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Political Economy of Development in Pakistan

May 08, 2011

By **Kalim Siddiqui**

Introduction

Since independence in 1947, successive governments in Pakistan have proclaimed a desire to remove poverty through rapid GDP (gross domestic products) growth rates. To this end, the country had earlier adopted Import-Substitution-Industrialisation (ISI)^[1] and later on neo-liberal (i.e. 'free market') economic policies^[2]. But what is the impact of these policies in terms of achieving the goals of reducing poverty and inequality in Pakistan?

Proponents of free-market policies ignore the poverty issues and emphasise mainly growth rates, unquestioningly assuming that 'trickle down' would solve poverty problems. The ruling elites cite high GDP growth rates as indicative of economic development and consequently the well-being of the people. Contemporary "liberalisation" is occurring within the context of a new, growing form of global financial capital which has slowed down the rate of growth of Western economies by rolling back Keynesian "demand management" policies and by encouraging speculation activities in the name of financial innovation over enterprise in the rest of the world. This in turn will adversely affect export prospects of Pakistani goods. It is also important to note that at present capitalism has entered into a period of protracted global depression and consequently markets in developed countries are not growing to provide a market for Pakistani goods.

Growth and Crisis

At independence in 1947 Pakistan inherited some skills from the colonial administration and army although severe financial shortages impacted on the running of the day-to-day government and the rehabilitation of millions of refugees from India. The country was largely an agrarian nation with a very small manufacturing sector. Initially, Pakistan's main concerns related to the difficult situation with its neighbour, India. Moreover, on an organisational level the *Muslim League*, the party which campaigned for a separate Muslim state, was weak, particularly in West Pakistan. State power rested predominantly in the hands of military and civil servants as the *Muslim League* was unable to organise at a grass root level. The party had drawn its leadership largely from civil servants, large landholders, merchants and tribal chiefs but witnessed great difficulty after its founder M.A. Jinnah died in 1948 and the Prime Minister Liaquat Ali Khan was assassinated in 1951^[3].

Pakistan and the United States entered into various military agreements which allowed the US to set-up bases in Pakistan against the Soviet Union. Pakistan joined US-led military alliances, SEATO, in 1954 and then CENTO in 1959 bringing the military even closer to the Pentagon. When General Ayub assumed power in 1958, US intervention intensified military and economic affairs. The US needed a strong military in the region to defend their interest in the Middle East and in the North against the Soviet Union. As Jalal (1990) argues, by 1951 the United States', "policy statement on Pakistan ... made explicit what had always been implicit, namely that the kingpin of US interests in Pakistan was its army"^[4].

In the 1950s South Asia became strategically important for the US when Iran's elected government, led by Musaddiq nationalised foreign oil companies, came to power. The US and UK opposed

Musaddiq's policy of promoting national resources and overthrew Iran's democratically elected government in 1953. The US was looking for local allies and Pakistani civil and military elites were already looking for opportunities to forge close alliances with the US. Various arms assistance deals were signed with Pakistan. In return for military aid Pakistani territories were used to support US interest in the region[5].

On the economic front, the country launched Import-Substitution-Industrialisation (ISI) policy in the 1950s. Between 1947-1958, Pakistan's GDP grew at the average rate of 3.1 % annually, ahead of the population growth rate. During this period foreign capital inflows were insignificant and mainly limited to technical assistance. During the 1960s the average growth rate in the manufacturing sectors was quite high and General Ayub's government called this a 'Decade of Development'. However, the broader consequences of the economic policies are important to note. As Ahmed and Amjad observed, "This period of rapid economic growth, achieved mainly as a result of the policies pursued, generated a great deal of economic tension...Increasing disparities in regional income between provinces, a concentration of industrial economic power and the failure of real wages to increase significantly"[6].

Development strategy was formulated by a group of Harvard University economists and Pakistani civil servants who had received brief training in the US. Officially it was conceived within the framework of Five Year Plans. In fact, in the early years of General Ayub's rule, profits for the domestic and foreign companies rose dramatically, while at the same time wages stagnated and even declined in a real sense as saturation in domestic demands for consumer goods created an economic downturn. In the 1950s and 1960s rapid growth rates were dependent on foreign aid and government support to business. Growth was seen as important by neo-classical economists who suggested that high growth would eventually 'trickle down' to the people. Harvard economists emphasised that the rich would generate savings and ultimately invest leading towards job creation and overall growth, but it did not happen. Moreover, during the 1960s the disparities across classes and regions widened. The public spending on the social sector did not witness any substantial rise resulting in stagnation or little increase in real wages in the organised sector[7].

