscal deficit have resulted in a substantial increase in the incidence of poverty as well as the inability to meet the external debt servicing obligation.

Ishrat Husain addresses the issue of what went wrong with the reform programme of the Government of Pakistan. He draws upon his rich experience of the implementation of adjustment programmes in many countries and proposes certain yardsticks to assess the nature of critical reform ingredients, the timing and sequencing of the reform components, and their timely implementation. From the political economy perspective he argues that reforms are not always carried through logically and, consequently, the reform process gets stalled due to opposing political interests if the losers outvote and outvoice the prospective winners on account of different reforms. The domestic ownership of the adjustment programme and the existence of implementation capacity are the two critical pre-conditions for success in the implementation of a reform agenda.

Ishrat Husain explains the reform impasse in Pakistan in terms of weak ownership and limited implementation capacity within the government. The policy-makers in Pakistan would benefit from the timely and pertinent contribution made by Dr Husain.

Sarfraz Khan Qureshi

INTRODUCTION

The broad literature on structural adjustment and economic policy reforms often falls into the habit of making wholesale judgements of the sort: "adjustment does or does not work because..." And, not surprisingly, the vast majority of this writing tends to view adjustment negatively. Not only are we thus subjected to holistic assessments of structural adjustment, we are also subjected to universalistic explanations. These criticisms encompass the whole spectrum of ideological predilections ranging from the left, which considers neo-liberal policies underpinning these reforms as pure anathema, to the libertarians, who consider any form of government intervention as repugnant to individual freedom. In addition, there are non-ideological critics too. Ayittey (1994), for example, denounces the World Bank for its support of adjustment programmes which he claims do not take account of political and social realities in Africa, and embody a host of other evils.

These wholesale views both of the relative success or failure of adjustment policies and of its causes are definitively challenged by a number of empirical studies. These studies demonstrate (1) that there is considerable variation in the economic results of adjustment programmes, and (2) that this variation is explicable in terms of the content, quality and sustained application of adjustment policies.

Author's Note: The views expressed in this paper are those of the author and do not necessarily reflect the views of the World Bank, its management or the staff.

The key questions which arise, therefore, are: If these policy reforms are associated with such high pay-offs, then why are these reform programmes not sustained and implemented consistently? Why are they derailed? Why is the record so poor in the case of Pakistan?

The determinants of sustainability of economic reforms cover a wide range of variables—initial conditions specific to each country; design, content and sequencing of reforms; ownership and political commitment, particularly from a strong, visionary leadership; administrative and implementation capacity; the conditionalities of international financial institutions and external donors; and unanticipated external shocks.

In studying the case of Pakistan there are added complications as the country moved from military rule to a democratically elected regime during the period of economic reforms. In the initial years—1988 to 1990—there was an uneasy fear of the re-emergence of military rule and hence the first democratically elected government was constricted by the various compromises it had to make in order to keep the Army off its back. Political survival was the key preoccupation. The subsequent elected governments had to live in the shadow of the constitutional provision introduced by the Zia regime empowering the indirectly elected president to dismiss the parliaments and the elected prime ministers. Invoking this provision, before they could complete their tenures, three elected governments were dismissed between 1990 and 1996. Since 1988 Pakistan has had four elected governments and four caretaker governments.

The second and the third elected governments did not have clear majority and had to form coalitions and alliances with disparate groups which had nothing in common except the motivation to remain in power. The survival instincts, therefore, overwhelmed the urge to make tough political decisions on the economic front. The element of political uncertainty and instability, exacerbated by the threats of floor-crossing by small splinter groups, the Sword of Democles of the presidential power to dismiss the government, and different political parties holding offices at the centre and the provinces did not create conditions conducive to strong political will or resolve to deal with key structural reforms in the country.

Under such circumstances, it becomes extremely difficult to disentangle the strength and magnitude of each of the variables at work. A more tractable approach is to group these variables together and analyse the contribution of each group separately, assuming that the appropriate functional form of relationships is additive and the interactive terms are at best weak or insignificant. The question of design, content and sequencing of reforms, and the specific initial conditions have been analysed in a number of earlier studies in Pakistan and by the World Bank and the IMF and is, therefore, not the focus of the present inquiry. This paper focuses on the political economy aspects of sustainability of economic reforms by introducing three basic hypotheses, and testing these hypotheses with the evidence from Pakistan.

The political economy of adjustment has become a burgeoning area of interest in the literature drawing on the inter-disciplinary tools of analysis and cross-country comparative perspectives. Several useful insights have been gained through this body of research. [See, Nelson (1990); Haggard and Kaufman (1992); Thomas and Grindle (1991);

Callaghy and Ravenhill (1993); Bates and Krueger (1993); Husain (1994) and Webb and Haggard (1994).] This literature can be roughly classified within three broad categories or approaches to the sort of questions we have posed.

The first of these focuses on external causes of economic stagnation. Although not inherently a topic of singular interest to the political left, the analysis of external causes sometimes appears to have become the monopoly industry of neo-Marxist thinkers. Despite variation in emphasis and approach, writers such as André Gundar Frank, Paul Baran, Walter Rodney, and Samir Amin all began from the unquestioned assumption that Third World underdevelopment stemmed from the prolongation of imperialist domination, via metropolitary power to manipulate markets and capital flows, into the post-colonial era [Ruccio and Simon (1992)]. While the end of the Cold War, coupled with the highly visible success of the East Asian economies, has cooled the ardour of dependency theorists, a variant of this line of reasoning lives on in a "Third Worldist" critique of the International Financial Institutions.

