



FRAMEWORK FOR ECONOMIC GROWTH PAKISTAN

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Pakistan Institute of Development Economics

My message to you all is of hope, courage and confidence. Let us mobilise all our resources in a systematic and organised way and tackle the grave issues that confront us with grim determination and discipline worthy of a great nation. – Muhammad Ali Jinnah



Core Team on Growth Strategy

This framework for economic growth has been prepared with the help of thousands of people from all walks of life who were part of the many consultative workshops on growth strategy held inside and outside Pakistan. The core team was led by Dr. Nadeem Ul Haque, Minister/Deputy Chairman, Planning Commission, and included:

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Foreword 2020

The Framework for Economic growth (FEG) was an innovative, reform-based strategy for sustained growth acceleration in Pakistan. We built on recent work summarized in Acemoglu and Robinson (2012) as well as developments in complexity theory [Haque (2017), Arthur (2014), Durlauf (2012), among others] to chart a new approach to policy. The objective was to change the country's growth policy from the traditional aid-led, project-based planning approach [Haq (1964)] to one based on evolving economic evidence and thought to use reform as an instrument to build, institutions, opportunity, productivity, innovation, and entrepreneurship [Romer (1990 & 1986), Lucas (1988) and others].

As recognized in the FEG, our systems of governance had limited flexibility or capacity to absorb this change. This approach, which was and is well received in academia, remains relevant but never found traction in the government.

We are printing this because it has academic and policy relevance and still needs to be read and debated.

I hope that the themes in this FEG will be further expanded and developed by researchers in the country. I also urge professors to use this document in the teaching of the Pakistan economy.

Dr. Nadeem UI Haque
Vice Chancellor, PIDE

Foreword 2011

Planning Commission is charged with developing growth policy and managing the Public Sector Development Program. In keeping with this mandate, I have the honour and the privilege to present the New Growth Framework (NGF)—a strategy that seeks accelerated and sustained growth and development based on economic reform and an emphasis on productivity. The NGF is based on widespread local and international consultation developing strong local ownership for a quality development strategy that is informed by the best knowledge and analysis available.

Pakistan has struggled with a chronic fiscal problem often sacrificing growth for short-term stabilisation. Examples in this regard are frequent reliance on distortionary tax and tariff policies and the instrument of first choice for controlling expenditures—a cut in development budget.

Yet, our growth policy is little more than development projects and some ‘incentives’ to industry, agriculture and exports. While incentives have hindered fiscal consolidation, sustained high growth has eluded us. Our development projects for building required human and physical infrastructure have not been able to impact growth and private investment because of continued cuts and inappropriate project selection. While the projects do generate employment and economic activity in the first instance, they lack strategic direction and coherence that is required for sustained high growth and the delivery of sustainable development benefits.

We have a young and growing population. Growth has been sporadic and inflation remains a problem. Our calculations also suggest that if we do not accelerate growth to over 7 per cent per annum on a sustained basis, the coming increases in labour force cannot be absorbed. Unfortunately, for the past four years per capita incomes have barely grown. Past data suggests that our long run growth is close to 5 per cent per annum. At this rate of growth, a very large percentage of the youth bulge will not find employment. New approach to growth is required which has the potential to sustain high growth levels remaining within fiscal limits.

Accelerating the economic growth rate and sustaining it at a high rate must therefore be treated as a national priority. And this must be achieved when resources are scarce as the country deals with a severe fiscal problem! The old paradigm of project- and government-led growth has to change. This reasoning has led the Planning Commission towards rethinking the traditional growth narrative in Pakistan.

Our “growth diagnostics” reveal several factors that increase the costs of making transactions in Pakistan. Today international indicators suggest that Pakistan has more of a software (management and productivity) problem than a shortage of hardware (physical infrastructure). The strategy emphasizes the need to reduce

economic distortions; improve functioning of domestic markets; create space in cities through proper zoning; energising youth; engaging communities; inducing investment in human and social capital; and enhancing connectivity and interactivity. Vibrant cities in an enabling environment will be the hotspot for entrepreneurship and innovation, assuring better returns through improved productivity on investments for all investors. In this context it must be understood that the urban-rural divide and the classification of cities has undergone a paradigm shift through demographic changes and the new ‘cities’ of Pakistan which occupy a large part of the landscape.

I would like to acknowledge and appreciate the hard work of the Growth Team and staff of the Planning Commission which was put in towards the preparation of this national document. I extend the sincere gratitude of the Planning Commission to our partners (donors, civil society organisations, and academia) who have been a source of guidance through out this process.

Implementing the growth strategy will require serious, sustained and disciplined reform over the next few years. A process of reform beginning with the Planning Commission has been outlined. ***Reform is a continuing process and it needs to be institutionalised!***

Dr. Nadeem Ul Haque
Deputy Chairman

Planning Commission
28 May 2011

Abbreviations

AERC	Applied Economic Research Council
ADB	Asian Development Bank
BASA	Bilateral Air Service Agreements
BV	Banverket
BISP	Benazir Income Support Programme
BOI	Board of Investment
CAA	Civil Aviation Authority
CCI	Council of Common Interest
CCOR	Cabinet Committee on Restructuring
CCP	Competition Commission of Pakistan
CDA	Capital Development Authority
CDWP	Central Development Working Party
CEO	Chief Executive Officer
CLL	Concurrent Legislative List
CLOT	Center for Liver Disease and Organ Transplant
CORFO	Chile's Technology Business and Incubation Program
CPRSPD	Centre for Poverty Reduction and Strengthening Social Policy Development
CSR	Corporate Social Responsibility
DDWP	Departmental Development Working Party
DFID	Department for International Development
EDB	Engineering Development Board
ECNEC	Executive Committee of National Economic Council
EFA	Education for All development index
EOBI	Employees' Old-Age Benefit Institute
ESSI	Employee Social Security Institute
EU	European Union
FBR	Federal Board of Revenue
FDI	Foreign Direct Investment
FLL	Federal Legislative List
GDP	Gross Domestic Product
GER	Gross Enrollment Ratio
GIK	(Page 57) Is it Ghulam Ishaq Khan Institute?
GST	General Sales Tax
HCM	Human Capital Management
HEC	Higher Education Commission
ICOR	Incremental Capital Output Ratio
ICT	Information and Communication Technology
IIT	Indian Institute of Technology
IIM	Indian Institute of Management
IMF	International Monetary Fund
IPDF	Infrastructure Project Development Facility
IPO	Intellectual Property Office
IT	Information Technology
IU	Innovation Union
JNR	Japan National Railway
KCR	Karachi Circular Railways
KCDR	Karachi Centre for Dispute Resolution
KPI	Key Performance Indicators
LECG	Law and Economics Consulting Group
LPI	Logistics Performance Index
MDG	Millennium Development Goals

MOC	Ministry of Commerce
MFN	Most Favoured Nation
MTBF	Medium-Term Budgetary Framework
MTDF	Medium-Term Development Framework
MTEF	Medium-Term Expenditure Framework
MTOE	Million Tonnes of Oil Equivalent
NADRA	National Database and Registration Authority
NAVTEC	National Vocational and Technical Education Commission
NCGR	National Commission for Governance Reforms
NEC	National Economic Council
NER	Net Enrolment Rate
NEPRA	National Electric Power Regulatory Authority
NGO	Non Government Organisation
NFC	National Finance Commission
NHA	National Highway Authority
NIA	National Innovation Agency (Thailand)
NIF	National Innovation Fund
NIP	National Internship Program
NTB	Non-Tariff Barriers
NTC	National Trade Commission
NTCIP	National Trade Corridor Improvement Program
NTN	National Tax Number
PaCCS	Pakistan Automated Customs Computerized System
PARC	Pakistan Agricultural Research Council
PASSCO	Pakistan Agricultural Storage and Services Corporation
PDF	Pakistan Development Review
PERI	Pakistan Economic Research Institute
PIA	Pakistan International Airlines
PIDE	Pakistan Institute of Development Economics
PHDEB	Pakistan Horticulture Development and Export Board
PKR	Pakistani Rupee
PPP	Public Private Partnership
PSDP	Public Sector Development Program
PSE	Public Sector Enterprises
PTA	Pakistan Telecommunication Authority
R&D	Research and Development
RBM	Results Based Management
SBP	State Bank of Pakistan
SECP	Security Exchange of Pakistan
SJ	Statens Järnvägar
SME	Small and Medium Enterprise
SRO	Statutory Regulatory Order
TARP	Tax Administration Reform Project
TCP	Trade Corporation of Pakistan
TFP	Total Factor Productivity
TVE	Town And Village Enterprises
TVET	Technical and Vocational Education and Training
UK	United Kingdom
UNDP	United Nations Development Program
UNICEF	United Nations International Children's Fund
UNIDO	United Nations Industrial Development Organisation
USA	United States of America
USC	Utility Stores Corporation
WAPDA	Pakistan Water and Power Development Authority
WWF	World Wide Fund
YES	Youth Engagement Services
YSLP	Youth Service Learning Program

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Executive Summary

Pakistan faces many challenges at the beginning of the second decade of the 21st century:

- Decades-long struggle with macroeconomic stabilisation arising from unsustainable fiscal policies
- Pressure of demography
- Legacy of economic distortions
- Battering from external events, including earthquakes, floods and a continuing longstanding low intensity conflict
- A large and loss-making public sector that impedes market development
- Low and declining productivity
- Heightened expectations of the population for a better life from a democratic government.

Our growth experience of the last four decades has been volatile annual growth and declining trend in long run growth patterns. In addition, productivity growth (a measure of efficiency) has been low in comparison to our comparators. For the last four years per-capita incomes have not increased in real terms while double-digit inflation has prevailed.

Our growth policy has been based on public sector projects and arbitrary incentives—subsidy and protection. The project selection process has considerably blunted the efficiency of infrastructure development while the system of incentives has not allowed the development of a vibrant and competitive marketplace.

This growth strategy is a new approach to accelerating economic growth and sustaining it. It has been developed with world renowned experts and all the stakeholders following extensive research and consultation. Our consultations clearly identified the need to develop a coherent approach to growth that goes well beyond projects and targets public service delivery, productivity, competitive markets, innovation and entrepreneurship.

The strategy is based on sustained reform that builds efficient and knowledgeable governance structures, and markets in desirable, attractive and well-connected locations. It recognises the severe resource constraint that the country faces and therefore focuses on ‘productivity’—improving the efficiency with which assets are used. Global indicators such as ‘competitiveness’ and ‘cost of doing business’ also highlight factors such as ‘management’, ‘innovation’, ‘quality of regulation and governance’ and ‘research and development’, as the more immediate constraints to growth. The thrust of this strategy, therefore, is to focus on the ‘software’ of economic growth (issues of economic governance, institutions, incentives, human resources, etc.)

so as to provide an environment in which the ‘hardware’ of growth (physical infrastructure) could be expanded and made more productive at every level.

The strategy argues that growth drivers such as entrepreneurship and innovation could be greatly encouraged by reforming and strengthening institutions such as the civil service, legal and judicial framework, the taxation system etc. The strategy also proposes measures, such as a reform of the restrictive zoning laws, which have impeded the growth of domestic commerce and hampered the role of cities as generators of economic growth.

The aggregate of such programs would vastly improve the investment climate, reduce the cost of doing business, increasing the profitability of enterprises and encouraging them to expand. The strategy also focuses on the improvement of productivity by, for example, increasing competitiveness in the market by easing the entry and exit of firms. In short, the strategy aims to increase investment in the country and to make investment more productive. The strategy proposes special programs to support key parts of the population, such as youth, who suffer disproportionately from unemployment.

Targeting Growth

Around 68% of Pakistan’s population is regarded as youth (under 30 years). Many of them are now coming into the labour force, increasing the size of the workforce by over 3 per cent annually. It is estimated that to absorb the youth bulge productively, Pakistan's real GDP needs to grow at an annual average rate in excess of 7 per cent. The strategy recognises that the country cannot jump immediately to these high rates of growth from the current low growth rate of about 3 per cent per annum.

- At the first stage, efforts will be undertaken to revive the economy to its short-term potential GDP growth rate of about 5–6 per cent a year. If issues regarding energy governance are resolved and some credible macro stability reached—this could be achieved in a short time.
- The strategy also suggests deep and sustained reforms—in areas such as public sector management, developing competitive markets, urban management and connecting people and places—as a way forward for accelerating growth to above 7 per cent.

What Constrains Pakistan’s Economic Growth?

Growth diagnostics point to two important constraints to economic growth:

1. Inadequate market development, (lack of competition, tax, tariff and policy distortions, entry barriers, government involvement, poor regulation, etc.), and
2. Lack of efficient public sector management to (a) provide core governance goods such as security of life, property, transaction and contract, (b) facilitate markets

and investment with informed policy and competent regulation, and (c) promote deepening of physical, human and social infrastructure.

This growth strategy is informed by the latest in economic thinking and seeks to strengthen both government and markets. It is not a ‘government versus markets’ approach but a ‘government and markets’ approach. An efficient government underpins a vibrant market. Much of the proposed reform is to get the roles of government and market in balance to develop efficiency within and between the two.

The Need for Productivity

Economic growth happens through the accumulation of labour and capital and through the efficient allocation of these assets—known as Total Factor Productivity (TFP). The contribution of productivity in the growth of Pakistan's GDP has been less than impressive. During the period 1960 to 2005, 80 per cent of the GDP growth rate in Pakistan was explained by capital accumulation and labour expansion and only 20 per cent by TFP. Labour productivity in Pakistan is growing at a comparatively lower rate than neighbouring countries. Research suggests several reasons, including market quality, poor governance, limited urban development, inadequate education, lack of competitive goods and factor markets, inadequate foreign competition and limited research and development capacity. Systems need to be built for monitoring and measuring productivity to motivate reform for sustained efficiency increases.

Building a Better Government

Our analysis and consultations have shown poor governance and dysfunctional markets to be among the most important reasons why growth in Pakistan has not achieved a sustained acceleration. Currently the government is an active player in every sector, as a direct market participant and competitor, obstructing private sector entry. The footprint of the government has been estimated to be as large as over 50 per cent of the national income, making it very difficult for the private sector to expand. Research by the Competition Commission of Pakistan has also established that government intervention is impeding the development of competitive markets. Better government should be established following a two-pronged approach a) reorienting the role of government—which focuses on an exit from markets and deeper deregulation, and b) improving public sector management—which includes reforming civil service, improving resource mobilisation, elimination of untargeted subsidies (particularly to loss making public sector enterprises), efficient public investment through results-based management.

Deepening and Maintaining Openness

While announcing export promotion in some sectors, policy has relied heavily on import substitution in others. Consumers have paid the price for these policies, through taxation for export subsidies and through high prices and sacrifice of quality goods where import substitution policies prevail. Meanwhile, innovation and entrepreneurship have suffered as the incentives are skewed in favour of lobbyists (rent seekers) rather than reliance on competitive markets.

The growth strategy advocates liberalisation of trade and investment regime to be a critical ingredient for sustained economic growth that in turn creates jobs, and raises productivity and wages. Unfortunately heavy protectionism was reintroduced in Pakistan during the second half of 2000–10, which brought back distortions in the overall trading system. Major distortionary policies adopted include (a) reversal of tariff cuts and increased tariff dispersion, (b) reversal of a number of liberalising reforms in agriculture, notably in wheat, sugar and fertilizer policies, (c) high and steeply escalated tariffs in specific industries, e.g. the auto-industry, following strengthened intervention by the EDB, (d) active use of WTO compatible regulations to restrict imports—including quasi-import licensing mechanism, (e) introduction and rapid expansion of anti-dumping practices, and (f) continuation of the long standing ban on imports from India.

The growth strategy recommends a) re-establishment of the unilateral trade liberalisation program, b) immediate abolition of the present system of distortive regulatory duties (SROs) that interfere with the tariff structure, c) maintain, *de minimis*, a neutral real exchange rate policy, d) immediate abolition of the ad-hoc system of quasi-import licensing being administered by EDB and various line ministries, e) thorough review of the economic justification for sectors/industries benefiting from above normal protection and/or subsidies, export subsidies, export taxes, and anti-dumping practices, and f) all economic policies including industrial and trade policies should be in line with the intentions defined in this growth strategy.

Vibrant and Competitive Markets

The growth strategy presents a clear road map for developing vibrant markets. Public enterprise reform and privatisation where necessary, will make space for increased entrepreneurship. Several markets require the government to move from producing and directly participating in markets to just regulation. For example, the current regulatory framework represses domestic commerce (retailing, warehousing, and transport) and construction and city development. Heavy government direct participation in agriculture, storage, transport, construction, to name a few, is stifling investment. Openness and city development combined with focussed public sector management would go a long way towards developing innovative markets.

Creative Cities

Almost half of the world's population lives in cities, producing more than 80% of global GDP. Dense high-rise cities are more productive, more inclusive and offer more than suburban sprawls which our city-planning paradigm favours at the cost of agriculture and the environment. In order to make cities as hubs of commerce, our growth strategy proposes a) relaxing of zoning and building regulations to allow space for mixed-use activities, energy efficiency, and facilitate vertical expansion of cities, b) privatising unproductive state owned land, c) encouraging foreign developers to compete in the Pakistani market, and d) focusing on research and development in low-cost energy efficient construction techniques.

Connecting to Compete

Commercial activity requires dense well-connected cities and communities. Connectivity is critical stratagem of the growth framework. While our PSDP has built physical infrastructure, given significant fiscal constraints, private investors should be encouraged to participate in development projects. In this regard, rules pertaining to project approvals, land acquisition and NHA Act must be revisited in line with promoting public-private partnership. Government should also consider its current policy of rewarding the loss-making enterprises such as NLC, Railways, and PIA etc. for their inefficiencies through consistent subsidies. Competition should also be encouraged at the domestic level by limiting regulators' role to regulating, e.g. CAA should not be responsible for running the airports but should concentrate on policy formulation and its implementation. Commercial routes, whether railroad or aviation, where multiple operators cannot operate due to congestion or some other limitations must be auctioned instead of giving a preferential treatment to any individual operator. In order to facilitate businesses, the country's custom posts should be automated so that clearance time could be reduced. Custom processes at dry ports should be computerised in order to reduce congestion at the seaports.

Pakistan will have to keep pace with trends in international connectivity. This will require strong efforts. Government should also pass electronic signatures act which should provide legal cover to the use of digital IDs. The use of ICT services, if encouraged across the board in the public and private sectors can greatly reduce the costs related to transport and logistics.

Youth and Community Engagement

The youth bulge is becoming eminent in coming years and it will change the age structure of the labour force over the next couple of decades. More than a third of youth currently lives in urban areas and their share is expected to reach 50 per cent by 2030. Compared to other growing economies of the region, Pakistan has a relatively large proportion (32%) of uneducated youth mostly with no vocational and life skills, who end up in elementary occupations or remain either unemployed or inactive. There is a need to provide for their health, education, and livelihood, and engage them in activities which convert their latent energy into positive outcomes for family, community, state and the global community. This is only possible through provision of quality basic and college education, market led skills development, instituting National Youth Service Policy Reforms, redesigning and rezoning cities to create space for youth, promoting nano- and micro-youth enterprises at local level through targeted youth entrepreneurship programs in major civic centres, promoting youth citizenship through civic engagement, promotion and continuum of youth sports and activities that encourage and support the development of active and engaged young people, National Youth Volunteer Services, programs to foster youth reproductive and general health, and establishment of Youth Service Learning Program with the help of educational institutions and civil society that integrates community and social service with academics.

Implementation: Results Based Management

“Who will implement?” is probably the most frequently asked question in Pakistan. This is so, because many good policy proposals and plans have been prepared but were never actualised. Our consultations have shown us that one reason implementation is poor in Pakistan is because plans are expected to be implemented by the very system that needs change. More often, there is no process or system in place for making change happen.

The new vision for economic growth will require:

- Periodic identification of emerging constraints to economic growth through research and dialogue with all sectors and stakeholders
- Consensus building through extensive consultations on the reforms and programmes that will be required for alleviating these constraints
- Building a system for measuring productivity and public service delivery
- Developing and monitoring quantifiable plans regularly

Under the post-18th Amendment milieu, the Planning system will exercise control over the development process through:

- Consultation, setting medium-term and annual development objectives for the government and for relevant ministries
- Identification of key economic reforms that are required for these objectives, development of quantitative indicators (which can be monitored) for these reforms and monitoring and reporting on them to government and the people
- Specifying government- and ministry-level reporting requirements for development results and their costs, to ensure accountability and track progress
- Strengthening the capacity of ministries and, by interaction and evaluation, ensuring that their strategies and services support national development priorities
- Developing capacity of planning system to act as an institution that develops and oversees the government’s reforms agenda

Six critical changes have been identified that need to be introduced to strengthen the linkage between the Planning Commission and government performance. These are:

1. Strengthen the Medium-Term Development Framework (MTDF) and the Medium-Term Expenditure Framework (MTEF) for setting medium-term priorities in line with growth strategy and reforms agenda
2. Support a unified results-based budget preparation process
3. Decentralise responsibility for projects to line ministries
4. Redefine the Planning Commission’s role and processes in respect of major capital projects
5. Establish a results-based monitoring and evaluation system.
6. Planning Commission should lead the reform and change process through identification and advocacy of critically required changes in policies.

Breaking Out of Our Past

‘Some men tend to cling to old intellectual excitements, just as some belles, when they are old ladies, still cling to the fashions and coiffures of their exciting youth.’ – Jane Jacobs

At the beginning of the second decade of the 21st century, Pakistan faces many challenges:

- Decades-long struggle with macroeconomic stabilisation arising from unsustainable fiscal policies
- Pressures of demography
- Legacy of economic distortions from previous policies
- Battering from external events, including earthquakes, floods and a continuing war
- Low and declining productivity
- Heightened expectations of the population for a better life from a democratic government

We need a bold new approach to seek sustainable and inclusive development and we must do this bearing in mind the resource constraint arising from our difficult fiscal situation.

Goals and Objectives

Growth strategy must be bold, seeking to generate opportunities

The goal is to maximise opportunity for all citizens so that they can obtain a better life through their hard work and ingenuity. Pakistan's population, until recently, was growing at 3 per cent annually, however is now increasing at an annual rate of about 2 per cent. As a result, our labour force is expected to grow at over 3 per cent annually over the coming years. To absorb this addition to the labour force, the GDP needs to grow at a rate of around 7 to 8 per cent annually and must be sustained in the coming decades.¹ The growth strategy must be bold, seeking to generate opportunities—employment and entrepreneurial (self-employment) opportunities. This is the policy goal!

Goal is to maximise opportunity for citizens through hard work and ingenuity

Recent thinking on growth indicates that growth generators need not be governments, but cities, asset classes, commodities, products, firms and people. Growth should not be difficult for those starting far behind since the recipe is long known and well established; give the vibrant young people quality education, new ideas and high ideals, strive for institutions that support free and fair markets, create a professional, well trained civil service, achieve economies of scale through a large domestic market and

¹ A number of studies have shown that the elasticity of employment with respect to GDP growth is about 0.5. This means that a one percentage point increase in the GDP growth rate leads to a one-half percentage point increase in employment.

open up for trade and investment; and, keep public spending on infrastructure and social sectors limited and focused only to critical and essential projects.²

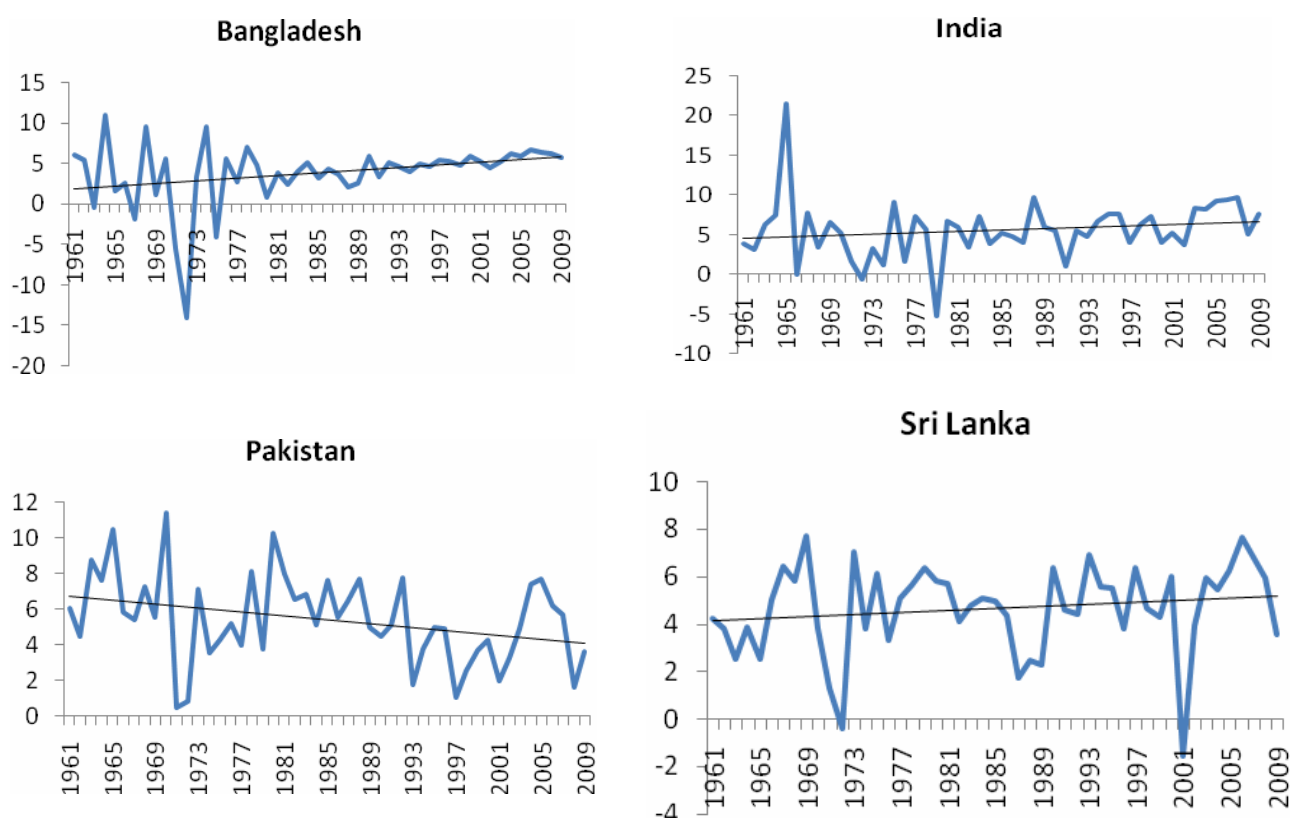
A Past of Volatile Growth and Poor Economic Governance

The history of global economic growth indicates that: a) past five decades have seen extraordinary growth worldwide, b) many developing countries sustained rapid growth for extended periods and achieved substantial increases in incomes for their populations, c) for the most part this growth came from policy reforms that provided macroeconomic stability, encouraged markets and embraced greater openness to trade and investment, d) there exist examples where high growth has been maintained for over quarter of a century (Japan 1951–88, China 1979–03, Korea 1954–98), and e) most of the extended declines in per capita income involve a collapse in governance.³

Between 1972 and 2010, our GDP grew at an average annual rate of about 4.9 per cent. However, growth was volatile and on a declining trend

Between 1972 and 2010, Pakistan's GDP grew at an average annual rate of about 4.9 per cent. However, our growth was volatile and showed a declining trend (Figure 1). In contrast, other regional economies such as India, Sri Lanka and Bangladesh, showed less volatility (particularly in recent years) and more importantly the trend in growth rate in these countries was increasing overtime.

Figure 1 Regional Economic Growth 1961–2009



Source: World Development Indicators

² W Buiter and E Rahbari, 'Global Growth Generators: Moving beyond Emerging Markets and BRIC', *Global Economics View*, Citigroup Global Markets, February 2011.

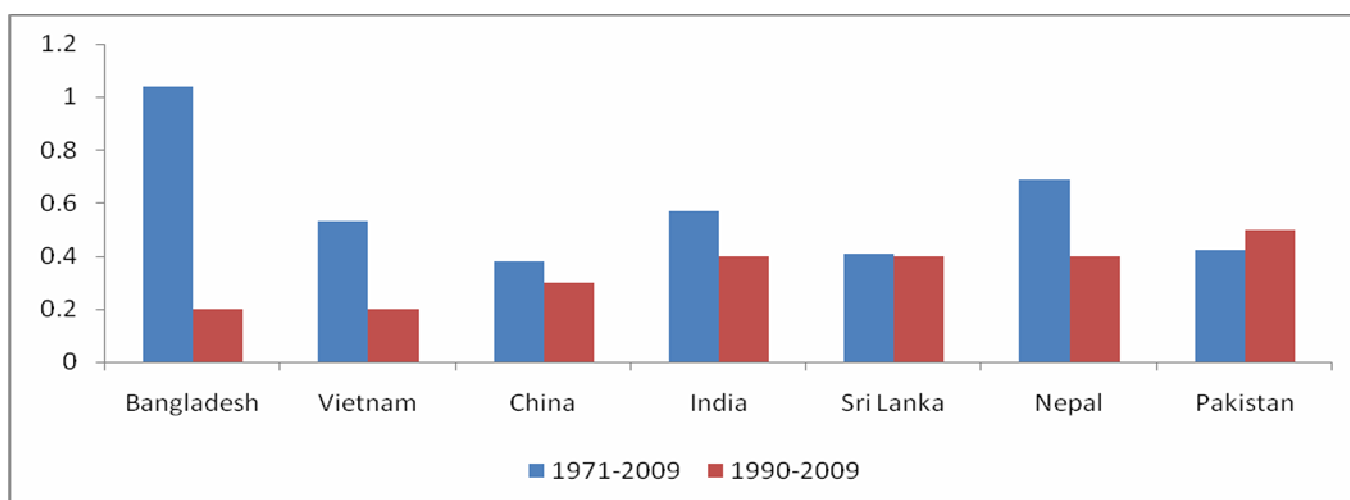
³ NH Stern, JJ Dethier & FH Rogers, *Growth and Empowerment: Making Development Happen*, MIT Press, Cambridge Massachusetts, 2005.

Figure 2 further reinforces two important features of volatility of growth in Pakistan:

- First the coefficient of variation (a measure of fluctuation in relation to the average) is higher for Pakistan than that of other regional economies, particularly for more recent periods
- Second Pakistan's variation occurs around a declining trend rate

Together these highlight increasing uncertainty in our economic outlook. In turn, this uncertainty deters investment.

Figure 2 Growth Volatility: Real GDP – Coefficient of Variation



Source: Computed from UNDP Data

Contemporary thinking in economic growth literature explains that key determinants of growth today are economic governance and human capital.⁴ The usual variables such as investment and savings should be regarded as endogenous to the system. This implies that we are in search of factors that allow space and freedom to invest productively. Economic growth is delivered and assets are accumulated through competitive markets and use of existing and new technology, productivity-inducing knowledge and business models.

Key determinants of growth today are economic governance and human capital

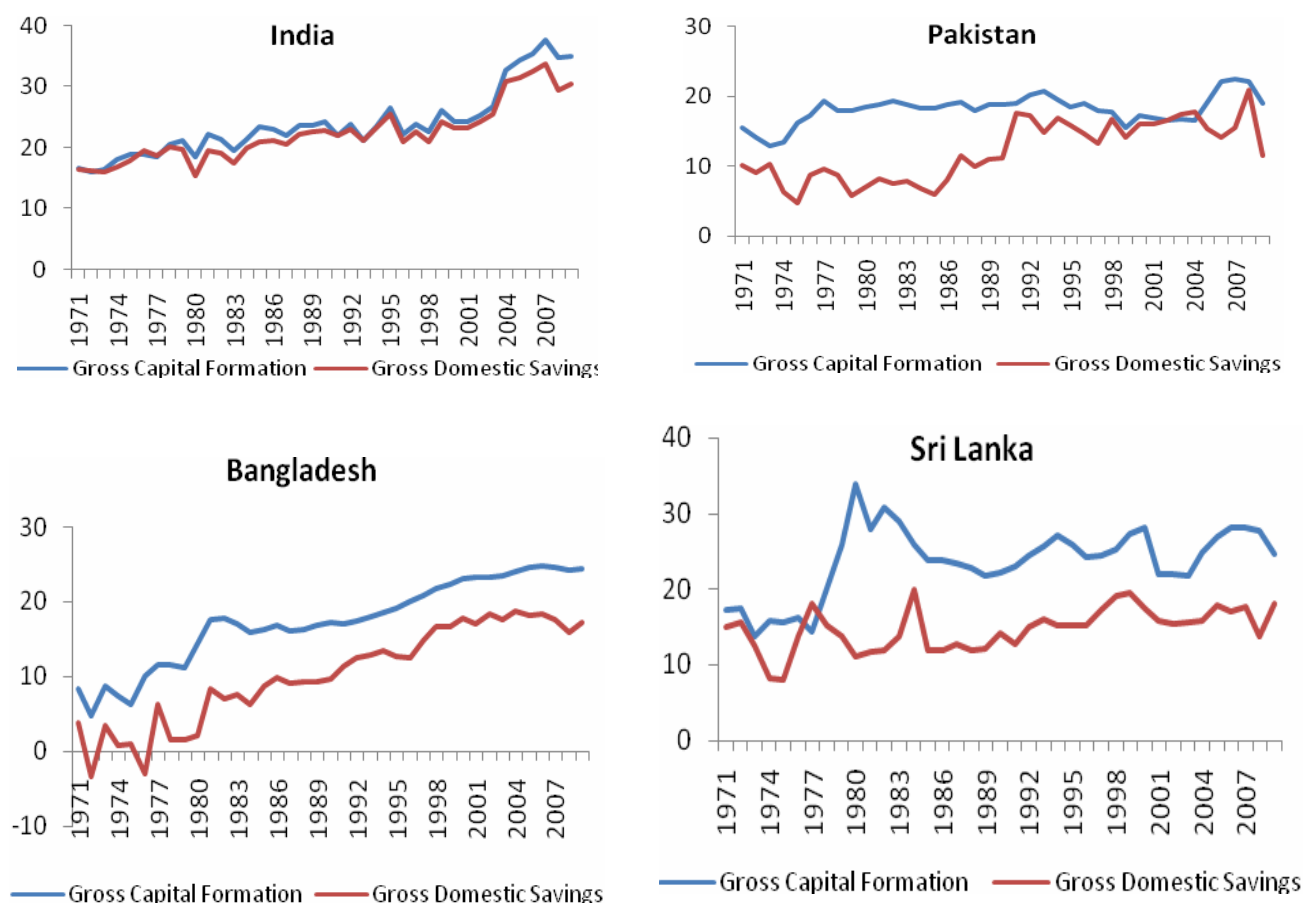
This view in no manner understates the importance of capital formation overtime. Figure 3 points to two important reasons for Pakistan's relatively slower GDP growth compared with countries in its neighbourhood.

- First, it has been investing a smaller share of its GDP than its neighbours. In virtually all countries in our region, the ratio of investment to GDP has shown a steady increase between 1971 and 2009
- Second, the share shows signs of decline

⁴ K Ward, *The World in 2050*, HSBC Global Research, January 2011. See also RJ Barro, 'Determinants of Economic Growth: A Cross-country Empirical Study', *Journal of Comparative Economics*, vol. 26, no. 4, pp. 822-824 and World Bank Policy Research Report, *The East Asian Miracle: Economic Growth and Public Policy*, World Bank, 1993.

A crucial question for accelerating GDP growth in Pakistan, therefore, is how to raise the investment rate, and how to increase its productivity so that the country can derive higher output at each level of investment. These are the two critical issues that this growth strategy is designed to address.

Figure 3 Investment and Savings as per cent of GDP, 1971–2009



Source: World Development Indicators

On a sustainable basis, while a certain amount of investment can be financed through an inflow of foreign resources (whether as external assistance or commercial borrowing), the bulk of investment must be financed by domestic savings. In this area also, Pakistan has performed less satisfactorily than many of its neighbours. During the past four decades (1971–2009) the ratio of fixed investment to GDP averaged only about 17 per cent, and the ratio of domestic savings to GDP merely 12 per cent. This performance compares poorly with the neighbouring countries (see Table 1).

A sustainable basis requires bulk of investment to be financed by domestic savings and not through inflow of foreign resources

Table 1 Growth, Investment & Savings 1971–2009 (Annual Average)

Country	GDP Growth (%)	Fixed Investment to GDP	Domestic Savings to GDP	ICOR
China	9.1	32.2	37.9	3.5
India	5.3	23.9	22.0	4.5
Malaysia	6.4	27.4	35.0	4.3
Indonesia	6.0	25.9	29.2	4.3
Thailand	5.9	29.5	28.8	5.0
Pakistan	4.9	16.6	11.9	3.4

Source: World Development Indicators

The gap between Pakistan's domestic savings and its investment means that about one-third of the country's fixed investment was financed by foreign resources. The corollary to this reliance on foreign savings was that the performance of Pakistan's GDP became significantly dependent on the availability of such resources — a phenomenon that maintained boom-bust cycles. Foreign injections have on occasion led to sharp upward spikes in growth rate. However, because the resources were not channelled into productive investments, GDP growth has not been sustained beyond periods of external inflows.⁵

No strong relationship between public investment and economic growth

It has also been argued that there was no strong relationship between public investment and economic growth,⁶ but it appears that public investment did have some effect in attracting private investment.⁷ The episodes of slowdown in the investment rate have also been associated with frequent changes of political regimes and economic policies, and balance of payments volatility.⁸

How the Economy has Evolved

Services sub-sectors are more value-added, more labour-intensive and have greater potential of growth

The economic structure has changed and way forward must seek to build on the ongoing structural transformation. Figure 4 shows that while in the past agriculture was the largest sector in the economy, today it is services. By 2010, the share of agriculture had dropped to about 20 per cent, while that of services exceeded 50 per cent. These changes have significant implications for the growth of productivity and employment. The services sub-sectors by definition are more value-added, more

⁵ V Ahmed and C O'Donoghue, 'External Shocks in a Small Open Economy: A CGE-Microsimulation Analysis', *The Lahore Journal of Economics*, vol. 15, no. 1, 2010, pp. 45–90.

⁶ E Ghani and Musleh-ud-Din, 'The Impact of Public Investment on Economic Growth in Pakistan', *Pakistan Development Review*, vol. 45, no. 1, 2006, pp. 87–98.

⁷ SNH Naqvi, 'Crowding-in or Crowding-out? Modelling the Relationship between Public and Private Fixed Capital Formation Using Co-integration Analysis: The Case of Pakistan 1964 – 2000', *Pakistan Development Review*, vol. 41, no. 3, 2002, pp. 255–276.

⁸ SM Naseem, 'Political Economy of Structural Reforms in Pakistan', *East Asian Bureau of Economic Research*, Working Papers, Bangkok, 2008.

labour-intensive and have greater potential of growth even under repressive circumstances which lead to curbing of growth in agriculture and industry.

Figure 4 **Structural Transformation 1970–2010**



Source: Economic Survey of Pakistan, various issues

Our ability to do business with other countries has also remained uncertain. The trade regime in Pakistan was never grounded in an overarching growth paradigm. We have seen phases of import substitutions, export orientation and revival back towards protectionism.

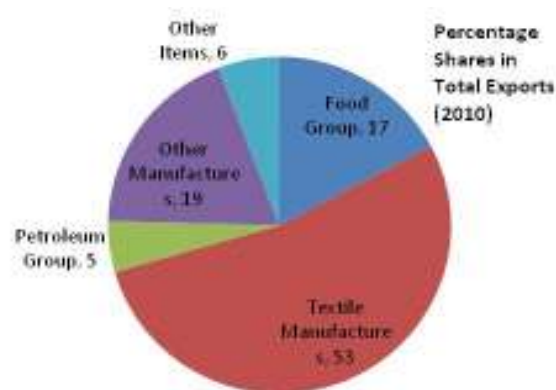
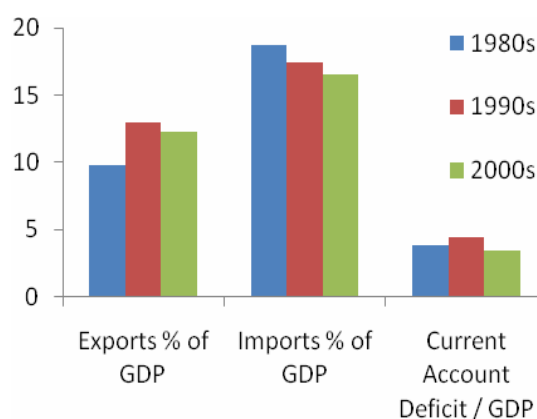
The trade regime in Pakistan was never grounded in an overarching growth paradigm

- Figure 5 illustrates the near-stagnancy in the structure of the trade sector. Exports and imports as a percentage of GDP have not changed much in the past three decades. In fact, the ratio of exports to GDP has declined from the average levels seen in the 1990s.
- Within the structure of exports it has been difficult for the industrial sector to diversify away from textile manufactures—which again were low-value-added.
- Pakistani exports are narrowly concentrated geographically, which makes them vulnerable to economic crises in economies such as the United States and the European Union.
- Finally, policy in Pakistan sought to boost exports through controls on domestic market. These controls included examples such as curbs on domestic consumption, resource utilisation and allocation and market development.⁹

Exports have failed to diversify

⁹ NU Haque, 'Beyond Planning and Mercantilism: An Evaluation of Pakistan's Growth Strategy', *Pakistan Development Review*, vol. 45, no. 1, 2006, pp. 3–48.