The government took the initiative to support the expansion of industries, mainly in the export sector, through the Export Bonus Scheme (also known as Export Boucher Scheme) in 1959 which critics suggest was largely responsible for high growth rates in the early 1960s. This was used to both subsidise exports and lessen import controls. The scheme provided additional income to a certain percentage of their export earnings (i.e. percentage varied from year to year and from commodity to commodity). Exports under the Bonus Scheme acted as import licences. Economic policies pursued during General Ayub's regime exacerbated the level of inter-regional disparity between East and West Pakistan. It was said that the resources had been transferred from East Pakistan with all benefits taking place only in West Pakistan. Also, in 1950, levels of per capita income were 10 % higher in West Pakistan than in East Pakistan but this disparity had risen to over 30 % by 1966 and in 1971 East Pakistan became the separate nation of Bangladesh. West Pakistan was able to successfully export to the market in East Pakistan. However, after the secession of East Pakistan a large portion of the market was lost as 50 % of the total West Pakistan's export and 20 % of its imports were from East Pakistan[8].

Zulfikar Ali Bhutto came to power after the collapse of the military regime in 1971. His emphasis was on rapid industrialisation in the public sector and this laid foundation of heavy industries such as steel mills and nationalisation of many private industries to increase state's role in the economy. Mainstream economists have often cited Zulfikar Ali Bhutto regime's (1971-77) for adopting policies which led to low growth and higher inflation. Let us examine the economic performance in the light of the facts. It is crucial to look at Bhutto's government performance in the context of the circumstances and problems that he inherited. Towards the end of Ayub's regime, private investment was already falling. After coming to power Bhutto nationalised banks and manufacturing industries which he saw as crucial industries with national importance, not be left in private hands. The Export Bonus Scheme was also withdrawn. During the first two years Zulfikar Ali Bhutto government witnessed impressive growth. Agricultural output rose largely due to tightened control over nationalised banks making more credits available to small farmers and medium enterprises. However, the last three years coincided with big investments in key industries with long-gestation

periods but economic growth slowed down sharply in both agriculture and manufacturing sectors^[9]).

Zulfiqar Ali Bhutto's economic policies of nationalisation of key industries such as banks, steel mills, insurance companies etc. was important, but lacked any long term commitments on how these sectors would contribute towards the modernisation of Pakistan's economy. Even managers appointed by the government to run these public companies had no enthusiasm, nor capital to modernise and improve productivity and efficiency. As a consequence, these industries soon experienced decline in productivity and profits. Thus, due to mismanagement, lack of funds and motivation, the crisis in nationalised industries deepened. However, the nationalisation programme of the Bhutto government did manage to increase public sector employment. In fact, when the Bhutto government was removed in 1976-77, development spending reached 11 % of GDP, the highest ever in Pakistan's sixty years history^[10]).

It will be interesting to look at global economic situation during the Bhutto tenure. In 1973, a four-fold rise in petroleum prices occurred and import costs of petrol, petroleum products and fertilizers rose sharply, which led to sharp price rise in domestic markets; followed by a world recession which depressed the demand for exports. All these international events were beyond control of the government. In 1973-74, prices rose exponentially to 30 %. Due to the global recession in 1973-74, exports dropped further, while a rise in import prices led to a dramatic rise in import bills. Moreover, the flood in 1974-75 damaged agricultural crops especially cotton, resulting in a decline of export revenue. In addition, a lack of fiscal and monetary discipline caused a high deficit budget so that monetary expansion and inflation rates reached new heights^[11]).