As a large number of critics have pointed out, the trouble with theories that place entire causal weight on external factors is that they neglect the dynamics *within* developing countries that might account in a very large measure for their growth or stagnation. Thus, a number of analysts have focused attention on the state and its political motives in guiding national economies toward growth or decline [Skoupl *et al.* (1986)].

Yet another major approach in political economy that relates to domestic causes of policy change stems from the pioneering work of Mancur Olson [Olson (1962)]. This vein of thought focuses attention on the power and motives of social collectivities or interest groups in influencing the state in ways that may impede economic growth. Writing in this tradition, Haggard and Kaufman (1992) posit that economic policy change is plagued by numerous collective action problems. Stable prices can be viewed as a public good, but individuals and firms can gain from policies that undermine stability and might be reluctant to bear the costs of stabilisation if others do not do so as well. Similarly, trade liberalisation or state enterprise reforms can generate overall efficiency gains, but individual firms or sectors will lobby to retain particularistic benefits. This literature is less clear on the how's and the *process* of managing the transition from a state of undesirable and distorted economy to a desirable and sustainable path. The uncertainties about the likely impact of various policy actions, and the gaps in information and knowledge about the responses of the diverse groups of economic actors under varying political regimes, make this an extremely difficult task.

THREE HYPOTHESES

We draw on all these schools of thought in formulating the following three hypotheses about the sustainability or otherwise of economic reforms and test these hypotheses by using the evidence from Pakistan.

Hypothesis 1: Variation depends on a set of initial conditions which precipitate the decision to undertake adjustment programmes. These conditions can be systematically identified in the realms of economics, local politics, and the approach of international donors.

The above conditions can be grouped in three categories:

(i) *Whether economic conditions are desperate or not.* When economic conditions have reached a complete collapse, then countries consider that the benefits from adjustment policies are likely to exceed the costs compared to the existing or other alternative strategies. The genuine commitment to initiate reforms in such conditions is expected to be stronger there than in countries where the economic decline is not perceptible.

(ii) *Whether economic interests are strongly or weakly organised, and whether they have previously established a degree of leverage over the state in its power to distribute appropriable rents.* Where economic interest groups of a rent-seeking character have such power over the state, then adjustment programmes may be implemented superficially, based on negotiations of the sort that Callaghy and Ravenhill (1993) has referred to as the "ritual dance" of African finance ministers before the International Financial Institutions (IFIs)—but which is not coupled with real commitment to overriding local interests.

(iii) *Whether leadership is committed to reform.* The quality and devotion of leadership to reform is an overlooked variable, and cannot be reduced to the nostrum "political will". It may prove to be critical whether leaders fully understand the need for adjustment, and whether they feel ownership.

Hypothesis 2: Variation depends on the country's sense of "ownership" of the reform process, which may be defined to include two basic elements: (1) Consensus among the social and political organisations that constitute national civil societies; and (2) the presence of a technocratic core group in government that is truly devoted to the reform process.

"Ownership" is presented as a hypothesis separate from that of initial conditions, because it may be possible to develop ownership after the initiation of reforms. Oftentimes, this takes place at the initiative of governments, who hold public discussions and debates involving trade unions, opposition political forces, community organisations, businesses, and so on.

Hypothesis 3: Variation depends on the presence of "capacity" in a given country. Capacity is defined as human capital and the resilience of institutions. The East Asian economic miracle shows the utter necessity of having in place the individuals capable of identifying, planning and implementing policy. This implies also strong civil service institutions, and norms and regulations which prevent political interference in the work of policy units.

We examine below the evidence in case of Pakistan to test each of the three hypotheses:

(a) Why did Pakistan decide to undertake adjustment programmes? (b) How broad-based was the ownership of these programs? and (c) How effective was the capacity to implement?

WHY DID PAKISTAN DECIDE TO INITIATE ADJUSTMENT PROGRAMMES?

The decision to initiate these programmes is reached—though not always consciously or deliberately—when the costs of continuing with existing policies exceed the net benefits that can be realised by pursuing adjustment programmes. One of the main elements in this calculus is the expectation of external resource availability from the IFIs and donors and the prospects of debt rescheduling in future. *The net benefits* can be conceived to consist of two components—first, the expected external resource availability including debt relief, and, second, the likely improvement in the domestic economic performance such as increased domestic savings, rise in export earnings, investment and output growth etc. Although the separation may not always be that sharp, this analytical distinction provides a useful way to examine the questions of ownership and commitment.

In countries where the decision to embark upon the programme is driven primarily by the considerations of the first component of the benefit stream, the implementation remains highly fragile, adversarial, and conditionality-ridden. There are two variants of this trend. First, there is a bargaining game in which the recipient country tries to extract maximum amount of resources with as little change in policies as it can get way with, and the IFIs and the donors placing as many conditionalities as possible and 'tranching' their releases of funds on pre-specified actions in policy changes. The second variant is that the IFIs themselves take the initiative, on the basis of their own analysis, to persuade and convince the countries about the need to undertake reforms.

Where the driving force is a genuine desire to bring about some improvement in the domestic economic performance, i.e., the second component of the benefit stream, the chances for sustained progress are bright. The ownership and commitment in this case are high, while the main tactic under the former case is to substitute adjustment by external resource inflows and delay *taking tough decisions* which may have negative political repercussions.

The first ingredient of the first hypothesis is the willingness to initiate comprehensive and radical reforms and is more likely to surface in countries where the economic system has failed or collapsed and the conditions are desperate. Pre-emptive reforms designed to ward off the disastrous effects of unsustainable fiscal deficits or to raise mediocre rates of growth will encounter greater resistance. The semblance of an orderly and apparently functioning economic system, but ridden deep down with serious distortions, may lull the craving for reforms.