Figure 5 Exports, Imports and Current Account 1980s–2000s



Source: Economic Survey of Pakistan, various issues

Inclusive and Sustained Growth is a Policy Imperative!

Every year Pakistan adds the equivalent of a New Zealand to its population; every two years, a Switzerland; every three years, a Greece; every four, a Chile or a Netherlands; and every five, an Australia.

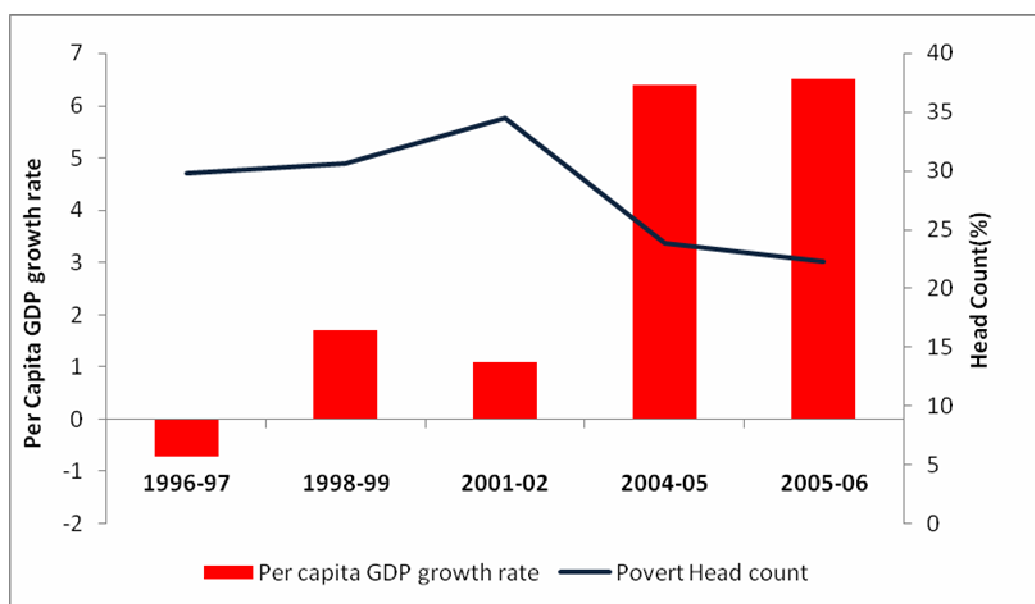
Alleviating poverty is only possible if GP increases at a pace which caters for population growth

Pakistan must get on to a path of high and sustained GDP growth as soon as possible. The size, growth, and age distribution of the country's population demands this. Every year Pakistan adds the equivalent of a New Zealand to its population; every two years, a Switzerland; every three years, a Greece; every four years, a Chile or a Netherlands; and every five years, an Australia. And of course, while it adds these populations, it does not add the assets and institutions of these countries.

Another important reason for the country to get onto a sustained high-growth path is the objective of alleviating poverty. Rapid increase in the GDP has proved to be a necessary (even if not sufficient) condition in every country that has managed to reduce poverty by a substantial amount. However, it is not only a high rate of growth that is required, which must also be sustained. As was discussed previously, the bulge in Pakistan's working age population is likely to continue for at least 30 years, and these additional numbers need to be provided employment.

It is evident from Pakistan's recent growth experience that growth has caused a significant change in poverty levels. Between 1996-97 and 2001-02 low growth in per capita GDP resulted in an increase in poverty, which started to decline sharply as per capita income grew during the period 2004-05 to 2005-06 (Figure 6).

Figure 6 Per Capita GDP Growth and Poverty Head Count, 1997–2005



Source: Economic Survey of Pakistan, various issues

It is estimated that between 1979–88 and 1988–94 the growth effect contributed around 84.9 per cent and 61.1 per cent reduction in poverty.¹⁰ It has also been shown that during the period 1992–93 to 2005–06 growth had a significant impact on reducing poverty while the redistributive effect was weaker.¹¹ These results suggest that if additional measures to improve the distribution of income had been taken, the decline in poverty would have been much larger. The strategy aims to make growth more inclusive and thereby speed up the movement out of poverty.

The strategy aims to make growth more inclusive and speed up the movement out of poverty

Box 1 Economic Growth and Social Safety

To complement the Growth Strategy, the government has already developed an effective and widely respected social safety net—The Benazir Income Support Program (BISP). It is attempting to meet several needs. First, it is based on cash transfers to help in smoothening household consumption and investing in human capital. Second, objective and transparent social safety nets have a positive impact on social cohesion, which assists connectivity (see the discussion on connectivity and its benefits later in this report). Third, the presence of an effective and targeted social safety net allows the government to avoid suboptimal economic policies (for example price subsidies) that interfere with the functioning of the markets; this is especially important in the power and agriculture sectors. Finally, social safety nets, such as cash transfers, community grants, or public works, help revitalise crisis-affected communities by filling in deficiencies in demand and kick-starting markets that may have shrunk or even closed down. All these factors influence both short-term and long-term economic growth through their impact on employment and productivity.

¹⁰ AH Khan and AS Azhar, 'Decomposition of Changes in Poverty Measures: Sectoral and Institutional Considerations for the Poverty Reduction Strategy Paper of Pakistan', *Pakistan Development Review*, vol. 42, no. 4 (Part II), 2003, pp. 879–892.

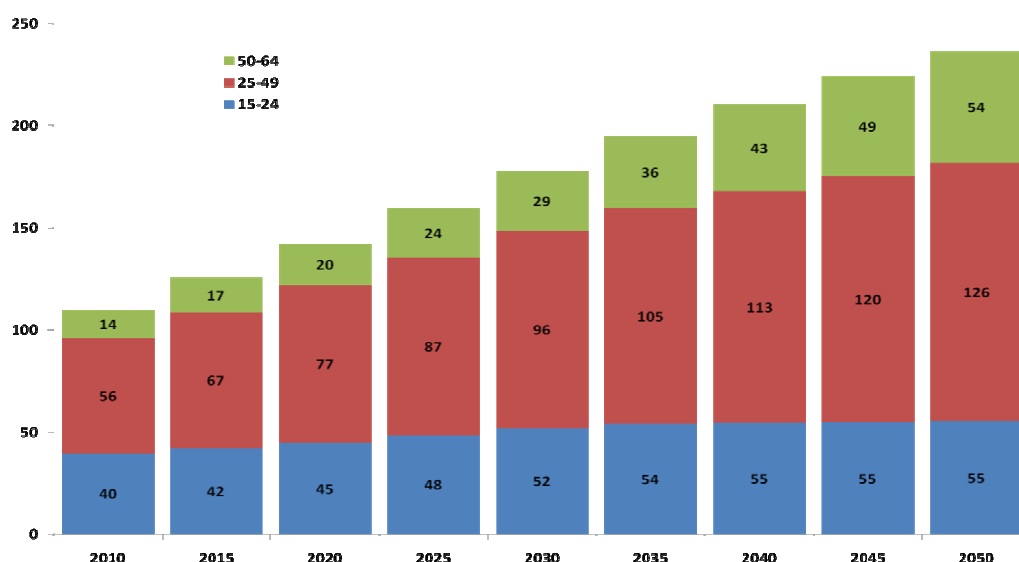
¹¹ AR Cheema and MH Sial, 'Estimating the Contributions of Growth And Redistribution to Changes in Poverty in Pakistan', *Pakistan Economic and Social Review*, vol. 48, no. 2, 2010, pp. 279–306

Unless Pakistan can sustain a high level of growth, its streets are likely to be crowded with young men and women desperately seeking jobs, justice, education, and medical attention for themselves and their families and demoralised by not finding them

Therefore, for a country with Pakistan's experience of substantial fluctuations in the GDP growth rate, protecting the poor and the vulnerable not only mandates a high and sustained growth of GDP in the future, but this protection, in turn, can also support a higher growth rate.

The age-distribution of the population provides another imperative for acting quickly. Nearly 50 per cent of Pakistan's population is below 20 years of age and over 60 per cent below 30 years. With growing unemployment, these youths become disconnected from the country's economy and disaffected with its political structure, and are vulnerable to the blandishments of extremists. The demographic projections in Figure 7 show this 'youth bulge' will continue to dominate the population for another 30–35 years. Unless Pakistan can sustain a high level of growth of its GDP, its streets are likely to be crowded with young men and women desperately seeking jobs, justice, education and medical attention for themselves and their families, and will eventually be demoralised by not finding them—a breeding ground for anarchy.

Figure 7 Projected Labour Force Size and its Composition (Millions)



Source: Based on Medium Variant, UN 2005

The demographic conditions are sufficiently important to warrant a more extended discussion. The population of Pakistan is projected to reach over 350 million by 2050.¹² It is not just the size but its age structure that is important. The number of those aged 0–14 years will start to stagnate after 2035 (due to fertility decline), but the number of the working age group (15–64 years) and the elderly (65 and above) will continue to increase (population echo /momentum). It is the increasing numbers in the working age group that might provide an economic opportunity for the country. By 2050, more than 236 million people will be in the working age group.

Due to the increasing proportion of the population in the working age group, the dependency ratio will continue to decrease, and is projected to reach its lowest point

¹² D Nayab, 'Demographic Dividend or Demographic Threat in Pakistan', *Pakistan Institute of Development Economics*, Working Papers, No. 10, 2006

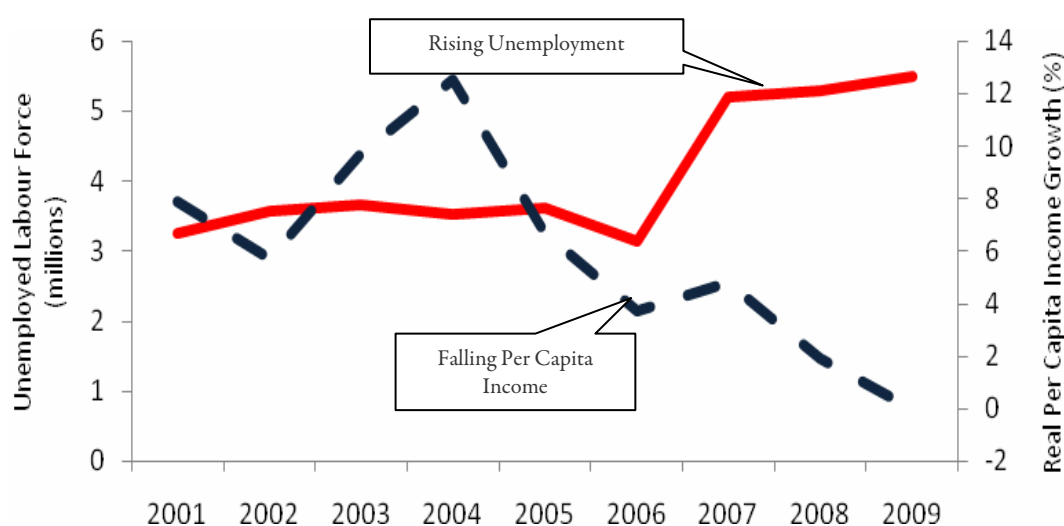
in the 2030s. A lowered dependency ratio has positive implications for economic growth, as there are more working people taking care of fewer people (young and/or old), thus improving the probability of more savings and increased productivity. The dependency ratio is expected to again show an increasing trend by 2050, but this time because of an increase in the old dependency ratio.

The demographic changes leading to a lowered dependency ratio are sometimes described as offering the potential of a ‘demographic dividend.’ The demographic dividend is basically an opportunity provided by the changing age structure when the growth rate of the labour force is higher than the growth rate of the total population. Demography started providing this opportunity to Pakistan in the early 1990s and will continue to do so till 2050, when the two rates will merge. This, however, is just an opportunity, and the dividend has to be earned by the imaginative utilisation of the additional workforce. On the other hand, an increasingly disillusioned younger unemployed cadre can be a time bomb, waiting to explode. After 2050, this ‘window’ is projected to close.

In the longer term, ageing of the labour force is another factor to be considered for the longer-term. The number of new entrants/younger workers (15–24 years) would start to stagnate by 2040, while the number of older workers (50–64 years) would continue to increase. Thus, an increasing number of older persons will have to be provided for by a decreasing number of productive workers.

By 2050, more than 236 million people will be in the working age group, a huge increase from the 110 million in 2010

Figure 8 Falling Incomes and Rising Unemployment, 2001-09



Source: Economic Survey of Pakistan, various issues

Sadly the recent growth history is not encouraging for the youth entering the labour force. Figure 8 shows the falling growth in per capita income and rising unemployment levels.¹³ A bulge in the working age groups in coming 40 years will increase the economy-wide potential productive capacity. However, if economic growth is not leveraged on a higher trajectory then the coming demographic changes

¹³ Moreover, it should also be borne in mind that about 30 per cent of the employed are actually “unpaid family help,” and thus not part of wage labour.

will imply rising unemployment, shortage of assets, difficulties in competing with neighbouring South Asian countries—which will also be benefiting from younger populations during the same period.¹⁴ Pakistan's demography, instead of providing a dividend may well prove to be a nightmare.

How Fast a Growth of GDP should Pakistan Target?

If economic growth is not leveraged on a higher trajectory then the coming demographic changes will imply rising unemployment, shortage of assets and difficulties in competing with neighbouring South Asian countries

The discussion earlier had estimated that Pakistan's GDP needs to grow at an annual average rate in excess of 7 per cent in order to absorb the new additions to the labour force and to start cutting into the ranks of the currently unemployed. The strategy recognises that the country cannot jump immediately to these high rates of growth from the present performance of under 3 per cent per annum.

The first order of business will be to get the actual performance of the economy up to its potential rate. It is estimated that, at the present level of investment and institutional functioning, Pakistan's potential GDP growth rate is of the order of 5–6 per cent a year. Given the right policies and a modicum of good luck, it should not be impossible to get the economy back to a growth rate of between 5–6 per cent in a reasonable time, especially given the extent of unused capacity that exists in the manufacturing sector.

The important second step is to develop policies that will allow growth to accelerate beyond the current potential to above 7 per cent. Through a combination of measures and reforms for increasing productivity, improving economic governance and developing physical and regulatory space for entrepreneurial and innovative investments, the growth strategy seeks to achieve this target in the medium term.

The most important step is to sustain this growth for a number of years. The growth strategy argues that this can be done through continued improvements in governance, institutional reforms, and focused efforts to augment human capital. This is precisely what fast growing economies have done and is the direction towards which Pakistan must move.

¹⁴ NU Haque, 'Towards Growth Strategy and Economic Reforms', Presentation at Pakistan Development Forum (PDF), Islamabad, 2010.

Rethinking Our Growth Paradigm

'Ideas shape the course of history'. – John Maynard Keynes

It is clear that we must aim to attain a high growth trajectory in an era of severe resource constraints. Through lengthy research effort and a widespread local and global consultation, it has been determined that a fresh approach that places much greater emphasis on the 'software' of growth—the manner in which markets, cities and communities are governed and organised—than on the 'hardware', which primarily consists of physical investment in brick and mortar. This approach will release the dynamism of entrepreneurship and innovation to accelerate growth considerably in this time of financial constraint.

It should be emphasised that the focused public sector investments for infrastructure will continue within the available resource envelope. The growth strategy will only make the process of infrastructure creation and use more efficient, facilitating better utilisation of resources. In this way the infrastructure that is developed will be made meaningful to citizens' lives.

Why is a fresh approach to planning needed?

Development planning in Pakistan started in the mid-1950s; growth strategies since then have followed an essentially similar pattern.

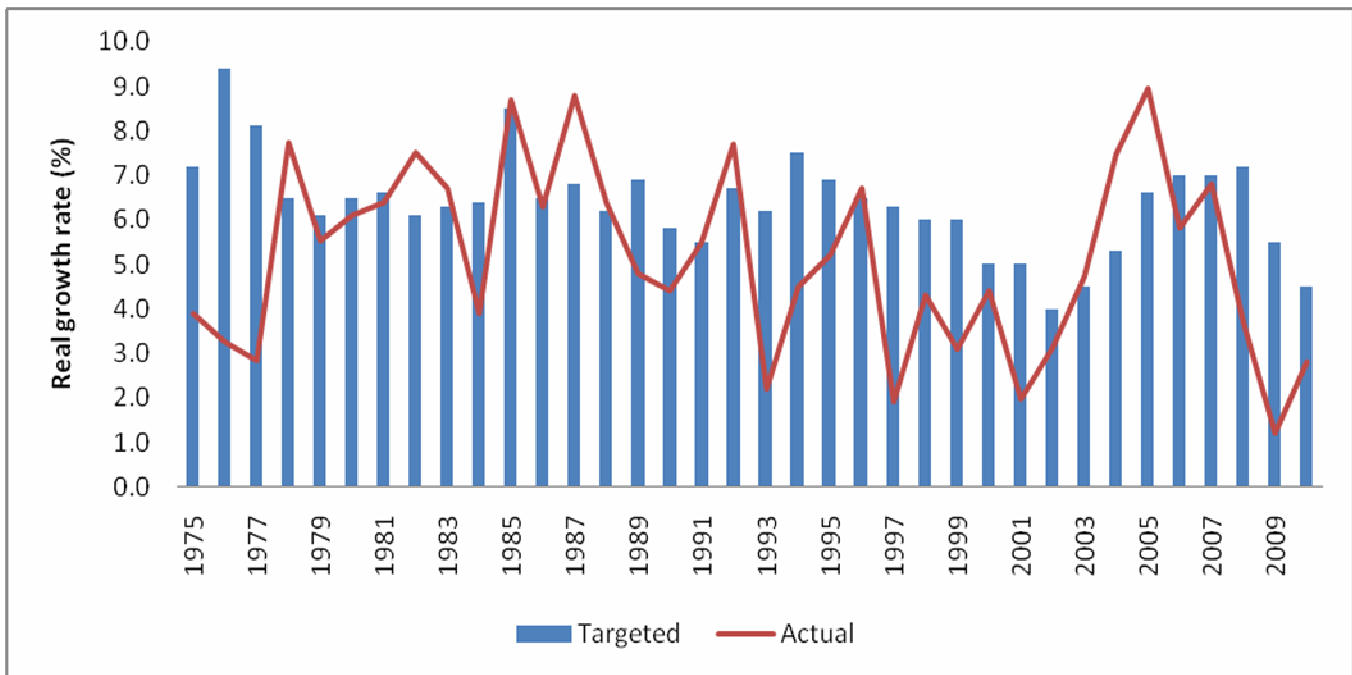
- They are characterised by a focus on the arbitrarily set growth and investment rates
- They provided more or less detailed projections for investment by the public sector with some rather general indications of that by the private sector, even though the latter was described as the major engine of growth
- They relied on the government playing a lead role through sector picking and market controls

It is perhaps not surprising that the plans had only limited success. Of the nine Plans that have been prepared so far, only the Second Five-year Plan (1960–65) managed to meet a significant number of its macroeconomic targets. Figure 9 indicates a clear deviation of actual growth from the targeted performance.

Through a lengthy research effort and a widespread local and global consultation, focus is on a fresh approach that places much greater emphasis on what might be called the "software" of growth

Figure 9

Pakistan: Targeted Vs. Actual Economic Growth



Source: Economic Survey of Pakistan, various issues

The earlier efforts suffered from three major weaknesses.

- First, they relied on a lead role for the government even during times which stressed upon privatisation and trade openness.
- Second, not much attention was paid to raising the productivity by which the country could obtain a higher output at each level of investment.
- Third, the structure and incentives within the governing institutions did not keep pace with markets.. Meanwhile evidence of the level of corruption and maladministration increased.

In short, the macroeconomic goals and structure of the plans were not anchored in sound microeconomic understanding and analysis.¹⁵

The PSDP and Growth

Over time the PSDP project selection has become politicised

The earlier planning approach relied heavily on public investment to develop much needed physical infrastructure. Even to this date the budget each year allocates somewhat ambitiously for public sector development only to substantially cut it later in the year as the fiscal gap begins to spin out of control. Continued cuts in the PSDP have brought it down to about 1 per cent of GDP.

Several factors are at work to rapidly increase the demand for projects far beyond the supply of resources. Over time the PSDP project selection has become politicised. The

¹⁵ See also: MU Haq, *Seven Sins of Economic Planners*, 1973.

hunger for projects is also fuelled by the incentives for project governance which allow the government ministries to control and misuse limited public resources largely beyond scrutiny. The current stock of projects in hand is worth around Rs 3 trillion while the size of the PSDP for 2010-11 was Rs 180 billion.

The existing planning approach with its heavy focus on the PSDP has several weaknesses:

- Undue emphasis (over 60% of PSDP) on brick and mortar and related civil work
- Little attention being given to completion and efficient utilisation of existing infrastructure
- Completed projects neither maintained nor used optimally
- Priorities are determined for reasons other than economic efficiency (e.g. road allocations being three times that of railways)

On the positive side, PSDP has developed roads, irrigation, energy, sports complexes, universities, schools etc. It is now time to see how these facilities can be better organised to improve the quality of life for the people. In future, productivity-maximising return (use) of existing resources must become a major theme.

Box 2

Institutions Matter!

Institutions have been defined as ‘the humanly devised constraints that structure political, economic, and social interactions. They consist of both informal constraints (sanctions, taboos, customs, traditions, and codes of conduct), and formal rules and regulations (constitution, laws, property rights).’

The 1990s saw a growing body of literature on institutions and their impact on economic growth. An excellent starting point is Lin and Nugent (1995) that provides review of the substantial literature on this subject. Hall and Jones (1999) on ‘social infrastructure’; Knack and Keefer (1995, 1997) on bureaucratic quality and social capital; Temple and Johnson 1998 on ‘social capability’; Rodrik (1999) on institutions of conflict management; and Acemoglu, Johnson and Robinson (2003) on the role played by institutions bequeathed by colonists. Work by Kaufmann, Kraay, and Zoido-Lobaton (1999) has developed aggregate indicators of six different aspects of governance-voice and accountability, political instability and violence, government effectiveness, regulatory burden, rule of law, and graft-showing that all of these are significantly associated with income levels in the expected manner.

Even markets require institutions because they are not self-creating, self-regulating, self-stabilising, or self-legitimising. At least five key institutions are essential for markets in order to address failures related to property rights, regulatory environment, macroeconomic stability, conflict management and social insurance.

Source: Adapted from One Economics Many Recipes by Dani Rodrik

What Constrains Our Economic Growth?

Stabilisation and growth
can be engineered
simultaneously

Pakistan's growth experience indicates a deliberate effort to pick and favour select sectors within agriculture, industry and services and a preoccupation with horizontal policies for macroeconomic stabilisation.¹⁶ More importantly, these stabilisation challenges increasingly focus on the short term. Changing the growth trajectory, is the requirement of our time, requires longer term consensus-driven thinking.

While achieving macroeconomic stability is a priority, many steps can be taken today to clear the path for entrepreneurs to trigger growth. Experience around the world is that many of the factors holding back the GDP growth rate are institutional- or policy-based in nature, and require correctional measures rather than the application of large amounts of financial resources. Thus, stabilisation and growth can be engineered simultaneously.¹⁷

Energy crisis in Pakistan
is a management and not
a capacity issue

The debate on underlying binding constraints (Figure 10) is often confused due to short-term concerns such as energy and security.¹⁸ Here again it may be argued that energy crisis in Pakistan is a management and not a capacity issue. The previously undertaken energy reforms remain incomplete. The energy sector is characterised by a lack of institutional strength to undertake effective integrated planning, policy development and implementation. The issues faced by the energy sector are not related primarily to capacity—i.e. implying a need to expand the infrastructure—but to management and organisational difficulties that result in cash flow constraints.

The ongoing war on terror and related security challenges have certainly impacted the socio-economy of Pakistan in multifarious ways.¹⁹ However today we have ready examples from economies across the global that are in a constant state of war (or political instability) for the past so many decades and have yet posted impressive gains in growth, competitiveness and creativity. Economies such as Israel, Lebanon, Sri Lanka, Philippines, Vietnam and Indonesia have all tried and succeeded in insulating economic incentives from geo-political tensions.²⁰ Pakistan must seek inspiration from nations who have challenged their worst circumstances.

¹⁶ R Hausmann and B Klinger, 'Structural Transformation in Pakistan,' 2008.

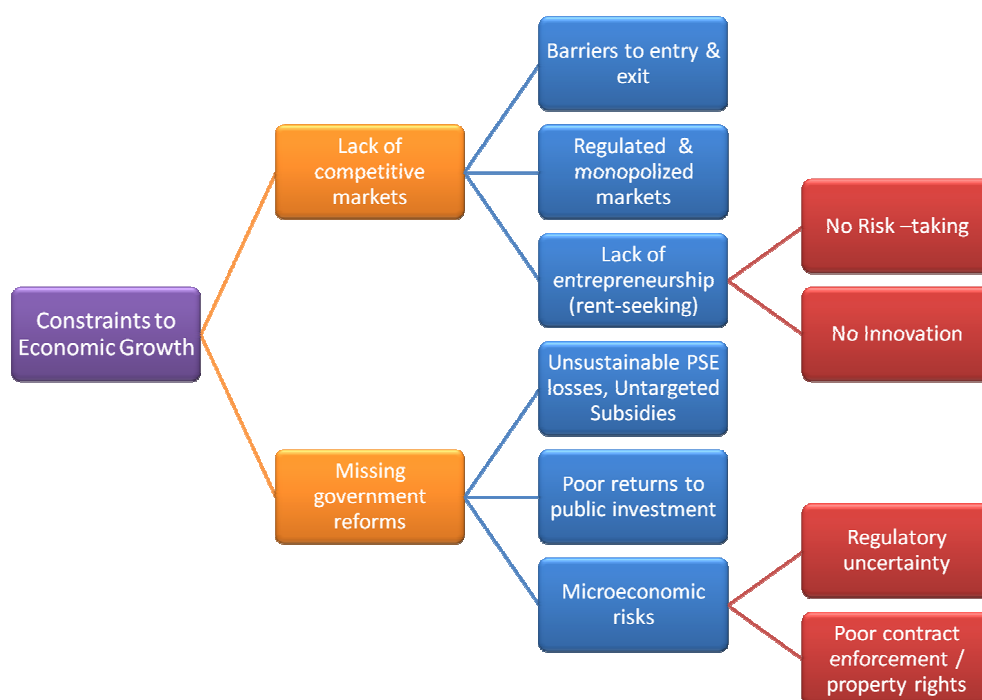
¹⁷ P Martin and CA Rogers, 'Stabilisation Policy, Learning by Doing, and Economic Growth,' *Centre for Economic Policy Research*, Discussion Paper 1130, London, 1995.

¹⁸ For a detailed discussion on binding constraints see *One Economics Many Recipes* by Dani Rodrik.

¹⁹ These include a declining GDP, reduction in foreign investment, loss of employment, incomes and exports (particularly from areas directly affected by war), damage to physical infrastructure, diversion of resources towards military operations, cutbacks in Public Sector Development Programme, capital and human flight, exchange rate depreciation and inflation. According to the Economic Survey 2010 the estimated direct and indirect loss to the economy since 2002 due to war on terror is around US\$ 43 billion.

²⁰ See *Israel's boom scores a victory over war* <http://ow.ly/4GQ9A>

Figure 10 Binding Constraints First



Software versus Hardware

Sources, such as the Global Competitiveness Report 2011, indicate that infrastructure in Pakistan (hardware of economic growth) is at least of a similar quality to that in our neighbours (See Table 2). However, they point out that other missing factors (such as innovation, entrepreneurship, markets etc.) impact negatively on the country's competitiveness and need urgent attention. While hardware of growth cannot be ignored given the current infrastructure shortages in the country,²¹ the point is of *relative* weakness—Pakistan is much weaker in software than in hardware.²² Development focus is therefore to be reoriented towards factors that are part of the software of economic growth.

Infrastructure in Pakistan (part of the "hardware" of growth) is at least of a similar quality to that in our neighbours

²¹ World Bank, *Pakistan: Investment Climate Assessment II*, Washington DC, 2007.

²² A comprehensive analysis that identifies the infrastructure gaps is urgently needed. This analysis should comprise: a) diagnosis of coverage, quality and efficiency, b) assessment of long term targets for physical infrastructure, c) institutional mechanism for improved service delivery, and d) financing arrangements

Table 2 Overall Infrastructure Quality (Out of 139 countries)

	Global Competitiveness Index	Quality of Electricity Supply	ICT Usage	Quality of Roads	Quality of Railroad	Quality of Port Infrastructure	Quality of Air Transport
Malaysia	26	40	50	21	20	19	29
Thailand	38	42	79	36	57	43	28
China	27	52	78	53	27	67	79
Indonesia	44	97	103	84	56	96	69
Vietnam	59	98	70	117	59	97	88
Philippines	85	101	106	114	97	131	112
India	51	110	118	90	23	83	71
Pakistan	123	128	109	72	55	73	81

Source: Global Competitiveness Report 2011

The software enables us to better manage what we have

The software of economic growth includes the organisation of institutions, incentives, markets, cities and communities that is in line with globally successful experiences. It supports innovation in developing better uses of new and existing resources and assets, which generate greater productivity. Policies to manage resources that align with global standards and best practices, and that allow for innovation and entrepreneurship at all levels, in all sectors and in all regions are required.

Till the 18th century, human societies experienced little or no growth resulting in a generally poor quality of life. Thereafter, human endeavour discovered

- technological change
- organisation of production for increasing productivity
- system of complex tradable property rights over physical items as well as ideas
- a system of contract enforcement that would allow complex transactions to be written and enforced across time and space

Human well-being has evolved in societies through enterprises which develop goods markets and new ways of doing business. It is human creativity that drives growth. The drive for innovation sparks the entrepreneurial spirit and distributes the benefits of development.

Human creativity is fostered in

- Competitive markets where state guarantees property rights and contract enforcement allow for continuous disruptive innovation to multiply variety of goods and services, and organisations of production and exchange
- Dense cities offer a variety of business and learning opportunities. Deft city regulation allows room for creativity, learning and enterprise while incentivising the minimising of negative externalities

Technology, productivity and innovation are all knowledge driven. Human society develops through knowledge acquisition. Knowledge acquisition depends both on quality formal and informal education. For knowledge to be useful and available to the most innovative, systems of property rights management and contract enforcement must complement competitive markets

Quality governance is critical to economic development and its role should be

- the provision of key social contract goods-security, justice and the rule of law
- the development and maintenance of policy and regulatory frameworks for facilitating enterprise and markets
- public policy for the provision of key public goods (such as infrastructure and education) and dealing with externalities (such as environment)

The learning aspect, in particular, has been missing in the practice of Pakistani firms. Table 3 indicates poor rankings in education, training, goods market efficiency and technological readiness. Again, one of the most fundamental components of growth software is the governance structure. Focused attention to define and strengthen the roles of judiciary, legislature and administration is urgent. Pakistan's global rankings in judiciary, enforcement of contracts, and corruption are disappointing.

Due to the market constraints, the declining share of the formal sector is clearly observable. By the definition used in Pakistan, 70 per cent of firms are classified as 'small'. These do not aspire to expand in scale, given the costs associated with formalisation of large businesses. In Pakistan only 8 per cent of firms are 'large' compared with 54 per cent in Sri Lanka, 47 per cent in Thailand and 52 per cent in Indonesia.²³

Focused attention to defining and strengthening the roles of judiciary, legislature and administration

8 per cent large firms as compared to other developing economies where 50% is the norm

²³ *ibid.*

Table 3 Property Rights, Markets and Technology (Out of 139 countries)

	Property Rights	Corruption	Education & Training	Goods Market Efficiency	Labour Market Efficiency	Financial Market Development	Technology Readiness
Malaysia	37	44	49	27	35	7	40
Thailand	87	71	59	41	24	51	68
China	43	47	60	43	38	57	78
Indonesia	74	65	66	49	84	62	91
Vietnam	88	61	93	60	30	65	65
Philippines	102	135	73	97	111	75	95
India	61	80	85	71	92	17	86
Pakistan	99	108	123	91	131	73	109

Source: Global Competitiveness Report 2011

Vanishing Human Capital

If Pakistan's demographic dividend has to be capitalised, resources must be diverted towards harnessing and improving human capital. This means implementing policies to encourage knowledge, creativity, and independent innovation in order to counter the currently poor performance of Pakistan in the education sector (Table 3).

One in ten of the world's primary-age children who are out of school live in Pakistan

The reform of education needs to address both public and private educational institutions. All tiers of schooling require an outlook that equips Pakistan's youth with tolerance, discourse and capacity for lifelong learning. Unfortunately, at present the country's education system ranks among the world's least effective and the current physical state of public sector schools endorses these low ranks.²⁴ Pakistan has had 10 National Education Policies in the past, 'unfortunately none have attracted and sustained political will needed to turn aspirations into better education'.²⁵ One in ten of the world's primary-age children who are out of school live in Pakistan. This makes the country second in the global ranking of out-of-school children. Access to education is marred with excessive inequality. According to UNESCO estimates, 30 per cent of Pakistanis live in extreme educational poverty – having received less than two years of education. This richest 20 per cent of Pakistanis receive almost 7 years of more education than the poorest. Less than half of women have ever attended school. Paradox is that 26 countries in the world send greater number to primary school, stand poorer to Pakistan in terms of GDP.

²⁴ AK Kronstadt, 'Education Reform in Pakistan,' *Congressional Research Service Report*, Washington DC, 2009.

²⁵ See *Pakistan Education Emergency 2011* <http://educationemergency.com.pk/>

Conceptual Framework of Growth Strategy

Countries that have attained and sustained rapid economic growth show three prominent commonalities:

- a) They had invested in their people. One cannot have developed countries with underdeveloped people—this is one of the greatest tests of development.
- b) They had opened their economies to international trade and competition. Those that tried to follow an autarkic path were left behind.
- c) They had a clear conception of the respective roles of government and market, and developed a competent, professional and a thinking government alongside a vibrant, competitive and innovative market

Countries with economic strategies relying heavily on the public sector have been left behind. Indeed, even countries with authoritarian political structures have made rapid economic progress by liberalising their economic structures.²⁶

Physical and regulatory space for investment, innovation and entrepreneurship is very limited. The influence of the public sector does not stop with the ownership and management of projects. The economy is riddled with rules and regulations that create arbitrary obstructions in doing business.²⁷ These rules and regulations are the source of distortive rent-creation. The regulators, usually with no technical background, are the same civil servants who have been running loss-making public sector enterprises.

While over the years, privatisation has taken the government out of sectors such as telecommunications, banking and finance etc., the public sector has expanded in many sectors like agriculture, transport, construction and trading. At present, not only is the public sector crowding out the private sector in the credit market, it is also preventing entry and competition in the marketplace through a) excessive regulation and b) direct market involvement. For the future, there is a need to correct the role of government. An important strand in the strategy, therefore, is to reduce the pervasiveness of regulations and to formulate a more nuanced role for government actions in the economic sphere.

With good government devoted to thoughtful, limited and focused regulation, investment space is maximised for innovation and entrepreneurship. Experience shows that growth happens in human clusters. Density and mixed use lead to creativity and ideas. Domestic commerce stands stifled as a result of excessively stringent zoning. Two of the largest employment sectors, construction and retail have been marred by multiplicity of regulations. Youth also needs to be engaged and an appropriate way to do so is to let city zoning allow for community and public spaces.

Space for investment, innovation and entrepreneurship is very limited. Space means both physical and regulatory

An important strand in the strategy, therefore, is to reduce the pervasiveness of regulation and to formulate a more nuanced role for government actions in the economic sphere

²⁶ AH Shaikh, 'Keynote Address at Economic Growth Workshop,' *Planning Commission and DFID*, Islamabad, January 2011.

²⁷ The dissolution of such impediments is always time consuming and frequently requires the payment of substantial bribes or 'gifts' to officials. According to the World Bank's study on Pakistan's investment climate in 2007, managers of firms in the sample reported that they had made payments to government officials of close to 35 per cent of the value of their enterprises' sales in order to 'resolve bureaucratic issues'.

What is the Thrust of the Growth Strategy?

While physical investment will be required for growth, it needs to be emphasised that such investment can only happen in an enabling environment.

The strategy comes at a time when Pakistan is passing through several external and internal challenges. It is therefore important to limit our focus on key ingredients in economic growth and not spread the agenda beyond control.

- Emphasis on productivity and efficiency beyond brick and mortar perspective²⁸
- Seeks to build a better government and a market taking the view that good government complements efficient, competitive and connected markets
- Recognises that economic well-being is a result of a variety and frequency of economic transactions. Policy, law and regulation must seek to minimise transaction costs and allow speedy and frequent transactions
- Focus on urban development as a crucible for the nurturing of innovation entrepreneurship and productivity.
- Include youth through community development and the provision of market opportunities while continuing to impart skills and education

In short, the growth strategy seeks to increase the return on investment through measures to improve the investment climate, to reduce the cost of doing business, and to dissolve the impediments to entrepreneurship.²⁹ While physical investment will be required for growth, such investment can only happen in an enabling environment.

²⁸ Studies of long-term productivity growth in Pakistan show that from 1970 to 2005, productivity growth accounted for roughly 20 per cent of the growth of Pakistan's GDP. On the other hand, productivity growth accounted for about 30 per cent of the growth of the GDPs of India and of the East Asia and Pacific region. Alarming, in recent years, productivity growth in Pakistan appears to have slowed down—in the decade 1998 to 2008 it accounted for only 11 per cent of the growth of Pakistan's GDP.

²⁹ These measures of course incorporate investment in physical facilities, for example, those required to provide a reliable supply of power.

Spotlight: Productivity & Innovation

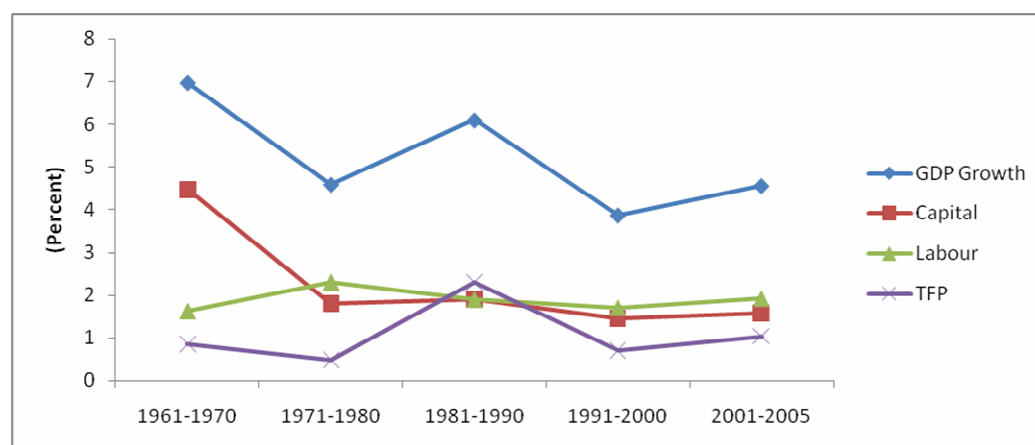
'Never before in history has innovation offered promise of so much to so many in so short a time'. — Bill Gates

Current & Past State of Productivity

Growth happens through the accumulation of factors such as labour and capital, and productivity through the efficient allocation of those assets—known as Total Factor Productivity (TFP). TFP is measured as the portion of growth that is not explained by factor accumulation i.e. increases in labour and capital. The contribution of productivity in the growth of Pakistan's GDP has been less than impressive (Figure 11). During the period 1960 to 2005, 80 per cent of the GDP growth rate in Pakistan was explained by capital accumulation and labour expansion, and only 20 per cent by TFP. The TFP fluctuated considerably during this period: it explained almost 38 per cent of GDP growth rate in the 1980s, fell to merely 18 per cent in the 1990s, and recovered somewhat during the period from 2001 to 2005 to 22 per cent.³⁰ More recently, during the period from 1998 to 2008, TFP growth has only contributed 11 per cent to the growth of GDP.³¹

The contribution of productivity in the growth of Pakistan's GDP has been less than impressive.