General Zia-ul-Haq removed Bhutto in a military coup in 1977 and when, in 1979, the Soviet Union invaded Afghanistan, the US provided huge military and economic aid to Pakistan. The US supplied military assistance to the *Mujahedeen* (holy warriors) through Pakistan. General Zia maintained the religious theocracy and extremist ideology to prolong his authoritarian rule. During the 1980s Saudi Arabia and the Gulf States also provided massive finance to the *Madarssas* (religious schools) in Pakistan with full support from the West to advance their strategic interests. Later on religious schools became the most potent vehicle of dissemination of extremist religious views and also encouraged sectarian division in Pakistani society. In fact, Saudi clerics were acting as incubators of religious extremism and fanaticism worldwide. As foreign mainly US military aid flowed in, General Zia ignored the tasks of building an independent, self-reliant and sustainable economic growth strategy, which would have set the country on the path of modernisation and long term development.

The average total GDP growth rates in Pakistan during the Zia regime were 7 % annually between 1978 and 1987, largely due to an expansion of the construction sector and demands for consumer goods. In the 1980s, nearly 2.5 million Pakistani workers left to work abroad. Remittances have played a crucial role in the country's economy since 1979 and by the end of 1985 it provided as much as 10 % of the GDP, but its role since then has diminished and is currently less than 3 % of the total GDP. The main reason for this situation stems from the expansion of domestic demands for consumer goods due to huge increase in remittances, which reached US\$ 3 billion in 1983. In addition, the steady flow of official foreign loans and grants, amounting to an annual average of US\$ 1.45 billion due to the Afghan war. After 1979, the Soviet Union's invasion of Afghanistan, both bilateral and multilateral aid provided substantial funds for Pakistan's economy. Foreign aid inflows were an important source to finance industrial investment during both the General Ayub and Zia period. Also, in Zia's period, remittances from the expatriates helped to remove foreign exchange deficits. However, at the same time talks of mobilisation of domestic resources for investment in modern industries in Pakistan were neglected; this gave the country a false sense of temporary economic security. By the end of the 1980s the remittances exceeded the value of the country's total exports. Hard currency was largely spent on buying land, building houses and on consumer durables. Also heavy industries set-up during the Bhutto period were operating and benefiting General Zia.

During the General Zia-ul-Haq regime (1977-88) the average growth rate of manufacturing industries was around 9 % per annum. However, a rapid rise in employment generation did not occur and the growth in labour productivity fell in the manufacturing sector during the same period.

occur and the growth in labour productivity fell in the manufacturing sector during the same period. In 1990, The *UNIDO report* on manufacturing stated, “an underlying feature of industrialisation in Pakistan is the deteriorating performance of the manufacturing sector in generating new employment opportunities. Although the decade of the 1980s has been a period of relatively high growth in manufacturing value added, the growth in manufacturing employment has remained insignificant. This partly represents more an increase in capital industry that labour absorption during the period of accelerated expansion”[\[12\]](#)).

Average total GDP growth rates in Pakistan during the Zia regime was 7 % annually between 1978 and 1987, largely due to an expansion of the construction sector and demands for consumer goods. Remittances have played a crucial role in the country’s economy since 1979 and by 1985 it provided as much as 10 % of the GDP, but its role since then has diminished and is currently less than 3 % of the total GDP. After 1979, the Soviet Union’s invasion of Afghanistan, both bilateral and multilateral aid provided substantial funds for Pakistan’s economy. At the same time, talks of mobilisation of domestic resources for investment in modern industries in Pakistan were neglected giving the country a false sense of temporary economic security. By the end of the 1980s, remittances exceeded the value of the country’s total exports. General Zia-ul-Haq regime had neither a long term vision on economy nor a clear economic strategy. In real terms, military spending rose by over 160 % under his rule, representing a growth of more than 9% annually. As Hasan (1998) argues “the unprecedented growth in defence spending, on the one hand, squeezed development spending and, on the other hand, fuelled fiscal deficits...Whatever, the merits of increased defence spending , the hard choices between defence and development were never really debated during the General Zia period”[\[13\]](#)).

Following the death of General Zia in a plane crash, Ms Benazir Bhutto was elected as Prime Minister in 1988. Soon after coming to power Ms Bhutto launched neo-liberal reforms, also known as structural adjustment programmes, under the supervision of IMF and the World Bank[\[14\]](#)). This meant that the government was unable to use fiscal and monetary policies to stimulate the economy. Their main concern was fiscal deficit and was asked to lower its deficit to 4 % of the GDP, to be achieved by increasing indirect taxes and decreasing public spending. For instance, the public spending in the area of development was 9.3 of GDP in 1986, but it declined to less than 3 % by 2004.