The main motivation for entering into adjustment programmes in case of Pakistan has consistently been the short term foreign liquidity infusion by IFIs and other donors and *not* the desire for longer term structural change. Economic conditions have never been desperate or the crisis has not assumed such an alarming proportion that the rulers had to take strong corrective measures such as were necessitated in Mexico, Indonesia, etc., in 1994 and 1997 respectively.

In the 1970s, when Pakistan was shaken up by the separation of East Pakistan, oil price shocks, and the nationalisation policies of ZA Bhutto's Government, the current account deficit had reached about 10 percent of GDP. The generous assistance from the OPEC member countries and the home remittances from the migrant workers in the Middle East came to the rescue of the country avoiding a hard landing.

In 1993 when the Nawaz Sharif Government was dismissed the external reserves had dipped to $300-400 million level, the interim Government of Moeen Qureshi negotiated a deal with the IMF and a shot in the arm was provided. The Benazir Bhutto Government had led the country in 1996 to the same precipitous situation but the caretaker government, by various kinds of borrowings and deposits of the friendly countries, was able to service the external debt on time. It must be said to the credit of both the Moeen Qureshi Government and the care taker Government of 1996 that they had initiated some strong reforms but these could not be sustained by the subsequent incoming elected governments.

The most severe crisis occurred in the aftermath of nuclear bomb testing on May 28, 1998. The seven month period upto the approval of the IMF programme in January 1999 was a period of real trial and tribulations and the closest the country came to the brink of default. A freeze on the foreign currency accounts, postponement of all external payments except to preferred creditors, inflows of deposits from a few friendly countries, forced decline in imports and fall in world prices of oil and other commodities, roll over of swap funds and accumulation of the arrears enabled the country to avoid the default but also caused a grievous shock to the credibility of the economic policies. It will take quite some time of consistent good management that private investment will revive. Availability of adequate food supplies in the country and low prices of imported commodities did save the country from inflationary pressures arising from a free fall in the value of the currency and the attendant volatility. The life of the ordinary citizen was not so harshly affected. Most of the hue and cry came from the élite this time who had converted their rupees into dollars and the freezing of these accounts hit them hard. But as this class gets hardly any empathy from the general masses the social consequences of the economic chaos remained limited and the prophets of doom and gloom were proved wrong.

Thus, unlike many adjusting countries mainly in Africa, East Asia or Latin America, Pakistan did not cross the minimum threshold of generalised suffering and misery over an extended period of time. Neither did the economic indicators such as economic growth, inflation, shortages of essential food items, insolvency of the banks etc. take a deep and sharp plunge. The absence of these perceptibly desperate conditions did not force Pakistan to adopt tough adjustment measures. Only limited actions were taken to win the approval of the IFIs and the external donors. But the discussion at the IMF and the World Bank Boards in January 1999 has revealed that this approach of soft options is no longer going to work in the future. Why? It cannot be that the IFIs are disappointed by the survival characteristics of the Pakistan's economy. Or is it that the Boards feel they have been taken for a ride!

The second ingredient associated with the launching of adjustment programmes is the relative strength or weakness of the dominant interest groups in the country. A study of political economy of reforms has aptly summarised; "Policy reforms have redistributive consequences for different groups which organise to protect their incomes and rents. Politicians respond to the constituent pressures because they seek to remain in office and they exchange policy distortions for political support. The fate of any reform effort thus hinges on the political balance of power between the winners and losers in the reform effort".

The distribution of the pains of adjustment is always highly skewed. The rent-seeking and privileged classes had already accumulated sufficient wealth, taking advantage of policy distortions in the period before adjustment and, thus, freeing themselves from the pains involved. But the rest of the society suffers in the immediate aftermath of adjustment programmes as food subsidies are eliminated, imported goods become expensive, real wages decline, and public sector employment is either frozen or cut down. Political leaders, whether elected or authoritarian, are hardly able to fathom this situation. This time inconsistency issue has been analysed in understanding the behaviour of economic agents and is equally applicable to political actors. Unless a *new domestic constituency* in support of the reforms emerges, the pressures from the rent-seeking and privileged élites, who are losers in the long run, would remain intense. But there is insufficient understanding as to how new coalitions of the potential beneficiaries of the reforms—small traders and entrepreneurs, informal sector and rural population—may be built.

The absence of a large scale and deep crisis in Pakistan was accompanied by the presence of strong vested interests organised around the ruling classes. The proposed structural adjustment reforms would have reduced the opportunities for rent-seeking and discretionary favours, brought those evading taxes under the tax net, forced the defaulters of loans to liquidate their assets to repay and stop the theft of power and gas. Import liberalisation and tariff reduction would have hurt the highly protected industrial enterprises. Value-added tax and documentation of the economy would reduce the economic returns of the traders and professional classes. Agricultural income tax and increase in irrigation water charges would diminish the unearned incomes of the landed gentry. Privatisation of state owned enterprises and reform of administrative system would threaten the powers of the civil servants and the managers of the enterprises along with the organised union leaders. Reform of financial sector would no longer allow the political leaders to dispense loans to their favourites and supporters. The delivery of social services by the NGOs, private sector or regulated by communities would no longer enable creation of employment opportunities which can be traded by the MPAs and MNAs.

It is obvious that every single economic reform, if implemented credibly, would turn the tide against the vested interests of the élite class. And as these classes are responsible for the design and implementation of the reforms, no wonder the track record of implementation has remained so poor for such a long period.