Figure 11 Growth Accounting in Pakistan by Decades, 1961-2005 (%)



Source: World Bank 2006³²

Labour productivity in Pakistan is growing at a comparatively lower rate than its neighbouring countries (Figure 12). Pakistani labour is the least productive and over

³⁰ Government of Punjab, *Poverty Reduction Strategy Paper*, Ministry of Finance, Government of Pakistan, Islamabad, 2010.

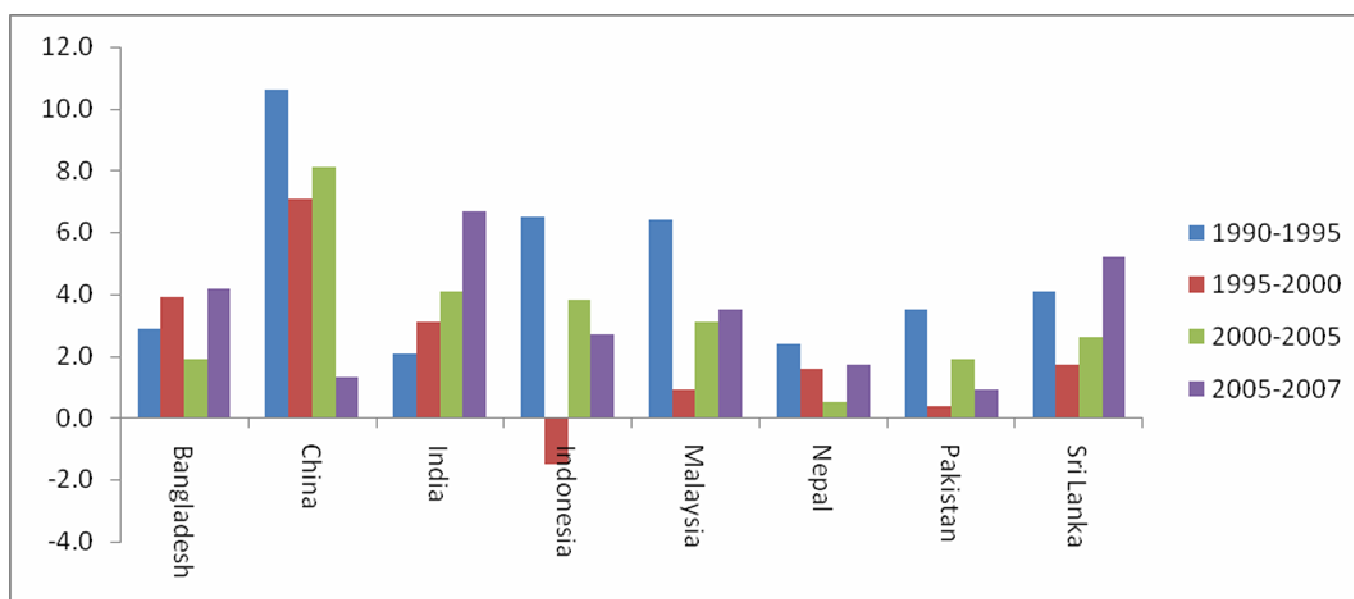
³¹ E Favors and F Koehler-Geib, 'Pakistan—A Fresh Look at the Crisis and Policy Priorities,' World Bank, Washington DC, 2009.

³² *Growth and Export Competitiveness*, World Bank, Washington, DC, 2006

Pakistani labour is the least productive in the region

the last two decades, its performance has deteriorated. Research suggests several reasons including the inadequate education systems, lack of competitive markets, inadequate foreign competition and limited research and development capacity.³³ However it is worthy to note that this same Pakistani labour, when abroad, becomes efficient and productive—a fact validated by many successful Pakistanis today working in labour markets in developing countries and the developed world. This underpins the call for improving the workplace organisation and regulatory environment within which our workers perform.

Figure 12 Cross Country Comparison of Labour Productivity Growth (%)



Source: Asian Productivity Organisation's Productivity Data Book 2010

Low productive key sectors with high labour intensity include agriculture, construction and commerce

The detailed sectoral comparison depicts that the performance of Pakistani labour is not exemplary in any of the major sectors of the economy (Table 4). In fact productivity is low in key sectors having higher labour intensity which includes agriculture, construction and commerce. The unsatisfactory performance in the wholesale and retail sectors emphasises room for improvement in connectivity and domestic commerce.

³³ S Khan, 'Macro Determinants of Total Factor Productivity in Pakistan,' SBP Working Paper Series No. 10, 2006

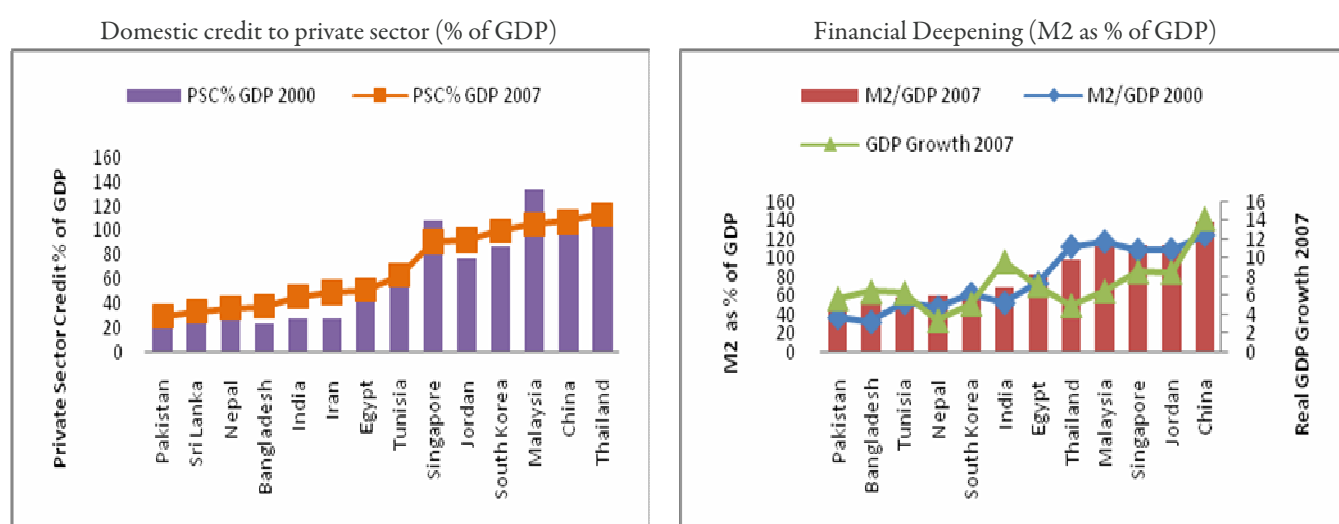
Table 4 Labour Productivity by Sector, 2007

Sectors	Pakistan	India	China	Bangladesh
Agriculture	0.2	2.2	6.8	1.4
Manufacturing	2.8	0.5	6.4	1.9
Construction	1.7	8.0	5.2	3.8
Wholesale and retail trade, hotels and restaurants	1.4	6.4	6.2	2.5
Finance, real estates and business activities	2.3	7.0	7.4	-8.4

Source: Asian Productivity Organisation's Productivity Data Book 2010

The last 10 years have witnessed considerable deregulation, liberalisation and privatisation in the financial sector. Starting with three-quarters of banking assets controlled by public sector banks in the late 1990s, almost 80 per cent of assets are now under private control, with the bulk of the remaining banking assets under government control of the largest commercial bank—the National Bank of Pakistan. Nevertheless, Pakistan has the lowest private sector credit-to-GDP ratio among leading emerging economies (See Figure 13), which may pose a challenge for promoting entrepreneurship. Financial markets need further augmentation through the development of public bond markets, low and stable real interest rates, and limiting crowding-out of the private sector by public spending along with measures to strengthen key functions of the State Bank of Pakistan.

Pakistan has the lowest private sector credit-to-GDP ratio among emerging economies

Figure 13 Financial Sector Indicators 2000-2007

Source: World Bank Indicators Online 2011

While labour and capital remain the traditional sources of economic growth, new thinking points towards the importance of how production is organised—which in turn is a crucial element in determining national competitiveness. This organisational aspect has to start from reforming the manner by which the government performs its

operations. The rampant corruption imposes a tax on productivity and competitiveness. Pakistan is ranked very low among the most transparent countries, which sends adverse signals to potential investors. Governance issues also add to the cost of doing business.

Firms in Pakistan spend on average 560 hours preparing, filing and paying taxes – double the South Asian average

The 2010 Doing Business Report estimates that firms in Pakistan spend on average 560 hours preparing, filing, and paying taxes, which is double the South Asian average of 284.5 hours. Pakistan's performance in the global competitiveness index also points towards increasing cost of business with respect to security, business cost of violence and institutional performance. Pakistan is continuously placed poorly in some sub-indicators involving public institutions, such as property rights (107), efficiency of the legal framework in dispute settlement (103) and transparency of government policy (115). The worsening security environment is reflected by the significant drop in rankings related to the business costs of terrorism (138), business costs of crime and violence (126), organised crime (127) and reliability of police services (119).³⁴ To make Pakistan's manufacturing sector productive and competitive, governance and institutional reforms are required.

Agriculture

Low productivity and yields in agriculture limit the growth of crop sector (See Table 5).

- The unachieved potential in this sector is estimated to be 67 to 84 per cent,
- out of this the extension gap³⁵ is 31 to 75 per cent, and
- the research gap³⁶ is 25 to 75 per cent.³⁷

Cotton production can be increased by 62.5 per cent with the use of certified BT seed and modern pest control techniques

Research shows that this large productivity gap is explained by factors such as traditional farming practices, inefficient irrigation methods, high input costs, lack of bio-safety regulations and insufficient institutional credit for poor farmers. Given the substantial yield gaps (Table 5), there are immediate opportunities to increase production through improved soil and water management, use of quality certified seeds, balanced use of fertilisers and proper plant protection measures. The existing certified seed coverage is unsatisfactory.³⁸ Resistance against genetically modified seeds like BT cotton is also a reason for low productivity. Pakistan can increase cotton production by about 62.5 per cent with the use of certified BT seed and modern pest control techniques.

The availability of water is the principle constraint on Pakistan's agriculture. The efficient use of water is the basic requirement for accelerating agricultural growth. Irrigation efficiency in Pakistan is very low and 60 per cent of irrigation water is lost during transmission from source to the field. Almost 50 per cent of the losses are at

³⁴ World Economic Forum, *Global Competitiveness Report 2010-11*, 2010.

³⁵ Difference between best practice and average yields

³⁶ Difference between research potential yields and the best practice yields

³⁷ M Iqbal and M Ahmed, 'Science & Technology Based Agriculture Vision of Pakistan and Prospects of Growth,' *Pakistan Development Review*, vol. 42, no. 3, 2003

³⁸ Certified seed coverage for cotton is 45%, rice 24%, maize 33%, Wheat 18%, Oilseed 13%, Pulses 12%, and fodder 16%

watercourse level and 33 per cent are at canal level, because of inadequate operation and maintenance of a deteriorating canal system.³⁹

In addition to stressing water conservation, an important part of the strategy for accelerating growth in the agricultural sector is to shift the pattern of production towards higher value-added activities. Comparative natural advantages have to be the guiding principles in agricultural activity selection. Two such activities are animal husbandry and dairy farming.

Table 5 Yield Gaps of Major Crops, 2008

Crop	World Best Yield (2008) (Tonnes/ha)	World Average 2008 (Tonnes/ha)	Progressive Farmers' Yield (Tonnes / ha.)	National Average Yield (Avg. of last 3 years) (Tonnes / ha.)	Yield Gap w.r.t Progressive Farmer (%)
Wheat	8.3 (U.K)	3.09	4.6	2.6	43.5
Cotton	1.9 (Australia)	0.73	2.6	1.8	30.8
Sugarcane	121.1 (Egypt)	71.51	200	54.5	72.8
Sindh Punjab			130	49.9	61.6
Maize	9.7 (U.S.A)	5.11	6.9	2.9	58.5
Rice	9.7 (Egypt)	4.31	3.8	2.1	45.6

Source: Agricultural Statistics of Pakistan 2008-09, Planning Commission, 2009

An important constraint on GDP growth, although it is not recognised as such in Pakistan, is the deterioration in the physical environment. The economic consequences of environmental degradation are significant—the World Bank has conservatively estimated the mean annual cost of environmental degradation at approximately 6 per cent of GDP.⁴⁰ This, let it be noted, is higher than the trend growth rate of Pakistan's GDP between 1972 and 2010. The highest cost was from inadequate water supply, sanitation and hygiene, followed by agricultural soil degradation, indoor air pollution, and urban air pollution. Even the foregoing cost estimate was a significant underestimate, since it omitted several important categories of loss—most notably fisheries and coastal zone degradation—because of the absence of adequate data. Environmental degradation disproportionately affects the poor and the vulnerable; therefore interventions that mitigate environmental damage not only accelerate growth, but also help to convert this growth into broader development benefits, such as a more equitable distribution of income.

Reversing environmental degradation can play a key role in accelerating Pakistan's GDP growth. A clear example is offered by the impact of environmental degradation on the prospects for the agricultural sector. Pakistan is largely an arid country and is further disadvantaged by its dependence on a single river system—that of the Indus—for its surface water. The country is therefore particularly vulnerable to the

Environmental degradation is costing Pakistan in terms of low GDP growth

³⁹ S Ahmad, J Mohyuddin, SM Siddiqui and MN Bhutta, 'Tree Plantation for Intercepting Canal Seepage and Controlling Watertable,' *Pakistan Journal of Water Resources*, vol. 11, no. 2, 2007

⁴⁰ World Bank, *Pakistan: Strategic Country Environmental Assessment*, Washington, DC, 2006.

consequences of basin degradation and water pollution. Agricultural growth is threatened by depleting soil fertility, degrading range lands and encroaching deserts. About two-thirds of the population is rural and relies heavily on natural resources for its livelihood. A degrading resource base, therefore, has a very direct impact on the incidence of poverty.

Estimates suggest that about 40 per cent of irrigated land has been affected by either salinity or water-logging

Land degradation, caused largely by salinity and water-logging (estimates suggest that about 40 per cent of irrigated land has been affected by either salinity or water-logging), limit Pakistan's ability to expand cropped area. This has been caused partly by physical factors, such as a leaky canal irrigation system, but also by issues of governance. The World Bank Report on the environment, cited earlier, pointed out that, paradoxically, in a country where water scarcity is a serious problem, there is evidence that in several years agricultural yields declined with increased water usage. This evidence was obtained from studies and satellite imagery for both Sindh and the Punjab. The relationship was a direct consequence of over-watering. Since irrigation fees have been set too low and are not related to consumption, there is a tendency to use all the available supply. The result is an increase in water-logging, damage to soil structures and an inevitable reduction in productivity. The World Bank estimated that the mean cost of salinity in 2004 amounted to nearly 1 per cent of GDP. Hence, a development strategy that relies on accelerating the GDP growth rate cannot afford to neglect the environment, even while looking at it from narrowly technical considerations. Environmental issues are of even more importance when one considers them as an essential element contributing to the quality of life.

The livestock sector contributes around 53.2 per cent of value-added in agriculture, provides employment to 1.5 million people and has a promising potential for growth in future.⁴¹ Although the livestock sub sector has improved over the last few years, there still remains considerable room for improving its productivity. In the dairy sector, there is a 78 per cent yield gap, if compared with minimum standards required to compete globally. The main determinants of this poor performance include an extension gap of 61 per cent and a research gap of 52 per cent. Moreover, 30 to 40 per cent of livestock is underfed and only 10 per cent is vaccinated, which makes it vulnerable to infectious diseases.

An estimated 20 per cent of current milk production is lost due to poor infrastructure facilities

Pakistan's dairy sector has an enormous potential, but it is still untapped. Pakistan is the 4th largest milk producer in the world, yet its share in the global milk market is negligible and only 3% of the total milk production is currently processed. Overall, the contribution of the dairy sub sector to the national economy is Rs 540 billion (with 97 per cent as informal non-documented economic activity), and is expected to grow at 4 per cent per year under the current scenario. An estimated 20 per cent of current milk production is lost due to poor infrastructure facilities. As a result of these factors, Pakistan is a net importer of milk and milk products (32 per cent of the milk powder requirement is met through imports). Almost 70 per cent of the dairy farmers are small-holders (with small herd size) who need well defined milk collection systems and cold chain on the model of Indian Dairy Cooperatives to get the fair price of their produce and better market access.

⁴¹ *op. cit.*

Public sector agriculture R&D institutes have overlapping responsibilities and the research output is not satisfactory. According to World Development Report 2008, the rate of return of public sector investment in agriculture R&D in Pakistan is almost half as compared with other developing countries and only 13% of the returns of developed countries. Professional capacity of research organisations (PIDE, PARC, API, PERI, AERC etc.) has considerably eroded over the years. There has been little research on policy related issues like price, subsidies, taxation of agriculture production and international market trends. Active presence of public sector in input and output markets is causing problems for the private sector to flourish. Role of government in certain legislative issues (Seed Act, Plant Breeders Rights Act etc.) is also decelerating the growth of agriculture sector.

Industry

During the 1990s, TFP growth in the manufacturing sector was only 1.6 per cent and over the period 1998 to 2007, it increased only by 0.9 per cent. The growth of the manufacturing sector was driven mainly by growth in inputs.⁴² Moreover, substantial excess capacity exists in the manufacturing sector. The Ministry of Industries and Production estimated excess capacity in the sector in 2009-10 at almost 51 per cent. It attributes the underutilisation of capacity to constrained energy sector, the high cost of production and depressed external demand. The problems with the energy sector are particularly significant and are taking a toll on manufacturing sector productivity—total manufacturing sector losses because of the energy shortfall are estimated at 2.5 per cent of GDP.⁴³

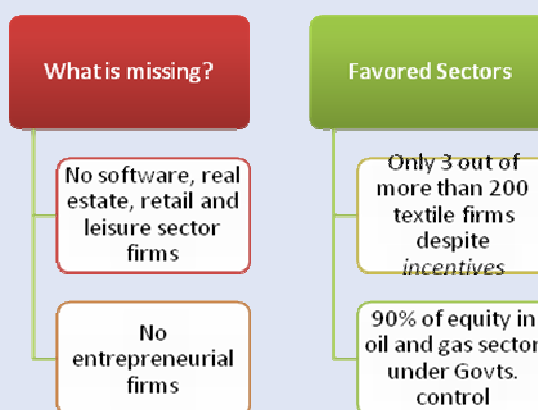
Consistent subsidies have adversely affected the risk taking culture in the private sector

It must be argued here that Pakistan's industrial sector is still far from open. The liberalisation of trade and investment regimes allow for new ideas and creative opportunities besides ensuring a handsome consumer surplus across the board. There is an urgent need to revisit the role of entities responsible for reducing tariff and non-tariff barriers. These include the Commerce Division, Industries Division, EDB, NTC and FBR. Similarly at the provincial level, the government entities (e.g. Department of Industries) must change their stance which favours domestic production over quality and competition. Box 4 indicates that our private sector has always relied on government subsidies while the move towards risk taking and innovating own processes and products has been missing.

⁴² AA Chaudhry, 'Total Factor Productivity Growth in Pakistan: An Analysis of the Agriculture and Manufacturing Sectors,' *Labore Journal of Economics*, vol. 14, 2009, pp. 1-16.

⁴³ Ministry of Finance, *Economic Survey of Pakistan 2009-10*, Government of Pakistan, Islamabad, 2010.

The top 100 firms at the Karachi Stock Exchange belong to sectors which have accrued substantial favours in the past through government policies. These include sugar, textiles, fertiliser, cement etc. The list does not include a single entrepreneurial firm. At the same time, none of the protected sectors have performed well. One finds that only 3 out of more than 200 textile companies make it to the KSE 100 Index. This is despite government support in terms of tax breaks, subsidies and other incentives which the sector has been receiving over past couple of decades. As of 2010, KSE had placed more than 40% of these 200 plus companies in 'defaulters' and 'non compliant' segments.



Public Sector Productivity

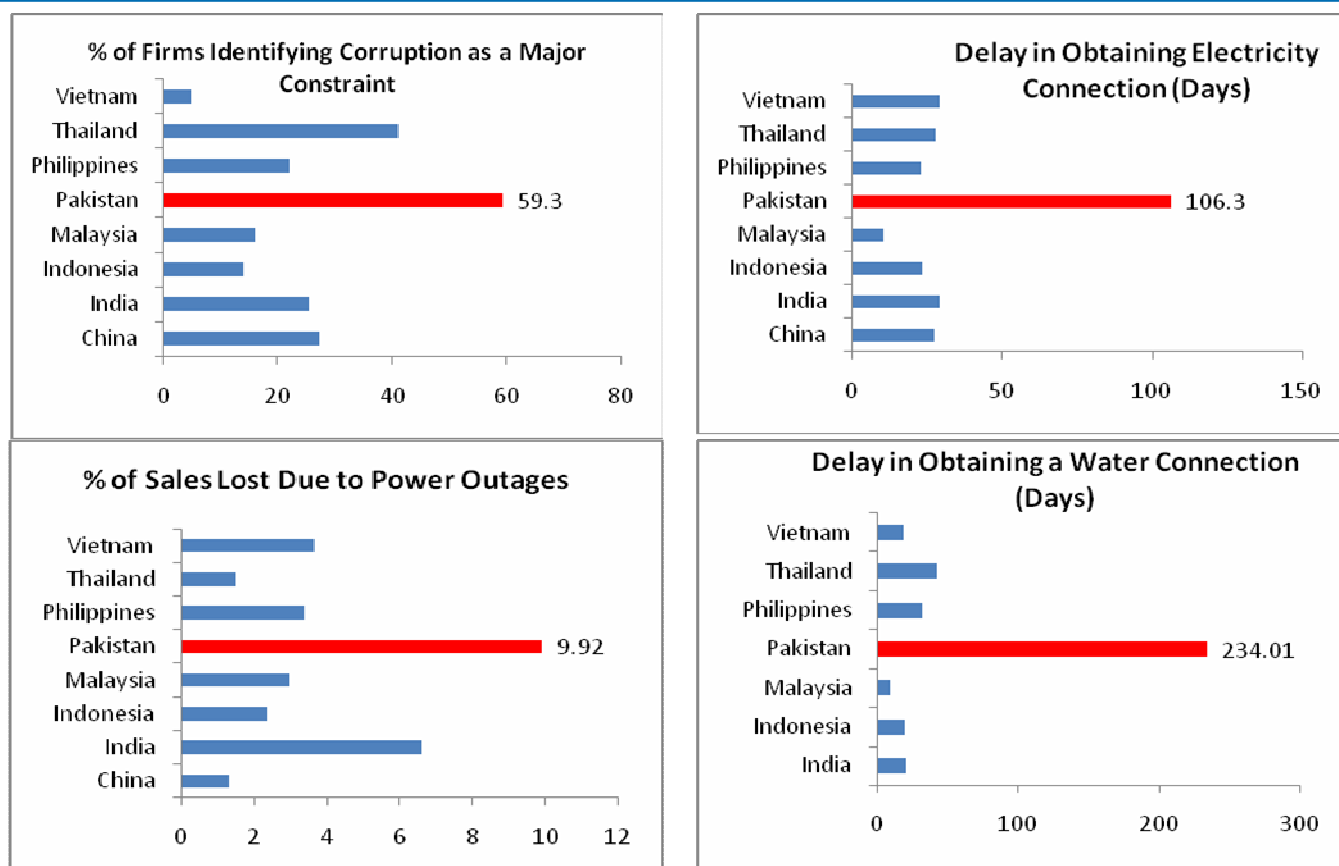
**Transform state's role
from owner-operator to
facilitator-regulator
across economic activities**

Public Sector Enterprises (PSEs) are a source of inefficiency and low productivity. For the last few years, the PSEs have incurred operational losses amounting to 1.5 per cent of GDP annually, and require regular budgetary support and sometimes distortive subsidies. These PSEs are also a major reason for huge government borrowings from the State Bank of Pakistan. These borrowings amount to nearly 65 per cent of total revenues of the government. The rising domestic debt adds fuel to the inflationary trends and also crowds out the private sector.⁴⁴

Public sector has to take on the enormous challenge of fundamentally transforming the state's role from owner-operator to facilitator-regulator across most economic activities. In order to address the investment climate constraints, the government has to step out of the markets and introduce regulatory simplifications to attract investment. The government must reform itself first, if it is to provide the simple prerequisites of business at the grass root level—which currently depict a dismal picture if compared regionally (Figure 14).

⁴⁴ State Bank of Pakistan, *The State of Pakistan Economy - First Quarterly Report 2010-11*, Karachi, 2011.

Figure 14 Impact of Governance on Firm Performance



Source: Enterprise Survey 2007

Reforms for Productivity

Cross-country comparisons of TFP in Table 6 indicate that both the historical performance of Pakistan in terms of TFP and the forecast for the next decade are not encouraging. Pakistan has the lowest TFP among the sample countries and the position will not improve in the future without deliberate and concerted action.

Table 6 Productivity Indicators, Actual and Projected, 1981–2030

Countries	TFP Growth			Capital Per Labour			GDP per Labour		
	1981 - 2007 (Actual)	2011-20 (Projected)	2021-30 (Projected)	1981-2007 (Actual)	2011-20 (Projected)	2021-30 (Projected)	1981-2007 (Actual)	2011-20 (Projected)	2021-30 (Projected)
	Annual Average Growth Rate								
China	4.07	2.36	2.17	7.80	7.50	7.02	7.73	5.75	5.06
India	1.34	1.16	1.26	3.78	3.56	3.68	3.35	2.94	2.90
Indonesia	0.59	1.37	1.37	3.25	3.79	3.84	2.21	3.16	3.08
Korea	1.35	2.14	1.91	6.43	4.08	3.93	4.51	3.97	3.66
Malaysia	0.71	1.67	1.58	4.19	4.02	4.16	3.15	3.59	3.41
Pakistan	0.78	1.04	1.19	1.29	2.85	3.38	1.84	2.70	2.83
Philippines	0.19	2.21	2.03	0.33	3.50	3.74	0.70	3.84	3.71
Thailand	1.50	1.74	1.72	4.02	4.16	4.01	3.59	3.87	3.64
Viet Nam	1.52	2.27	2.07	6.08	2.91	3.08	4.08	3.73	3.37

Source: ADB, “Economic Growth in Asia: Determinants and Prospects,” Economics Working Paper Series No. 220, September 2010.

It is important to move the efficiency of the average firm towards that of the most efficient

In addition to learning from the experience of other countries, it is also essential to mimic and disperse the best practices within the country; in other words, it is important to move the efficiency of the average firm towards that of the most efficient. Table 7 shows how Pakistan could improve its global position in doing business by adopting its own best practice benchmarks.

Table 7 Improvement in Doing Business 2009

Indicators	Existing Ranks	Improved Ranks with Pakistan's Best Practice
Starting a business	63	59
Dealing with construction permits	105	46
Registering property	119	87
Enforcing contracts	158	138
Paying taxes	143	107
Trading across Borders	78	73

Source: Cost of Doing Business, World Bank 2010

Competitive Markets

Markets must be allowed to determine optimal allocation of resources

Competitive markets are the starting point towards increasing efficiency and sustained economic growth. Free and flexible markets allow businesses, which have run the course, to exit and be replaced by more efficient firms. Markets must be allowed to determine the optimal allocation of resources instead of providing fiscal incentives based on sector-specific biases. Incentives should be formulated to cultivate innovation and entrepreneurship.

The growth strategy stresses the immediate need to address missing and incomplete markets. To summarise, major initiatives in this regard may be:

- Limiting the role of government in goods and factor markets
- Strengthening the role of private sector enterprises through:
 - Rewarding ideas-led innovation
 - Resolving the energy crisis by accelerating power sector reforms
 - Abolishing the bottlenecks in doing business
 - Supporting the creation of an entrepreneurial eco-system within the country
 - Computerising the land and revenue records
 - Speeding the enforcement of contracts
- Preserving autonomy of the State Bank of Pakistan in order to limit government borrowing
- Restructuring PSEs and ultimately divesting control to the private sector
- Removing imperfections from farm-to-market channels, including storage and transport
- Promoting the culture of commercial research and development. Respecting intellectual property rights to attract mature investments
- Removing statutory requirements in labour markets that cause hiring inflexibilities

In order to make the overall trading process efficient there is a need to further simplify customs procedures, develop an integrated supply chain management service with real-time cargo monitoring and internet-based transactions. The potential offered by regional trade (e.g. trade with India) needs to be exploited.⁴⁵

Sectoral reforms must complement the above-mentioned changes. Agriculture must diversify into high value-added products, reduce the loss of fertile land to real estate speculations, improve marketing systems (especially for perishable commodities), improve water management and set up centres for agro-genomics. The livestock sector can access productivity gains through improving the quality of feed, deepening health coverage, breeding genetically superior livestock and upgrading marketing facilities. In the manufacturing sector apart from the investment in increased capacity and technology, there is a need to improve local design capacity through new clusters for training, design and testing, better managerial practices and adaptation to technology. One should not forget the export potential of the services sectors in Pakistan, particularly transport, communications, banking, insurance and retail sectors. In order to achieve competitiveness in these sectors, quality investments in human capital are long overdue.⁴⁶

Simplification of arduous procedures is a requirement to develop integrated supply chains

⁴⁵ See Planning Commission's *Panel of Economists Report 2010*. The report also recommends expanding trade activities with India and other regional partners.

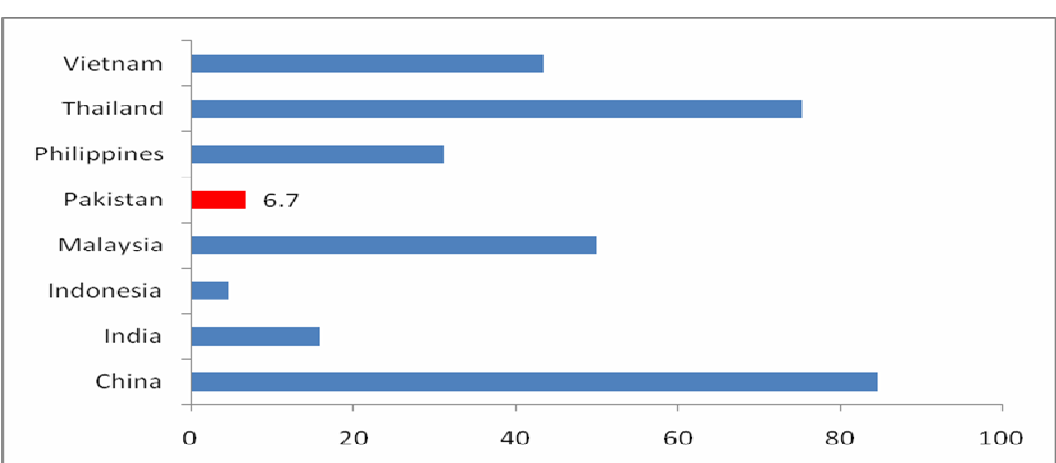
⁴⁶ Planning Commission, *Vision 2030*, Government of Pakistan, August 2007.

Physical capital will come to naught unless backed by adequate human capital.

A Productive Human Resource

The growth strategy recognises that while improving the infrastructure, correcting market imperfections, strengthening institutions and so on, though vitally necessary measures, are not enough. Productivity will never increase sufficiently unless the men and women who work the infrastructure, run the institutions, labour in field, factory, school, hospital, shop, and office are themselves healthy, trained and efficient. The physical capital will come to naught unless backed up by adequate human capital. Human resource development thus plays a crucial role in the strategy.

Figure 15 Percentage of Firms Offering Formal Trainings



Source: World Bank Indicators – Business Environment

Training employees is highly underrated in public and private sector organisations

The cross-country comparison of firms imparting training to their employees indicates that only a very small percentage of Pakistani firms offer training to their employees (Figure 15). Moreover, the public sector organisations responsible for human resource development are not producing high-end labour force, the deficiency of which is hampering firm level productivity.

A Healthy Population

Human capital and resulting productivity are vital determinants of economic growth. Besides other factors, health has also been regarded as crucial in fostering growth. However, fragmented health system and relatively poor health status in Pakistan require a process of reforms so as to have an optimum impact on growth.

There is a persistent increase in non communicable diseases

Health indicators in Pakistan have witnessed relative improvement within South Asian region but still are not satisfactory. Pakistan ranks 125 in the Human Development Index with a maternal mortality of 276, infant mortality of 72 and skilled Birth Attendance at 39 per cent. There is persistent increase in incidence of non-communicable diseases. The last national nutrition survey in 2001-02 reveals that no substantial change in the nutritional status has been recorded, particularly among children less than 5 years. The maternal malnutrition is estimated at 26 per cent and is resulting in Low Birth Weight Babies (LBW).

Some of the reasons for low health indicators are lack of mechanisms like proper implementation of policies; monitoring and evaluation; result-based management; governance; socio-economic disparities etc. Pakistan's MDGs Report 2010 indicates that health related targets cannot be achieved by 2015 unless some concentrated effort is made.

The health infrastructure consists of 968 hospitals, 4,813 dispensaries, 5,345 Basic Health Units, 572 Rural Health Centres, 293 TB Centres etc. In addition, there exist 73,652 health facilities in private sector. There is one doctor available for 1183 persons in 2009-10 as compared to 1245 persons in 2007-08, and one dentist for 16914 persons as compared to 19417 persons for the same period. The 2008-09 PSLM survey shows that utilization of public sector health facilities is quite low.

An assessment of the previous decade shows a declining trend in public sector health expenditures during the years of high as well as low growth. At present, Pakistan spends 0.54% of GDP on health. The private expenditures constitute two third of total health expenditures, out of which 99.6% are out-of-pocket expenditures indicating a large gap in health service delivery.

Weak health systems and policy linkages need to be addressed

Historically, five year plans have been playing the overarching role of policies in the health and other social sectors. However, during the last two decades health policy documents have become focus of sectoral priorities. An assessment of previous health policy and the Medium Term Development Framework (MTDF) suggests mix results with policy implementation remaining weak. Similarly, national health programs show mixed results with achievement of some of the targets.

The fundamental issues regarding poor health indicators and performance suggest weak health system with an isolated project-wise approach; weak linkages between policies, plans, PC-1s, strategic plans etc. In addition, socio-economic disparities; weak oversight mechanisms of the programs; centralised institutional mechanisms are some of the major factors responsible for overall poor outcomes.

An elemental shift has taken place through passage of 18th Amendment. The Concurrent List in the Constitution has been abolished making health a provincial subject. Therefore, planning for the next five years would focus on aggregated policy priorities of provinces with an advisory federal role within the parameters of the Constitution.

Health is a provincial subject with an advisory federal role

The strategy recommends the following major elements as a response to the challenge of improving health and nutrition outcomes.

- Revamping/management of primary, secondary and tertiary healthcare: The pre-hospital/emergency care and health interventions in catchment areas should be strengthened through scale up of Rescue 1122 and linked with programs in catchment areas of primary care facilities. All programs working at the level of primary care shall be integrated i.e. maternal, child health, immunisation, malaria, nutrition etc. Secondary care should be strengthened through modernising

District Headquarter Hospitals through public-private partnerships. The tertiary care hospitals should be strengthened through hospital autonomy.

- **Healthcare Financing Reforms:** A multifaceted and comprehensive healthcare financing strategy must be prepared so as to move towards a National Health Services (NHS) program. In this regard, social health insurance should be introduced for extremely poor at the platform of BISP. Moreover, this insurance should cover both formal and informal segments. Private health insurance schemes should be encouraged to ensure maximum coverage.
- **Governance reforms in Health Sector:** Intervention should be initiated in terms of building partnerships, aid effectiveness, career structures, capacity building, accountability, quality and access to medicine etc. In the short to medium term, consolidation of services must be emphasised including enforcement of quality standards, regulatory mechanisms, introduction of essential health services package. Health partnerships should be built with parastatal organisations, charities, philanthropies, private sector, development partners/INGOs for service delivery at each level. Moreover, aid effectiveness should be ensured for transparency and efficiency. Human resource development is another area where reforms are required mainly through career structures. Access to affordable and quality medicine must be ensured. For enhancing accountability, a new structure of Health Ombudsman in the office of Federal Ombudsman should be introduced.
- **Food Safety and Security:** During short term (one year), a minimum dietary requirements package be prepared and promoted through print and electronic media. It should include home-grown food and must ensure household food security which is one of the causes for prevalence of malnutrition. Furthermore, 'street food' provides cheaper diet for millions of working people across the country, with a minimum level of quality and safety standards setting, it can become a safe and nutritious diet. A regulatory mechanism must be introduced in this regard which is the case in some other countries. A subsidised nutritious food package shall be introduced for mothers and children in the most vulnerable segment of the population. In addition, school nutrition program shall be re-introduced in the form of cash transfers for food.
- **Micronutrients and fortification:** There are quite a few initiatives being implemented through the public sector as well as through parastatal and INGOs regarding micronutrient and fortification methods (Vitamin A supplementation, Iodine salt, iron supplementation etc.). These programs should be integrated and interlinked at primary healthcare level.
- **Mass Awareness:** Mass awareness campaign through print and electronic media should be initiated for behavioural change communication with regard to nutritious dietary habits.

Making Education Meaningful

A much stronger performance in education is the key to improving productivity. Table 8 shows the average years of schooling in Pakistan and comparable developing countries. While there has been some improvement in the indicators between 2000 and 2009, Pakistan's performance still is significantly worse than that of the other countries in the sample (Table 8).

Improving educational outcomes will require a considerable effort. Pakistan ranks 118 out of 129 countries on the Education for All (EFA) Development Index. In 2007, the Gross Enrolment Rate (GER) for primary school (ages 5–9) was 91 per cent; substantially lower than in neighbouring countries such as India (112 per cent), Bangladesh (103 per cent) and Sri Lanka (108 per cent). Because of the significant number of over-aged children in primary schools in Pakistan, the Net Enrolment Rate (NER) is substantially lower at 55 per cent. There are also substantial regional and urban-rural income disparities in primary enrolment. Primary NER for the rural female child in the poorest quintile is 26 per cent, compared with 81 per cent for the urban female child in the richest quintile. Gender differences are larger in the rural areas and more pronounced in the poorer quintiles.

Table 8 Average Years of Schooling

Country	2000	2005	2009
Brazil	4.18	4.59	4.9
Sri Lanka	7.32	7.74	6.9
China	4.84	5.35	6.4
India	3.30	3.63	5.1
Indonesia	4.40	4.93	5.0
Malaysia	5.26	5.92	6.8
Mexico	5.11	5.59	7.2
Pakistan	2.49	2.81	3.9
Peru	5.68	6.19	7.6
Philippines	6.80	7.25	8.2
Turkey	3.60	3.95	5.3

The transition from primary to secondary education is low. About 15 per cent of children in the 10–18 year old age group who have attended primary school drop out before completing primary school. The primary school GER level drops from 91 per cent 53 per cent at the middle school level (ages 10–12). At the Matriculation/High School level (ages 13–14) the GER is estimated at 50 per cent. The tertiary education enrolment rate is estimated to be less than 4 per cent of the eligible age cohort (ages 17–23), compared with 8 per cent in India and nearly 30 per cent in Malaysia.

The private sector has come to play an important and growing part in the delivery of educational services, especially in the urban areas, but also increasingly in rural areas. The sector has expanded rapidly from 3,300 institutions in 1983, to about 90,000 in 2009 and now caters to around 40 per cent of total enrolment. In urban areas, private schools account for well over half of total enrolment. In tertiary education, half of all universities are in the private sector and account for 25 per cent of all enrolment.

The improvement in the country's education system will require a combination of efforts both on the hardware and the software sides. Moreover, because of the focus of government and donors on primary education, often at the expense of higher levels, a significant imbalance has developed between facilities available at different levels. Thus, there are on average six government primary schools for each middle or higher level school, and in some parts of the country this ratio is as high as 1:13. A successful growth strategy, especially for the longer term, must pay attention to correcting imbalances between the different levels of education.