Another area of neo-liberal reforms was a reduction in import tariff rates, reduced from 125 % in 1992 to 25 % in 2004. As a result, a large number of domestic industries were closed down as they were unable to compete with cheap imported goods. This resulted in job losses and a decline in tax revenue for the government. In the name of ‘openness’ and ‘competition’ the economy was opened for foreign businesses, without providing any protection to domestic producers, resulting in closure of business units and a rise in unemployment.

Once Nawaz Sharif became the Prime Minister of Pakistan, he too carried out IMF’s led Structural Adjustment Programme and the role of the state in the provision of social and infrastructural facilities was further reduced under a wave of denationalisation and privatisation. The public owned industries were handed over to the private sector. A large-scale privatisation was carried out in the 1990 under Nawaz Sharif’s government. A disinvestment and de-regulation committee was formed to identify industries to be privatised in order to raise revenue. Following the Prime Minister Nawaz Sharif’s decision to carry out a nuclear test in 1998, Western governments imposed economic sanctions and the IMF withdrew all aid to Pakistan. As a result, the country faced a serious balance of payment crisis. Depositors started to withdraw their deposits in panic, which led to a huge capital flight and depletion of reserves. Exports were stagnant around US\$ 8 billion during the second half of the 1990s and remittances did not rise as witnessed earlier in the 1980s. In 1997, Pakistan had witnessed a massive foreign debt in excess of 100 % of the GDP. Debt servicing was taking away revenue from developmental and social expenditure projects.

Pakistan was in a deep economic crisis when General Musharraf took over in a military coup in October 1999. Soon after taking over General Parveez Musharraf appointed Shaukat Aziz, then a senior manager of Citibank, as finance minister in 1999. Aziz was promoted to prime minister in 2004 and he was given the task of stabilising the macroeconomic situation. His policies of deflating the economy to control inflation and domestic demands resulted in a dramatic decline in growth rates

to just 2 % in 1999. The government cut down the developmental and educational expenditure, leading to a further fall in growth rates 1.9 % in 2001. Shaukat Aziz, in order to tackle the balance of payment crisis, sold a number of state owned enterprises such as banks, telecommunications and power into private hands.

After the 11th September 2001 attack on World Trade Centre and soon after the US invasion of Afghanistan, once again Pakistan became a strategic ally in the war. The economic and military aid again started flowing-in and soon after the IMF approved new aid amounting to \$1.5 billion and previous debts were rescheduled to Pakistan. The rise in foreign aid and the transfer of payment provided a short-term boost to the economy and the country witnessed a current account surplus. However, the upswing in the economy did not last very long and in 2005 the economy began to slow down, the price of consumers goods rose and the current account deficit increased. This was partially due to poor domestic food grain production and also a sharp rise in global food and petroleum prices. In fact, many other developing countries experienced a similar situation but proved to be better prepared, while the Pakistani government failed to show any viable strategy to resolve the crisis. The trade deficit rose to US\$ 15 billion in 2008 from \$10 billion in 2007. Foreign exchange reserves plunged to \$8.5 billion in 2008 from \$13.5 billion in 2007. Since 2005 prices were rising at the rate of 12 % annually and inflation further rose to 20.2 % in 2008. In 2007 the poor harvest and higher import prices, especially food, exacerbated an overall price rise. The deteriorating living conditions of the people coincided with a conflict with judiciary and opposition political parties. Moreover, the rich decided to invest their wealth in shares and properties for quick profits. As a result, share prices and urban property went up along with multilateral and bilateral aid which was claimed as a success story. These so-called high growth rates by passed the majority of the people who saw their living conditions deteriorated due to rising unemployment, high inflation and corruption, which led further disenchantment with the military regime.

Khan's study regarding the nine years of Musharraf regime, finds that there was an increase of 2 percentage points in the unemployment rate while real wages of both skilled and un-skilled declined by 4 to 9 % despite the share and bond market boom. Macroeconomic stability was achieved by cuts in development spending and wages. The number of people living below the poverty line sharply increased, despite inflows of massive foreign aid and the World Bank led anti-poverty reduction programme. Under General Musharraf (1999-2008), corruption and nepotism became more widespread and inequality and unemployment increased further^[15].