This leads to *the third ingredient* under the first hypothesis, i.e., the quality and commitment of top political leadership. The reason for the domination of the vested interest group of actors arises primarily from the lack of commitment to long-term development and the absence of a clear vision by the top political leadership of the direction in which the country should be moving. If there was such a long-term framework and vision of the future, it would become clear that economic reforms are only one of the several elements necessary to attain the long term development goals. Leaders who are too preoccupied with fighting day-to-day crises and have limited mental horizons consider economic reforms—quite understandably—as irritants and external impositions without realising their links with long-term development. For them, the political costs of these reforms are paid upfront when they have the responsibility, while it is not obvious if they would be in power at the time when benefits start accruing. A leader with vision of history rather than a politician unable to lift his sights beyond the next elections is more likely to provide the support and commitment to reforms.

The entanglement of successive political leadership with the élite class coupled with the fragility of the political system that was being re-established in the post Zia period do not make it very easy to tease out the commitment of political leadership to these reforms from other intervening variables. Both Benazir Bhutto as well as Nawaz Sharif were quite supportive of economic reforms in their public pronouncements and their policies, on paper, did not look much different. The actions taken by Benazir Government in attracting foreign investors to the power generation sector and by the present Government to set WAPDA on the right track do speak in favour of the commitment to reforms but such examples are few and far between.

A longer view of the situation does however show that the commitment has been uneven at best in terms of results. Each successive government has started with a programme of privatisation, liberalisation, deregulation, budgetary deficit reduction, export promotion, financial sector restructuring but the results and outcomes have been disappointing. All big loss makers among the public enterprises such as WAPDA, Steel Mill etc. continue to weaken public sector finances. Import tariffs are still high although they are lower than the past levels. Worse, the discretionary powers of issuing the SROs have been flagrantly misused. The formal and informal stranglehold of the state apparatus on private business decisions remains unscathed creating unpredictability in the rules of the game. Multiple taxes, charges, cesses, levies at various levels of the government have added to the extortionary powers of the state functionaries. Attempts at deficit reduction have been made without initiating the underlying changes in the revenue and tax system and at the expense of reduced development expenditure. Export base remains narrow and growth seems to have tapered off in recent years. The major nationalised banks and DFIs still dominate the financial markets.

The above outcomes do attest to the lack of both commitment and credibility of the political leadership of all persuasions over an extended period of time. The pressures of keeping coalition partners happy to retain power may have softened the resolve in the past but the large mandate given to the present government, the elimination of the Eighth amendment to the constitution and the withdrawal of the army chief from effective decision-making role do provide an excellent opportunity for bringing about genuine structural reforms in the country.

HOW BROAD-BASED WAS THE OWNERSHIP OF THESE PROGRAMMES?

The earlier World Bank studies of adjustment lending have concluded that the chances of success are higher if there is ownership of the programme by the country. These findings also corroborate Kahler's (1992) earlier work which showed that prior commitment and policy action (taken before external support is offered) are a good predictor of successful implementation. Successful influence is more likely if governments commit themselves to an adjustment programme and only then are supported financially by the IFIs.

The meaning and definition of ownership have, however, remained fuzzy, despite the World Bank's OED's (Operations Evaluation Department's) attempt to elaborate on the definition of ownership and its application to the World Bank's own lending experience for adjustment in Africa. There are several other practical problems. First, what is the appropriate time path for strengthening the ownership? If the reforms produce fairly early pay-offs, does this help strengthen the ownership or slow the pace? Neither theory nor evidence provide any guidance to answer these questions. Second, the stability of the government itself is equally critical. If the governments keep changing rapidly, it is difficult to establish ownership. A third problem is that the economic generosity of the donors, in so far as it results in a soft budget constraint or allows the governments to postpone taking tough decisions, may also slow down the progress towards owner-ship. Finally, at the intellectual level, there are still remnants of ideological resistance to "market friendly" paradigm of development which underpins the adjustment policies. The neo Marxian, "dependency" school of thought, anti-colonialists and others, who genuinely believe that the "markets" are anti-social, create inequities, hurt the poor and are repressive, still command considerable influence particularly among the non-economists. There are well-meaning scholars who fear that *integration in the world* economy is beset with disastrous consequences as poor developing countries cannot compete with the rest of the world.

The extraordinary and more visible influence, or in popular jargon, the "imposition" of the World Bank and the IFIs in the conceptualisation and design of the policy changes, has also affronted a number of serious scholars and policy makers and, in some cases, strengthened opposition to otherwise sensible economic policy changes. Many academics, practitioners and private sector groups may broadly concur with the basic policy thrust of these programmes, but they find it annoying that their advice and analyses on the same lines are ignored by their own governments, while the same governments follow the IFIs without any questioning. This group of potentially natural allies for ownership of economic reforms has either distanced itself or joined the opposition. This nationalist sentiment can, in fact, be harnessed to enhance the ownership of the programmes rather than leading to alienation.

"Ownership" should not be construed in a very narrow sense, i.e., of the government in power, or, more specifically, the economic team of the government consisting usually of the Finance Minister, Governor of the Central Bank, Secretary Finance and their staff. Ownership should be much more broad-based, with a shared vision and a sense of direction in which the economy is to move. In the absence of clarity of goals and objectives, agreement on the time path required for achieving these goals and the open discussion and debate about the various trade offs required to achieve these goals, it would be difficult to mobilise support from other socio-economic forces in the country such as private businesses, professionals, political parties, NGOs, students and labour unions. The assumption that external approval from donors or IFIs will persuade or generate a commitment to economic reform is unlikely to prove valid.