Weak governance is the key reason for poor performance of the education system. Some of the key governance challenges that have been identified in recent studies include:⁴⁷

- an overly centralised education system where distant ministries and directorates determine syllabi, post and transfer teachers and manage budgets without results
- no results-based systems
- weak or nonexistent accountability of teachers and educational administrators to parents and communities
- a complex structure, where the provincial government has policymaking responsibility while the district governments are responsible for implementation
- limited capacity for planning and monitoring, especially at the district and lower levels of government
- poor management of available sector resources
- no efforts to build the capacity of parent-teacher councils to contribute to school management
- a lack of clarity regarding policies for private sector participation and public-private partnerships in education

Pakistan is one of only 12 countries where public spending on education is less than 2 per cent of GDP

Thus, while the improvement of education will require larger allocations of resources—Pakistan is one of only 12 countries where public spending on education is less than 2 per cent of GDP⁴⁸—the country will have to recognise that these resources cannot be directed solely to expanding the physical infrastructure. Without efforts to strengthen the governance of the sector, much of the higher expenditure is liable to be wasted and will fail to produce the educational outcomes that are desired and are necessary.

Connecting markets and people

An efficient connectivity structure is pre-requisite for rapid growth. Low productivity of transport infrastructure is annually costing Pakistan almost 5% of GDP, while 30% of agricultural output is being wasted due to inefficient farm-to-market channels, lack

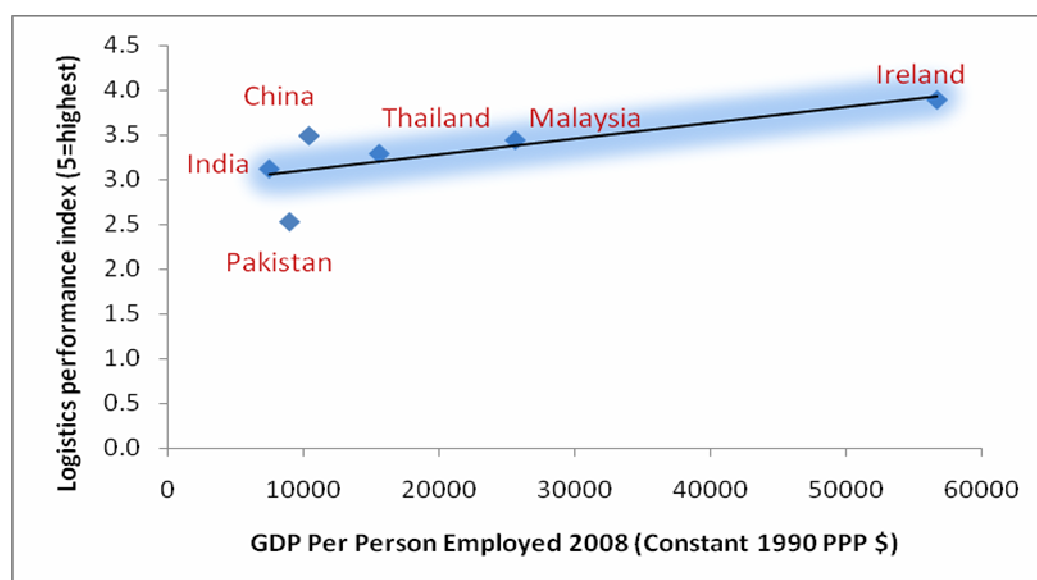
⁴⁷ M Aslam, 'The Relative Effectiveness of Government and Private Schools in Pakistan: Are Girls Worse-off?' *Education Economics*, vol. 17, no. 3, 2009.

⁴⁸ International Crisis Group, *Pakistan: Reforming the Education Sector- International Crisis Report*, Asia Report No 84, 2004

of cold storage facilities and an obsolete and underpowered trucking fleet. Figure 16 illustrates that Pakistan performs poorly in terms of Logistics Performance Index (LPI) as compared with the regional economies. In order to make our rail, road and aviation infrastructure much more productive, the following interventions are required;

- Revisiting the role of Public Private Partnership (PPP) in infrastructure development
- Creating a sophisticated market for Railways
- Creating a level playing field for all market players in aviation sector
- Improving trade facilities through adoption, incentivising and promotion of ICT

Figure 16 Connectivity–Growth Nexus



Knowledge Creation & Commercialisation

The Government needs to decouple the implementation of knowledge-driven innovation policy from the rest of its bureaucratic skeleton. It needs to form a flexible, innovation-centric, autonomous body to orchestrate, implement and gauge the innovation strategy. Such a National Innovation Agency (NIA)⁴⁹ must be guided by thinkers, innovators and corporate leaders, who are able to form alliances with the private sector, and be able to bring in foreign expertise and capital. It should also be mandated to:

- Integrate and inject the country's research centres/think tanks with defined, market oriented, commercially feasible, cohesive research direction. An unproductive practice of producing research-for-sake-of-publication must be replaced by research-for-application.

⁴⁹ J Aubert, 'Promoting innovation in developing countries: A conceptual framework,' World Bank Institute, Washington DC, 2004.

University programs must increasingly be tuned to the requirements of the industry

- Build inter- and intra-university alliances ‘especially between the engineering and business schools’ for commercialisation of technology-business ideas, preliminary research and to forge industry-wide contacts within and outside the region.
- Relevant university programs must increasingly be tuned to the requirements of the industry, and must provide skills that are required by the market. Successful corporate and non-governmental entities should be made to ‘own’⁵⁰ critical university programs as curricula designer, mentor, selector, fund-raiser and trainers in return for foreign grants and fiscal incentives.
- Government must agree to dual-use investments⁵¹ (those possessing socially constructive spin-off capabilities) where the government stands as early user/first buyer by socialising the risk involved.
- Sponsor a nation-wide battle of minds, creative ideas, products, processes and competitions in every major sector; held by universities, corporations, NGOs and chambers (with the process of instantly funding and mentoring best feasible ideas on-the-spot).

Diffusion and Absorption

Developing innovative ideas is not in itself sufficient to spur development unless they are commercially ‘diffused’.⁵² If new ideas are to be instrumental in development, they need to be spread and adopted on a wide scale. The following are some of the ways in which this could be done.

The talented members of Pakistani diaspora must be utilised to spur innovation and development

- Invite talented members of the Pakistani diaspora through the “National Rejuvenation Program” as lecturers, mentors and consultants, invigorating public (in particular) and private sector enterprises and institutions (in general).
- Involve the diaspora as liaison⁵³ mediating between their places of work and Pakistani firms by building strategic linkages, providing valuable local information, helping them to find local suppliers and expertise thus engaging them in lifting the outsourcing potential of Pakistan.
- Direct and facilitate Non-Government Organisations (NGOs) in instituting social entrepreneurship⁵⁴ (blending of social cause into profitable business) at the grass root. Encourage them to transfer technological and managerial knowledge to rural areas (Town and Village Enterprises)⁵⁵ to enhance productivity, efficient utilisation of resources and generation of local employment.⁵⁶

⁵⁰ Engro, Packages, Pakistan Military, USAID, Aga Khan Foundation have been behind the establishment of Pakistan’s prestigious centres of excellence like KSBL, LUMS, NUST, IBA, AKUMC.

⁵¹ For instance by promoting indigenous production of renewable energy hardware, followed by massive acquisition, installation by government helps grow a new industry, overcome energy shortage in far-flung under developed areas.

⁵² The large-scale project on “Science and Civilisation in China” at Cambridge University, originated by Joseph Needham, and which currently comprises close to 30 volumes, bears ample testimony to this remark.

⁵³ Israel, India, Ireland have demonstrated capability of utilising their Diaspora in valuable ways.

⁵⁴ Anil Gupta’s Honeybee Network, Muhammad Yunus’s Grameen Micro Credit Bank.

⁵⁵ SPARK program of China’s Ministry of science and technology <www.idrc.ca/en/ev-55213-201-1-DO_TOPIC.html>

⁵⁶ eChopal kiosk spread across the rural India <www.echopal.com>

Cluster Development

If we look closely at Pakistan's context, the country has already built pseudo-clusters across its spine from IT cluster 'Karachi', automotive manufacturing 'Port Qasim', textile and leather 'Faisalabad', sports and surgical 'Sialkot', furniture 'Gujranwala', light engineering 'Gujrat', heavy industries 'Wah' and even light weapons manufacturing 'Landikotal'.

In order to underpin these 'traditional' clusters, an emphasis on regional and industrial regeneration policies would play an effective role in bolstering the region's advantages. However, for the new cluster development, for example in hi-tech, a focused effort will be required in areas such as science and technology, attracting talent and investment, venture capital and education policies that promote enterprising traits. Apart from such definite prioritisation, Pakistan needs to learn from various available models such as: National Advantage Model (capitalising on natural strengths of the country for instance cheap labour, youth bulge, natural resources, location), Networking Model (banking on and monetising the country's huge network of SMEs both documented and un-documented), Regional cluster development model (clusters as described above) and Research-Industry relationship model (making of clusters in or around academic institutions).

Modern day hi-tech, hi-growth clusters are made around the latter model where one powerful research university (see also Box 5) acts as a nursery to raise, attract and flourish relevant industry around itself. For instance Stanford University gave rise to the Silicon Valley, Cambridge University established the Cambridge Cluster, Indian Institute of Technology transformed Bangalore into an IT hub and Technion and Weismann institutes founded the hi-tech Israeli industry. Industry-University linkage plays a decisive role in exploiting the fruits of such market-researchers fusion—a domain where Pakistan severely lags.

Knowledge-driven innovation policy must be decoupled from the rest of its bureaucratic skeleton

Industry-University linkages play a decisive role in fostering innovation

Box 5

Innovation Councils

Several countries have adopted broad-based and systematic approach in creating an enabling environment for innovation 'encompassing both incremental improvements and absolute new initiatives' with the help of formulation and execution bodies, and discreet initiatives. Some of the successful models across the developing and developed world are Sweden's Agency for Innovation Systems (INNOVA), National Innovation Agency of Thailand (NIA), Pan-European initiative for Innovation and Entrepreneurship under the Innovation Union (IU), Chile's Technology Business and Incubation Program (CORFO) and its complementary National Innovation Council for Competitiveness, Denmark's newly revamped Agency for Science, Technology and Innovation, joint programs of the likes of Swedish-Brazilian Research and Innovation Centre, Finish Innovation Agency (TEKES) and India's National Innovation Fund (NIF). All these initiatives have more or less the same mandate of building a strong and active co-operative framework that builds on the strength of triple-helix 'Industry, University and Government' nexus.

4

Building a Government for the 21st Century

'If you put the federal government in charge of the Sahara Desert, in 5 years there'd be a shortage of sand'. – Milton Friedman

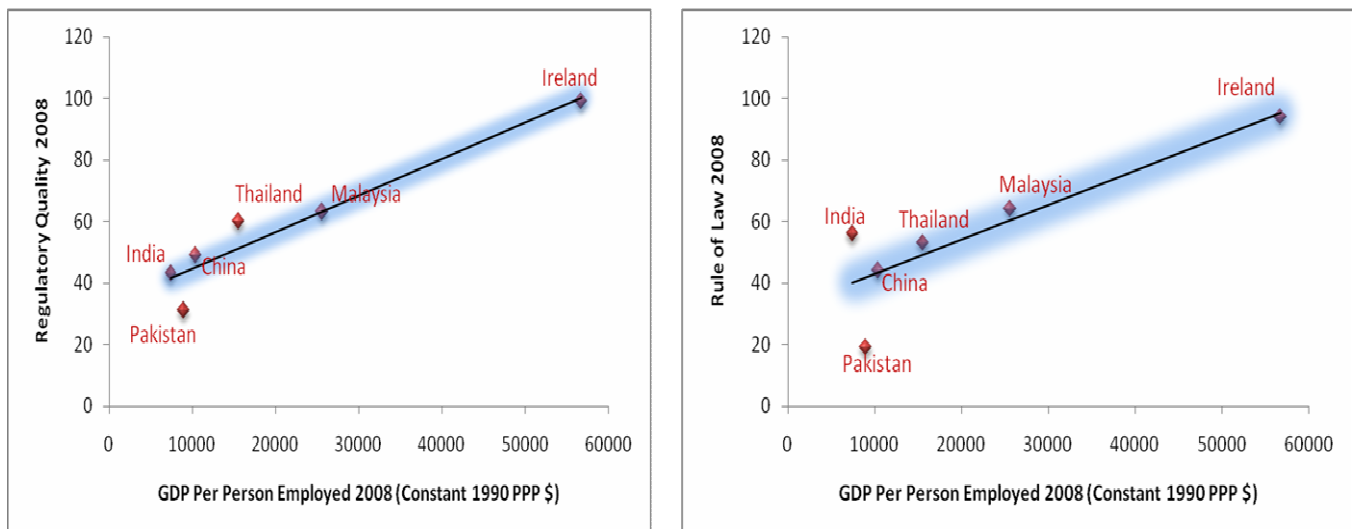
Build Better Government and Better Market

We have all moved beyond the simplistic 'governance vs. markets' debate. There is now a general agreement that a well run government complements and may even be essential to an efficient and competitive market. Analysis and consultations have shown (See Chapter 2) poor governance and dysfunctional markets as among the most important reasons of why growth in Pakistan has not achieved a sustained acceleration.

Governance includes the workings of the bureaucracy, judiciary, taxation and regulatory framework, price and institutional mechanisms

Surveys by the World Bank of the investment climate and of the cost of doing business in Pakistan (in 2003, 2007, and 2010) have consistently shown governance related factors to be the most important constraints to growth. 'Governance' is a rubric for addressing the workings of the bureaucracy, judicial system, taxation system, regulatory framework, price mechanism, institutional arrangements for education and technical training, and so on. On most global indicators measuring governance, Pakistan is currently ranked low and often even below trend. Two such important indicators—regulatory quality and rule of law—are presented in Figure 17 which shows that Pakistan is not only ranking low but well below the trend line.

Figure 17 Impact of Regulatory Quality and Rule of Law on Productivity



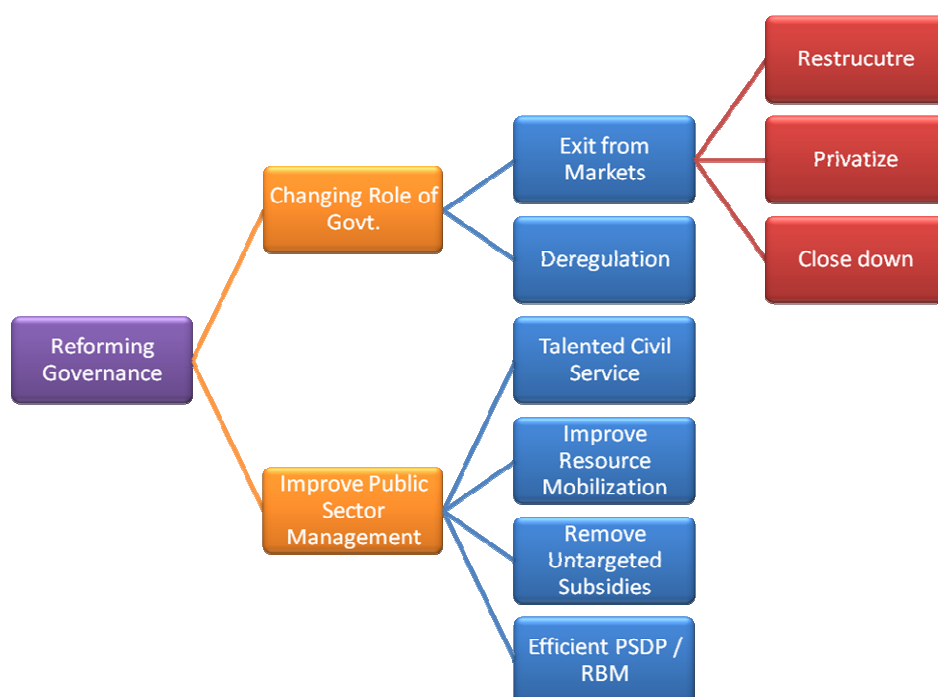
Distortive policies are ruining the budgetary process:

- Public sector enterprises (PSEs) are hemorrhaging about Rs 300 billion annually pushing the fiscal deficit to unsustainable levels
- While the BISP has been developed as a targeted mechanism for addressing poverty, generalized and untargeted subsidies continue
- The government's attempts at delivering public services have often fallen well short of expectations

The large government footprint (50% of GDP) crowds out private investment

A major thrust in the coming period must be building a focused government that complements an efficient competitive market. This will require reorienting the role of government (Figure 18). Currently the government is in every sector as a direct market participant obstructing private sector entry. The foot print of the government has been estimated to be as large as over 50 per cent of the economy making it very difficult for the private sector to expand. Competition Commission too has found that government intervention is impeding the development of competitive markets.

Figure 18 Reorienting the Role of Government



The current dominance of government in markets and its poor quality of regulation in others is limiting the space for private investment. Building a better government will therefore clear space for private investment. The growth strategy therefore focuses on several reforms of government to catalyse private investment. For this, the role of government has to be clearly defined and reform undertaken to move government in that direction.

Better governance will clear space for private sector

Reorienting Role of Government

Excessive regulation
hurts business milieu

The government's role must be to concentrate on protecting public interests and rights, providing necessary public goods, enforcing laws, punishing exploitative practices and operating with transparency and accountability. This may well be a counsel of perfection, but it is the direction in which the government must move.

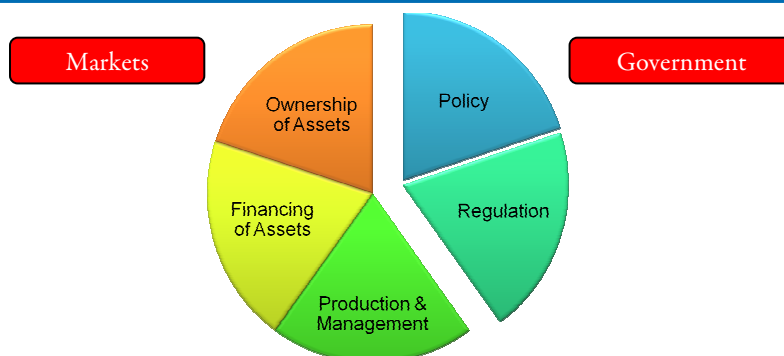
The process of generating wealth in a society may be divided into five main areas: policy, regulation, ownership of assets, financing of assets and production/management of assets. The government will increasingly confine itself to the first two segments, i.e. policy and regulation. The remaining functions, in line with global practices, will be left to the market (Figure 19).

Similarly, sectoral policies must not foster sector picking and should lay down rules of the game that facilitate a level playing field for all. Government should also be careful with regulations in order to ensure minimum level of economic freedom to all citizens. Excessive regulation hurts business milieu. A clear appraisal is required as to which sector should be regulated and to what limits.

Government must exit
from production

Governments exit from production can take three specific forms. These are: a) complete privatisation of government owned productive units, b) partial privatisation of assets in sectors which have become extreme liability for the government, and c) unbundling of supply chain. Given the current state of political economy, the latter two seem like a doable option.

Figure 19 Directions in Reforming Governance



Existence of Monopolies

Consultations with CCP reveal some critical impediments to business which are strengthening existing monopolies. Brief account of some major industrial licensing and financial sector policies of the Federal and Provincial governments leading to existence of monopolies is as under:

- Infrastructure industries are still controlled by the public sector and is thus shut to the private entrepreneurs, just naming a few e.g. railways, gas marketing, ports,

airports and baggage handling, civil aviation, post office, electricity transmission, supply of potable water in cities etc.

- The current bilateral air services agreements (BASAs) between Pakistan and other countries creates monopoly of PIA by granting exclusive rights to PIA for operating direct scheduled services between Pakistan and other countries
- Electricity is sold to just one state owned entity without any choice to the producer to choose its customers
- Lack of public transport in most of the cities is a pointer to restrictive licensing/regulatory regime with threat of creation of monopolies
- Putting up fertiliser plant requires prior allocations of natural gas quote. Thus strengthening the influence of existing firms
- Pharmaceutical prices fixed by government act as an entry barrier and keep monopoly of existing firms. Such actions by the government have also not led to reduced prices for the consumer
- Fixing minimum paid up capital requirement for banking and insurance companies fosters monopolies in this sector
- Fixing prices of certain essential commodities by the Government in consultation with associations of manufacturers not only allows the mafia in each association to grow stronger but also discourages the raw material provider
- Regulatory regime regarding setting up of retail markets of fruits and vegetables is acting as a catalyst for monopolisation by existing businesses

The CCP responsible for promotion of competition and enforcement of the competition law is working under a weak support environment. The autonomy of CCP has always remained under threat. There are still some pending issues that are hindering the actualisation of competition law (Competition Act 2010). These include lack of financial autonomy, poor competition advocacy, lack of human capacity in CCP and slow judicial processes (slow implementation of judicial orders) with regards to already pending cases. Furthermore the Competition Appellate Tribunal has still not been established despite CCP's insistence on various occasions.

CCP needs to be independent in order to promote competition and enforce competition law

Public Sector Enterprises (PSEs) - Critical Surgery

The loss making PSEs will be classified according to three possible remedial measures that have to be driven firmly.

- First, the utilities (such as electricity and gas) need better management and improved regulation. In case of each utility two key issues of pricing and business process reengineering must be addressed. The top tier must be market-trained professionals who can keep the corporate culture entrenched. The top most priority of these professionals should be to make this entity efficient to a maximum extent so that it becomes attractive for privatisation at a later stage.
- Second, the category of PSEs which are directly privatisable. For example we now know from decades of experience that government entities responsible for agricultural procurement and marketing have not only added to fiscal deficit but

PSEs that have outlived their purpose must be considered for closing down

have also led to shortages of strategic food reserves. These must be privatised. Similarly Privatisation Commission’s website gives a vast list of entities placed on the privatisation list. This process needs to be fast tracked.

- Finally there are PSEs that have outlived their purpose and must be considered for closing down. Institutions such as Railways, PIA, Steel Mill etc. have been restructured many times in the past. However, simply changing the corporate faces on the top has not made them viable organisations in financial terms. Even if these are privatised at a notional sum, they will still save the exchequer in the vicinity of Rs. 300 billion annually.

Box 6

Current Status of Restructuring

An institutional framework for appointment of Chief Executive Officers in PSEs has been approved by the Cabinet Committee on Restructuring (CCOR). Status of restructuring is as follows:

- Board of Directors of Pakistan Steel and Railways has been reconstituted. Operational restructuring plan has been presented in the CCOR and it is under implementation.
- Operational restructuring plan of USC has been presented to CCOR and it is being finalized.
- SBP, Planning Commission and Finance Division are finalizing a restructuring plan for TCP.
- Operational restructuring plan of PASSCO was presented to CCOR and various options are being considered.
- Public power sector entities are being restructured
- PIA has presented an initial restructuring plan.
- NHA is in the process of preparing an operational restructuring plan.

There is a need to devise a framework for the effectiveness of Board of Directors. The Boards should be enabled to act autonomously yet their performance may be monitored. Derailment of the restructuring of PSEs can negatively impact the fiscal deficit

Source: Budget Strategy Paper, Finance Division

Unnecessary Subsidies

Until the government switches to targeted subsidy, its fiscal position will remain under pressure

The list of entities receiving mostly untargeted subsidies includes the Pakistan Electric Power Company (PEPCO), Karachi Electric Supply Company, Trading Corporation of Pakistan, Utility Stores Corporation and PASSCO. In addition, the government also subsidises oil refining, wheat and sugar retail, spinning sector mark-up, fertiliser and research and development for the textile and the motorcycle industries. Most of these untargeted subsidies find their place in the budget because of political pressures and not poverty-related arguments.

Table 9 shows the trend of subsidies in recent past. The power sector tops the list followed by commodity operations. Until the time government better targets the subsidies (only for vulnerable segment of the population) its fiscal position will remain

under pressure. The concern here is that if issues such as circular debt and agricultural market distortions become a recurrent feature, the fiscal administrators will keep on resorting to borrowing (particularly from SBP) in turn creating inflationary expectations.

Table 9 Subsidies by Federal Government 2005-10

	July-June	July-June	July-June	July-June	July-June	July-June
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
PEPCO	22.2	19.5	41.9	113.7	91.1	146.6
KESC	13.8	17	16.6	19.6	18.7	32.3
FFC Jordan	0.3	1	1	0.9	0.2	0
Oil Refineries	13	11.2	25	165.9	67.7	11.2
Servicing of Outstanding Liabilities (GIK)	0.1	0.1	0.1	0.1	0	0.1
R&D Support to Textile Sector	0	0	0	17.5	2.3	0
TCP	6	9.3	2.8	45.7	26.6	20.2
PASSCO	1.4	1	0.1	0.4	0.3	0.6
USC	0	0	0.2	5.3	2.7	1.4
Others	0	5.2	19.8	0	2.8	0.3
Sale of Wheat, Sugar etc.	0	0	0	0.7	0.8	0.9
Total	56.8	64.3	107.6	369.7	213.3	213.5
Grants to Railways	4.2	4.8	6.9	7.3	9	18.4

Source: Planning Commission Calculations

In addition to huge hidden subsidies to fertiliser, motorists (CNG) and selected industry through below economic pricing estimated to be of a similar amount as the direct subsidies.

Inefficiency in Resource Mobilisation

Pakistan has a narrow tax base and high enforcement costs. The tax administration is further challenged by complex compliance procedures. The experience with World Bank funded Tax Administration Reform Project (TARP) has yet to materialise into a higher tax-to-GDP ratio. The key objective of this reform includes raising tax revenue through improved compliance with tax laws and broadening of the tax base; improving effectiveness, responsiveness and efficiency of tax administration through institutional and procedural reforms; improving collection through transparent and high quality tax services; and strengthening audit and enforcement procedures.⁵⁷ However, even after several years of this reform effort, tax policy remains complex, and gives favour to a selected few while corruption and poor administration weakens collection and allows vested interests to prevail.

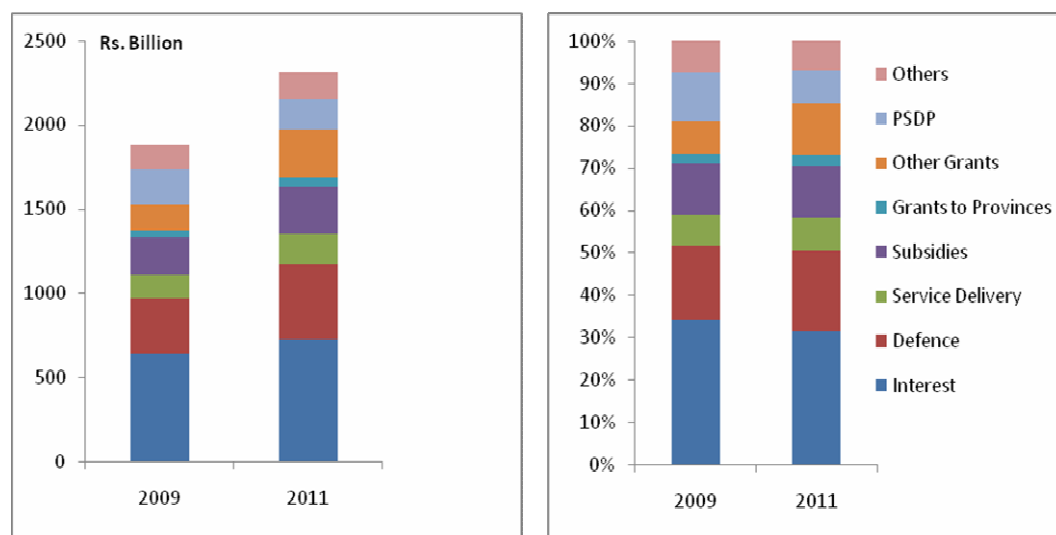
Broadening the tax base and widening the tax net may not by themselves solve the government's liquidity problems. However, if the government reorients its role

Even after several years of reform effort, tax system remains complex and gives favour to a selected few

⁵⁷ For a stakeholder perspective see <<http://ow.ly/4Lgmc>>

towards the efficient delivery of basic public goods, a sound resource base can ensure that visionary projects by the government are not vulnerable to aid injections from abroad. Tax reforms must be complemented with expenditure reforms. The Medium Term Budgetary Framework (MTBF) in Finance Division should be strengthened and also extended to the provincial level. Only in this manner will Pakistan be able to move away from the currently constrained space for improved service delivery (Figure 20).

Figure 20 Budgetary Expenditures



A persistent disconnect exists between increases in income and wealth, and the government's ability to tax these implements

There has also been a persistent disconnect between increases in income and wealth and the government's ability to tax these increments. First, agricultural income earners are not in the direct tax net, thus increases in rural incomes resulting from the surge in commodity prices cannot be taxed by the government.⁵⁸ Second, the very substantial additions to income by rapidly increasing workers' remittances are also excluded from the tax net. Third, most of the income from the rising exports is also exempted from taxes, except for a negligible withholding tax. Fourth, owners of assets and beneficiaries of speculative gains have found it easy to evade taxes; for example, for purposes of official registration, urban property transactions often take place at a fraction of the actual market value. Rural land is exempt from any wealth, property or capital gains tax, other than a modest levy of land revenue. Tax rates on urban immovable property in the main cities of Pakistan are kept low because ownership is concentrated among the elites.⁵⁹ It should not, therefore, be surprising that according to 2005 estimates, the overall tax gap⁶⁰ for Pakistan was more than Rs 600 billion.⁶¹

⁵⁸ S Ahmed, V Ahmed and A Abbas, 'Taxation Reforms: A CGE-Micro Simulation Analysis for Pakistan,' *Development Economics*, 2:182, October, 2010.

⁵⁹ I Husain, 'Disconnects & Mismatches', *Dawn*, February 6, 2011, p.7.

⁶⁰ The tax gap measures the extent to which taxpayers do not file their tax returns and pay the correct tax on time

⁶¹ RA Ahmed and M Rider, 'Pakistan's Tax Gap: Estimates by Tax Calculation and Methodology,' Andrew Young School of Policy Studies, International Studies Program, Working Paper, 8-11, Atlanta GA, December 2008.

18th Amendment and NFC Award

The new NFC and the 18th Amendment to the Constitution of Pakistan will impact the manner in which the federation and provinces interact. The change can be quantified in terms of provincial autonomy, abolishing the concurrent list, strengthening the Council of Common Interests and devolving more subjects to the provinces. There will now be increased responsibility on the provinces for improved public service delivery. In order to carry out the additional tasks, all provincial governments will have to come up with their own medium term budgetary frameworks to increase implementation capacity. The requirements for capacity and better governance should be chalked out at all operational levels, i.e. provincial legislators, provincial government officials and provincial assembly staff.⁶² Planning Commission will stand ready to support all provinces for developing their own provincial growth strategies. At the lower tier, cities with 1 million population and above will be encouraged to design their own urban development strategies.

The success of 18th Amendment will be dependent on how the public service delivery improves in coming years. Enhancing of productivity should involve moving from input-based to results-based management.

Public Sector Management – Heart of the System

There has been a gradual shift in recent years towards the critical role played by human resources in improving and sustaining institutional effectiveness and development performance. Human resource issues have been identified as major constraints for governments not being able to meet their reforms and service delivery targets. No public sector setup can intervene effectively without competent and dedicated public servants.

The capacity development of public servants needs to move to the centre stage in institution building. This realisation has unfortunately often been lost in the negative debate in both developing and developed countries on the role of the public sector in society—a debate that has tended to portray public servants primarily as a cost that can be slashed rather than as an asset that will grow in value if properly nurtured and utilised.

In recent years pursuit for a talented civil service has become a priority in Pakistan. This interest is reflected by the various government attempts to reform the structure and incentives of civil service in Pakistan during the past decades through the 1973 Civil Service Reforms, establishment of the National Reconstruction Bureau, Civil Service Reform Unit at Establishment Division and the National Commission for Governance Reforms (NCGR). The Poverty Reduction Strategy Paper II stressed that a competent, effective and neutral civil service is the backbone of the country's governance structure and proposed widening the talent pool and professionalising the

Success of 18th Amendment will depend on how well the public service delivery is improved

Capacity development of public servants needs to move to the centre stage in institution building

⁶² Pakistan Institute of Legislative Development and Transparency, *Impact of the 18th Constitutional Amendment on Federation – Provinces Relations*, Briefing Session for the Members of Punjab Provincial Assembly, July 2010.

service. Similarly, the NCGR developed a comprehensive report ‘Reforming the Government in Pakistan’ which placed an emphasis on adopting a holistic approach towards human resource management to ‘turn civil servants into competent, motivated, well trained problem solving individuals rather than demotivated, ill equipped, poorly paid sticklers for rules’.⁶³ The reforms outlined by NCGR in the context of reforming civil service need to be urgently implemented.

The civil service in Pakistan has been unable to cope with its increased responsibilities as the role of the state expanded over the past decades. Moreover, the distortive incentive structure and lack of accountability have led to a substantial decline in quality of public service delivery. The current structure is characterised by declining real wages and a non-merit promotion and reward system.

Box 7

The Four Phases of Civil Service Reform in Sri Lanka

Sri-Lanka initiated civil service reforms with the support of multilateral donors in the mid 1980s. In the first phase of the reforms, a comprehensive report on public management was developed by the Administrative Reforms Committee. The report contained detailed measures such as increase in salary of public sector employees. However, many critical reforms such as downsizing were not undertaken due to the lack of political will. The second phase was a structural adjustment—era in which resources were allocated towards the downsizing program. However after the programs had been implemented, the government had more employees than when it began. Many officials believed that the retirement packages were too generous. The third phase featured strategic objectives, management restructuring, and performance appraisal. According to an external evaluation, these measures existed mainly on paper. The management restructuring, was mismanaged, resulting in more ministries than before.

After the failure of the first three phases, Sri-Lanka began to lose donor support. In 2001, the government took a new turn and implemented an amendment to the Constitution restoring the independence of the Public Service Commission which had earlier been manipulated by politicians. It created parallel Police and Judicial Service Commissions, with the leader of the opposition having a real say in the appointment of their members, who would serve three-year terms separate from the electoral cycle. The three main parties and civil servants through their staff associations all supported the reform: “The Public Service Commission means we have justice” was one representative’s view. In one service cadre, political interference had gone down “from 90–100 per cent to 5–10 per cent,” according to a very senior officer in that service.

Source: McCourt, *The Human Factor in Governance: Managing Public Employees in Africa and Asia*. London: Palgrave, 2006

Internationally, civil service reforms became a key component in development policies in the early 1990s. Many governments, under budgetary pressure, directed efforts at downsizing and capacity building. Most of the reforms in developing countries have remained unsuccessful due to:⁶⁴

- Poor information on civil service reform performance – There have been no standardised indicators for measuring the effectiveness of civil service reforms.
- Limited role for strategic management and cultural change – Most reforms did not account for resistance associated with culture change. For example, many initiatives failed to acknowledge the detrimental impact of employing expatriate consultants on the credibility of standard operating procedures, as well as on the morale of civil servants.

⁶³ National Commission for Governance Reform, *Reforming the Government*, Pakistan, 2006.

⁶⁴ World Bank, *Evaluation of Civil Service Reform Programmes*, 1999.

- Absence of coordination arrangements – Many governments carried out interventions without establishing coordination arrangements between government bodies. In many countries, poorly defined authority between budgeting and personnel departments allowed overstaffing and the proliferation of ministries to continue, even after downsizing efforts.
- Checks and balances – In the absence of external checks on political interference, civil service hiring remained a primary mode of dispensing patronage.
- Failure to appreciate the labour markets and institutional constraints – Many World Bank funded civil service reforms relied mainly on budget scenarios to guide the design of civil service reforms. Civil service system models that could account for labour market and institutional trends (for example, projected demand for civil service jobs or the level of political appointments in the civil service) when elaborating reform scenarios were not employed.
- The governments focused on downsizing and procedural changes without reforming the outmoded incentive system. Civil service reforms can only be successful if public sector human resource management is ‘reformed at an early stage to establish incentives for productivity in the public sector’.⁶⁵

State of HR in Public Sector

Currently no federal ministry, provincial or attached department in Pakistan has its own human resource unit that can determine size, skill-mix, compensation and capacity building of its employees.

Civil service compensation should be based on an in depth analysis and comparison with the private sector. The government should commission a survey of private and public sector salaries and perks. Under the present compensation structure, 85 per cent of the Government’s salary bill goes to subordinate staff from Grades 1-16 who are relatively well paid compared to the private sector.⁶⁶ New recruitment to the latter category should be frozen except for teachers, health workers, and policemen. Budgetary savings freed up by a reduction in the size of the workforce will, overtime, enable the Government to double or triple the salaries of the gazetted officers/technocrats/specialists.⁶⁷

Perks do not affect job performance and should be eliminated.⁶⁸ Monetisation of perks will result in efficiency gains and significant financial benefits for the government. The increased pay and open competition resulting from monetising the perks will attract better talent into the government and encourage more mobility to and from the government. It will sensitise senior civil servants towards the impact of their policy designs by exposing them to housing, car and financial markets. Rent seeking activities will either get discouraged or eliminated. Emphasis on government land development, done only to provide subsidised plots to bureaucrats and army officials, should be eliminated (Box 8).

**No Human Resource Unit
exists to determine the
right skill-mix**

**Perks to be monetised to
achieve efficiency gains
and financial benefits**

⁶⁵ NU Haque, ‘Why civil service reforms do not work’, *PIDE Working Papers* 24, 2006.

⁶⁶ World Bank, *A Framework for Civil Service Reform in Pakistan*, Islamabad 1998.

⁶⁷ National Commission for Governance Reform, *Reforming the Government*, Pakistan, 2006.

⁶⁸ NU Haque, ‘Why civil service reforms do not work’, *PIDE Working Papers* 24, 2006.

When state provides perks, it reduces productivity by not only adding to the overall expenditure (more bureaucracy is required for managing the perks) but by also encouraging rent seeking. Currently civil servants in Pakistan are receiving perks in addition to their cash pay. These perks include transportation, housing, plots, land, membership to clubs and membership of boards etc. In most cases even sanctioned entitlement of officers are discretion of the top boss who can choose whom to favour. The following case study focuses on transport and housing perks for officers of grade BS 20 and above.

Perks to BS 20 and above alone cost the government Rs 4.7 billion annually. Add to this the administrative expense and the figure will easily reach Rs 6 billion. Once monetised, the cash pay per officer will increase significantly (post monetisation scenario below). Given 100% compensation, annual cost to government will reduce from Rs 6 billion (current) to Rs 3.1 billion.

Monthly (Rupees)	Current Scenario			Post Monetisation	
	Cash Pay	Transport	Housing	Wages (100% Compensation)	Wages (50% Compensation)
BS 22	144,316	186,205	200,000	530,316	337,316
BS 21	119,019	171,164	150,000	440,019	280,019
BS 20	107,130	118,124	80,000	305,130	206,130

Barriers to enter Civil Services to be removed

An objective performance appraisal system for civil servants should be introduced. The system should set goals, targets and key performance indicators at the beginning of the year. Similarly, barriers to entry in the civil service should be reduced. Recruitment to the civil service should be carried out through an open merit-based competitive system. Job descriptions and specifications need to be developed in line with international best practices. Technical and professional cadres need special attention. For example in the Economist and Planners group of the Government of Pakistan, there is no weight given to a PhD degree or scientific contributions, during the promotion process.

Sources of recruitment for the Civil Services need to be diversified

The sources of recruitment for the Civil Services need to be diversified. The Federal and Provincial Public Service Commission should arrange participation in job fairs and make presentations to institutions with potential candidates for civil service employment. Initial screening and psychometric testing should help in assessing the attitude, team work and other personality traits of the candidates.

The civil service pension schemes need to be revamped. The current benefit structure for these schemes does not allow transfer of pension rights in case of early departure—to encourage lifetime employment, prohibiting the flexibility to attract young and vibrant minds. Portable pensions should be introduced as early as possible.

Spirit of Public Service

Public service can be an important incentive for joining the public sector if the government machinery is genuinely service-oriented. The government can attract new employees by offering an opportunity to engage in life changing experiences. For this initiative to be successful, public service must be held in high regard by society and

clearly seen to provide benefits. Government will produce a clear statement of values to discourage corruption and nepotism.

Independence of Public Agencies

A government agency is more efficient and focused on its mission if it is independent. For example, the international trend towards the independence of central banks has resulted in the reduction of inflation. Similarly, independence of public agencies will assist in dealing with the 'common agency problem' that is endemic to government.⁶⁹ There has been demand for greater autonomy by SBP, CCP and SECP in order to fend against market imperfections. A common issue in Pakistan is the sanctity of socio-economic data released by the government. Giving greater autonomy to organisations such as Federal Bureau of Statistics will actually imply improved credibility of the government.