Pakistan's macroeconomic indicators show that inflation has risen since 2004. For instance, the prices rose 7.4 % 2004, which increased to very high levels i.e. 20.2 % in 2008 and declined to 13.9 % in 2009 (see Table 1). The literacy rate is low i.e. 59.8 % (see Table 1).

Table 1: Pakistan Statistical Summary

	2004	2005	2006	2007	2008	2009
Inflation (% change)	7.4	9.1	7.9	7.6	20.2	13.9
Birth rate (per '000)	31.2	30.9	30.6	30.4	30.1	29.8
Total exports (US\$ billions)	13.34	16.03	16.93	17.84	20.48	17.53
Total imports (US\$ billions)	17.9	25.33	29.82	32.59	42.14	31.7
Infant mortality (deaths per '000 live birth)	71.1	69.5	68.2	66.9	64.6	63.6
Adult literacy	49.4	49.9	54.2	54.9	57.7	59.8

Source: Pakistan's Economic Survey (various years) Government of Pakistan, Ministry of Finance, Islamabad: Printing Corporation of Pakistan.

Pakistan is the only country to have approached the IMF more than 15 times and received numerous bailouts from the World Bank since 1988. However, poverty has risen sharply during this period and the overall economy has failed on many counts. Since 1988, the IMF has been involved in formulating and advising the economic policy in Pakistan.

Pakistan's failure to lay the foundation of long-term sustainable and self-reliance growth represents the main challenge facing the country. Mr. Gilani, who became Prime Minister in 2008, has simply continued the neo-liberal economic policies, which were adopted since 1988 on the advice of IMF

and World Bank. The constraints appear to be poor human resources and low levels of skills leading towards declining competitiveness in the country's traditional export sectors like textiles and leather. Any radical change requires government intervention to enhance competitiveness in export sectors and improve levels of skills to boost productivity. However, given the active role of the IMF, which is against any state intervention, seems to be long way off.

The macroeconomic instability lowered the foreign investors' confidence and the FDI experienced to \$ 5 billion in 2004 to less than \$2 billion in 2007. Prime Minister Gilani sought assistance amounting to \$15 billion from IMF in 2008. Since 2008 the deepening economic crisis such as high inflation, depleting foreign exchange, deteriorating balance of payments and declining value of Pakistani *Rupees* has been witnessed. The government led by Prime Minister Gilani is unable to resolve these economic problems, despite the large amount of aid from IMF, the US, Saudi Arabia and Gulf States. However, most observers have overlooked the close relationship between the western countries, international financial institutions and the ruling elites in Pakistan and the how these relationships have shaped the country's economic policies. The country provides a very clear example of the limitations of the IMF prescriptions and its adverse impact on the common people.

Table 2 shows that GDP growth rates were higher in the 1960 i.e. 6.7 % average per year. However, it declined in the 1990s to 4.6 and continued to 4.3 % in 2003. The manufacturing sector declined from 9.9 % in 1960 to 4.8 % in 2003. Services did not do any better i.e. 6.7 % in 1960 to 4.5 % in 2003. During 2008 and 2009 the GDP growth rates declined to 3.1 % and 2.7 % respectively. In 2009, the growth rate was only 2.7%, lower than rate of population growth (see Table 2).

Table 2: Average Annual Growth Rates in various sectors in Pakistan (in %)

	1960-69	1970-79	1980-89	1990-99	2000-2003	2004-2007	2008	2009
GDP	6.7	4.8	6.4	4.6	4.3	5.6	3.1	2.7
Agriculture	5.0	2.3	5.4	4.4	3.7	4.1	3.6	2.5
Manufacturing	9.9	5.5	8.2	4.8	4.8	5.8	3.6	2.8
Service sector	6.7	6.2	6.6	4.6	4.5	6.5	4.1	2.9

Source: Pakistan Economic Survey (various years) Islamabad: Government of Pakistan; and also World Development Indicators, World Bank, 2010.