Open discussions and debates, communication and interaction among diverse parties and groups are the only feasible ways to enhance the acceptability of the programmes.

Trade Union leaders in particular have often made the point that, if they were duly consulted, explained the rationale and justification for various policy measures, and informed about the likely consequences and objectives, they would be in a better position to make a healthy and constructive contribution to both the diagnosis and the required prescription.

It is also conceivable that ownership and commitment could be associated with some select elements of adjustment programmes, while other elements of the programmes that are not perceived to have popular support may lack ownership. The implementation capacity may therefore vary under those circumstances, with the non-controversial elements of the package moving forward rapidly while others being pulled back.

Academic literature, on the issue of participation, seems to make a distinction between two different stages of the design and implementation of policy reforms. At the first stage, the executive authority must be firmly convinced of the necessity for economic stabilisation and liberalisation, for without such a commitment, the leadership will be unlikely to forge ahead with stringent recovery programmes. As the initial stage usually involves changes in the incentive structure by altering key relative prices—the exchange rate, producer prices, interest rates, price decontrols, removal of quantitative restrictions—these can easily be carried out by a select group of competent and responsive civil servants. The reforms need to be embedded in solid technical analysis and can, therefore, be entrusted to a small group of technocrats.

The problem usually arises when the second stage of reforms is proposed for implementation-downsizing the civil service, reducing consumer subsidies, closing down, commercialising or selling public enterprises, restructuring the financial sector, exposing industrial firms to competition, etc. During this phase, broad-based consultation and interaction with those likely to be affected by these measures can result in finding alternative and mutually acceptable solutions, and agreeing on the timing of actions. Listening to the genuine concerns of those who will be potentially hit by the reforms, and taking these into account at the time of designing the programme, will facilitate implementation later on.

But the limitations of this participatory and consultative approach should also be recognised. The technical nature of the issues is bound to keep the discussion to a much smaller audience of educated and well informed groups and individuals. It is quite likely that the debate and consultations could end up making concessions to this "participatory" group at the expense of a much larger segment of the population. Public policies have been pro-urban in developing countries historically, with only a few exceptions; subsidies intended for the poor have been hijacked by the well-to-do and the political influence of the rentier class has been disproportionately strong. The urban class, media, large private businesses, trade unions and academics still favour rapid urbanisation and industrialisation at all costs as the preferred model for solving economic problems, although their rhetoric and justification for this model are couched in terms of helping the poor, the unemployed and the socially-disadvantaged groups.

In a country with a free and vocal media, and with an articulate intelligentsia, it would have served well if the Government had carried out a more intense process of consultation and communication, and used the feedback either to modify the elements of the programmes that were resented most or to explain the rationale and consequences candidly. It is not always easy to convince the public at large about the need to reduce subsidies, but a candid and frank analysis of the beneficiaries and losers from abolition of subsidy would have certainly helped.

In case of Pakistan, there is no single constituency which seems to identify itself with reforms. As discussed above, the strong élite classes find these reforms threatening to their immediate interests. The political leadership considers them as irritants which constrain their populist instincts to spend money. The media have begun to play a useful role by raising questions, reporting indiscretions, asking for more information but the standards of economic journalism leave much to be desired. But what is really missing is the broad based participation of various groups and constituencies which are likely to be affected directly or indirectly by the reforms in the process of formulation of policies. Until recently, the agreements negotiated with the IFIs were kept secret and the contents were not disclosed even to the Parliament. The NGOs and advocacy groups are becoming increasingly involved in policy discussions in the recent years. The process of formulation of the environmental law is a good example of participation of the stakeholders in the policy making. But this kind of interaction is still not common *and* the scene is still characterised by mutual suspicion and distrust among the bureaucrats who would like to keep the matters closed from public scrutiny and the members of the civil society who start with the presumption that all actions of the civil servants and politicians are malafide. There is little doubt that the open, transparent, participatory methods of policy design and implementation do help in generating the desired results.

Another interesting question that needs to be explored in the context of ownership is: Is there a tension between conditionalities of external donors and the country's ownership of the programme?

First of all, why should the donors use conditionalities to enforce implementation of reforms by the recipient countries? The debate on this issue is highly complex, but we will provide one explanation that has been put forward by Collier (1991). He thinks that one fundamental change in Africa's external economic relations since 1960 has been the lack of "agencies of restraint"—the institutions which protect public assets from depletion, prevent inflationary money printing, prevent corruption, protect socially productive groups from exploitation, and enforce consensus. For such agencies to function effectively, they must be protected from the pressures and strengthened as to the principles they are designed to uphold. He hypothesises that because African presidents typically could not tolerate autonomous centres of power, the donors have become the new agencies of restraint. These agencies use "conditionalities" as instruments of restraint.

A different perspective is provided by Herbst (1990), who argues that "There is, in fact, every reason to believe that without dramatic external pressure, poor economic policies in African countries will continue". He worries that "should assorted proposals alleviate the debt burden of even the poorest countries, there may be a strong temptation on the part of African leaders to reduce the pace of economic reforms". Both these views underpin the donor conditionalities that have been subject of debate and controversy within and outside Africa. The literature on the donor conditionalities specific to the case of Pakistan is relatively thin and therefore the arguments are drawn largely from the African experience.

There is ample justification for both types of arguments to apply to Pakistan. The absence of strong domestic agents of restraint calls for external agents and it is expected that this external pressure may help bring about good economic policies. The matter of fact, however, is that external influences are not only strongly resented but have also not been particularly successful in turning the policy regime around in the right direction.