**Autonomy to
organisations for better
performance**

Professionalisation

The public sector should aim to recruit professionals at all levels of the government, eliminating the current practice of lifetime public sector careers. Professionalising the public service places the public sector agencies and their missions under the scrutiny of peers.⁷⁰ Professions are communities that share knowledge, standards and a culture of work, and arrange peer-reviewed contests for achievement and excellence. This ensures that professionals keep their colleagues' work under review at all times. Professional networking and monitoring is a safeguard against the common agency and multitasking problems. Similarly as the professional is networked in his or her profession and expects rewards through the peer review process, the structure of incentives then becomes performance-driven. Moreover, professionalising an agency and networking it with the professional community further protects autonomy as direct interference and professionally observed work becomes difficult.⁷¹

**Professionals tend to
stay away from the
government as senior
positions are occupied by
generalists**

Professionalisation also encourages inward and outward mobility. Many professionals tend to stay away from the government as senior positions in the bureaucracy are occupied by generalists and research is outsourced to donors or consultants. To attract technocrats to the public sector, appropriate monetary and non-monetary incentives should be offered.

Service Delivery and Accountability

One of the major factors that contribute to poor human development is the systemic failure in the delivery of services such as health, education, provision of water and electricity to poor people. In South Asia, most of the public spending on health and education benefits rich people.⁷² For example, in India, more than a third of health care subsidies are enjoyed by the richest 20 per cent of the population. In Bangladesh,

⁶⁹ NU Haque, 'Why civil service reforms do not work', *PIDE Working Papers* 24, 2006.

⁷⁰ *ibid.*

⁷¹ JQ Wilson, *Bureaucracy: What Government Agencies Do and Why They Do it*, Basic Books, New York, 1991.

⁷² N Chaudhury and S Devarajan, 'Human Development and Service Delivery in Asia,' *Development Policy Review*, vol. 24, no. 1, 2006, pp. 81-97.

the absentee rate of doctors in rural primary health clinics is 74 per cent. Pakistan has many similar cases. This is caused by a lack of accountability among citizens, policymakers and service providers.

Many countries have dealt with the issue by introducing innovative programs to strengthen accountability. Indonesia issued grants to communities enabling them to build their own bridges, roads and wells, which not only improved maintenance but lowered costs. In Cambodia, a health system was contracted out to non-governmental organisations which led to an improvement in health service delivery and built trust with rural poor.

Citizen report cards, by providing the government with feedback on its services, can improve service delivery. A survey of local services was commissioned by the Public Affairs Centre in Bangalore, India, which invigorated public debate on service delivery and possible measures to improve it. Governments should also institutionalise impact evaluation of programs to gauge how successful different initiatives are.

Capacity Building

Training of civil servants with quantifiable results should be a priority agenda for developing countries.⁷³ Most public employees have no formal training for their technical assignments. Public employees should not only be provided induction training, but repeated trainings to ensure that their skills don't erode and are in line with the global best practices.

**Training of civil servants
with quantifiable results
should be priority agenda
for Pakistan**

⁷³ World Bank, *Evaluation of Civil Service Reform Programmes*, 1999.

Annex – Energy: A Governance Issue

Background

The energy sector in Pakistan is still largely state controlled. In the power sector the Independent Power Purchasers (IPPs) supply about 7000 MW of power as opposed to PEPCO operated GENCOs and WAPDA who supply another 8000 MW at peak supply. However market development as envisaged in the cabinet approved reforms of 1992 has remained stalled and a single monopolistic buyer/seller model still remains. The public sector organisations involved in the power sector remain plagued with managerial and administrative problems, extreme lack of funding due to tariffs being set at below cost recovery, nonpayment of receivables, and delayed payment of subsidy by the Government.

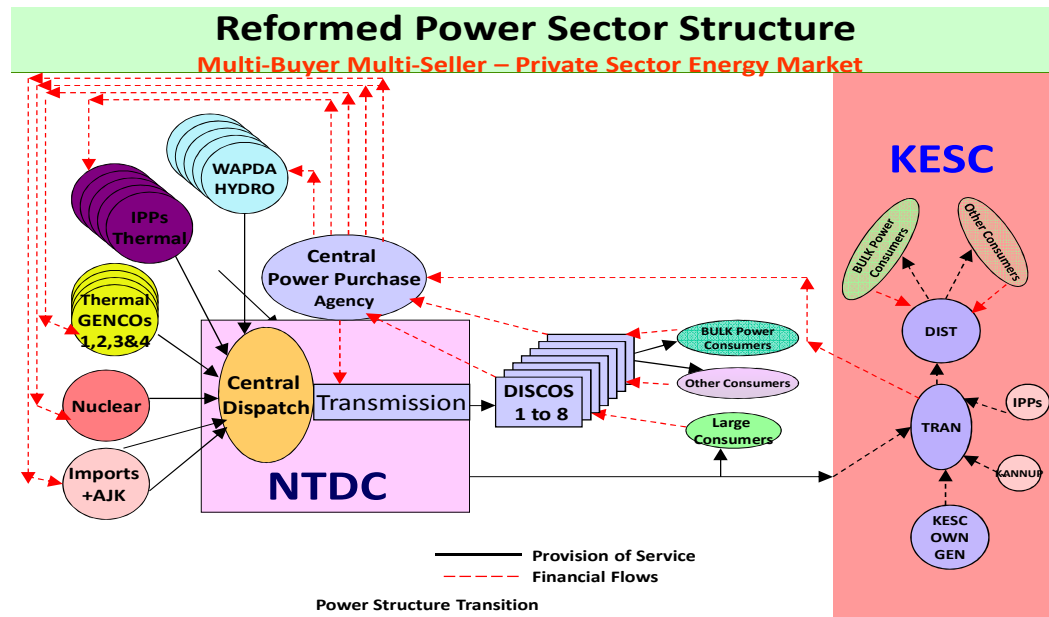
Similarly the petroleum sector is dominated throughout by parastatals, right from the exploration to marketing. The standard managerial problems of state enterprises as well as all pervasive, stringent regulation and the circular debt have not allowed the private sector to invest appropriately in exploration, development, transporting, refining or otherwise with the result that the Pakistan's dependence on imports is increasing exponentially. The shortage of gas is just a manifestation of the obstructive policies of hidden subsidies and extremely low producer and consumer pricing as well as inappropriate management of the exploration process by the parastatals engaged in exploration. In fact development of some of the discovered reserves of gas has been inordinately delayed by over 10 years in some cases.

All the above mentioned problems stem from the reality that the state is deeply involved in controlling all aspects of the energy sector and has not been able to provide the enabling environment, and as a result large scale investments required have failed to materialize. Good governance, financial stability, deregulation and an open door policy for private sector investment and private sector participation are a prerequisite for the large scale investments required by the sector if it is to contribute to the rapid growth of the economy.

Way Forward

The key to improved performance in the energy sector is development and implementation of a national integrated energy policy, followed by an integrated energy plan. An energy policy will be developed by the Planning Commission and implementation will be initiated by December 2011. Next steps will be to complete restructuring of the power sector, such as strengthening of the Ministry of Water and Power, corporatisation of companies, operationalisation of CPPA; strengthening of NTDC and a complete revamp and strengthening of the capacity of the regulators. Power sector reforms will be followed by a complete overhaul of the petroleum sector entities.

Figure 21 Reformed Power Sector Structure



Institutional strengthening has started with the power sector companies. A baseline has been set with technical & commercial audit of the GENCOs and DISCOs which has further highlighted the crisis in governance. New comprehensive business plans have been developed for all the DISCOs and GENCOs. The Ministry of Water and Power will oversee timely implementation of these plans through the respective Board of Directors. The change process is expected to take 2-3 years, after which the power sector companies should be financially solvent and should be prepared to serve their customers on a vastly improved basis. Losses will be significantly reduced, and when combined with cost based tariffs with a working mechanism to enable collection of billing the companies will be financially solvent and ready for participation of the private sector in their management through outright privatisation or management contracting.

Table 10 **Losses in the Power Sector**

1. Loss due to Generation issues			Rs. (Billion)
a. Capacity lost at GENCOS due to mismanagement	1500 MW	Capital Cost	130.0
b. Efficiency loss at the GENCOs due to mismanagement (on average)	5%	Per Annum	8.6
c. Extra use of fuel due to inefficient plants which should have been replaced.			103.0
d. Leakages in fuel supply estimated			10.0
2. Loss due to distributions issues			
a. Loss reported by PEPCO	20%		
b. Technical loss computed (average)	8%		
c. Allowance for Administrative losses	2%		
Net Loss due to mismanagement & theft	10%		
Annual sales Rs. 600 Billion 10% savings possible		Per Annum	60.0
3. Non recovery over billing etc.			80.0
Total annual Loss due to mismanagement			158.6
Additional saving if plants are replaced with modern equipment		Per Annum	103.0

Greater accountability and efficiency is being introduced at petroleum companies. The Ministry of Petroleum and Natural Resources & OGRA will be required to monitor steady improvements in efficiency and the introduction of performance based returns to the companies. Well designed incentives are being formulated for the sector companies to increase productivity and to attract investment.

The existing stock of circular debt will be paid off. Recurrence will be avoided by putting in place a revised tariff determination mechanism for NEPRA and an amendment to the act to enable cost recovery and automate application of determined tariffs. The tariffs in both the petroleum and power sectors will be efficiency based with disincentives for inefficiencies. This will create an enabling environment in which the companies will have to improve their performance in order to survive. Tariffs will however be set at levels which will allow the companies to finance capital expansion, maintain plant and equipment in good condition, under take exploration of tight gas, develop unexplored gas, and add capacity in the power sector.

Table 11 **Subsidy on Gas**

	As a percentage of alternative fuels (Average)	Subsidy
Domestic	20%	80%
Commercial	25%	75%
Industrial/Power	30%	70%
CNG	44%	56%

Cross and hidden subsidies exist in the entire energy chain. As a matter of prudent policy subsidies should only be paid if absolutely unavoidable and then only as direct targeted subsidies which are fully transparent. As a consequence of the hidden subsidies which are not subject to debate, the country's economic resources are

underutilized and thus fail to contribute to realisation of potential for economic development in the country. A fundamental change in the method of allocation of natural resources is therefore of paramount importance for sustained high levels of economic growth.

There are potentially dramatic gains in supply to be realized from energy efficiency. Savings from energy efficiency could reach 18% of total energy consumed in the country. According to the National Energy Conservation Centre (ENERCON), annual energy savings of up to 25% are possible in all sectors equaling \$3 billion in savings annually and a 51% reduction in oil imports. The Government of Pakistan will expedite the promulgation of an energy efficiency framework law covering provisions for codes, standards, energy reporting, labeling, testing, mandatory audits, fines and incentives, monitoring, and compliance mechanism in 2011. At the same time fundamental changes in the administrative setup of the efficiency and conservation agencies will realize the substantial potential gains from conservation and efficiency improvements.

Both Ministry of Water and Power and Ministry of Petroleum and Natural Resources will fast track the ongoing public sector investments in the energy sector. Further investments will however be fostered primarily through the private sector by an enabling environment and market oriented tariffs and deregulation of the sector.

Improvements in sector governance will greatly enhance the ability of the energy sector to attract capital for expansion. Greater reliance on private capital is absolutely essential if Pakistan is to meet its future economic potential and provide jobs for Pakistan's growing population. A review and amendment of the mechanism to induct foreign direct investment is required to actualize the potential investment in Pakistan the quantum of which is substantial. It is estimated that the Energy Sector alone requires an investment of over US \$ 35 billion in the next five years. Demand is expected to increase to 25,000 MW by 2014-15.

Table 12 Demand Forecast for Short-term

Year	PEPCO	KESC	Total Country
2010-11	18274	3194	21467
2011-12	18091	3198	21289
2012-13	19030	3335	22365
2013-14	20212	3522	23734
2014-15	21598	3752	25349

The state cannot finance these investment requirements and therefore the private sector must be provided the environment whereby these investments can be forthcoming. Pakistan must regain the ability to attract the public and private financial resources necessary across the energy sector to meet this growing demand. Reformed governance is the critical success factor. If the governance issues are fully and successfully addressed, then, and only then, will it be possible to resolve the fundamental problems of the energy crisis.

Deepening & Maintaining Openness

5

'No nation was ever ruined by trade'. – Benjamin Franklin

Pakistan's growth potential relies on taking creative advantage of the global economy. Success story in growth accelerations worldwide has not featured exclusive inward-looking growth. Furthermore, no small country located next to a large one has prospered economically by confronting rather than working with its neighbour. And whether Pakistan trades with its economically optimal trading partners is an open question, considering 'gravity' variables (distance, proximity, language, colony legacy, and economic characteristics). Given these parameters it is apparent that Pakistan under-trades with Japan, India, Russia and Brazil.⁷⁴ All success stories also feature productive diversification, with countries moving from traditional low-productive, low-wage activities, to new, more productive and sophisticated higher value products.

No small country located next to a large one has prospered economically by confronting rather than working with its neighbour

Securing Pakistan's place in international markets is vital for the success of this growth strategy. The country's position in world trade has barely changed over the past three decades, despite numerous opportunities to expand exports, especially manufactured goods, in developing countries. While declining for Pakistan during the last few years,⁷⁵ world market export shares for Malaysia, Mexico and Thailand have doubled, and have increased three times for China. Trade openness has not improved. The country's average trade-to-GDP ratio in the late 2000s was roughly the same a decade earlier. Pakistan's exports remain geographically concentrated—three markets (the U.K, the US and the EU) absorbed 64% of total exports in 2010. A positive development, however, is an initial sign of exports diversification—from a total of 45 (four-digit) products accounting for around 83 per cent of exports, 10 mostly from textiles and garment represented 57 per cent in 2007-08, down from 68 per cent in 2003-04. The list of emerging products is encouraging (e.g. rice, mangoes, jewellery, mining, meat, IT services, among others).

No success story in growth accelerations worldwide has featured exclusive inward-looking growth

The growth strategy considers openness in trade a critical ingredient for self-sustained growth, that creates jobs, and raises productivity and wages associated to higher private investment. Openness stimulates to be internationally competitive with reduced and minimum government intervention or assistance. Openness allows reaching new markets, and brings other benefits like knowledge and technology, two central channels for innovation and competitiveness, either through foreign direct investment, education, networks and experience.

Openness allows reaching new markets

⁷⁴ Private Sector Development Task Force, Government of Pakistan.

⁷⁵ Hausmann also finds a steady decrease in Pakistan's share of world exports in the last two decades.

Current Trends in External Trade Liberalisation

In the last fifteen years, Pakistan's trade patterns have closely followed a cycle defined by major departure from and return to protectionist import substitution policies. Between 1997 and 2003, the Government implemented a radical trade liberalisation program, with significant reduction in government intervention—government trading monopolies were eliminated, especially in the agriculture sector—and significant unilateral opening of the trade regime. The latter included the removal of import quotas, import surcharges and regulatory duties. Significant tariff cuts and rationalisation also took place. The un-weighted (i.e. simple) average statutory tariff fell from 47.1 per cent in 1997-98 to 17.3 per cent in 2002-03. These changes were also accompanied by a steep depreciation of the real exchange rate (Figure 22).

Openness in trade is a critical ingredient for self sustained growth that creates jobs and raises productivity

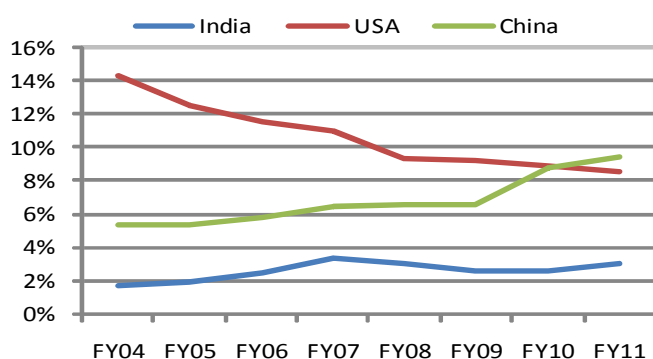
Not surprisingly, these reforms converted Pakistan as the least protected market in the South Asian region, whose openness ratio rose from 25 per cent in 1999-00 to almost 30 per cent in 2004-05, and for the first time reached double digit export growth rates in 2004-06. The World Bank estimated that within the group of structural reforms during the period 2001–05, trade openness was third among the most important factors contributing to growth, following improvements in infrastructure quality and economic governance.⁷⁶ Despite these gains, Pakistan's export growth rates were still modest by international standards—i.e. the 110 per cent increase in its exports (in nominal US dollars) during the 2007–08 period (compared with 2001–02) was lower than India's increase in its exports by a factor of three in the same period. However, by the mid 2000–10, Pakistan's trade system was starting to take better advantage of extraordinary opportunities in global markets.

⁷⁶ World Bank, *Pakistan: Growth and Export Competitiveness*, Report No. 35499-PK, Washington DC.

Figure 22 Pakistan Trade Liberalisation: A Story of Stalled Reform

Pakistan's trade share with neighbours as India and India is very low and stagnant...

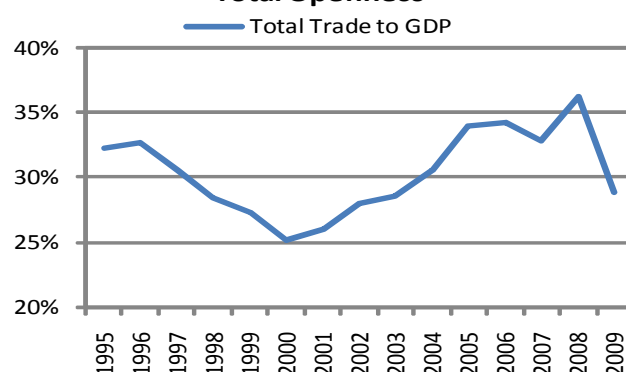
Trade Share--Selected Countries



Nine months data for FY11

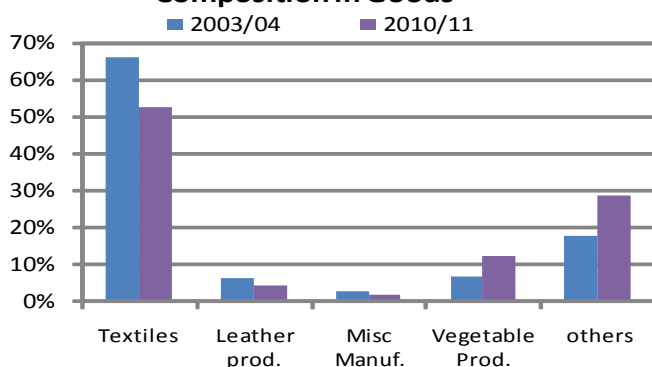
The country's degree of openness is dramatically falling in recent years...

Total Openness



Exports remain highly concentrated, about half of exports come from textile, which makes the country vulnerable to adverse price shocks...

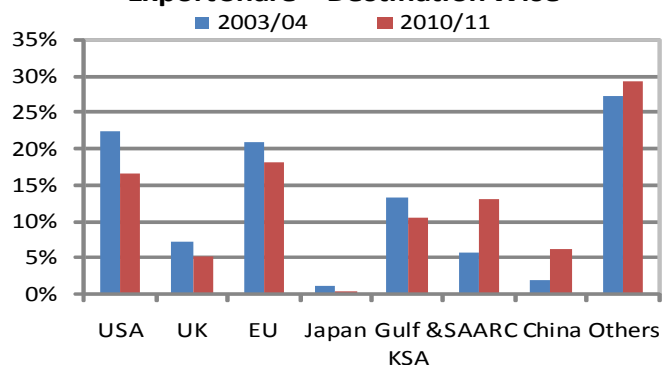
Composition in Goods



Nine months data for 2010/11

High concentration on distant export markets also adds to vulnerability concerns...

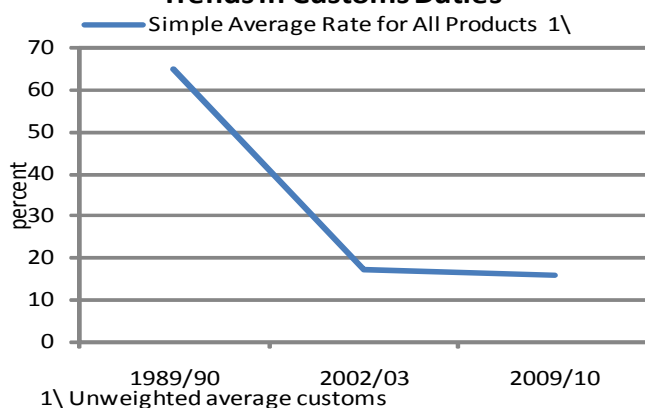
Export Share --Destination Wise



Nine months data for

Trade liberalization has stopped (or reverted) following steep fall in tariffs in late 1990's...

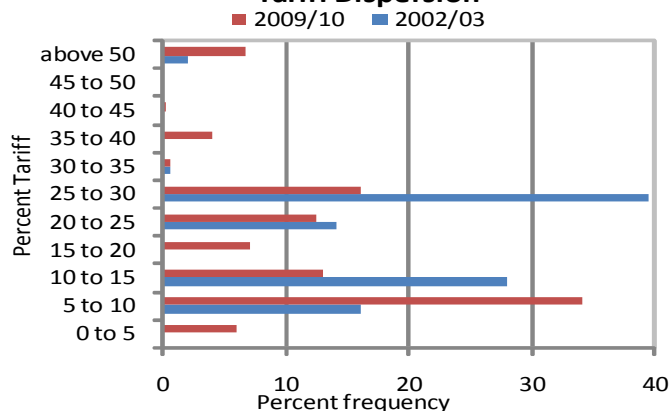
Trends in Customs Duties



1\ Unweighted average customs

And tariff dispersion has further increased in recent years (9 vs 4 prior slabs), not counting added new non tariff barriers...

Tariff Dispersion



Tariff system has become distorted, non-transparent and exposed to corruption

The second half of the period 2000–10 saw a dramatic reversal of this policy, especially after the global financial crisis of 2008. The crisis found Pakistan with twin high deficits—fiscal and current account. In response, heavy protectionism was reintroduced by the Government, which not only served to correct imbalances, but to reintroduce major distortions in the trade system.

The best example of backtracking reform is the tariff system, which has become distorted, non-transparent and exposed to corruption in a gloomy institutional environment (see next section). Firstly, significant increases have taken place at the maximum level, dispersion and complexity of customs duties. There are now at least nine standard ‘normal’ statutory tariffs⁷⁷, ranging from zero to 50 per cent. This compares with just four standard normal rates ranging from 5 per cent to 25 per cent in 2002–03. Second, statutory tariffs have become less relevant as a measure of the true level of protectionism as they are now modified through massive and uncontrolled use of SRO exemptions bringing extra protection to determined industries. Thus, if a final product is (nominally) protected by a statutory tariff of 25 per cent, its (effective) protection could be further enhanced by a reduced tariff on its raw material inputs and components. This has not only made the process of identifying the exact effective tariff for a product quite cumbersome, but caused bigger distortions across import substitution activities, while increasing the general anti-export bias in the system. Third, further complexity of the tariff system is a result of preferential trade agreements, including the one with China (see below).

The Need for Addressing Coordination Failures

Implementation Issues related to poor governance and management structures need to be overcome

Contrary to unilateral liberalisation that took place in the late 1990s and early 2000s, current trade policies have become essentially guided to provide extra protection to the processing margins (effective protection) of determined local producers. This is a major policy shift that deserves outmost attention. Indeed, the Strategic Trade Policy Framework 2009–12 acknowledges important ‘implementation issues’ related to poor quality of governance and management structures, which are a clear example of government (coordination) failures in trade policy. These include weak coordination in government, poor coordination with the private sector, dispersal of responsibilities among implementing agencies, and absence of a mechanism for monitoring and resolving policy issues. In the same vein, coordination failures are apparent on two areas, one, more subtle, is on the distorted application of the guiding principles for setting tariffs and the other is on the explicit reintroduction of new non-tariff barriers (NTBs).

The two guiding criteria for setting tariffs of the National Trade Commission (NTC) have basic problems either in terms of principle or implementation. NTC recommends tariffs that will provide protection against competing imports after taking account of the Pakistan producers’ ‘cost disadvantage’ and applied to a ‘specific’ period. The NTC should also verify that ‘the additional costs to the consumer will not

⁷⁷ Including the regulatory duties (but omitting outliers such as the very high tariffs in the auto sector).

be excessive'. Thus, effective protection rates are used in analysing incentives to producers, and nominal protection rates in analysing their effects on consumers.

In practice, however, there is an asymmetric application of NTC criteria. Whereas there is hardly any estimation of the additional costs on consumer interests of nominal protection rates, the definition of protection levels to compensate for production cost disadvantages relative to imports, is the only activity implemented by NTC. Not only does this asymmetry punishes the Pakistani consumer, but also results in multiple inefficient (higher costs) industries getting high protection and for an unlimited period. There are many multiple cases of a similar product being subject to more than one nominal (and effective) tariff.

The best way to illustrate this is with an example. EDB 'in consultation with stakeholders' has compiled and updated a list of 906 manufactured products (Customs Government Order 11. 2007) that enjoy tariff exemptions. From this list, 91 per cent of listed products benefit a single local monopoly producer, and 5 per cent benefit two producers, while other producers of the same good, especially small and medium producers do not receive same treatment. In this way, NTC determines '*the required protection needed* for the healthy growth of quasi-monopoly industries'. The 'cost plus' tariff protection, systematically creates differences ('distortions') in protection rates (both nominal and effective) and between different import substitution activities, and reduces the relative attractiveness of export production unless exports are subsidised. It also indirectly taxes all tradable activities through the effect of protective tariffs. This 'tax' is especially important for unprotected exports which by definition have to compete at world prices, and typically outweighs the positive effects of export subsidies, such as low preferential interest rates or tax holidays. In sum, extremely high protection slows down the development of efficient and competitive industries, and promotes rent-seeking (quasi-monopoly) behavior.

Extremely high protection slows down the development of efficient and competitive industries, and promotes rent-seeking behaviour

The second criteria for setting tariffs recommends the 'cascading principle', i.e. tariff escalation that also promotes high protection. Tariff escalation is widely applied by developing countries and is generally intended to promote domestic production of the final higher value added products. The 'cascading principle' does this by setting relatively low tariffs on 'upstream' input products and systematically higher tariffs on 'downstream' final products. However, the application of such principle often leads to excessive high protection of final products, discourages the production of intermediate inputs and aggravates the anti-export bias. Recent estimates show that effective protection rates for poultry meat increase to 60 per cent if lower tariffs and exemptions on inputs (through SROs) are taken into account, and 100 per cent or more for assembly, vendors and car production as a single integrated process.⁷⁸

The active use of non-tariff barriers is an area featuring coordination failures in the government

The second area featuring severe coordination failures in the Government is the active use of non tariff barriers since the second half of the period 2000–10. Historically, EDB eliminated import licensing—discretionary—programs in the late 1990s as they

⁷⁸ This basic misunderstanding of the nature of protection typically leads to the further misunderstanding that a local industry will only be receiving some positive protection if the tariffs protecting its finished products exceed the average of the tariffs applied to its inputs. Conversely it is typically and wrongly concluded that if the average output tariff is lower than the average input tariff, that the industry is necessarily unprotected.

contravened the WTO-TRIMS Agreement (industrial ‘local content’ programs). However, more recently, EDB has reintroduced these programs with substitute programs, thus becoming effectively involved, jointly with several ministries, in quasi-import licensing schemes that are subject to a concessionary regime. This has led to prohibitive tariffs on final products used to preserve against import competition. This failure is even more apparent when the NTC—a MOC agency—is in theory the central agency in charge of setting tariff changes, following a prior study. In practice, many changes in tariffs are being affected without recourse to NTC, and rather following EDB-sponsoring of *ad hoc* ministerial committees—jointly with representatives of major firms in each industry—set up to look (and correct) tariff ‘anomalies’, often through SROs issued by FBR.⁷⁹ Furthermore, the new protectionist policy is making more intensive use of anti-dumping, customs barriers and explicit prohibitions to trade like the ‘positive list’ applied to India.

Trade Logistics Issues

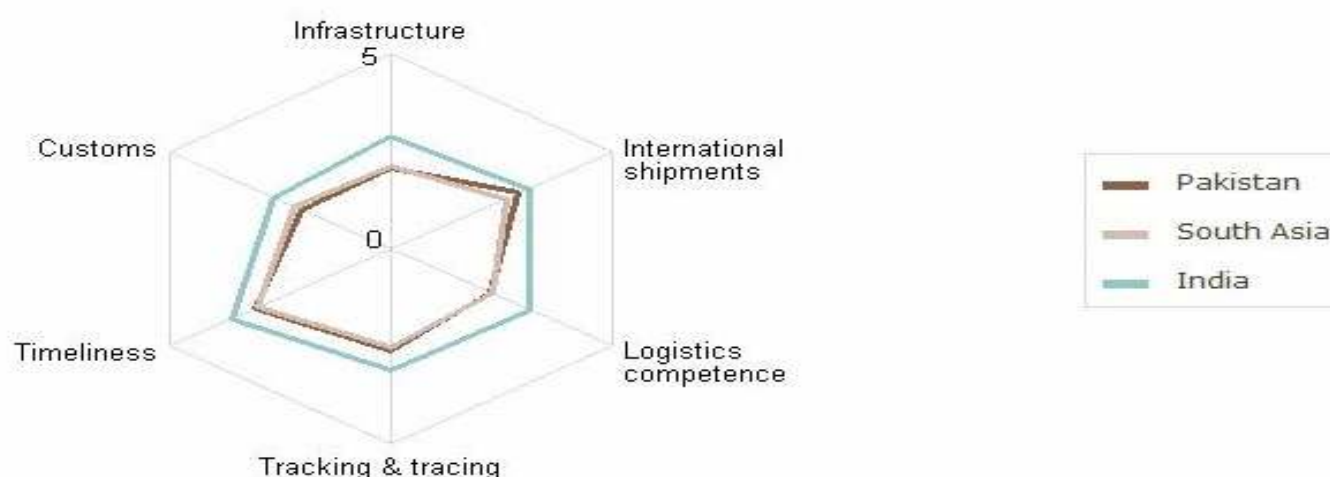
Besides tariffs and NTBs, good logistics is also critical for trade and competitiveness due to its wide ranging impact on the economy. Superior logistics performance is strongly associated with trade expansion, export diversification, ability to attract foreign direct investment and economic growth. Evidence from the 2007 and 2010 World Bank Logistics Performance Index (LPI) indicates that for countries at the same level of per capita income, those with the best logistics performance experience additional growth—on average, one per cent in gross domestic product and two per cent in trade per year.

Good logistics is critical for trade and competitiveness due to its wide ranging impact on economy

The Logistics Performance Index is based on a worldwide survey of operators on the ground (global freight forwarders and express carriers), providing feedback on the logistics ‘friendliness’ of the countries in which they operate and those with which they trade. They combine in-depth knowledge of the countries in which they operate with informed qualitative assessments of other countries with which they trade, and experience of global logistics environment. As shown in Figure 22, Pakistan’s logistics services currently rank at par with the average of the South Asia region for practically all dimensions covered by the LPI—customs, infrastructure, logistics competence, timeliness, shipments, and tracking and tracing components. In fact, the two brown lines are almost similar in Figure 22. In 2010, Pakistan’s rank and score were 110 and 2.53 respectively, while the average regional score was 2.49. However, when compared to India, the country with the best performance in the region (blue line), Pakistan is lagging behind in two dimensions in particular—logistics competence and infrastructure (See Figure 23).

⁷⁹ G Pursell, A Khan and S Gulzar, *Pakistan’s Trade Policies: Future Directions*, Planning Commission, 2011.

Figure 23 Comparison of Logistics Performance



A New Era for Trading with India and China

The fact that Pakistan under trades with several large and fast growing emerging economies, like India and China, could be due to historical reasons, but this is no excuse for not taking advantage from regional trade. This could be two of the most promising moves for improving Pakistan's growth prospects in the short and medium term.

India

Trade potential between Pakistan and India is extraordinary. Upon its creation as an independent state in 1947, 70 per cent of Pakistan's trade happened with India, while 63 per cent of Indian export went to Pakistan. In the late 2000s, however, India barely represents around 3 per cent of Pakistan's global trade. Given the proximity of the two countries and their historical and cultural similarities, such amount of trade is insignificant and well below potential.

Pakistan's global trade with India has gone down from 70% in 1947 to around 3% in late

China

Economic relations with China have been spurred by the bilateral trade agreement signed in November 2006. The agreement calls to reduce or eliminate tariffs on all products (in two phases) starting from July 2007; and both parties are committed to 'endeavor to eliminate the tariffs of no less than 90 per cent of products, both in terms of tariff lines and trade volume within a reasonable period of time on the basis of friendly consultation and accommodation of the concerns of both parties'.

Trade between Pakistan and China has almost doubled from \$2.4 billion in 2005-06 to \$4.5 billion by 2009-10. In addition, Chinese foreign direct investment is expected to multiply with Pakistan as plans for opening a Free Trade Zone are expected to materialise in the near future.

Chinese foreign direct investment is expected to multiply with Pakistan to \$4.5 Billion by 2009-10

The Way Forward

The strategy aims for a flourishing export sector supported by further reductions in the anti-export bias and improved logistics, thus regaining the trade liberalisation path undertaken fifteen years ago. How to get there? Although the list of proposed actions is far from being exhaustive, priority recommendations are presented below in three broad headings.

General Recommendations

Five actions would make a significant difference in terms of major strategic policy shifts with high impact on growth in the near and medium term, these are:

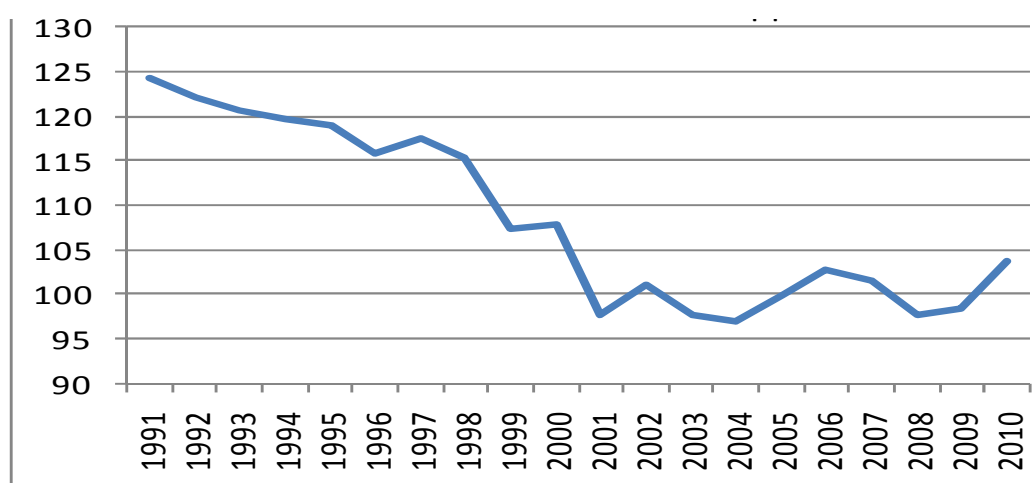
- a. Re-establishment of the unilateral trade liberalisation programme, regardless of ongoing multilateral, regional or bilateral trade negotiations. Setting of low tariffs is important in Pakistan in order to keep down smuggling and under-invoicing, which is generally recognised to be rampant in many products.⁸⁰ More specifically, this action involves: (a) gradual reduction of the normal maximum tariff (10 per cent could be a reasonable target); (b) gradual reduction of tariff peaks towards the normal maximum tariff rate; (c) speedy elimination of tariff exemptions (i.e. in 2–3 years); and (d) special tariff reduction programs for ‘special’ industries (e.g. automobile industry).
- b. Immediate abolishment of the present system of distortive regulatory duties (SROs) that interfere with the tariff structure.
- c. Maintain, *de minimis*, a neutral real exchange rate policy. There is no question that the sustained nominal and real depreciation of the exchange rate that took place between 2002 and 2004 contributed to sustain strong export growth and some diversification in those years. Another episode of active exchange rate policy will not fit well with present anti-inflationary efforts. However, as the real exchange rate has mildly appreciated since 2008, thus eroding some loss in the competitiveness of Pakistan’s exports (Figure 24), a neutral real exchange rate policy would be called for.

Re-establishment of
unilateral trade
liberalisation
programme would have a
high growth impact

Real exchange rate policy
required

⁸⁰ Pursell et al. (2011) estimate US\$ 385 million in smuggling and under-invoicing in Afghan transit trade, and US\$ 368 million in trade with other countries.

Figure 24 Pakistan: Real Effective Exchange Rate (2005=100)



Source: IMF's IFS: Increase means appreciation

- d. Accelerate the re-establishment of normal trade relations with India, including border opening (see above).
- e. Accelerate the maximum potential possible under already signed free trade agreements, for example with China and Malaysia.

Specific Sectoral recommendations

In order to deal with other coordination failures identified, the following measures are proposed:

- Issuance and implementation of a general trade policy statement — It should state that (a) non-tariff measures including import licensing will not be used to control imports and exports; (b) specific ad-hoc duties will not be used; (c) tariff cuts will be examined and pre-announced by NTC exclusively—thus eliminating the common misperception that ‘in Pakistan, nobody knows how tariffs are set’; and, (d) all concessionary tariffs should be available to all, not just a few importers, especially trader-importers.
- Immediate abolition of the ad-hoc system of quasi-import licensing being administered by EDB and various line ministries.
- Thorough review of the economic justification for sectors/industries benefiting from above normal protection and/or subsidies, export subsidies, export taxes, and anti-dumping practices.

The ad-hoc system of quasi-import licensing must be immediately abolished

Recommendations on Information Gaps and Transparency

A fundamental change in support of reduced discretion and opacity in trade policy would also require a few key actions:

- Publication on the FBR website of a substantially improved computable version of the detailed Customs tariff schedule. This should include for each tariff line

customs duties, sales and other domestic taxes, preferential tariffs, and changes due to SROs.

- Thorough inventory and review of tariff distortions introduced by SROs and its publication, prior to their elimination.
- Publication of MOC regular statements indicating the reasons for adopting or not adopting the recommendations of NTC on tariff enquiry reports.
- Publication and easy access to information on appeals against anti-dumping decisions.
- All economic ministries to frame their policy and regulatory stance based on the intentions defined in this growth strategy.

Vibrant & Competitive Markets

‘Open markets offer the only realistic hope of pulling billions of people in developing countries out of abject poverty, while sustaining prosperity in the industrialized world’. – Kofi Annan

Traditionally, Pakistan’s growth strategy has been confused, while announcing export promotion in some sectors, it has relied heavily on import substitution in others. Consumers have paid the price for these policies, through taxation for export subsidies, high prices and sacrifice of quality goods, where import substitution policies prevail. Meanwhile, innovation and entrepreneurship have suffered as the incentives are skewed in favour of lobbyists (rent seeking) rather than competitive markets.⁸¹

Market development is impeded for several reasons:

- As explained earlier in detail, there is a high degree of government involvement in most markets ranging from agriculture to manufacturing, from retail to transport and from trading to construction.
- Government actually is a player/competitor in many of these markets making it difficult to define a transparent competitive market. One dominant player with recourse to taxpayers’ funds limits entry and competition.
- Government regulation in many markets is not professionally organised and informed by research leading to contradictory and cumbersome regulation. Often this ends in regulatory capture. Some times the regulator is taxing entry too heavily to maximise revenue at the expense of competition.
- Lack of clarity in government policy – importing commodity one year, buying from the local market next year, allowing imports then disallowing—strengthens rent seeking at the expense of the consumer. Government policies, regulation and rules must be clear and stable over time.
- Better configuration is required between law and economics – particularly in the case of property rights and sanctity of contracts.
- Ultimate incidence of public policy should be judged on welfare grounds – there should be no favourites and the focus should only be on increasing consumer welfare.
- Domestic commerce which defines value at the exchange point employs substantial work force but has through neglect been heavily taxed. Yet it completes the value chain and without it production runs blind and the quality of good remains poor at the expense of export competitiveness.⁸²

There is a high degree of government involvement in most markets

In public policy there should be no favourites

⁸¹ NU Haque, ‘Awake the Sleeper Within: Releasing the Energy of Stifled Domestic Commerce’, *PIDE Working Papers No. 11*, Pakistan Institute of Development Economics, 2006

⁸² Ministry of Finance, *Economic Survey of Pakistan 2010-2011*, Government of Pakistan, Islamabad, 2010.