The tension between "ownership" and "conditionalities" can arise when the recipient country agrees to undertake actions as part of the conditionalities under the World Bank loan and/or the Fund arrangements or donor programmes, and the loan conditions are either inappropriate to the economic context of the country or the country has no real intention of complying with those conditions.

Mosley (1991), in their study of nine countries receiving adjustment loans from the World Bank, illustrate this point by matching the commitment of reforms favoured by the World Bank with the actual implementation of the loan conditions. The zero or partial implementation indicates low commitment, while full implementation indicates high commitment. But they also find that there are two other cases. First, there are cases where full implementation of a loan takes place but the commitment is low. This is the case where all formal conditions are scrupulously performed but, at the same time or shortly afterwards, other actions are taken the effect of which is to neutralise the result of implementing the original condition. The other situation arises when loan conditions are not fulfilled but commitment to reform is high. The authors hypothesise two causes for this deviation. The first concerns trivial conditions—other too broad in scope or peripheral—a matter of detail such as the hiring of consultants, the design of a minor study, etc. Second, when the required conditions are infeasible or improbable

If we apply the methodology used by Mosley (1991) to the case of Pakistan the generalised conclusion one can draw is that there was only partial implementation of loan conditions with low degree of domestic ownership and commitment. The frequent breakdown of the programmes, incomplete reviews, large number of waivers granted by the IFIs all do confirm this conclusion.

HOW EFFECTIVE WAS THE CAPACITY FOR IMPLEMENTATION?

Aside from the interest groups and political economic considerations which we have discussed above, the most critical missing element in most developing countries is the implementation capacity not only within the government but, more broadly, within the civil society. The slow accretion of the right skill mix, the dilution and depletion of the stock of already trained and experienced professionals through migration, and the non and low utilisation of existing capacity for professional work characterises Pakistan. The excessive dependence on foreign technical expertise, the donors' own disposition to employ outside consultants to design the projects and set up new implementing agencies outside the normal governmental machinery and the penchant of the political leaders to find "loyalists" rather than the "competent" among the civil servants to head these donor-assisted projects, have contributed to the existing state of poor capacity.

Even if there was political commitment and willingness, it is doubtful if the desired changes can be brought about due to this capacity constraint. The combination of competent technocracy and reasonably enlightened and popular leadership is rare to find in most reforming countries.

As implementation capacity is, by and large, weak in most developing countries, the distinction between "capacity saving" and "capacity using" reforms becomes important. As we have argued earlier, the first phase of reforms, which alter the relative prices, liberate the capacity of key government officials and, hence, are implemented fairly rapidly once consensus is reached. The other set of reforms that entail more deep-seated change are highly demanding on the limited administrative capacity of the government officials, and broad-based participation of other groups can also help the process of implementation.

We believe that capacity is also endogenous to the ownership, commitment and a sense of long-term strategic vision and direction on the part of leaderships. In Korea, when President Park, who had a clear vision of the direction in which Korea should move, decided to promote exports, he assembled a team of the most competent civil servants and entrusted the task to them. The President personally reviewed and monitored the situation and allocated rewards and penalties on the basis of performance in relation to the agreed targets. This mode of intervention soon had a salutary and positive impact on other civil servants, who wanted to demonstrate that they could also do the job equally well. Capacity building in this case was the direct result of commitment and ownership by the top political leadership in the country.

In our view, implementation depends not only on a set of technocratic measures that can take place by the acts—decrees and orders of civil servants—but also on the capacity to manage the political support for these measures. The upfront identification of winners and losers from the various reforms has to be an integral part of the feasibility of structural adjustment programmes. There is a diverse array of subgroups and interests within the government itself that will react differently to various reforms. For example, public enterprise managers would oppose reform if it involves closing down or retrenchment. Ministries charged with revenue collection and fiscal balances would respond favourably if a reform package added significantly to available budget resources.

Civil servants might respond negatively to pay scale reform and cut back in employment levels, but they might be deterred from opposition if a reform lessened or removed legal restrictions on their private economic activities. As Haggard and Kaufman (1992) point out "For governments to reduce their role in the economy and expand the play of market forces, the state itself must be strengthened". On the one hand, economic liberalisation entails the curtailment of powers of the state through privatisation, deregulation, elimination of central planning and reduction in the work force. The ensuing uncertainty, lower real wages and lack of job security de-motivate the civil servants and, in some cases, lead them to leave the public service. On the other hand, the tasks of the government to design, implement and operate myriad components of the structural adjustment programme, maintain and operate a framework of macroeconomic policies that provide incentives to the private sector, resolve the structural problems, and mediate conflicts within the civil society, would demand scarce technical and administrative skills. If the civil servants have lost their zeal and motivation, the required technical and administrative skills will not be available to lead the implementation of reforms.

The absence of a strong development-oriented visionary leadership fully committed to economic reforms, and the dilemma outlined above have worsened the implementation capacity problem. The process of reforms should be conceived and presented in the context of long-term development vision. But in the absence of such a vision, the process is overtaken by considerations of political and administrative expediency. Thomas and Grindle (1991) argues that because of the absence or weakness of pluralist institutions that mediate between society and the state, the implementation process may be the major arena in which individuals and groups are able to pursue conflicting interest and compete for access to scarce resources. This conflict finally gets resolved through the mechanisms of patronage and opportunities of self enrichment in which the civil servants play not a restraining but a facilitating role for the political leaders in power. As Sandbrook (1993) shows, the administrative decay in Africa is rooted in the pervasive clientelistic nature of politics pursued by most African "presidential-monarchs," who treat the public administration as their personal property. According to Bendix (1992), these public officials, in patrimonial fashion, then "treat their administrative work for their leader as a personal service based on their duty of obedience and respect". Unless fundamental restructuring and professionalisation of the civil service takes place in these countries, the prospects for building implementation capacity will remain bleak despite donors' efforts and external pressures. The whole structure of governance needs a thorough re-examination and overhaul.