Key Issues in Markets

The key issues in Pakistan's markets can be identified as below:

Outmoded Urban Management and Zoning for Domestic Commerce

Urban areas have excess demand for retail, office and mixed-use space

The state of domestic commerce in Pakistan is partly apparent by the poor condition of the retail markets in our cities. They are mostly small, cramped, and congested areas with limited square feet allocated to every shop. There is an excess demand for not only retail space but also office space, hotels and mixed-use areas. Excess demand for office space is evident by the high rents. Due to these high prices as well as poor provisions for office complexes, a large number of offices, small businesses, guest houses and salons operate illegally in residential areas. Besides the lack of proper commercial space, high commercialisation fees are also charged that raise investment costs considerably. Figure 25 shows the share of domestic commerce activities in the GDP of Pakistan and the growth of these activities over the past decade.

Inadequate Transport and Storage Facilities for Agricultural Markets

Pakistan Railways handles only 4 per cent of domestic cargo, a decline from 14 per cent in 1990.⁸³ The trucking fleet is aging, truck sizes are small, cargo facilities do not meet internationally certified standards, and transport efficiency is very low. While the government has deregulated the trucking industry to a certain extent, the railway remains heavily regulated.

Storage facilities are grossly inadequate

There is no zoning for warehousing and distribution and Pakistan has few facilities with very little spaces for modern and up-to-date storage facilities. Grain storage is primarily in the public sector and is the responsibility of PASSCO, but the current facilities are not adequate both in terms of quantity and quality.⁸⁴ The storage is very basic and ranges from storage in a heap within the home compound to storage in specially constructed mud bins or bags.⁸⁵

About 30% to 40% of agricultural produce is wasted due to inefficient farm-to-market channels

Inadequate cold chain storage and refrigerated vehicles are a serious problem and lead to considerable wastage of perishable goods, including vegetables and fruits in wholesale and retail markets. According to an estimate, about 30 to 40 per cent of the produce is wasted due to inefficient farm-to-market channels.⁸⁶ Low quality packaging materials and faulty methods of loading and unloading also contribute to wastage of perishable goods.⁸⁷

⁸³ *Ibid.*

⁸⁴ PASSCO is a Department of the Ministry of Food and Agriculture, Pakistan.

⁸⁵ Innovative Development Strategies, *Storage*, Study for Ministry of Commerce, Government of Pakistan, 2006.

⁸⁶ World Bank and IFC Foreign Investment Advisory Service, *Improving the Performance of Housing, Tourism and Retail Sectors, Pakistan*, Washington DC, 2005.

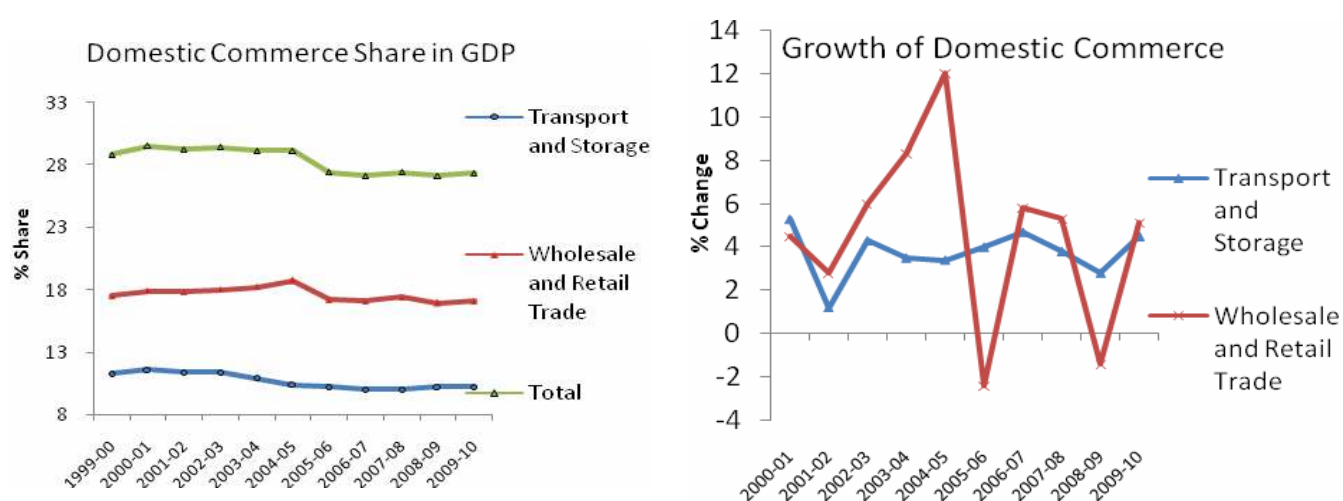
⁸⁷ Innovative Development Strategies, *Wholesale Markets*, Study for Ministry of Commerce, Government of Pakistan, 2006.

The Agricultural Produce Markets Act of 1939, established during British rule, is still in effect in Pakistan (albeit with amendments in Punjab and Sindh). This outdated act places control of the agriculture markets in the hands of the government. Moreover, since it affects small farmers more than the big landlords, it reduces development at the lower income levels.

Agricultural Produce Markets Act of 1939 is outdated and requires fresh legislation

The foregoing represents a very small number of obstructions to the growth of productivity in agriculture. Virtually all these would fall under the rubric of 'governance', and can be resolved with very little expenditure of financial resources. Modifying or eliminating these impediments would give a substantial boost to growth in the agricultural sector.

Figure 25 Share in GDP and Growth of Domestic Commerce, 2000-10



Source: Economic Survey of Pakistan 2009-2010

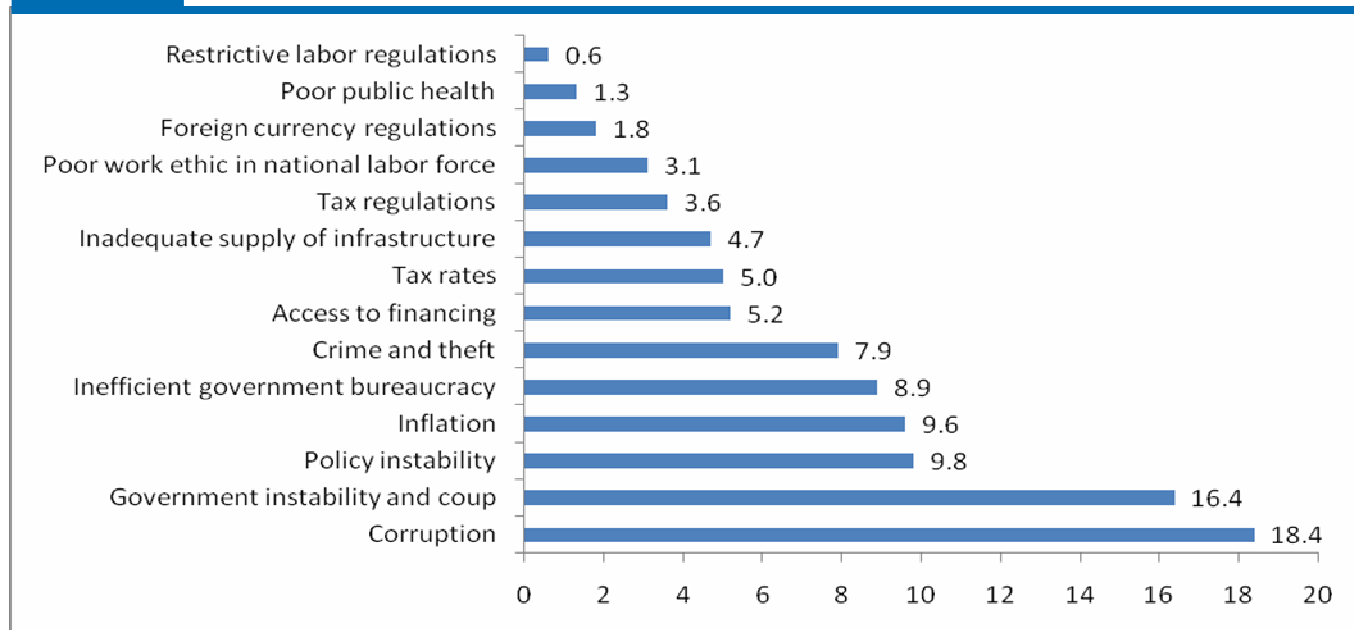
Legal Issues and Regulatory Environment

The most problematic factors for doing business in Pakistan are reflected in Figure 26. Pakistan ranks 85th out of 183 countries with respect to ease of starting and running a business.⁸⁸ With weak property rights, corruption and inefficiencies in the legal system, Pakistan has failed to strengthen its domestic commerce or make a strong impact in foreign markets.

Pakistan ranks 85th out of 183 countries in ease of doing business

⁸⁸ The World Bank and International Finance Corporation, *Doing Business* database, 2010

Figure 26 The Most Problematic Factors for Doing Business, 2010



Source: Global Competitiveness Report 2010-11

Macro-level Reforms

a) Promoting Trade Openness and Competition

Further strengthening of the CCP would help to maintain competitiveness

Bringing international quality goods to consumers promotes innovation. The measures outlined in growth strategy aim to promote competition in the development of value chains.⁸⁹ This entails free entry and exit of participants in the market (without special privileges or licenses) as well as a liberal policy that allows mobility with greater fairness and competition for wholesalers. The CCP has proved successful in the past few years in dealing with non-competitive activities in various sectors, including sugar, cement and textiles. The further strengthening of the autonomy of this organisation would help to maintain competitiveness and pressure on enterprises to keep increasing productivity.⁹⁰

b) Land Reforms

Land is a basic factor of production for most economic activities, and its efficient use will require a number of reforms. Prominent among these would be the following.

- **Disallowing oral transfer of land:** This entails an amendment to the Transfer of Property Act 1882. This Act permits the oral transfer of land, creating confusion about the ownership of the land and frequently leads to litigation that takes years to resolve in the courts. Transferring property through oral gifts should be disallowed.

⁸⁹ Value chain (also known as supply chain) includes the various processes that are involved in producing goods (and services), starting with raw materials and ending with the delivered product.

⁹⁰ Competition Commission of Pakistan <www.cc.gov.pk>

- Repealing the Punjab Pre-Emption Act 1991: Disallowing the neighbours to a property the right of first refusal.
- Centralising land title records: Consolidating the steps taken when purchasing land (i.e. visiting only one agency instead of several bodies including SECP, Land Registrar, Revenue Department, Excise Department and local Development Authority).
- Computerisation of land records: This has been initiated in Punjab under the Punjab Land Records and Information Management Systems project, and it would be advantageous to extend this to the rest of the country. The aim would be to set up a Multi-Listing Service to have a computerised record of available land for sale.
- Auctioning off government held land: Transferring government owned land (on 99 year leases) to full freehold.
- Tenancy Laws: Revisiting the tenancy laws and the rented premises ordinances and acts in order to give protection to the small and medium land owners from various land mafias, particularly in the urban commercial areas.
- Financing for Businesses: Advising the SBP of possible amendments to the Banking Policy Department circulars affecting mortgage financing for businesses, and encouraging the SBP to enforce the prudential regulations by increasing financial sector training requirements on credit risk evaluation.

Land title records must be centralised by consolidating the steps of land purchase

c) Taxation Reforms

- Amending the Income Tax Ordinance 2001 and Sales Tax Act 1990 to limit the discretionary power of the Federal Board of Revenue and to improve the administration, the auditing system and the tax refunds system. Simplifying the tax system and tax administration by creating one-window cells for tax registrations at the sub-national level to cater to all taxes (Federal, Provincial and Local).
- Unifying NTN and GST registration to one Tax Registration Number through amendments to the Income Tax Ordinance 2001 and the General Sales Tax Act 1990.
- Improving technology and e-governance strategies to facilitate tax registration and tax filing system at the FBR.
- Setting time limits: Modifying tax laws to include deadlines for speedy disposal of pending and new court cases.
- Reforming data warehouse in FBR (with help from NADRA) in order to check multiple bank accounts of tax payers.

Tax system and tax administration must be simplified through one-window operations

d) Labour Reforms

- Amending the EOBI Act and the ESSI Act to create one Social Security provision institution at the provincial level.
- Reducing the number of procedures and time taken to register for labour regulations by amending the EOBI Act, ESSI Act and the Directorate of Labour Welfare Act.

- Increasing the number of employees requirement after which the social security provisions are mandated (e.g. from 19 employees to 70 employees).
- Introducing technology and online procedures at the EOBI and ESSI to reduce the number of procedures and time.
- Upgrading and consolidating laws and acts into fewer pieces of legislation, such as upgrading Companies Profits (Workers Participation) Act (1968), Apprenticeship Ordinance (1962), Workers Children (Education) Ordinance (1972), Workers Welfare Ordinance (1971) and consolidating them into one law, and as well as instituting checklists at the Directorate of Labour Welfare and the BOI to ensure compliance with laws.

Meso-level Reforms

The growth strategy has identified a number of areas in which reforms would help to greatly boost productivity and output. Some of these suggestions and recommendations are discussed below.

a) Agricultural and Rural Markets

- Improve transport efficiency and storage facilities: Private storage activity needs to be encouraged and space needs to be made available for warehouses. Moreover, good storage facilities would provide much needed hedging opportunities to farmers and facilitate the development of forward and futures contracts with banks and open exchange markets. The government has announced a number of measures to promote cold storage facilities in the private sector to be implemented through the Pakistan Horticulture Development and Export Board (PHDEB).⁹¹
- Provide training in packaging: Farmers need to be trained in packaging the agricultural produce and loading/unloading in order to minimise damage to perishable goods.
- Encourage private sector involvement: It would be advantageous to repeal the Agriculture Produce Markets Act 1939 and replacing it with a more updated and market-friendly set of rules that allow small private farmers to sell their produce directly.
- Deregulate agricultural markets: This has been initiated through the 'Pakistan Mercantile Exchange' on which, out of the agricultural products, IRRI rice has been listed so far. Sugar is awaiting final approval from SECP, and is expected to start trading very soon. Wheat, maize, basmati rice and cotton are also expected to start trading soon. This process should be further strengthened and the government must gradually exit from regular commodity operations.

b) Reforms for Manufacturing Sector

- Amend the legal framework to change the nature of the subsidies and include strategies to improve or promote different subsectors, especially those with higher value-added outputs (e.g. in textile).

⁹¹ Innovative Development Strategies, *Storage*, Study for Ministry of Commerce, Government of Pakistan, 2006.

- Improve governance to guarantee uninterrupted gas and electricity supply for industrial sector.
- Institute effective monitoring by the CCP to reduce chances of collusion or hoarding in the market.

c) Trading Processes

The Strategic Trade Policy Framework 2009–12 suggests some changes for overall facilitation of importing and exporting. These include:⁹²

- Inland clearing facilities: With only 1046 km of coastline, Pakistan needs to establish additional dry ports to effectively handle import and export. These dry ports can reduce administrative delays and provide more capacity than otherwise available in inland cities.
- Computerisation: Strengthen existing customs clearance system by removing uncertainty and making the system compliant with customs procedures.

Additional dry ports need to be established to effectively handle exports and imports

Firm-level Reforms

In addition to reforms that affect the economy or the markets as a whole, a number of initiatives could help improve the functioning at the firm-level. Some recommendations to this end are as follows:

a) Initial Setup of Business

- Merge steps and offices: Consolidate steps to set up business under either the local registrar or the Chamber of Commerce. Collaboration between the Ministry of Commerce and the sub-national governments would help facilitate the operation of one-window cells to speed up establishment of new ventures.
- Improve construction and planning regulations: Cities in Punjab have adopted uniform zoning and building regulations, which have reduced the time taken by businesses in cities such as Lahore and Sialkot to obtain a construction permit. Such efforts can be generalised to other cities.
- Tailor procedures to the requirements of the business: Different types of businesses require different regulatory procedures. Large city-scrapers and manufacturing units require extra regulation since they are more risky in terms of health and safety of employees and the masses. However, small retail outlets do not need much regulation and inspection. The procedures for registration and inspection should keep these aspects in mind, making it easier for small retailers to start and operate a business.
- Build capacity of staff working at the offices responsible for registration and issuing permits. Their training can make them significantly more efficient and skilful on how to handle varied cases.

Implementing local best practices can save an average business a substantial amount of capital

⁹² <<http://www.commerce.gov.pk>>

By simply replicating the local best practices (i.e. reducing the number of days for each procedure to that of the city which takes the least amount of time) can save an average business a substantial amount of capital (Table 13).

Table 13 Average Amount Saved By Business, 2009

Indicator	Average Amount saved (US \$)
Starting a business	73
Dealing with construction permits (better procedures)	49
Dealing with construction permits (better time)	845
Registration of property	613
Total	1,580

Source: Based on data in *Doing Business in Pakistan 2010*

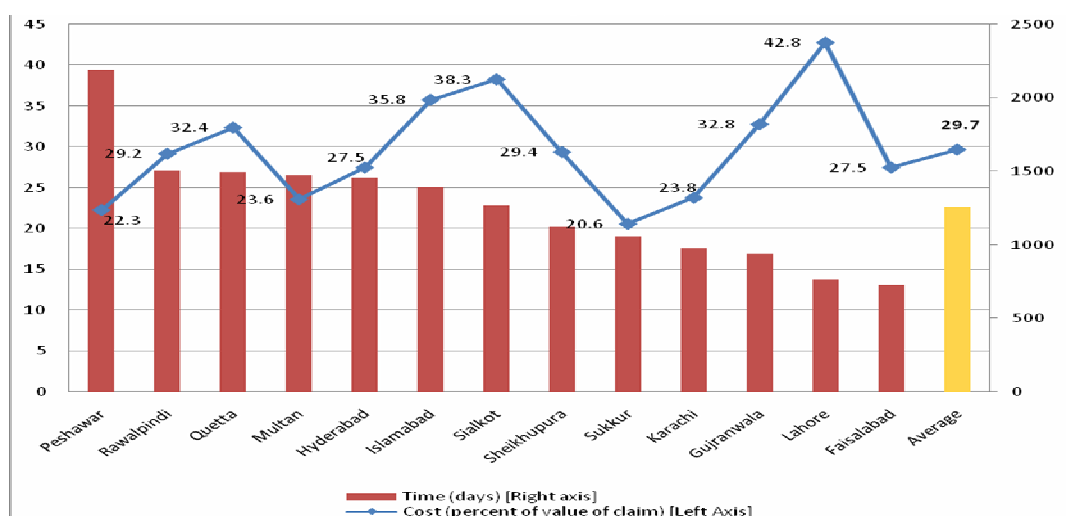
b) Enforcing Contracts

It is impossible to overstate the importance of strengthening the legal and judicial framework and the institutions for enforcing contracts. The lack of mechanisms for the efficient enforcement of contracts limits contestability, inhibits corporatisation, increases project risk, and restricts technology transfers, especially from foreign partners. It can also hamper the development of the financial system by raising the cost of collecting on securities and collaterals. A strong contract enforcement mechanism is thus essential to the functioning of a market economy.

The time and cost of enforcing a contract varies widely between different cities in Pakistan. This is shown graphically in Figure 27. Simply improving the performance of the least satisfactory to come up to the standard of the most efficient city would dramatically reduce time and costs, and thus provide a significant incentive for additional investment by firms.

Time and cost of enforcing contract varies widely between different cities in Pakistan

Figure 27 Time & Cost of Enforcing a Contract, 2009 (days and % of claim)



Source: Computed from data in World Bank, *Cost of Doing Business in Pakistan*, 2010.

A significant number of Pakistani businessmen claim that the current state of the courts is one of the key constraints to investment.⁹³ The National Judicial Policy (2009) aims to guarantee independence of the judiciary, clear the backlog of cases and reduce corruption. Some further measures may be taken to improve the situation:

- Establishment of commercial courts can provide a specialised environment for the firms to deal with their problems. These courts can either be set up as separate entities or as a separate chamber in the existing courts.
- Strengthening Alternative Dispute Resolution systems.⁹⁴
- Setting up time limits can lead to the quick handing of commercial cases.
- Lawyers and judges should be trained in handling commercial cases effectively and quickly.

To sum up, short and medium term reforms must cover three broad areas. First, city zoning laws and building regulations must be reformed to allow land use to respond to market demand. Second, since openness and competition bring international quality goods to the market agricultural markets should be deregulated. And third, our legal and judicial framework must be made supportive of the complex needs of market development.

Pakistani businessmen claim current state of courts as a key constraints to investment

⁹³World Bank Enterprises Survey, <<http://enterprisesurveys.org>>

⁹⁴ An example of a successful ADR system is the Karachi Centre for Dispute Resolution (KCDR), that had received over 924 cases (till end 2009) and as a result US\$ 27 million had been released in out-of-court mediations. <<http://www.kcdr.org>>

Creative Cities

‘Creativity is a great equaliser that knows no bounds, no gender, no social class, no skin colour, no sexual preference. It is not produced in institutions, but comes from the streets. Towns with a large creative class have a ‘buzz,’ an ‘excitement,’ a ‘creative energy’ that’s palpable. Creativity should be a goal, such as fitness. People want to be in a community where they can be who they are’. – Richard Florida

‘There is no such thing as a poor urbanized country and there is not such thing as a rich rural country.....International evidence shows that, on average, as the share of a country’s urban population increases by 10%, the country’s per capita output increases by 30%. Per capita incomes are almost four times higher in countries where a majority of people live in cities than in those countries where a majority of people live in rural areas’. – Edward Glaeser

Around 600 urban centres generate approximately 60% of world GDP

We live in a world where urbanisation is expanding rapidly. Almost half of the world’s population lives in cities, producing more than 80% of global GDP. Around 600 urban centres (hosting fifth of the world’s population) generate approximately 60% of world GDP. Cities provide facilities and encourage interaction among people of various age and ethnic groups. These are the hubs of knowledge, innovation, creativity, and institutions.⁹⁵ Cities have been perceived as the fundamentals of diversity and difference. The best cities have been places of learning and ideas development. Cities such as Paris, London and New York have been the birthplace of modernisation and inspiring vision. Creative cities enable people to be more innovative and productive, individually or collectively, by having easy access to information and interaction.

People inevitably migrate to cities for ideas and variety of choices

People inevitably migrate to cities for ideas and variety of choice. The multiplicity of opportunities allows minds and bodies to come together and exercise multifarious activities. The creation of wealth needs space – physical and regulatory. It is the way we organize and manage our cities that plays fundamentally important role in determining the competitive edge of people and nations.

Placing city development (with an emphasis on density and commerce) at the heart of our growth strategy in the coming years will have several advantages:

- Dense multi-function urban areas create jobs and are free from barriers to entry and exit.
- The creation of density and the many new functions (commerce, entertainment, housing, offices etc) will attract investment and the growth of a construction industry.
- Construction is employment friendly as is commerce.

⁹⁵NU Haque and D Nayab, ‘Renew Cities to be the Engines of Growth’, *PIDE Policy Viewpoint*, Pakistan Institute of Development Economics, 2007.

- Construction growth linked with the growth of commerce will allow space for the inclusion of women and youth as well as the demand for many new skills.
- Density, construction and the many functions of commerce will spur innovation and emergence of demand for new services and goods. This is the beginning of the innovations cycle that Pakistan badly needs.

Cities are open to people with different backgrounds and affiliations

How Cities Affect Economic Growth?

Cities affect the growth and inclusion in three ways.

1. Proximity and density create large markets for goods and services. In turn, large markets build social capital; allow interactivity; nurture innovation and entrepreneurship. Large-scale production and diverse services demand efficiencies and specialisation. Innovation occurs in dense clusters, where there is intense competition.
2. Proximity and density increase the speed and amount of learning and efficiency. Large and dense markets, hosting entrepreneurs, offer incentive for learning—they increase productivity by allowing people to organise into teams and become more efficient.
3. Cities are poor-friendly. They are open to people with different backgrounds and affiliations and offer jobs and self-employment. Social mobility—from rags to riches happens in cities.

Growth strategy in most countries is now focusing on cities as engines of growth

Cities and poor-friendly

It is because of these factors that growth strategy in most countries is now focusing on cities as engines of growth.

Box 9 Advantage of Large Cities – Case of Shanghai, China

Of 858 cities in China, only 13 have populations over 5 million. Yet these cities accounted for more than 25 per cent of China's GDP in 2007. Without doubt, history, location, economies of scale, and broad preferences granted by the central government (for example, Special Economic Zone status) have contributed to this success. Three main factors, below, explain why larger cities have a competitive advantage:

1. Larger cities attract talent. Shanghai has the skills and talent it needs to fuel economic growth. It attracts 100,000+ graduates from higher education institutions every year. As a result, 28 per cent of its labour force has college education.
2. Large cities attract more capital. Foreign direct investment (FDI) primarily lands in larger and expanding cities. FDI in emerging markets, at least initially, tends to go to areas with well developed markets, better infrastructure, more services and tax incentives—i.e. to the large cities. Shanghai has been more competitive than smaller cities in offering these and other benefits to investors.
3. City networks stimulate economic growth. Large urban centres are surrounded by suburbs and satellites. They allow network effects to spur economic growth and productivity. Shanghai sits in the middle of a close-knit cluster of economic centres on the Yangtze river delta, and this proximity has driven growth in the entire region.

Source: McKinsey Global Institute

Pakistani Cities

The challenge is to develop visions and strategies for cities to attract and management resources

Planning Commission's Task Force on urban development has emphasised the need for a policy that can transform cities as engines of growth. The challenge is to develop visions and strategies to attract and manage resources with optimal use of land (where people work, live, shop, entertain) and building infrastructure (roads, schools, hospitals, sewerage lines, water and utilities) and delivering services (health services, education, sanitation, etc.) This requires coordination across several levels of government and building and applying new governance arrangements.

The urban-rural divide has become blurred

With an increasing population, Pakistan is the fifth most populous country in the world and is second largest in South Asia. Pakistan's urban population is expanding rapidly. Urbanisation was only 32% of the population in 1998 and is expected to be over 50% in 2025. Actual urbanisation is probably much higher since the definitions of urban areas used in Pakistan are administrative rather than density-based. By this amended definition, estimates of actual urbanisation at present place 50% population in cities.

On current definitions there are, at present, 9 cities with population exceeding 1 million (Table 12). In addition there are about 75 cities with population between 100,000 and a million. Some of these cities are located closely into clusters. For example, the Gujranwala-Sialkot-Gujrat cluster has a population of 2.6 million and has specialised in engineering and surgical goods development. The cluster has also shown social capital development as the chambers of commerce in Sialkot have through private initiative constructed a privately owned airport in the middle of the cluster.

These human settlements if allowed to develop as centres of trade, commerce and leisure, could become the drivers of growth and productivity. These cities and clusters must find their identity and their comparative advantage to become destinations and nodes of ideas and entrepreneurship. They would then offer opportunity not only for economic betterment but also for a better quality of life.

Current zoning and building regulations favour a suburban sprawl where cities are expanding into peri-urban rural areas

Current zoning and building regulations favour a suburban sprawl where cities are expanding into peri-urban rural areas. Not only is rich agricultural land being taken up in some cases, the sprawl is making the delivery of urban services very difficult. The sprawl is also environmentally unfriendly as city-spread is happening at the expense of nature and more and more energy is required to service the spread.

Most importantly, the current mindset on city development, which favours a sprawl, is hostile to density, high-rise and cities that are people- and commerce-friendly. The current regulation also favours single family homes, cars, large parks and other amenities that largely favour the rich at the expense of commerce—retail, offices, warehouses etc—and more inclusive housing such as flats.

In the coming years, it is planned to change this mindset and encourage a construction boom by allowing dense high rise and people- and commerce-friendly cities to emerge.

This will also be the most inclusive policy that has been adopted so far as it will create many jobs for youth and women while also making room for all. Moreover with cities as the melting pot for immigrants, the dynamics on innovation and entrepreneurship will be unleashed.

Cities create jobs for all, in particular youth and women

Networks of these dense cities and city clusters will be the beacons of production and exchange. These networks have the potential of realising the large market that Pakistan is being the fifth largest country in the world. These will lead the coming growth acceleration in Pakistan. The Planning Commission and the Planning system will have to engage with all levels of government to realize this vision to re-engineer cities to be dynamic individually and a powerhouse of investment, innovation and growth as a network.

Table 14 Growing Population in Cities

City More than 1m	Population 2030 (‘000)
Karachi	27993
Lahore	14626
Faisalabad	6192
Rawalpindi	4149
Multan	3025
Hyderabad	3005
Gujranwala	3143
Peshawar	2778
Islamabad	3175
Quetta	2038
Sargodha	1074
Bahawalpur	1903
Sialkot	1087
Larkana	1174
Sheikhupura	1019

9 cities have population of more than 1 million today
15 cities will have population of more than 1 million by year 2030

Source: Planning Commission

Deregulation of Cities to Include the Poor

Zoning decides how land is used in cities. In particular, zoning determines what can be built in neighbourhoods where businesses (industry, shops, offices, warehouse, entertainment etc.), public spaces (parks, leisure facilities etc.) and community infrastructure (libraries, community centres, playgrounds etc.) will locate.

Together zoning and building regulations determine the density and character of a city

In addition, building regulations determine the height, width, and quality of construction to encourage safety, efficient use and emerging efficiency of the properties within cities. Together zoning and building regulations determine the density and character of a city. Mixed use and high density creates productivity synergies and allows for effective provision of transport, sanitation and other areas, while also creating problems of congestion.

City planning uses zoning and building regulations to manage the tension between agglomeration benefits and congestion costs. Experience has tilted planning increasingly in favour of mixed use city centres that become hubs of creativity centres and commercial activity and the nodes of global connectivity. The building landscape is continuously changing in such vibrant city centres.

Mixed-use city centres are now recognised as hubs of creativity and commercial activity, and nodes of global connectivity

Dynamic planning in cities is now developing a city identity and competitiveness (Box 10). In doing so, cities are continuously redefining themselves and creating space for new activities. These new activities are continuously unleashing new construction and with it new business. In this manner innovation and entrepreneurship is always simmering in urban cities. More importantly many new employment opportunities are created and this is the reason vibrant cities attract migration.

Box 10 Major Types of Zoning Observed in Modern Cities

1. Single family homes
2. Duplexes
3. Condominiums
4. Trailer parks
5. Apartments
6. Suburban residential
7. Urban residential
8. Commercial (including offices to retail stores, shopping malls etc)
9. Heavy industrial zones
10. Light industrial zones
11. Limited industrial
12. General industrial
13. Historic residential and business zones for areas with historic value
14. Agriculture
15. Mixed-use

Zoning laws in Pakistan require immediate transformation

Currently Pakistan has two zoning categories, residential which allows only for single family housing, and commercial which includes all else. In addition, commercialisation is on a plot by plot basis at a large financial cost called commercialisation fee. Building regulations are very stringent disallowing high rise, dense and mixed use development. The result is the visible excess demand for many activities such as schooling, offices, shops, warehousing etc. Evidence of such excess demand is the situation of all these activities in residential properties. Box 11 shows the zoning regulations in Islamabad.

Box 11**Zoning Breakdown and Regulations in Islamabad**

Islamabad is divided into 5 main zones (CDA, 2005):

Zone 1: Residential (including sectors for luxury housing—sectors E&F; economical housing—sector G; poor class housing— sector I).

Zone 2: Private Housing Schemes

Zone 3: Margalla Hills Park and protected ranges and forest areas

Zone 4: Initially for poultry and vegetable farms but now re-classified as residential for private housing schemes.

Zone 5: Private Housing Schemes.

CDA has outlined the following standards for residential schemes being built in Zones 2, 4 and 5:

Residential	55%
Open/Green Spaces/Parks	8%
Roads/Streets	26%
Grave Yards	2%
Commercial and Parking	5%
Public Buildings	4%

Building Restrictions in Commercial Areas:

5% allocated in residential sectors – height restriction of 4 storeys (current average height of 2 storeys)

Zoning Laws in Islamabad show a disproportionate bias towards residential housing

The zoning laws for Islamabad outlined above show a disproportionate bias towards residential housing – specifically large houses for the elite. Coupled with the restriction on conversion of residential areas, a large number of offices, restaurants, schools and businesses are illegally operating through houses in these areas. Commercial areas and parking are allocated just 5% in the schemes (compared with 55% for housing). The maintenance of current commercial areas like Blue Area has been severely neglected resulting in a drastically deteriorated outlook – explaining the reluctance of these businesses to move to commercial areas. Existing maintenance standards lack efficient implementation.

In contrast, other countries have multiple zonings including an emphasis on mixed use. Box 10 shows a typical zoning in US cities while Box 12 shows the zoning law in Dubai.

Zone	Code	Designation
Residential	R1	Medium density
	R2	High density
	R3	Worker accommodation
Commercial	AC	Activity Centre
Mixed-Use	MU1	Residential/commercial/office
	MU2	Academic and R&D
	BP	Business Park
Industrial	IN1	Food and Beverages
	IN2	Base Metals
	IN3	Logistics
	IN4	Transport Equipment
	IN5	Machinery and Equipment
	IN6	Minerals
	IN7	Chemicals
	IN8	Workshops/showrooms
Community Facilities	CF1	Education
	CF2	Religious Facility
	CF3	Health Facility
	CF4	Police Station
	CF5	Civil Defence (fire station)
	CF6	Library
Open Space and Recreation	OS1	Neighbourhood Park
	OS2	Community Park
	OS3	District Park
	OS4	Sport and Recreation
	OS5	Conservation/buffer
Utilities	UT1	Water
	UT2	Electricity
	UT3	Sewerage
Transportation	TR1	Road Reserve

Mixed-use, Density and City Centres

Mixed-use areas are conspicuously missing from zoning laws affecting city productivity and employment opportunities

Mixed-use areas are conspicuously missing from the zoning laws. City productivity and employment generation needs the growth of entertainment, hotels, shopping areas and offices in large complexes. Moreover, mixed use areas and city centres ideally contain high-rise buildings as land prices are at a premium, making tall buildings economically favourable. Height restrictions imposed by the CDA discourage high-rises, and has resulted in the small shopping areas in every sector and small shops in Blue Area that provide an unsatisfactory shopping experience.

Urban zoning in Pakistan remains unfriendly to high rise buildings, mixed use development (live/work areas) and commercial uses such as retail and warehousing. In fact, what is observed is construction of large elite houses at the expense of commercialisation, as is evident from the case of Islamabad above. In virtually all cities, a huge excess demand for office, apartment, retail, warehouse, education as well as community space is visible. Businesses are forced to move to residential areas as they are faced with high commercialisation fees and cumbersome procedures. Commercial fee, which has to be paid prior to any complex construction, ranges between 10% to as high as 40% of the property cost. Commercialisation fees in Karachi for example are exhibited in Box 13.

Box 13 Commercialisation of Fees in Karachi

- Range from PKR 750 to PKR 8000 per sq. yard (depending on the location of the building)
- For a medium sized residential plot of 667 sq. yards (6000 sq ft), this means a commercialisation fee ranging from PKR 500,250 to PKR 5,336,000.
- For buildings in the cooperative housing schemes, an additional amount of PKR 1000 per sq. yard along with a Ministry of Housing charge of PKR 400 per sq. yard need to be paid.

High rise buildings are discouraged

- Floor to plot area ratio of 1:3.5 to 5, which results in four storey buildings being termed as high rises

As shown in the box above, commercialisation of residential property in Karachi is difficult. Violation of the bye-laws results in a fine of 5% of the commercialisation fees and a further 10% for each year the violation is not corrected. Commercialisation process is also cumbersome laden with paperwork and red tape. Applications have to be filed for change of land use to Master Planning Department of the City District Government Karachi and the Office of the Nazim of the Union Council, along with a newspaper advertisement for comments from the public. The Union Council can take 30 days to accept or reject the application and if there is a clash of decision between the Master Planning Office and the Union Council, the decision is taken by the district assembly. Commercialisation has also been restricted to 'strip development' along the 17 major roads of the city rather than having business and commercial districts within the city. This leads to poor usage of space and shows lack of coordination among the different agencies when it comes to city development.

Commercialisation process is cumbersome and laden with paperwork and rapid tape

There are also other building regulations that can hinder construction of commercial buildings. Parking requirements are stringent with one parking space required of every 100 sq ft. in places of public assembly, 800 sq ft. of floor area for retail shopping, 1000 sq. ft. of business office space and 1200 sq. ft for residential apartment buildings.

Punitive Building Regulations Retard Construction

Increased building regulations increase costs and hassles for new construction businesses in Karachi

Private sector activity faces additional regulations in the form of high and multiple taxes (e.g. 2% cost of surety/performance bond has to be deposited with the KBCA in cash) along with facing increasing procedures and corruption. Date of completion regulations are also restrictive with 2% of the value of the project is subjected to deductions in proportion to the period of delay, if the delay is not approved by the Authority. Renting out property is also discouraged in Karachi. Rented-out properties are required to pay twice the property tax of similar owner-occupied properties as well as high rate of stamp duty (3% of the value of the contract) and registration fee (1% of the value of the contract) on the registration of lease documents. The Sindh Rented Premises Ordinance, 1979 also tends to favour the tenant, by allowing the tenant to seek intervention of the Controller to assess the fair rent and disallow revision in the rent of a residential building over 3 years. This discourages construction for rental purposes, stifling commercial growth.

Increased building regulations can increase costs and hassles for new businesses to carry out construction in different areas of Karachi. As such, high levels of government intervention can stifle income and economic growth of the city by discouraging new investments.

Policy

City planning should be revised for deregulation to unlock productivity and innovation

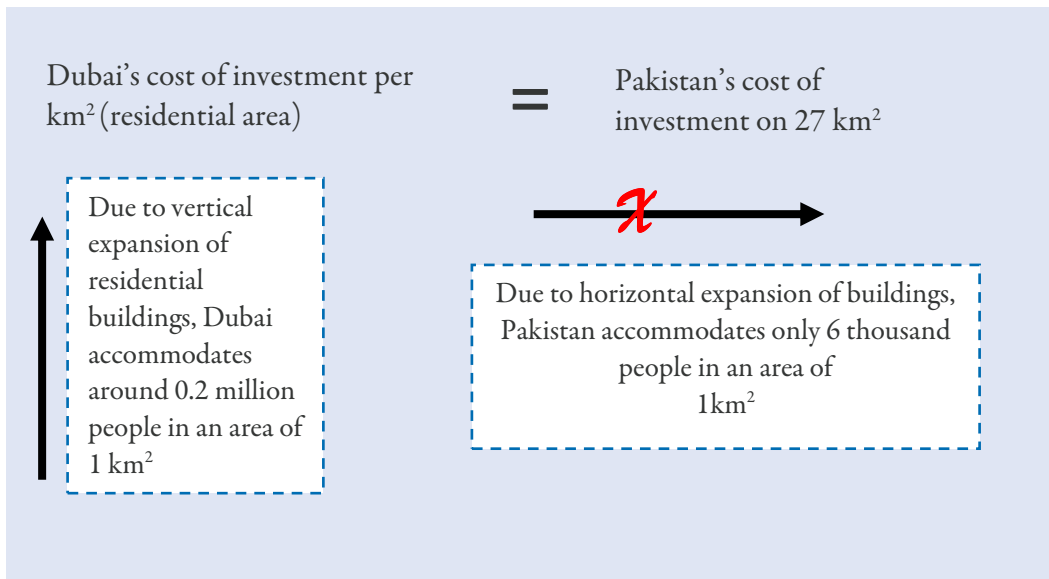
If city planning is revised to the need for deregulation, considerable construction and activity can be unlocked. The need is:

1. Rezoning of current residential areas which are facing demand pressure and that are nearer city centres to be characterized as “mixed use”
2. Reform of building laws to allow high rise, mixed use and dense construction
3. Strengthen property rights and exchange mechanism to facilitate consolidation of property to allow large commercial complexes to be developed
4. Developing property rights for joint ownership of buildings and maintenance of common areas.

These simple changes could make cities to become engines of growth and beacons of investment. Very quickly poverty will be significantly alleviated, middle class substantially included, and the growing youth population properly occupied. This is the most expedient method for the economy to pick up.

Dubai because of its affinity to high-rise and density spend 27 times more than Pakistan in

The potential for construction activity can be seen from the comparison between how much construction we undertake in our cities and the construction investment in Dubai. As Box 14 shows Dubai because of its affinity to high rise and density spends 27 times more than Pakistan in each kilometre of built up city centre land. Similarly in the dense areas while Pakistan only accommodates 6000 people, Dubai houses 200,000 people.



Who Owns the City?