One of the strong assets in Pakistan had been the tradition of a merit-based, competent, technocratic public services structure inherited from the British colonial days. Until 1973, the insulation of civil servants from political interference, the security of tenure, and promotions based on seniority had made the public service an effective tool of good governance. The subsequent actions of lateral entry, nominations based on political loyalty rather than competence, removal of constitutional guarantee on the security of service, blatant interference by politicians in the appointments, transfers, and postings of officers of their choice have transformed the character of the public service. This has taken a heavy toll on key economic policy and decision-making institutions of the country. The Planning Commission along with the Provincial Planning Departments, the Ministry of Finance, and the State bank of Pakistan were soon bereft of professionals in their respective fields. They were substituted by amateurs who were loyal to the party in power. The technocrats who still possessed courage of conviction and expressed their professional views and opinions without mincing words were soon sidelined. The message to the rest of the bureaucracy was loud and clear—either shape up and tow the party line or ship out as OSDs*. The gradual erosion of a technocratic group that was really devoted to the reforms and could manage them competently led to the ascendancy of external actors, particularly the staff of the IFIs. The

*An OSD is an Officer on Special Duty in the Government of Pakistan who retains his seniority in the respective cadre but is deprived of any specific post or powers in the system—usually the least desired position.

ungrudging acceptance of various conditions prescribed by the IFIs by the new crop of pliant bureaucrats who neither challenge their assumptions or validity nor show any skills in implementing these programmes has resulted in the loss of credibility for Pakistan.

A comparative study of 17 countries by Nelson (1990) has concluded that the cases of clear failure all traced collapse in large part to deeply divided economic teams. In Pakistan, this indeed has been the case. Most of the time the members of economic team have been fighting each other and giving mixed and contradictory signals to the IFIs in their negotiations.

Related closely to the loss of a technocratic core group in government, which is capable of designing an appropriate set of reforms in a properly phased and sequenced manner, is the overall capacity of the institutions in the country. In addition to the macroeconomic management, which resides with the Ministry of Finance, State Bank, etc., we are concerned with each sectoral ministry, public corporation and the attached departments, the provincial and local governments, the judicial bodies, the parliament and provincial assemblies, the private sector, the NGOs, and other civil society organisations.

There is now a general agreement among virtually all segments of society that we have suffered terribly as a country by the decay of these institutions. The selection of wrong people to top positions, lack of delegated authority, highly centralised and personalised decision-making, and absence of accountability for results have weakened the institutional capabilities. Detailed preparation and cumbersome approval process combined with fairly lengthy period of implementation have invariably resulted in cost overruns of the projects and reduction in the expected benefits.

Insulating key parts of the bureaucracy from political pressures has worked well in many East Asian countries but this can serve the cause of reform if the bureaucrats are technically capable of designing and carrying out the measures themselves.

A number of empirical studies do suggest that there is some urgency to put in place measures during the process of implementation that will neutralise the losers from the reforms and find ways to cushion them from abrupt and large shocks. For example, spreading ownership of public enterprises to workers and the middle class could reduce the opposition to parastatal reform. Similarly, involving civil servant groups in civil service reform could win their support. At the same time, the potential winners will need to be mobilised to keep up the pressures for staying on course. Widner (1994) argues that, in East Asia, liberalising economic reform was a consequence of more or less explicit "deals" negotiated between leaders, technocrats and the heads of the networks or groups that structure political life. These compromises insulated policy making in the short- and medium-term. But in the multi-ethnic and fragmented politics of Africa, striking such compromises has proved more arduous.

While neutralising the losers from the reforms is in practice problematic, building coalitions of winners from the reforms is even more difficult. The problem is particularly severe when, for example, as in the case with trade reform, the gainers (e.g. consumers) are many, but each gains a small amount, while the losers (e.g. textile workers) are few, but each loses a large amount. In most other cases of reforms, typically the costs are in the present and very certain, but the benefits are in the future and uncertain. This makes the task of building coalitions of winners arduous.

CONCLUDING OBSERVATIONS AND LESSONS FOR THE FUTURE

Pakistan has not been a successful example of implementing structural reforms although the country has entered formal programmes of adjustment with the IFIs on five or six different occasions in the past decade and more than a dozen times since 1980. This paper has demonstrated that the two variables generally correlated with success, i.e., domestic ownership and capacity, were found absent in this case. To recapitulate:

(a) The main motivation underlying these programmes was not longer term transformation of the economic structure but short term injection of liquidity to avert foreign exchange shortages and replenish reserves. Adjustment was thus taken as a purely short term palliative measure to buy time rather than an opportunity to introduce much desired policy and institutional changes.

(b) The vested interest groups which were likely to lose out from these reforms, if they were implemented seriously, had strong political and economic hold on the decision-making process under every elected government. They were therefore instrumental in ensuring that only some cosmetic changes were made to obtain foreign funding and then go ahead with business as usual.