A key issue is also the non-uniformity of building codes administered by a number of agencies within a city, each with its own bye-laws and little coordination between them. For example, various institutions and agencies in Karachi that have their own set of building by-laws and regulations for commercial development are: Cantonment Boards (6 of them); Karachi Building Control Authority (KBCA); Defense Housing Authority (DHA); and Private/Cooperative Housing Societies. Also there are a number of different agencies keeping records related to property rights, including Land Registrar, Revenue and Excise Departments as well as local Development Authority, Municipal Corporations, Cantonment Boards and others (World Bank, 2005). Similarly, in Lahore, there are three main agencies which regulate construction (CDGs, DAs, and Cantonment Boards) in cities, each administering its own building bye-laws with little coordination with each other.

If cities are to become the powerhouses of growth and employment as in other parts of the world, they must become self-aware and search out their own identity and approach to providing their citizens a good life.

Lack of Affordable Housing

While the government is continually struggling with the inadequacy of housing for the poor and the middle classes there are several impediments to the increase in the supply of housing. Perhaps the most important of these are the lack of density and the aversion of building regulation to high rise construction. The current urban sprawl and lack of dense city centres is not poor friendly (see figure 28)

Cities must become self-aware and search out their own identity

Impediments exist in supply of housing to poor and middle class

Figure 28 Housing Sector Issues



Legislation for Density

Developing a Land Market

Relax zoning and building regulations to facilitate dense mixed-use development

- Modernise land registration system by electronically recording all transfers of land titles in a centralised data base.
- Establish a 'housing information system' to provide data on housing demand and supply from district to national level. It should include a Housing Price Index and Housing Access Index, with assistance from the Federal Bureau of Statistics, NADRA and FBR.
- Establish a regulatory body to register all property dealers.
- Relax zoning and building regulations to enable dense development of housing and vertical expansion. All legislative bodies must review rent laws and remove clauses that unjustifiably favour tenants and restrict the functioning of rental market.
- Establish a Land Privatisation Commission with the task of releasing unproductive land belonging to the State.
- Reduce the cost of construction by encouraging foreign developers to compete in the Pakistani market. Facilitate research and development in low cost and energy efficient construction techniques.
- Increase access to housing finance by enacting sound foreclosure laws and incentivising computerised credit information.

- Curtail growth of *katchi abadis*—use market based solutions to produce low income housing.
- Expand land supply in urban areas through renewal (high-density and mixed-use) projects in the inner areas and promoting densification.
- Halt the use of the Land Acquisition Act 1894 for acquisition of housing. Instead of compulsory land acquisition, land should be procured from owners at market prices.
- Require property dealers to get certification that ensures minimum knowledge of property law and real estate markets.
- Lift height restrictions on apartments for low and middle income groups and ensure a minimum density of 2000 persons per hectare.
- Review land development procedures especially the Cooperative Housing laws which are perpetuating suburban sprawl.

Developing Rental Markets

Rental laws in most cities in Pakistan are unfavourable to landlords (Box 15). As a result, investment in constructing rental properties is low, which has led to a very small rental market. Only 6 percent of housing in Pakistan is available for rent.⁹⁶

At the municipal levels there are no standardised rental contracts. Where rent related ordinances do exist, their enforcement is uncertain. It is a common practice to see that after the expiry of rent agreement the lessee refuses to vacate the premises and the local trader union protects the lessee against any eviction, even after court has directed for ejectment of lessee. As a result, vast numbers of commercial and residential properties remain idle as landlords are reluctant to let.

There are not standardised rental contracts at the municipal level

Box 15 Rent Control Legislation and Disincentives for Renting Property

Rented properties are liable for multiple taxes paid by owners of occupied properties. Furthermore, taxes paid to various authorities are treated as an expense against taxable income and not as tax credits, thus raising the effective tax on rental income. This has contributed to dysfunctional land markets, characterised by high prices and few rental units. Another disincentive for renting out properties is the high rate of stamp duty (3% of contract value) and registration fee (1% of contract value) on compulsory registration of rent lease documents.

Rent control legislation, such as Sindh Rented Premises Ordinance 1979, is biased in favour of the tenant, creating disincentive for construction of rental property. Specifically, the ordinance authorises the controller to assess fair rent and disallow revision in the rent of residential building for a period of 3 years. In case of non-residential properties, the increase in rent is restricted to 10 per cent per annum.

⁹⁶ Federal Bureau of Statistics, *PSLM 2008-2009*, Government of Pakistan.

The Forgotten Community

Cities provide space and infrastructure for communities to thrive. Through ages, cities have provided space for communities through the provision of public spaces such as town squares, community centres, libraries, theatres, forums, playgrounds, shopping centres etc. This community infrastructure has been deeply instrumental in developing social capital—trust, connectedness, teamwork etc. It is increasingly being recognised that social capital is crucial for the development of productivity and many other outcomes for growth.

Need to develop more community space in cities for libraries, museums, science centres, parks and community centres

In the coming years, there is a need to develop more community space in cities by allowing more space for libraries, museums, science centres, community centres and parks for under-privileged areas. This has to be done in the context of developing density, high-rise and mixed use. Needless to say city administration should make efforts to integrate heritage conservation into cities / towns planning and development process. However, given past neglect, greater weight would have to be given to the provision of spaces for community, intellectual and recreational activities (Figure 29).

Figure 29 Governance for Cities



Annex–Recommendations for Urban Development

The Taskforce on Urban Development that submitted its report to the Planning Commission further recommends:

- **Expand Inner City Markets:** There are substantial opportunities in inner-city areas. Market intelligence can help discover under-served markets in urban areas and attract investment, broaden retail services, and create jobs
- **Promote City Cluster Development:** Promoting linear commercialisation along inner-city roads and supporting the growth of multiple commercial and central business districts (induced by the urban sprawl) would accelerate growth in urban areas
- **Sub-National Government Financing:** The local governments should be given financial autonomy and encouraged to raise more revenues from local taxes
- **Roads and markets and other infrastructure already exist in urban areas.** Instead, attention should be paid to strengthening employment opportunities for the poor in key sectors through enhancing their employability by focusing on technical education, vocational training and skill development that is in line with market demand
- **Land supply in urban areas should be expanded through renewal (high density and mixed use) projects in the inner areas**
- **Provincial Revenue Departments and urban local governments need to coordinate the conversion of agricultural land to urban uses**
- **State land with metropolitan areas should be reserved for low income housing and delivered through market mechanisms**
- **Amend the zoning and building regulation and match the market preferences at different locations and zones to support high density high-rise and un-segregated land use patterns**
- **Heritage conservation should be integrated into the overall cities/towns planning and development process**
- **Revitalising HBFC by encouraging it to venture into new avenues such as community mortgage programmes, housing credit assistance to public and corporate organisation employees, support to bankable housing projects in the private sector**

- Low income housing should consist of 60 square meter plots, long and narrow: width to depth ratio 1:3, with permission to build ground plus 2-1/2 floors. The built-up area of the plots should be a minimum of 65 per cent and a density of 2000 to 2500 persons per hectare may be achieved
- Planning should create independent neighbourhoods around open spaces rather than along streets. Each neighbourhood should not exceed 300 households
- Cross subsidising low income housing from high income commercial and residential development should also be initiated
- Apartments for lower middle and middle income groups should have no restriction on height and should have a minimum density of 2000 persons per hectare
- All commercial and office complexes should be mixed use with 30 per cent of the floor area reserved for residential and recreational purposes
- No development scheme should have plots of over 400 square meters. If such plots are created then they should be heavily taxed to discourage such developments

Connecting to Compete

'Measured in time of transport and communication, the whole round globe is now smaller than a small European country was a 100 years ago'. – John Boyd

Connections and linkages can either be domestic in nature or in a global/regional context. While border cities are made hubs of regional trade through rail and road links, and automated custom posts, domestic markets with no artificial barriers need to be made efficient so that they could exploit their comparative advantage.

Connectivity is traditionally seen as road or railroad network, trucking, number of airlines, computer network, cell phone penetration, copper wire and fiber optic cables. Connectivity is considered in a broader context—specifically, how networks enhance interactivity with efficient use of physical, human and social capital and how these resources are interwoven to produce desired outputs.

Discussing human and social capital in terms of connectivity becomes essential when we talk about improving the productivity of the underlying physical infrastructure. It is a known fact that much of the basis for physical capital cannot exist in the absence of the cognitive and technical capacity (human capital) to establish physical capital in the first place, and to use it in the most efficient way thereafter.

At the same time it is inconceivable that there could be much use of hardware or software of economic growth without a network connection. What use are laptops and applications we run on them, if we cannot connect the devices to other servers and users? Networks bring people together to interact, by utilising the infrastructure, and enhancing our productivity. The value of networks is social capital.

State of Physical Connectivity

Transport

As per World Bank estimates, poor performance of the transport sector is costing Pakistan about 5% of GDP. Simply put, if our transport were improved and then maintained to a level commensurate with other countries with similar range of GDP as ours, then our GDP might increase by 5% on one-time basis. Furthermore, 30 per cent of agricultural output is currently wasted due to inefficient farm-to-market channels, lack of cold storage facilities, and an obsolete and underpowered trucking fleet.

Connectivity is how networks enhance interactivity with efficient use of physical, human and social capital

Inefficiencies in the transport sector is costing Pakistan 5% of GDP, annually

The term connectivity has been used by social scientists in different contexts. Where economists have focused on the promotion of trade through better physical connectivity, sociologists have looked at connectivity as some sort of social linkages based on informal rules, trust, societal values which ultimately result in improved social capital and hence growth.

A World Bank working paper 'Connecting to Compete' speaks only in terms of physical connectivity. However, it provides a chart of individual countries on a very broad canvas which not only includes connectedness to virtual market via internet but also freight forwarders, railroad network etc. The role of communications network in economic growth has gained a new vigour in the last decade.

On the other side, connectivity is seen as a network between '... friends, colleagues, and more general contacts through whom you receive opportunities to use your financial and human capital'. Later, Fukuyama defined it as a product of great social capital by saying that 'social capital is an instantiate informal norm that promotes cooperation between two or more individuals'.

Glaeser, however, talks about connectivity with respect to cities as within and across city networking. Where a greater emphasis is put on physical network when it comes to across city, people-to-people interaction via means of clusters and high density mixed-use areas is highlighted for within city networking.

ICT: The Connectivity Scorecard

The Connectivity Scorecard takes a holistic view of connectivity and looks at more than merely physical connectivity (ICT). It also includes the complementary assets and skills that determine just how productively the hardware and infrastructure are used. In 2009, Pakistan was 24th in a total of 25 developing economies in the 'resource and efficiency driven economies' category. In 2010, Pakistan fell one position to the bottom of the Connectivity Scorecard (Table 15).

Table 15 Connectivity Scorecard Rankings

Year	Pakistan	India	Iran	Malaysia	Turkey
2008	N/A	8	N/A	1	N/A
2009	24	20	12	1	2
2010	25	21	14	1	7

Source: M Zaidi, *Disconnected?*, Report for the Planning Commission 2011.

Human Resources Connectivity

As pointed out earlier, effective utilisation and management of physical infrastructure depends on quality of human capital (skills, knowledge and experience).

Reserved bureaucracy and stringent rules and regulations make it hard for professionals to participate in the economic affairs of the country

Human resources connectivity is a measure of how easily can a country recruit (and later manage) domestic and international professionals. This question is essentially important for countries like Pakistan, where most of the human capital comprises low to medium skilled labour. High skilled human capital, finds itself better off in migrating to developed world. The end result is brain drain. If it is to be believed that transmission of knowledge/skills takes place from high to medium to low skilled labour force in society, where high skilled workers keep up with the trends in their profession, brain drain can significantly affect the overall welfare of the home country.

In Pakistan, professionals/technocrats find it very difficult to participate in the economic affairs of the country. Where monopoly of civil service in running day to day affairs of the government institutions keep domestic professionals away, there are several regulations which do not allow institutions to hire foreign professional at top positions.

Social Connectivity

Social connectivity, which is not well understood in Pakistan, has also not been seriously considered as a vital resource for improving people's welfare. Investment in instruments which affect and reflect the intensity of interaction (social connectivity) within a community such as libraries, community centres, and recreation and athletic facilities, have either not been discussed or remained a low priority.

Box 17 Contribution of Social and Human Networks towards Growth

Social capital can also be of global nature—in the form of Pakistani diaspora. India presents a good regional case study. Students graduating from Indian Institute of Technology (IIT) and Indian Institute of Management (IIM), both having many campuses nationwide, go to the developed world, especially to the U.S., for higher education (Masters and PhD degrees). Since 1953, more than twenty thousand Indians migrated to the U.S. Although these institutions of higher learning have been criticised for encouraging brain drain from India, the highly educated and well connected Indian diaspora have provided a vital platform to India for greater international networking and creating the technology hub in Bangalore, Hyderabad and other cities in India, during the past 20 years.

After liberalisation of the Indian economy, in the early 1990s, the past trend of brain drain is now seeing a gradual reversal. Now, Indian diaspora is not only investing in India but is cultivating social capital that emerged from the human capital context (i.e. IIT and IIM alums) by bringing in business contracts from the U.S. (banks, multinationals, and even U.S. domestic firms) by using their international contacts. Return of the diaspora and their networks and networking skills which are being fused with domestic networks and know-how are now contributing significantly towards development of Indian markets, commerce, institutions and to overall economic growth. Over the last decade, emerging scientific and manufacturing industries and outsourcing of technical jobs from North America and Western Europe to India has created significant opportunities for the graduates within India.

Pakistan also has a significant diaspora. However, volatility in economic growth and lack of political consensus to push essential reforms discourages the diaspora from investing in Pakistan or collaborating with local enterprises and institutions.

Social divide between people belonging to different economic class is consistently widening

There is no official estimate for the total number of libraries in Pakistan. Officials at the National Public Library estimated the number of public libraries to be around 400, which included a cautionary note about what constitutes a ‘public library’ at the *tehsil* level – often no more than a few shelves of books inside the district or *tehsil* headquarters, which is almost never used.

Similarly, data on public spaces in Pakistan is also very limited. Little anecdotal evidence available suggests that such public spaces are either not at all or poorly managed. As people with greater purchasing power move towards few places which are better managed, social divide between people belonging to different economic class is consistently widening.

In developed countries libraries provide a space for not only self study but also for group study, community meetings, computer facilities etc. Significant area in the library dedicated for various ‘collective’ activities for interacting develops social connectivity. In addition, managers of public spaces (Central Park, Time Square, Trafalgar Square), frequently organise festivals, fairs, concerts, marathons and sporting events. In the US, school parks are open to communities after school timings—an impressive way of utilising existing infrastructure.

Impact of Poor Connectivity

Disintegrated Markets

Local markets are not fully integrated. With truck operating speeds on main corridors only half of the truck speeds in Europe and the productivity of Pakistan Railway’s freight services only 1/8th and 1/3rd of China’s and India’s respectively, the transport system in Pakistan not only takes longer but also costs more, creating significant price differentials between different markets.⁹⁷ Lack of useful connectivity also increases the risk of getting into joint ventures for businessmen of different areas. This discourages innovation by forcing people to stick to their traditional ways of doing business.

Horizontal expansion of cities requires citizens to wait and travel more to complete similar number of tasks per day

The situation gets further exacerbated due to the absence of significant cross-community social capital, especially rural communities. In the absence of credible accountability infrastructure, which is the case in rural areas, social capital acts as a threat in the form of social exclusion, hence mitigating for the risks attached with business transactions.

Lethargic Cities

Over the last decade, cities have increasingly faced traffic congestions. Unorganised and infrequent public transport with no safety and quality control has forced people to resort to personal transport such as cars and motorcycles. However, city planners

⁹⁷ *op. cit.*

continue to look for solutions in underpasses and flyovers instead of improving the public transport system.

The problem gets multiplied due to poor zoning regime which discourages development of high density mixed use areas. Planners focus on horizontal expansion of cities while doing almost nothing to improve public transport network, and this increases problems for the citizens who are now required to wait more and travel more to complete similar number of tasks per day.

Youth with Unemployable Skills

Physical, professional and social connectivity between universities, entrepreneurs, trade associations, professional and certifying associations, and enterprises in different sectors is very low in Pakistan. There are virtually no trade shows and conferences where the parties could meet, learn and attend professional training courses and interact for mutual benefit.

Pakistan is ranked 92 out of 133 countries in university-industry linkages index, much lower than the ranks of China and India, which are 23 and 46, respectively.⁹⁸ Due to the weak university-industry-professional nexus in Pakistan, our youth is not able to acquire the skills sought by employers. This skill mismatch is a fundamental reason our enterprises and universities do not compete effectively in the global markets.

Skill Mismatch is a fundamental reason our enterprises and universities do not compete effectively in the global markets

Reforms for Connectivity

Public Private Partnership (PPP) in Infrastructure Development

The project selection process (PC-1) should ensure that the project is floated first to the private sector. Only if the private sector is not interested should the government be approached for funding. An approach to reforming the project selection process has been initiated and should be speeded up.

Other constraints are in the form of procurement laws and processes. Procurement should include requirement for the public body to consider infrastructure service delivery through the private sector, while procurement processes should be decentralised. PPP projects which do not require sovereign guarantee or government funding should not require approval from highest level of government.

PPP projects which do not require sovereign guarantee should not require approval from highest level of government

Restriction on local governments against financing development projects through user charges or fees is also a major constraint to PPP at the municipal level. Land acquisition laws are cumbersome and have often resulted in delays and sometimes abandonment of the project. Evaluation process, under land acquisition laws, should take into account adverse social impact, including land acquisition, loss of assets, businesses and income.

⁹⁸ World Economic Forum, 'Global Information Technology Report', 2010

The NHA Act, which does not contain any requirement for PPP options, also discourages private sector participation. For example, it does not permit the assignment of toll receivables to the private company executing the project.

Currently many PPP based projects have been planned by the government such as Karachi Circular Railways (KCR), Centre for Liver Disease and Organ Transplant (CLOT) at PIMS, Faisalabad Solid Waste Management Plant and Cool Chain System etc. and are currently at different stages of evaluation with the Infrastructure Project Development Facility (IPDF).

However the past record of PPP projects (before that passage of PPP policy in 2010) has not been a very successful one. Much of the failures have been attributed to the reasons mentioned above.

Improving the Public Transport Network

Urban planners should provide appropriate space for transport infrastructure

In a situation where rail-based city transport alone is seen as an expensive proposition and beyond the means of most local governments, a mix of rail and road-based network integrated fully to cater to the needs of Pakistan's rapidly growing urban population has become a necessity. For such integration of the transport network, it may be desirable to establish at the provincial level strong regulatory institutions in charge of maintaining the transport infrastructure and regulating private transport operators.

Urban planners, apart from urban development, should also be responsible for providing appropriate space for transport infrastructure such as truck stands, bus terminals, bus depots, workshops, etc., and transport-related activities like wholesale markets and warehousing. Efforts should also be focused at implementing traffic management measure such as: one-way traffic, footpaths and cycle ways, improved signals, intersection improvements, bus bays, road maintenance, road drainage, removal of encroachments etc.

Creating a Sophisticated Market for Railways

Pakistan Railway's equipment and technology are obsolete

Pakistan Railways has a network of 7791 route kilometers, of which only about one-third is used for core commercial purposes. The rail system is passenger-oriented, and was reported to have carried 25.7 million passenger km in 2009, with freight traffic limited to 5.9 million tonne km. Passenger traffic is subsidised, and the railways' main focus continues to be on improving passenger rather than freight services, even though the latter are more profitable.

Pakistan Railways' equipment and technology are obsolete, and the organisation lacks managerial and financial autonomy. It is, therefore, not surprising that the railways have continued to lose market share. In the 1970s, Pakistan Railways was the primary mode of transportation between cities, and its share of inland traffic was estimated at 41 per cent of passenger traffic and 73 per cent of freight traffic. However, its share has declined steadily, and in 2009 was estimated at about 10 per cent for passenger and 4 per cent for freight traffic.

Japan: In Japan privatisation of the former state-owned railway, Japan National Railway (JNR), took the final form of public stock offerings. Privatisation was preceded by restructuring JNR into seven separate companies—six regional passenger railways and one national freight railway. The reform process took 10 years, from the time that it was recognised that radical restructuring was needed until the first of the JNR successor companies was offered to the public.

Sweden: Swedish state railways were separated into two activity centres. One centre became the state-owned rail operating company, Statens Järnvägar (SJ). SJ held a monopoly for freight transport over the entire network and for passenger services over the main line network. The second centre is Banverket (BV), the National Rail Administration. BV is responsible for providing and maintaining the country's railway infrastructure.

United Kingdom: Reorganisation of British Railways defines one extreme form of the railway structuring envelope. In the process of reorganisation, BR was unbundled. The discrete value-adding functions, such as car maintenance, terminal operations, locomotive maintenance, track repair, unit train operations etc., which are vertically connected in most other railways, were separated into numerous relatively small-scale enterprises. Each enterprise was offered for sale as an operating franchise to private operators. Ownership and management responsibility for the main line infrastructure was also privatised.

United States of America: Railway restructuring in the United States has involved industry segmentation into two kinds of private carriers: (1) large inter-regional carriers and (2) small local carriers. Structural changes in the industry were initiated primarily by the private sector within a regulatory framework that was supportive of railway reorganisation. Since the liberalisation of economic regulation in 1980, the U.S. rail industry has transformed itself in the face of strong competition from other modes. A distinguishing aspect of this restructuring process has been the creation of hundreds of small railways.

Source: R Kopicki and L Thompson, 'Best Methods of Railway Restructuring and Privatisation', CFS Discussion Paper Series Number 111, World Bank

In the first phase (next two years) Pakistan Railways can adopt partial privatisation measures, for example, outsourcing stations management, rail hospitals, allowing companies to run their own container trains, letting suburban trains run as separate companies.

In the second phase (three to five years) Pakistan Railways should be privatised completely. There are two possible ways of doing it. Firstly, through separation of infrastructure (unbundling) and secondly, by privatising regional railways while allowing them to remain vertically integrated. Unbundling may include privatisation of rail track, station management and services (passenger and freight) separately.

However, for successful results, two important conditions must be fulfilled. First, to effectively regulate railways sector after private operators enter the market, an independent regulatory body should be established with the sole responsibility of promoting competition and controlling quality. Second, prices should be deregulated and businesses should be allowed to charge marginal cost of servicing any route, or portion thereof, plus a mark-up which is agreed with the appropriate government regulator.

Railways can either be unbundled and then privatised or specific routes/regions can be sold independently

6 million passengers used Karachi airport, compared with nearly 23 million in Delhi

Towards Becoming a Regional Hub of Aviation

Pakistan does not compare favourably with regional competitors for air passenger traffic. In 2009, less than 6 million passengers used Karachi airport, compared with nearly 23 million in Delhi (which is only one of at least four competitive international airports in India). Moreover, between 2007 and 2009, Karachi was the only major airport in the region in which air passenger traffic consistently decreased. The higher number of passengers using Delhi is mirrored by the number of airlines that use its facilities—nearly 70, compared with 25 for Karachi. If Karachi is to start moving back towards its former role as one of the premier airports on the subcontinent, a number of policy reforms will be required.

Pakistan's existing regulatory regime is too restrictive and gives significant advantage to airports of regional countries. It must therefore create a level playing field for itself. In this regard, the right to carry passengers or cargo from a second country to a third country by stopping in one's own country (6th freedom rights) should be introduced. This will make Pakistan more attractive for potential investors and facilitate current players by increasing the profitability of the sector. Singapore Airlines and several other companies use this right extensively to fly passengers between Europe and Australasia. Given Pakistan's strategic location, this can significantly improve connectivity on Central Asia to Africa and Europe to Australasia routes. Thinking on similar lines, the design of the new Islamabad airport (under construction) must envision itself as a hub catering to Central Asian requirements.

The CAA, by the nature of its mandate, should not have control over any assets that makes it a market player

While an effort is being made to become competitive at the regional level, competition must also be encouraged at the domestic level. To make this happen, the Civil Aviation Authority (CAA) should continue pursuing an open skies policy in both passenger and cargo traffic. All airlines should be free to operate on routes of their choice. Routes which are congested should be auctioned instead of giving a preferential treatment to the PIA. International routes where open skies or multiple designations of airlines are not available, should be auctioned to all airlines, including the national carrier, in a transparent manner.

Currently, landing rights fee and timing slots allocated to private airlines by the CAA also favour PIA. The CAA, by the nature of its mandate, should not have control over any assets that makes it a player in the aviation industry. However, all the national airports are under its control. Therefore, to create a level playing field for all market players, airports should be privatised. This will not only reduce the fees through healthy competition between airports, but will also improve overall efficiency by improving check-in procedures, flight management, and facilities.

Improving Trade Facilities through Adoption of ICT

Customs clearance in Pakistan averages four days, compared with only a few hours in the most efficient ports in the region, for example, Singapore. A large part of the delay in Pakistan can be attributed to the use of manual clearance systems and institutional weaknesses that do not stress transparency and accountability.

In order to facilitate trade activities, electronic customs declaration forms must be adopted. The form is already available and Pakistan can simply consolidate other information onto the form, in line with integrated systems of France or Hong Kong (World Bank 2010). Only doing this will significantly reduce the number of documents required for exporting/importing purposes.

Pakistan Customs Computerised System (PaCCS), which was piloted in Karachi, is still to be rolled out throughout the country's customs posts. Its successful implementation at country's seaports helped reduce the congestion and enhance the overall transparency by providing a comprehensive, user-friendly and interconnected electronic data interchange system. At the time of this writing, FBR and Agility (company which designed PaCCS) are in talks on how to improve PaCCS and make it more relevant to country's tax regime. It is also expected that FBR may purchase the software once the issues are completely resolved.

**Successful
computerisation of
custom posts will help
reduce congestion and
enhance transparency**

The Sialkot Dry Port Trust model should also be adopted for all the national dry ports to allow traders to clear their goods in their cities. Most of the goods are currently sent to the seaport for clearance, largely because of longer clearance times, insufficient capacity, and higher costs at the existing dry ports.

Incentivising ICT Services

In the e-government evolution process, Pakistan stands at an early stage where government institutions provide only limited services using their websites. Recently, the FBR has taken some important initiatives to provide options for paying taxes online. By providing more services online, government can incentivise broadband usage by reducing waiting time, travel costs and administrative hassle.

The passage of an Electronic Signature Act would provide legal cover to the use of digital IDs, signature certificates and electronic authentication and verification. The proposed law should ensure that the electronic signature is uniquely linked to the signatory, capable of identifying the signatory, created using means that the signatory can keep solely under their control and linked to the data to which it relates in such a manner that any subsequent change of the data is detectable.

The Secretariat is the apex decision making body of the state and deals with a large number of departments. It involves an enormous amount of communication, keeping, maintaining and processing a large volume of data files. The manual creation, movement and maintenance of files involved enormous delays and inefficiencies. The government of Karnataka has recently set up a Secretariat Local Area Network by connecting 1,000 computers in 40 state departments and 6,000 secretariats. The National Informatics Centre of the state provided software support. The project has the following components:

- a) Patra-the Letter Monitoring System. This is designed for the management of a large number of letters received in the secretariat by scanning these letters and moving them from desk to desk, or department to department
- b) Kadatha-File Monitoring System is the decision support system to monitor, track and decide/dispose the files without delays. Through this system, electronic files are moved from desk to desk and from department to department without waste of time
- c) Mokaddame-Court Case Monitoring System monitors the court cases in which government is the party. Cases received, petitioners/respondents details, court orders, cases put up for hearing on a particular day/type can efficiently be managed
- d) Aayayaya-Budget Monitoring System helps in making budget estimates. It also monitors budget proposals once a budget is allocated to departments
- e) Sibbandi-Personal Information System maintains information about details of employees. Within a single click, the entire history of the employee can be viewed
- f) Customer Support System provides an online system to lodge any complaints regarding hardware, network, and application software system. This system also provides online instructions for the solutions to problems

Source: Mahbub ul Haq Human Development Centre, *Human Development in South Asia*, 2008

Open Domestic Talent Market

**Openness in Civil Services
increases overall
efficiency of government
functioning**

In order to improve the quality of human capital and increase the degree of human capital connectivity, Pakistan must open its domestic talent market to global pool of talent. Some steps have already been taken in this direction and foreign faculty is increasingly being welcomed to local universities. To promote this further, however, regulations should be revisited in order to make it legally possible for any institution to hire foreign professional at top slots.

Civil services should also be reformed through steps which may promote openness and hence competition. Such a step will not only increase the overall efficiency of government functioning but will also reduce human capital flight by increasing number of opportunities for high skilled in domestic market.

Like in the US and many other countries, the global market place should be used to attract professionals with advanced skills to Pakistan. Of course domestic residents will show a desire for the high-end jobs and be prepared to work for a discount and not need compensation for moving costs as would be sought by professionals abroad. But like their richer counterparts, developing countries, too, should not be parochial, relying only on nationals, when it comes to filling key management and research positions. Instead they should open up all such positions to the global talent pool.

By thinking in these terms, the emphasis moves from naïve ideas of curbing or taxing the 'brain drain' to managing the desired skill requirements at home. Human capital flight then becomes relevant only insofar as it takes away from the required skills at home. Rather than worry about who stays or who goes, we worry about measuring the required skills and how to get the Skill Incentive Parity (SIP) right in the economy. At the same time, by placing emphasis on the human capital requirements of the economy, and maintaining the analogy with physical or financial capital, we can move from the current view of retaining human capital of domestic origin to the current practice in advanced countries of attracting the requisite skills from anywhere. This will make developing countries also active in the global market for human capital that is currently only accessed by advanced countries. For example, it is difficult to understand why the academic market is fully globalised in the richer countries, with them picking professors from all countries while in the poor countries it remains the monopoly of domestic residents? When governance skills are not widely available, why should governments not delve in the international market for skills? Moving the emphasis to SIP and Human Capital Management (HCM) will bring these issues to the forefront.

Source: NU Haque. 'Brain Drain or Human Capital Flight', Pakistan Institute of Development Economic, 2005

Youth & Community Engagement

'Much education today is monumentally ineffective. All too often we are giving young people cut flowers when we should be teaching them to grow their own plants'. – John W. Gardner

A vibrant and evolving community by definition is based on high intensity of interaction, exchange of information and practice of new ideas. Furthermore solid educational foundation, sound health and intellectual standards also play an important part. However, for communities to grow stronger, the mere provision of more schools and hospitals is not enough. Youth and communities grow if provided space to conceptualise and actualise their ideas. The growth strategy argues that what is most important today is to provide youth, education with opportunity.

Education with Opportunity

Poor quality education in public schools has created parallel education systems

The failure to engage our youth and community as a whole has resulted in unintended consequences. The poor quality of education in public schools has created parallel education systems, disconnected and producing two different types of individuals: the highly trained, skilled and westernised elites and the conservative masses. Moreover, the failed experiences with democracy over the past 64 years and the episodes of external and internal threats have resulted in alienation among youth.⁹⁹

The next generation stands on a weak footing to deal with the challenges of an evolving competitive environment across the globe. The school curricula have seemingly ignored the importance of childhood and adolescence in shaping the lives of individuals. The education providers especially in the public sector have focused on the quantity of education rather than the quality, which has had negative implications for our youth, reflected by their lack of sense of citizenship and the problem of self-identification.

Majority of our youth has become school drop-out

Unfortunately, it appears that the majority of our youth has become school dropouts, and even those who do complete their education have little or no life or vocational skills. This leaves very few options for them when it comes to choosing livelihood or employment opportunities (Figure 30). The growing frustration among youth can be well understood from the educational and skill profile on the supply side and the declining job opportunities on the demand side (Figure 31). Such youth are likely to be vulnerable to prejudice and polarisation, which can lead to extremism.¹⁰⁰ Hence a failure to engage the large youth population and convert its latent energy into a dynamic force may result in very unfortunate consequences for the country.¹⁰¹

Failure to engage the large youth population will be very unfortunate for the country

⁹⁹ British Council, *Pakistan: The Next Generation*. Islamabad, 2009

¹⁰⁰ R Winthrop and C Graff, 'Beyond Madrasas: Assessing the Links Between Education and Militancy in Pakistan,' *Working Paper 2*, Centre for Universal Education at Brookings, Washington DC, 2010

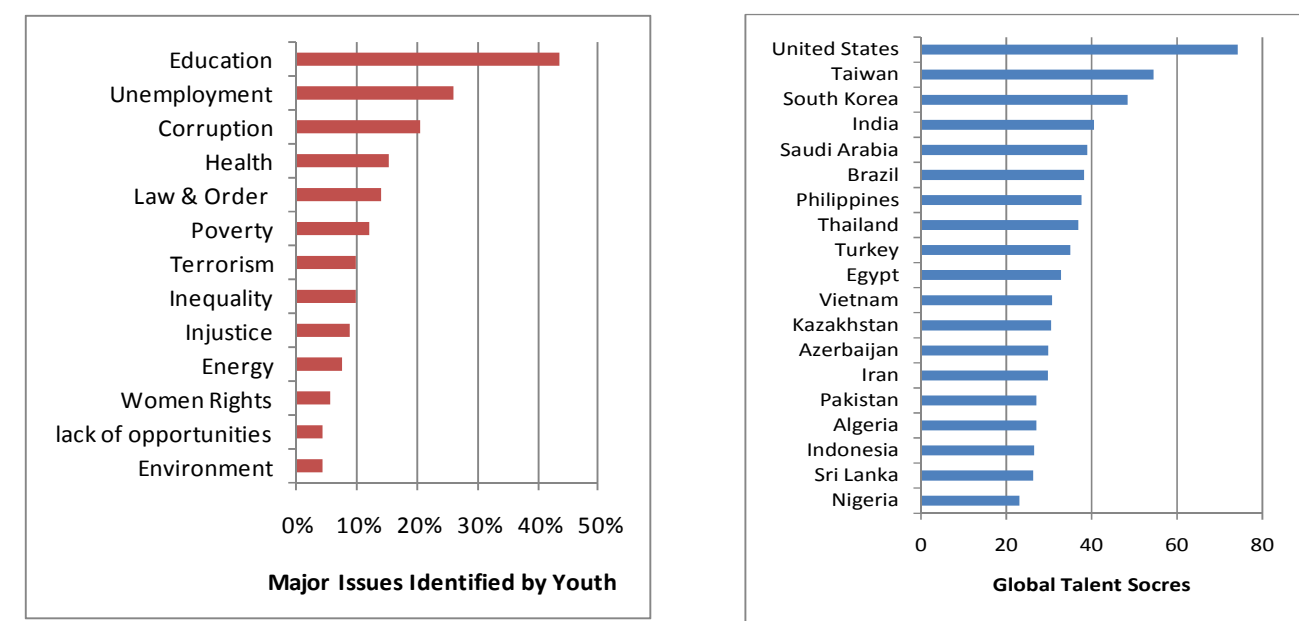
¹⁰¹ D Nayab, 'Demographic Dividend or Demographic Threat in Pakistan?', *Pakistan Development Review*, vol. 46, no. 2, 2007

A youth survey of around 100 students conducted in 10 major cities of Pakistan by CPRSPD reveals that youth accords poor planning and the law and order situation as major impediments to Pakistan’s economic progress.

Approximately, 23 per cent want to start their own businesses, but consider corruption, restrictive laws and regulation, and lack of financing as major stumbling blocks. Those who want to become entrepreneurs have no clue how to start their own business, which indicates that the educational curricula are not geared towards preparing youth for innovation and entrepreneurship.

23% of youth consider corruption, stringent laws and financing as major impediments to self employment

Figure 30 Issues Faced by Pakistani Youth and Global Talent Rankings



Lack of education, unemployment and corruption are identified as major issues affecting Pakistan in a youth survey conducted by CPRSPD (Box 22). For creating a better future for youth as well as Pakistan, these issues need to be dealt with. Among these education and skills is the most important because Pakistan’s poor performance on the Global Talent Index is primarily due to the poor quality of basic and university education.¹⁰² Experts exert that youth can significantly contribute to country’s socio-economic development through quality education and training. Youth and community engagement is a fundamental pillar of the growth strategy and should receive due importance.

Pakistan’s poor performance on the Global Talent Index is primarily due to poor quality of basic and university education

¹⁰² Education assumes the largest weight in Global Talent Index

- 71% have reported that their school does not provide career counselling, while 83% regarded it important for nurturing the potential of youth
- 79% are not satisfied either with the schooling system or the curriculum
- 47% do not have sports and recreation facilities in their locality
- More than 90% want extracurricular activities and facilities ranging from sports, discussion forums, libraries, computer labs, art labs, stress management and health check-up facilities at their school and are unsatisfied with the current state of facilities
- 28% feel syllabus/curriculum is not relevant to market demand
- Only 12% do not want to learn any occupational skills
- 100% hold that poor accountability is the most important reason for corruption in Pakistan
- More than 95% believe education can resolve the problem of extremism

Source: Youth Survey by CPRSPD

Current State of Youth

Pakistan is going to experience a youth bulge in coming years which will change the labour force

With almost two-thirds of the population (68.4 per cent) below the age of 30, Pakistan is going to experience a youth bulge in coming years,¹⁰³ which is likely to change the age structure of labour force over the next couple of decades.¹⁰⁴ The 15–29 year olds form 27.63 per cent of Pakistan's population—defined as the youth cohort. Between 2006-07 and 2008-09, this cohort increased by 1.8 million.¹⁰⁵ The need to provide education, health and livelihood for the growing youth population will now increasingly become important.

Pakistan has the largest proportion (32 per cent) of uneducated youth mostly with no vocational and life skills

More than one-third of youth live in urban areas and their share is expected to reach 50 per cent by 2030. Compared with other growing economies of the region, Pakistan has a larger proportion (32 per cent) of uneducated youth mostly with no vocational and life skills, who end up in elementary occupations or remain either unemployed or inactive.¹⁰⁶ Among these, females account for the larger share.

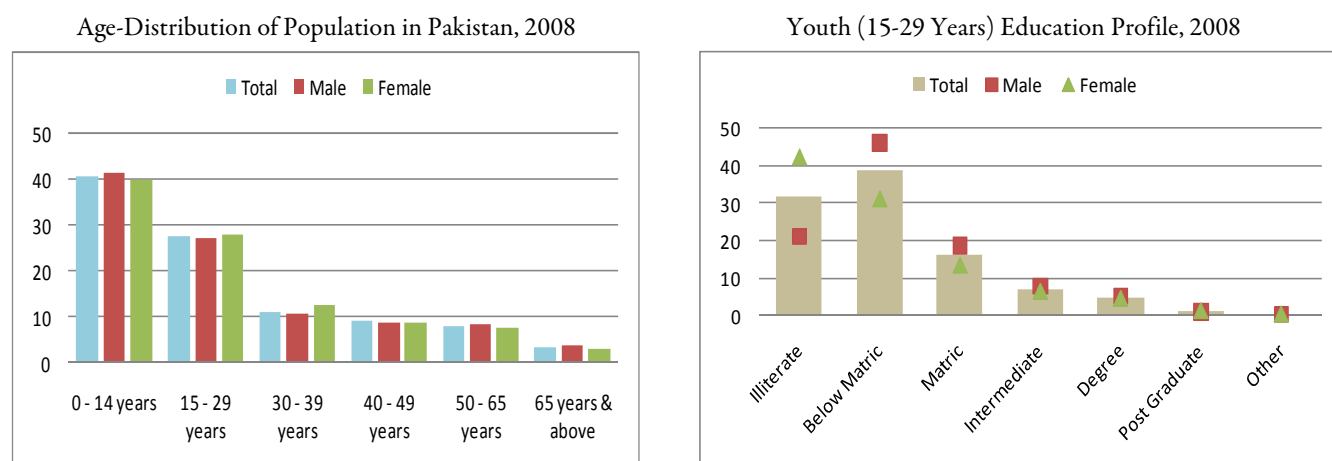
¹⁰³ GM Arif and N Chaudhry, 'Demographic Transition and Youth Employment in Pakistan,' *Pakistan Development Review*, vol. 47, no. 1, 2008.

¹⁰⁴ Based on LFS 2008-09 statistics, almost 2/3rd of the population is below the age of 30. The current estimates of population suggest a total size of 170 million people.

¹⁰⁵ If we expand the definition of youth as per Pakistani standards to accommodate people between the ages of 25 to 30 years as well, then 41 per cent people are concentrated in the age range of 10 to 29 years in 2008-09. The size of this cohort has increased by 1.8 million over 2006-07.

¹⁰⁶ For comparison with other countries, "youth" refers to 15-24 year old population; however, PSLM data reveals that the illiteracy rate for 15-24 and 15-29 year population is almost the same.

Figure 31 Age Distribution of Population and Education Profile



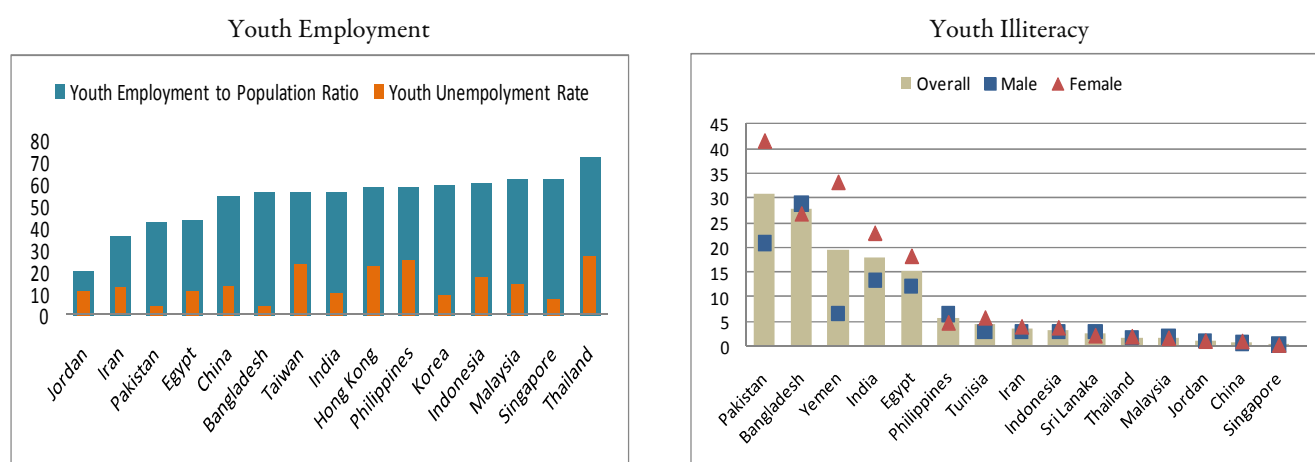
Source: PSLM 2008-09

According to the PSLM 2008-09:

- The illiteracy level among Pakistan's youth at around 30 per cent is the highest in the region.
- The disparities among enrolment and literacy rates of boys and girls are immense at all levels of education.
- Hardly 16.3 per cent of the youth cohort completes secondary education
- More than three-quarters exit the educational system without any foundational or life skills.
- Less than 6 per cent of the youth population has been reported to have acquired any technical skills through Technical and Vocational Education and Training (TVET)
- Only 2.5 per cent have reported On-Job-Trainings.

Illiteracy among Pakistan's youth is highest in the region

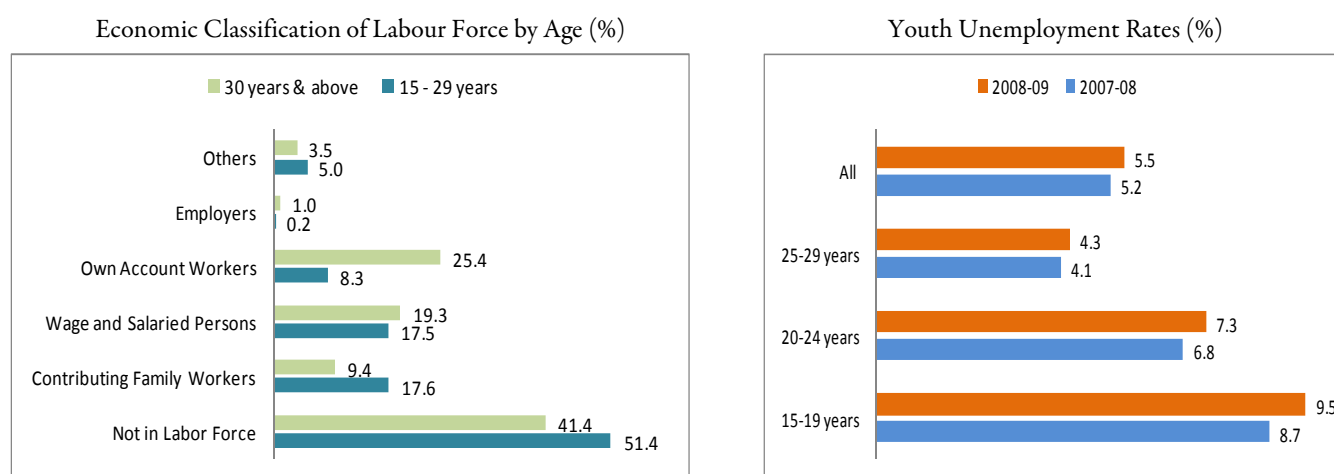
Figure 32 Youth Employment and Illiteracy in Selected Countries



Source: Key Indicators of Labour Market, ILO

Youth employment and illiteracy is shown in Figure 32. It is evident that the majority of Pakistan's emerging labour force is either without education and skills or has very little of both. In addition, skill sets taught to young boys and girls vary drastically and reinforce the prevailing concept that traditional labour intensive home-based work is for women. It is therefore not surprising that even though the reported overall unemployment rate was 5.5 per cent in 2008-09, the age-specific unemployment rate for the youth cohort in the range 15 to 24 years stood at 9.5 per cent (Figure 33).

Figure 33 Classification of Labour Force & Youth Unemployment Rates (%)



Source: Economic Survey of Pakistan 2008-09

The youth cohort also appears to lack entrepreneurship skills. Only 8.3 per cent of the youth cohort is reported as self employed outside agriculture and only 0.2 per cent have reported acting as employers (Figure 33).¹⁰⁷

The curriculum does not prepare the youth for the job market

The factors that account for this state of affairs emanate from both the supply and demand sides. On the supply side, for the most part the curriculum does not prepare the youth for the job market—there is a mismatch between the skills with which the youth graduates and those demanded by the market. There are only a handful of internship opportunities available, which do not hone their skills due to unstructured internship programs. Initiatives like National Internship Programs (NIP) should be expanded to local level and strengthened. On the demand side, the issue is the slow growth of the economy. Above all, public policies in the past paid insufficient attention to creating employment for the youth making them further vulnerable. Hence, it is extremely important to create entrepreneurship opportunities for the next generation.

¹⁰⁷ Calculated from Labour Force Survey 2008-09 for youth cohort reporting as employers or own account workers. The Labour Force Survey covers workers outside agriculture.

Box 22**National Internship Programme**

The national internship program has successively inducted unemployed graduates and post-graduates from all over the country since 2008 and provided hands-on-experience and temporary financial relief. The scheme has provided fresh graduates an opportunity to keep themselves engaged and gain real life experiences, thereby facilitating their improved employability in the country. It has not only benefited the unemployed to establish their professional networks but also facilitated government institutions, which lack full strength. The NIP can be further streamlined by monitoring and evaluation, defining terms of reference for internees in each government organisation and ensuring the placement of internees in government organisations relevant to their skill sets. It shall also be expanded to private sector by giving tax incentives for Corporate Social Responsibility (CSR).

The entrepreneurial activity among youth can be increased if the students are provided with business wisdom, inspiration and motivation, either through mentorship by experts or by stressing on the importance of business opportunities in the curriculum. Furthermore, economics as a subject is only taught under the Cambridge International Examination system in private schools. Most public and private educational initiatives have not given importance to education in economics and entrepreneurship in their curriculum to promote economic awareness, and introduce entrepreneurship education with simulation and nano-incubation enterprises. The curriculum and legal framework is more geared towards the provision of jobs by the public sector rather than the promotion of the private sector, competition and market efficiency. The absence of rules and framework that allows the establishment of enterprises needs to be dealt with to promote youth entrepreneurship.

**Rules and framework
need to be established to
promote youth
entrepreneurship**

Box 23**Youth is a Solution, Not a Problem!**

By establishing a net of indigenous Youth network throughout the country, Youth Engagement Services (YES) Network Pakistan, institutionalised the concept of Youth Service in Pakistan and demonstrated the impact of Youth Service in disadvantaged communities. This non-profit organisation provides youth with opportunities to become self-reliant and contributing members of the society through Youth service programs, Youth Social Entrepreneurship Programs and Service Learning programs. YES Network focuses on re-integrating youth into the society as active-citizens and not as citizens in-waiting. Its programs sensitise young people with the concept of bringing positive change in the society and provide young social entrepreneurs financial assistance and material to run a youth service project. So far, it has sensitised and trained over 50 principals of leading educational institutions, trained and engaged over 1,200 teachers, engaged over 20,000 young people in designing and implementing community-based micro social enterprises and established over 100 Youth Service Networks.

Source: <<http://www.yesnetworkpakistan.org>>

If properly engaged, and not considered as a problem, youth can contribute to both economic and social development. Many developed countries have engaged their youth in service learning networks for community services and delivery of social services. The YES Network in Pakistan has operationalised this concept. Similarly, the

**Developed countries
have engaged their
youth in service learning
networks for community
and social services**

Orangi pilot project and Khudi Ki Basti models have registered success in changing lives of many. Such community initiatives will be encouraged at local levels in all provinces.

Box 24 Success of Orangi

Good quality public service is the right of both rich and poor alike. Orangi showed how the poor can transform their environment and reduce costs and corruption to a small fraction of 'standard' costs by technical innovation and self-help. It also showed the importance of high-quality technical support, and why eventually there must be a partnership between the informal sector (which can handle much of the local infrastructure better than the municipality) and the local government. Similar examples of success are provided by Khuda Ki Basti model in Karachi (particularly in the case of low cost settlements). All these point towards an innovative partnership between government and natives which involves: a) addressing the problems of the poor with participation, b) shifting government policy from pure provider to sharing responsibilities, c) accepting people's development initiatives and complementing these, and d) mobilising local resources.

The Real Challenge

Despite being a provincial subject there are no youth development programmes in the provinces

Youth is considered a provincial subject, but provinces do not have effective youth development programmes. Unlike developed or emerging economies there are no youth programs at the local level. Given the increase in youth population, it needs to be addressed as a crosscutting theme and should get due importance in all sectors of the economy. Making an effective youth development program work across all provinces at local level is the real challenge (Box 25).

The empowerment of youth and the community as a whole requires us to examine critical reform issues in education and health sectors—now being devolved to provinces. The most significant change introduced by the amendment is the abolition of the Concurrent Legislative List (CLL); limiting the role of the Federal government to a few strategic areas listed in the Federal Legislative List (FLL). Many aspects of areas such as social welfare, environment and education and health will fall within the provinces' jurisdiction. The FLL (part 2) has also been amended to include new entries. While subjects in Part 1 are exclusively within the jurisdiction of the federation, those in Part 2 are subject to the overall direction of the Council of Common Interests (CCI), comprising of the Prime Minister, three Federal Ministers and four Chief Ministers. The size of the provincial share in the National Finance Commission has been increased to allow the provinces more autonomy with respect to budget allocation.

The aforementioned changes will have a significant effect on the governance structure of the social sectors, which has implications for youth development. For example in the health sector, the abolishment of the CLL has resulted in the transfer of areas such as drugs, medicines, mental illness, population planning and statistics to the provinces. Before the 18th amendment was passed, the federal Ministry of Health—functioning according to the 1973 Rules of Business, was responsible for most of the aforementioned activities. Now a significant amount of service delivery responsibilities are being devolved to the provinces to strengthen the governance and structure of service delivery according to regional needs.

Similarly, the 18th amendment also holds major implications for the education sector. The amendment includes an important and commendable insertion (Article 25A) which makes education compulsory for children. Another major implication of the 18th Amendment for education is that the curriculum, syllabus, planning and policy will fall within the jurisdiction of the provinces. However, as in the case of health, the federal government retains, to an extent, the function of ensuring and monitoring the standard of education.

The Implementation Commission is in the process of devolving ministries and their functions to the provinces. Some areas of concerns have been highlighted by the civil society regarding the standardisation and regulation of medicines in health sector and education quality and are considered as functions that should be retained at the federal level.

Opening Windows of Opportunity

Young people are the future of Pakistan and their aspirations matter; therefore, a comprehensive youth engagement strategy should build upon the following:

National Youth Service Reforms

Reforming policy and regulation to involve young people in community service, volunteerism and service-learning. This will provide a framework for youth development at federal, provincial and local levels, which mobilises the youth, especially women for moving towards non-traditional roles and responsibilities.

Youth Education and Skill Development

A program for developing the employment potential of Pakistan's youth will require:

- bridging the gaps between two polarised educational systems by improving quality

Reforming policy and regulation to involve young people in community activities

of public education; b) developing a national qualification framework; c) introducing courses related to economic choices and decision making for all disciplines; d) introducing 'work study programs' for youth; e) strengthening functional adult literacy initiatives to help workers increase literacy and learn life skills relevant to the job market; f) promoting career counseling services at community and school level; g) introducing youth entrepreneurship and leadership curriculum in primary and secondary level of education and advanced business skills at higher education; h) focusing on the software of education through teacher training and minimising teacher absenteeism, particularly in public schools; and i) mandatory health checkups and awareness programs on regular basis at school level to ensure better health for the next generation.

Youth and Women Entrepreneurship

Social and economic entrepreneurship opportunities remain the most promising path for the constructive involvement of the youth. For this purpose, the country's cities need to be community-friendly. Pakistan's cities do not promote vibrant communal and commercial activity that may be considered youth friendly.

The potential for youth and women entrepreneurship can be enhanced by creating space and opportunities for the youth in cities. This requires rezoning of cities which allows the construction of recreational space, sports centres, public transport networks, technology and commerce parks, retail chain strips and micro kiosks on major crossroads. This will boost domestic commerce which will allow absorbing the youth in micro and nano enterprises. In other countries, shopping malls and micro enterprises thrive around arterial public transport networks as millions of commuters stop by in layovers and do their shopping on their way home.

The female youth which is particularly at a disadvantage in the labour market will be able to find decent employment or business opportunities in a thriving business environment. In the past, cultural inhibitions limited the role of females in job markets and restricted their employment to specific occupations in education and health. Recently, an increased trend of hiring young women in marketing and front desk positions has created new occupational choices, but with low salaries. However, thriving economic opportunities can open up larger windows of opportunities for them as well.

Developing an entrepreneurship culture also entails the following: a) introducing courses related to economic choices and decision making for all disciplines; b) establishing 'Work Study Programs' for the youth; strengthening functional adult literacy initiatives to help workers increase literacy and learn life skills relevant to the job market; c) promoting career counseling services at community and school level; d) introducing a youth entrepreneurship and leadership curriculum in the primary and secondary levels of education, and advanced business skills at higher education; e) reducing the cost of setting up small businesses; g) expanding the national internship program with the involvement of both public and private sectors; h) creating equal opportunities for men and women; and i) providing local and foreign venture capital for entrepreneurship.

Youth Volunteer Services

One of the most effective ways of developing civic and national responsibilities of the youth cohort would be to engage them in economic, social, and community services supported or mandated by the national and provincial governments. Such services would be offered minimal compensation, but could be utilised for further education or for learning skills. The implementation of such a program may require revisions to the curricula of academic institutions, and perhaps even a formal requirement that educational institutes would implement, say, 40 hours of voluntary service before a degree could be awarded.

Youth needs to be engaged in economic, social and community services

Give Them Space!

The community lacks crucial infrastructure for recreation, education, and youth engagement such as community centres, theatres, cinemas, libraries, parks, sports centres, book stores, and malls. The prevalent real estate development culture which has its foundations in land grab and greed discourages building space for youth. To develop a youth friendly culture in a city, the urban areas need to be redesigned and rezoned so that they become youth and commerce friendly.

'You were born to win, but to be a winner you must plan to win, prepare to win, and expect to win.' – Zig Ziglar

“Who will implement?” is probably the most frequently asked question in Pakistan. This is so, because many good policy proposals and plans have been prepared but were never actualised. Our consultations have shown us that one reason implementation is poor in Pakistan is because plans are expected to be implemented by the very system that needs change. More often, there is no process or system in place for making change happen.

Implementation of change must alleviate constraints to productivity and facilitate growth

The Planning system needs to develop a process for implementation of the changes that will alleviate the constraints to productivity and facilitate growth. The Planning Commission will:

- Enhance its role to concentrate on national reforms through: a) creating mechanisms and consultation processes necessary for conception, analysis and implementation of national reforms, and b) providing advisory services to the Council of Common Interest on the matters of socio-economic importance
- Concentrate its planning functions on the national strategic level and analyse challenges and define directions for the nation as a whole, and not just for the public sector
- Provide stronger guidance to the ministries and departments within a framework of increasingly decentralised planning and service delivery as the ministries develop their strategic and service delivery plans
- Establish and maintain a system of monitoring and evaluation of the results achieved through the utilisation of public resources by the Government as a whole. The Planning Commission will also formulate processes to enhance accountability for results

Placing Economic Growth at Centre Stage

Emphasis on performance and results that affect people's lives

The Planning system—the Planning Commission, Planning and Development Division and Provincial Planning and Development Departments—in the country will be reformed to take a more proactive role in delivering development objectives to the people of Pakistan. This will mean a reorientation from traditional input- and project-monitoring and evaluation system to a sharper focus on performance and results that affect people's lives. Many successful nations have taken this approach. It involves regular monitoring and evaluating 'national' performance; this includes the private sector, civil society, central government, provincial and local governments, and public service enterprises. Because of the unpredictability of politics and markets, modern planners give less emphasis to traditional national plans.

The existing system of project-based planning is dysfunctional because:

1. Pakistan's planning resources are heavily committed to the approval, funding, and oversight of thousands of projects administered through line ministries/departments
2. This approach is proving unsound because projects are appraised without counting their fiscal consequences, approved without assurance of funding, and implemented through separate systems for planning and accounting for recurrent and development inputs
3. Because of the project focus, strategic oversight and direction of overall development effort is impaired, existing capital assets are not maintained, ministries are not developed as strategic development actors, and costs are not well controlled; also, there is little accountability for results
4. The duality of the approval and reporting processes produces a confused management environment in which perverse organisational and individual incentives thrive

The current system does not make growth and employment a core objective of policy

The current system does not make growth and employment a core objective of policy.

Moving to Productivity and Performance

The approach being followed in most countries (and that is used here) is to identify critical constraints to economic and social development, and then develop and facilitate national strategies to remove those constraints. For the modern planning body, government's direct development investments are less dominant in the national development process. It is placed in the wider context of the nation's institutional, policy and regulatory framework, the mobilisation of non-governmental resources, and the use of government's initiative to engage the private sector and communities in the development process.

Critical constraints must be identified to improve productivity and performance

The new vision for economic growth will require:

- Periodic identification of emerging constraints to economic growth through research and dialogue with all sectors and stakeholders
- Consensus building through extensive consultations on the reforms and programmes that will be required for alleviating these constraints
- Building a system for measuring productivity and public service delivery
- Developing and monitoring quantifiable plans regularly

Under the post-18th Amendment milieu, the Planning system will exercise control over the development process through:

- Consultation, setting medium-term and annual development objectives for the government and for relevant ministries

- Identification of key economic reforms that are required for these objectives, development of quantitative indicators (which can be monitored) for these reforms and monitoring and reporting on them to government and the people
- Specifying government and ministry-level reporting requirements for development results and their costs, to ensure accountability and track progress
- Strengthening the capacity of ministries and, by interaction and evaluation, ensuring that their strategies and services support national development priorities
- Developing capacity of planning system to act as an institution that develops and oversees the government's reforms agenda

In its new and more strategic role, the Planning Commission will continue to operate through the government apparatus. Implementation of the new strategies will require the government's line ministries to be fully aligned to the new approaches. This requires an overhaul of the interface between the Planning Commission and the line ministries. Ultimately, the strategic plans and the ministerial and sectoral performance and reform reviews must have NEC or Cabinet approval on a regular basis.

The interface with the government apparatus is already in the mandate of the Planning System. The Planning Commission guides the line ministries through perspective, medium and annual plans. While the basic system exists, it needs to be sharpened for the future.

The Federal Government has developed a Medium-Term Budgetary Framework (MTBF) which requires the government to set three-year priorities for ministries, and for government as a whole. The MTBF also requires ministries to develop strategies and budget bids based on intended results, and to report on the results achieved to the government and the National Assembly. While the MTBF has been rolled-out across the federal government, provincial Planning and Development departments and Finance departments will also be encouraged to adopt the MTBF-based planning and budgeting framework.

Five critical changes have been identified that need to be introduced to strengthen the linkage between the Planning Commission and government performance. These are:

- Strengthen the Medium-Term Development Framework (MTDF) and the Medium-Term Expenditure Framework (MTEF) in setting medium-term priorities in line with growth strategy and reforms agenda
- Support a unified results-based budget preparation process
- Decentralise responsibility for projects to line ministries
- Redefine the Planning Commission's role and processes in respect of major capital projects
- Establish a results-based monitoring and evaluation system

Results-based Management

Governments around the world are under pressure to evaluate their own performance. Results-Based Management (RBM) is a system through which the government can evaluate its performance. RBM is a management strategy by which government ensures that its processes, products and services contribute to the achievement of desired results (outputs, outcomes and impacts). RBM rests on clearly defined accountability for results, and requires monitoring and self-assessment of progress towards results, and reporting on performance.

RBM provides the change agenda for a greater degree of implementation assurance

Studies from around the world suggest that a change agenda driven through the principles of RBM provides a greater degree of implementation assurance. Most of the countries around the world have implemented RBM system in one form or another to support the strategic priorities and policies of the government and to improve efficiency and effectiveness in their spending. The system is being successfully used in most of the OECD countries including United Kingdom, Australia, New Zealand, United States, Korea, etc. More than 70%¹⁰⁸ of the OECD countries implemented output-based measures (based on RBM principles) 5–10 years ago. The system has also been successfully implemented in South Africa and several other African countries. Many more countries from around the World are either at the intermediate or advanced stages of implementing RBM system.¹⁰⁹

The RBM requires the government's management to focus on achievement of 'results' and utilisation of 'resources'. In Pakistan the focus of public sector management has been on achievement of 'inputs' or resources (human, financial and material resources). Thus the system of budgeting is purely based on 'inputs', the system of monitoring is based on progress of projects and utilisation of expenditure, the incentives schemes for the civil services are designed to reward / penalise the utilisation of 'inputs'. The management of government will now need to shift from 'inputs' to 'outputs' and 'outcomes'.

RBM helps government to focus on achievement of results and utilisation of resources

As per the RBM principles, the focus on results will be increased at the time of: a) formulation of sectoral policies and strategic plans, b) budgeting, c) monitoring, d) evaluating national performance, e) aligning incentives/rewards to the civil services, f) aligning ministerial/departmental structure and culture to achievement of results, g) transparency of use of government funds, and h) accountability.

¹⁰⁸ OECD, Performance Budgeting in OECD Countries, 2007.

¹⁰⁹ 'Results-Oriented Governments shift accountability for inputs (Did you follow the rules and spend according to the appropriate line items?) to outcomes or results. They measure the performance of public agencies, set targets, reward agencies that hit or exceed their targets, and use budgets to spell out the level of performance legislators expect for the price they are willing to pay'. See Osborne and Plastrik, 1997, p. 348.

- The Integrated Results-Based Management system incorporates a long-term macro-planning framework through effective horizontal and vertical integration for national development and capacity building.
- Integrated Performance Management Framework, part of Results-Based Budgeting, provides baseline data that allows measurement of comparable progress and results at predetermined intervals.
- Performance data are explicitly focused on measuring progress areas such as key objectives, outcomes, outputs, and activities. Such performance data are monitored against predetermined targets.
- A well-structured national level strategic plan lays the foundation for focused sector and program level plans and allows ministries and departments to establish linkages to higher-level key result areas. The targets under the Millennium Development Goals (MDG) typically form part of such a macro strategic planning framework.
- The system is critical to meeting Malaysia's national needs and the challenges of globalisation and regional competition.

'The Malaysia Modified Budgeting System provides greater managerial flexibility and accountability ... it performs on par with international best practice and is being used in some developing countries as a model.' (World Bank: Public Expenditure Management in Malaysia: How Malaysia Performs – 1999)

Source: Tax Division, Ministry of Finance, Malaysia.

There is at present no system for monitoring the results achieved by government, and as a result, there is no feedback from the implementation stage to the planning stage for the next round of the cycle. Put simply this means there is no system for the public sector to learn from its own experience, positive or negative. Monitoring can only be undertaken when clearly-defined plans have been prepared and adopted and which form the basis for the services to be delivered or investments to be undertaken through the use of public-appropriated funds. The ministerial strategic plans in line with the growth strategy will be developed on the basis of outcomes and outputs.

Introducing RBM in Government

RBM requires systematic implementation of key processes led by the overall growth strategy

Introduction of RBM in the government will require systematic implementation of the following key processes led by the overall growth strategy. The processes include:

- Fiscal allocations – Each year the Planning system will work with the finance ministry/department to articulate the medium-term budget strategy within the overall macroeconomic situation. The budget strategy will lay the basis for allocation of rolling 3-years indicative budget ceilings.
- Ministerial/departmental policies and plans – the policies and strategic plans of ministries/departments, will be aligned with the overall growth strategy. The plans will be systematically articulated along the lines of goals, impacts, outcomes, outputs and inputs.
- Budgeting – the ministries/departments based on their strategic plans and 3-years budget allocation will be required to prepare 'Output-Based Budgets'. This will require ministries/departments to cost their outputs and outcomes and also to present key performance indicators (KPIs) of outputs and outcomes.

- Accounting – the Planning Commission will work with the Public Financial Management reforms team in the finance ministry/department to support development of accounting systems capable of recording and reporting actual expenditure on based on outputs and outcomes.
- Monitoring – In future the Planning Commission will work with the line ministries to enhance their monitoring of outputs and outcomes. The Planning Commission will continue to act as an apex monitoring and evaluation organisation of the government. It will also provide output and outcomes monitoring reports (performance and budgets) to the Cabinet on regular basis and will also ensure processes exist for accountability for results to Parliament. In the coming months the Planning Commission will define the instruments for monitoring and reporting. This system will include the quarterly submission of summary reports on results achieved by each and every Principal Accounting Officer in the Federal Government.

**Output-based budgets
must emphasize on
outputs, outcomes and
Key Performance
Indicators**

Provinces and Local Governments will also be encouraged to adopt MTBF, RBM and evaluation mechanisms. The Planning Commission will interact with the provincial Planning and Development Departments and Finance Departments to ensure necessary processes are in place to enhance planning, budgeting and monitoring within departments of the provincial governments. The Planning Commission will support the provincial governments to foster the development of comparable systems at the local level.

Appendix – Action Matrices

Governance and Institutional Reforms				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
a) Revisiting Civil Service Reforms				Establishment Division, Provincial Governments, Attached Departments
b) Strengthen National Accountability Mechanism				Federal and Provincial Ombudsman, Auditor General, Public Accounts Committee
c) Restructuring of Public Sector Enterprises				Ministry of Finance, Cabinet Division, Public Sector Enterprises
d) Rationalisation of Subsidies				Ministry of Finance, Planning Commission, Provincial governments, SBP
e) Reforming Resource Mobilisation				FBR, NADRA, Provincial Finance Departments
f) Strengthen Legal and Judicial Framework				Ministry of Law, Justice and Human Rights, Planning Commission

Competitive Markets				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
a. Facilitating entry of new firms				SECP, CCP, FBR, Financial Institutions
b. Deregulation of Agricultural Markets and improving storage and warehousing facilities				Ministry of Food and Agriculture, CCP, SECP, TCP, PASSCO, Pakistan Mercantile Exchange
c. Improving legal and judicial environment for domestic commerce				FBR, IPO, Ministry of Commerce, Ministry of Law, Justice & Parliamentary Affairs, Provincial Governments
d. Re-establishment of the unilateral trade liberalisation program, and immediate abolishment of the present system of distortive regulatory duties (SROs)				CCP, SECP, Ministry of Commerce, Ministry of Industries, EDB, BOI, FBR, SBP

Creative Cities				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Reforms for Commercialisation				
Amend zoning laws and building regulations				Municipal Authorities
Auction/privatize state-owned land				Privatisation Commission, Provincial Governments, Municipal Authorities
Build linear commercialisation along inner-city roads				Provincial Governments, Municipal Authorities
Improve capacity of urban planners, facilitate research in low cost energy efficient construction				Higher Education Commission, Universities with departments of urban management
Reforms for Land and Housing				
Modernise land registration system by electronically recording all transfers of land title in a centralised data base				NADRA, Ministry of Law, Justice and Human Rights, Provincial governments
Establish a housing information system to provide data on housing demand and supply. It should also include a Housing Price Index and Housing Access Index.				Municipal Authorities, Federal Bureau of Statistics, NADRA
All legislative bodies must review rent laws and remove clauses, which unjustifiably favour tenants and restrict the functioning of the rental market. A regulatory body for real estate markets should be established.				Ministry of Law, Justice and Human Rights, Provincial governments, Municipal Authorities
Increase access to housing finance through sound foreclosure laws and computerised credit information.				SBP, Financial Institutions
Curtail growth of katchi abadis by using market-based solutions to produce low income housing.				Provincial Governments, Civil Society Organisations, Municipal Authorities
Use of the Land Acquisition Act 1894 for the acquisition of land for housing should be immediately halted.				Ministry of Law, Justice and Human Rights
Community Development				
Identify and remove/modify all laws, regulations and procedures that prevent the promotion of community centres, libraries and related mixed use spaces				Provincial governments, Ministry of Law, Justice and Human Rights, Municipal Authorities
Heritage conservation should be integrated into the overall cities/towns planning. Job centres for youth should be established at municipal level				Provincial governments, Municipal Authorities

Connectivity				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Reforming Public Private Partnership				
i) Revised Project Selection basis				Planning Commission
ii) Review Land Acquisition Laws				Ministry of Law, Justice and Human Rights, Planning Commission
iii) Decentralise PPP Project Approval processes				ECC
iv) Make NHA Act 'PPP' friendly				NHA, Ministry of Communications
Reforms for Railways				
i) Corporate restructuring of Pakistan Railways				Ministry of Railways, Ministry of Finance
ii) Deregulation of railway's fares				ECC/ Ministry of Railways
iii) Partial Privatisation e.g. Outsourcing station management; allowing companies to run their own container trains				Ministry of Railways, Privatisation Commission, Ministry of Finance
iv) Auction routes and unbundling of rail track services				Ministry of Railways
v) Independent Regulatory body for Railways				Ministry of Law, Justice and Human Rights, Cabinet Division
Reforms for Aviation Sector				
i) Review Draft Aviation policy (allow sixth freedom rights; equal treatment to all airlines)				CAA; Ministry of Defence; NTCIP, ECC
ii) Privatisation of airports				CAA; Ministry of Defence, Privatisation Commission
Other Reforms				
Shipping: modifications in the existing Merchant Shipping Ordinance 2001				Ministry of Ports and Shipping
Establishing road link between Gwadar and up-country (M-8)				NHA; Government of Balochistan; Ministry of Ports and Shipping
Trucking: Reduce Custom Tariffs				FBR; ECC; Planning Commission
De-linking and "corporatisation" of National Logistics Cell's trucking units				NLC; Planning Commission; Ministry of Commerce
Freight: upcountry licensing/registration of freight forwarders				Ministry of Commerce
Space for Warehousing, Cold				Municipal Authorities; Ministry

Connectivity				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Storage, Trucking Zone, Value Added Services, Container Yards and Infrastructure and Amenities				of Commerce
Establishment of inland water transport network				Ministry of Commerce; Planning Commission
Reforms for ICT				
Increasing human Resources in ICT				Pakistan Computer Bureau and Provincial IT Departments
Computerisation of Custom posts (including dry ports)				FBR; Ministry of Communications; Ministry of Railways
Electronic Signatures Act				Ministry of Law; Ministry of IT
Legislation protecting e-commerce transactions				Ministry of IT; Ministry of Law

Energy Sector				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Governance <ul style="list-style-type: none"> • Independence of Boards • Induction of professional management • Appropriate legislative changes • Government only to provide policy guidance through the Boards • Discipline in enforcement of rules and regulations • Strengthening of Ministry and regulatory bodies oversight and coordination role • Realignment of sector administrative and regulatory bodies 				Ministry of Water and Power Ministry of Petroleum and natural resources Ministry of Finance Planning Division Establishment Division Ministry of law and Justice Cabinet Division
Energy Pricing <ul style="list-style-type: none"> • Phase out of hidden and cross subsidies • Rational producer and consumer pricing • Economic basis for all sectoral pricing • Full cost recovery of prudently incurred cost of service 				Ministry of Water and Power Ministry of Petroleum and natural resources Ministry of Finance Planning Division NEPRA OGRA

Energy Sector				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Disengagement of Government from direct investment and management of sector activities- Providing enabling environment through appropriate Integrated energy planning, policy, governance and appropriate level of regulation				Privatisation Commission Ministry of Water and Power Ministry of Petroleum and natural resources Ministry of Finance Planning Division NEPRA OGRA

Water Sector				
Themes	Short Term (1 year or less)	Medium Term (3 to 5 years)	Long Term (More than 5 years)	Institutional involvement
Integrated Water Resources Management (IWRM): The Water Resources use and management has to be integrated for economic value of water				Planning Commission, Provincial P&Ds & M/O W&P.
Demand management, governance of urban water sector				Planning Commission for guidelines preparation, WASA for implementation, and Provincial P&DDs for full cost recovery and non-revenue water.
Legal support for water governance				Planning Commission, Provincial P&Ds & M/O W&P & M/O Law & Justice.

Results-Based Management				
Themes	Short Term (1 year or less)	Medium Term (3 to 5 years)	Long Term (More than 5 years)	Institutional involvement
Implementation of Medium Term Budgetary Framework at Federal and Provincial Levels				Finance Division, Provincial Governments
Start Monitoring of Outcomes in Line Ministries/departments/planning system				Line Ministries, Provincial Departments [coordination: Planning Commission]
Prime Minister Secretariat and Planning Commission should monitor socio-economic performance based on overall reform agenda given in growth strategy				Planning Commission, Provincial P&Ds & M/O W&P & M/O Law & Justice.

Health, Nutrition and Education				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
HEALTH & NUTRITION SECTOR REFORMS				
Revamping/management of primary, secondary and tertiary healthcare (Rescue 1122; Strengthen DHQs; tertiary hospital autonomy)				Provincial Departments of Health; Federal govt. support as and when required
Healthcare Financing Reforms (Social Health Protection for poor; Health Insurance; other financing options)				Provincial Departments of Health; BISP; Federal Govt. support as and when required
Governance reforms in health sector (setting quality standards; essential services package; aid effectiveness; service structure; capacity; access to affordable medicine; Health Ombudsman; federal-provincial coordination)				Provincial Departments of Health; Federal Government
NUTRITION				
Food Safety and Security Reforms (minimum dietary requirements package; home grown food; household food security; Street food quality; subsidized nutritious food packages for mothers and children; school nutrition program/cash transfer for food)				Provincial Departments of Health, Food and Agriculture, Education, district governments, Federal Govt. (as and when required)
Micronutrients and fortification initiatives integrated at primary healthcare level and at community level with other health programs				Provincial Departments of Health, Industries, Federal Govt. (as and when required)
Mass awareness campaign (implementing regulations (Breastfeeding Ordinance etc.)				Provincial Departments of Health, Information, Education, Federal Govt. (as and when required)
EDUCATION SECTOR REFORMS				
Revamping primary, secondary, college education (primary based on English/mother tongue/Urdu literacy; basic arithmetic; secondary based on Secondary School Certificate and Technical School certificate; college based on diverse discipline				Provincial Departments of Education, Federal Govt. (as and when required)
Enhancing Literacy, GER, NER (cash transfers for school meals, attendance; teachers training, primary education commission)				Provincial Departments of Education, District governments, Federal govt. (for overall coordination of information, results)
Extra-curricular activities (mandatory volunteering at secondary schools, colleges, universities; Sports activities; youth/social clubs)				Provincial Departments of Education, Sports and Culture, Youth Affairs, Federal govt. (as and when required)

Environment and Climate Change Sector				
Themes	Short Term (1 Year or less)	Medium Term (3 to 5 Years)	Long Term (More than 5 Years)	Institutional Involvement
Ensuring economic growth is sustainable and climate resilient.				
<p>Protect economic growth from the risk, and associated economic cost, of climate induced natural disasters by mainstreaming risk reduction and management concerns within the Government's planning processes.</p> <p>Overall Objective: Allocate adequate financial and other resources to implement the NDMA's "National Disaster Risk Management Framework" and Medium Term Plan (2011-2015)</p>				Planning Commission, P&D Departments, Urban Unit, NDMA, PDMA's, DDMA's, NIMD
<p>'Climate proof' economic growth from the impacts of climate change, in particular on the agricultural, water and energy sectors</p> <p>Overall objective: Allocate adequate financial and other resources to implementing the adaptation measures in the Government of Pakistan's Climate Policy and accompanying Action Plan (upcoming).</p>				Planning Commission, MOE, MFA, EAD
<p>Promote 'green growth' by attracting investment in low-carbon technologies.</p> <p>Overall objective: Allocate adequate financial and other resources to implementing the mitigation measures in the Government of Pakistan's Climate Policy and accompanying Action Plan (upcoming).</p>				Planning Commission, NDMA, PDMA's, NIMD, AEDB, Engineering Universities.

Appendix – Consultations for Growth Strategy

Economists/Professionals

Helen Clark (Former Prime Minister of New Zealand), Ambassador Robin L. Raphel (U.S. Coordinator for Economic and Development Assistance), Alan Winters (Chief Economist, DFID), John Williamson, Ricardo Hausmann (Harvard University), Lant Pritchett (Harvard University), Philip Auserwald (George Mason University), Hilton Root (George Mason University), Mohsin Khan (International Monetary Fund), Salman Shah (Former Finance Minister), Shahid Yusuf (World Bank), Homi Kharas (Brookings Institute), Peter Montiel (International Monetary Fund), Dennis Detray, Shahid Kardar (Governor, State Bank of Pakistan), Ehtisham Ahmed, Hafiz A. Pasha (Former Finance Minister), Shahid Javed Burki (Former Finance Minister), Abid Hasan (World Bank), Tariq Banuri, Ahmed Khalid (Bond University, Australia), Ehsan Chaudhri, Ijaz Nabi, Adil Najam, Mosharraf Zaidi, Rafay Alam, Faisal Imam, Kamal Munno, Zahid Adamjee, Razzaq Dawood, Asad Umar, Aqeel Karim Dhedi, Members of Economic Advisory Council, Pakistan Business Council, Private Sector Development Taskforce, and Chambers of Commerce (Karachi, Lahore, Sialkot, Gujranwala, Karachi),

Academia

Consultative workshops on growth strategy were held at F.C. College Lahore, Higher Education Commission, Municipal Research & Training Institute (Karachi), Comsats Institute of Information Technology (Gujranwala), Institute of Future Technologies (also attended by University of Gujrat and University of Sargodha) and National Management College. Video conferencing was held with private school systems in Lahore and Islamabad.

Civil Society Organisations

Consultative workshops on growth strategy were held at SDPI, PILDAT, Economic Freedom Network Pakistan, Competition Commission of Pakistan and RSPN. Growth Strategy document circulated to all leading civil society organisations and received feedback from SAHIL, SAPPK, WWF, OXFAM and LEAD Pakistan.

Development Partners

Consultations were held with all development partners including Pakistan Development Forum, Heads of all multilateral and bilateral donors, Donors Working Group on Governance organised by UNDP, Donors Economists Group and One UN Group. Separate meetings were held with UNICEF / UNIDO / UNESCAP / WWF / DFID, CIDA, World Bank, Asian Development Bank, USAID and British Council.

The meetings with development partners and consultative sessions were facilitated by Haroon Sharif, Zahir Dasu and Jean-luc Stalon.

Provincial Governments / Line Ministries / Regulatory Bodies

Consultations were held with all line ministries, regulatory bodies and provincial governments. A special session was steered with help from Advisor to CM for Planning & Development, Government of Sindh and Finance Minister, Government of Sindh. This included provincial secretaries and all heads of public sector departments in Sindh province. Similar meeting was held in Punjab which was steered with help from Chief Secretary, Government of Punjab. Additional Chief Secretaries of provincial planning departments visited Planning Commission twice for briefing and consultation on growth strategy. A roundtable on youth engagement was held in Planning Commission and was attended by all stakeholders. A Youth Idea Challenge for Pakistani Youth was launched by CPRSPD.

Parliamentarians

Detailed presentations were given to Senate Standing Committee on Finance and Planning and National Assembly Standing Committee on Finance and Planning. Meetings were also held with a vast number of members of provincial assemblies.

QUALITY OF LIFE . . .

. . . human development

. . . CREATIVE CITIES

urban development . . .

QUALITY GOVERNANCE . . .

. . . institutional strengthening

. . . community engagement

ENERGETIC YOUTH . . .

. . . VIBRANT MARKETS

. . . innovation