(c) The leadership in Pakistan during the last decade remained preoccupied mainly with the challenges of retaining power in the face of a vigilant military oversight, building political coalitions and alliances and thus sticking to the lowest common denominator acceptable. It is only after the 1997 election that Pakistan has witnessed a government enjoying clear cut majority and the demise of the troika consisting of the President, Prime Minister and the Army Chief of Staff which held the real power.

(d) The reform packages have never had a broad ownership even within the Government apparatus. These were designed mainly by the IFIs and negotiated by a narrow technocratic group drawn from the Ministry of Finance and the State Bank with the blessing of the Prime Minister in office. At no occasion, except for the most recent agreement, the contents of the agreement were discussed with the Parliament or disclosed to the general public.

(e) Finally, the quality of human capital and the resiliency of institutions—the two essential ingredients required for domestic capacity to implement these reform packages—has badly eroded over time. Leaving aside the narrow, small technocratic group at the centre, the ministries, corporations, autonomous bodies and the provincial governments charged with implementation of the reforms lacked the requisite capabilities, autonomy and accountability.

What are the broad lessons learnt from this experience for the future management and political economy of reforms?

(a) The design of the programmes should usually follow two phases. In the initial phase when changes are sought in the incentive structure by altering relative prices such as exchange rates, interest rates, tariffs and taxes, producer prices, public utility prices, etc. a team of competent technocrats insulated from political pressures can be more effective in introducing and implementing these changes. At the second stage, when far reaching changes are the objective such as privatisation of public enterprises, downsizing of civil service, restructuring of key institutions, de-protection of manufacturing sectors, etc., widespread consultations and discussions with affected groups and economic actors are helpful in clarifying issues and building consensus.

(b) The political commitment to the programme will be strengthened if the economic reforms generate recovery and supply response in the earlier years of the programme, thus mobilising the potential beneficiaries; otherwise a sense of fatigue and cynicism creeps in to erode the commitment. Foreign inflows in the right amount and right time help reinforce the commitment, but the positive results early on are the only solid basis on which further reforms can be built upon. In a sequenced approach to the reforms the more difficult reforms can withstand resistance only if the earlier reforms had shown some positive results. Open communications and education of the population at every stage of implementation are the sine qua non for the success of the programme. Early sensitisation and involvement of the parliamentary groups in the design and supervision of the programme may prove helpful. The challenge is how to convert the widespread populist sentiment of the elected leaders to a more prudent management of scarce economic resources for the larger benefit of the society rather than themselves or their allies.

(c) The general finding from the successful examples of adjustment is that the urban bias of the past was largely reversed as the population in the rural areas benefited substantially, while key urban groups shouldered a large share of the cost. However, new coalitions of beneficiaries were not created which could support the reform programmes. As a consequence, powerful urban groups—trade unions, middle class professionals, and students-unions form the main opposition to certain reform policies and programmes. It is important to neutralise the losers from reforms, who are likely to be adversely affected by the liberalisation and ensuing competition. It is not enough to *either ignore* them lightly as vested interests or repress them. They are important potential contributors to development process and also have a tremendous influence in organising and mobilising public opinion. Those who are truly committed to their professions will either withdraw from the scene and emigrate thus depriving the country of valuable skills.

Although this challenge of neutralising the losers is daunting, the involvement of NGOs, professional associations, opinion makers and other interest groups, and consultations with these groups in the design and implementation of policies affecting them, will be helpful in understanding their view points and concerns and arriving at mutually acceptable solutions. The current practice of "secrecy" and inadequate communication and consultation accentuates the feeling of mistrust and suspicion.

(d) Once the reform package has been designed after broad consultations and consensus building the government should persevere with it even in the face of adversity and hostile opposition. This will maintain the credibility of the programme and enhance the chances of its successful completion. Where the executive authority is fully behind the programme, on the basis of its own internal conviction rather than external pressure, it does make sure that the execution and implementation do take place with due diligence and at the requisite speed to achieve results within the given time frame. The leadership assigns this task to the most competent individuals and most efficient groups and institutions, then monitors the progress and results from time to time and rewards and punishes the individuals concerned on the basis of performance.

(e) Flexibility and agility in responding to exogenous and unanticipated shocks and surprises—either external or domestic—differentiate those who have succeeded in keeping the reform process on course from those who failed to stop the derailment. The response from the IFIs and donors should be equally prompt and adequate. The performance criteria negotiated originally should be modified and contingency financing mechanisms triggered off immediately without waiting to determine whether the shocks are transitory or permanent in nature. The protracted discussion on the question as to whether or not the response to these should be through further adjustment or additional financing can potentially disrupt the reform process.

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ABSTRACT

The wholesale views of the relative success or failure of adjustment policies or its causes are challenged by a number of empirical studies. These studies demonstrate that there is considerable variation in the economic results of adjustment programmes, and this variation is explicable in terms of the context, quality, and sustained application of adjustment policies. This lecture focuses on the political economy aspects of the sustainability of economic reforms by introducing three basic hypotheses, and testing them with the Pakistani evidence. According to these hypotheses, variation in the result of economic policy reforms depends on: (i) a set of initial conditions which precipitate the decision to undertake adjustment programmes; (ii) the country's sense of "ownership" of the reform process as indicated by the consensus among the social and political organisations and the presence of a technocratic care group in government devoted to reforms; and (iii) the presence of "capacity" in the country in terms of human capital and resilience of institutions.

In the case of Pakistan, the main motivation for entering into adjustment programmes has been the short term foreign liquidity infusion by international financial institutions and other donors. The ownership of reforms has been narrow and domestic capacity to implement them has eroded over time. Several lessons for future management of the reforms can be drawn from this analysis.