Pakistan's financial imbalances are startling. In 2001 debt and defence amounted to more than two-thirds of the total public spending, i.e. US\$ 4.2 billion on debt, interest repayment and US\$ 2.5 billion on defence, compared to tax revenues of US\$ 6.9 billion. The IMF delivered a rescue package known as Structural Adjustment Programmes, included de-regulation, re-sale of public assets, further rise in indirect taxes, reduction in import duties and devaluation of Pakistani *Rupees*. As a result real wages declined and with fiscal spending cuts joblessness rose to new heights. The devaluation of *Rupees* could not boost exports, as IMF was expecting, while the lowering of import duties further deteriorated the balance of payments situation. Devaluation also causes foreign-currency debt to swell in domestic currency.

Increasing Poverty

Industrialisation was seen as a means to eliminate poverty, create employment and to combat illiteracy and disease, the legacies of the colonial past. Pakistan's economy at the eve of independence inherited an economy, where exports of raw materials such as cotton, leather etc. were prevalent, unlike India where British capital investment had created some pockets of industrialisation. In Pakistan, it was problematic to establish modern industries in the almost complete absence of any indigenous capitalist class to accomplish it. There were a few small production units that did exist but their owners were *Hindus*, who migrated to India during the partition.

The concentration of land in the hands of a small proportion of the rural population appears to be the main cause for the impoverishment of the rural poor because they do not own the vital assets^[16]. This opens up vast possibilities for their exploitation, misery and abuse. The unequal power that derives from the unequal landownership is the reason behind the continuing injustices in the rural areas. Although in Pakistan, land reforms legislation was passed in 1959, 1972, and in

the rural areas. Although in Pakistan, land reforms legislation was passed in 1959, 1972, and in 1977, the impact of these land reforms has been negligible as far as the land concentration is concerned[17]. Under cosmetic land reform provisions landlordism became more established and entrenched. In rural areas, access to land is considered as a major avenue for social status and most of the key activities are related directly or indirectly to the agriculture sector[18].

However, in the late 1960s and early 1970s the 'Green revolution'[19] was launched with full support from the US amidst claims that it would remove rural poverty and injustice. Key variables for the success of the 'Green revolution' technology package were new seeds, chemical fertilizers and irrigation to increase the total output of agricultural commodities. The rural rich constituted less than 5 % of the rural population were the principal beneficiaries of the 'Green Revolution'. As Hussain notes, "The new technology made it possible to accelerate agricultural growth substantially through an 'elite farmer strategy', which concentrated the new inputs on large farms. Now the crucial determinant in yield differences became not the labour input per acre in which small farms had been at advantage, but the application of the seed-water-fertilizer package over which the large farmers with their greater financial power had superior access. Thus, the technocrats felt that the Green Revolution had made it possible to accelerate agricultural growth without having to bring about any real change in the rural power structure"[20].

In Pakistan, there was an utter neglect of enhancing productivity of the workers through training and education to the possibility of moving from the production of simple consumer durables towards the production of more sophisticated consumers and high tech capital goods, which could be sold to the Western markets. As such successful transformation did happen to countries of East Asia such as Japan, South Korea, Singapore, Taiwan etc[21].

Poverty, inequality and unemployment have increased since 1988 with the adoption of neo-liberal economic reforms and the country has also witnessed high inflation and slower GDP growth[22]. According to official statistics, the percentage of households living in absolute poverty has risen from 21.4 % in 1991 to 30.6 % in 2008. Moreover, nearly 60 million people, 30 % of the population, now live below the officially defined poverty line, increased in the last ten years by 15 million. Public spending on education in Pakistan is one of the lowest in South Asia. According to official figures, 70 % of female and 41 % male are illiterate. The reason for implementing such disastrous policies and seeking continued IMF assistance was due to the fact that the ruling elites are unwilling to carry out essential economic reforms to address the main problems of the economy. Much of the wealth of the country has been transferred by the rich to overseas bank accounts or invested abroad, exacerbated since the policy of de-regulation and privatisation was adopted in the country, which did away with domestic capital control on the advice of World Bank and IMF. Moreover, having accumulated wealth through the nexus of corruption, many former civil servants and the military officials has set-up businesses directly or through their relatives[23].

Rich Pakistanis have accumulated wealth but they are very few and operate as junior partner to metropolitan capitalism. Much of the wealth of the country have been transferred to overseas bank accounts or invested abroad, which was exacerbated since the policy of de-regulation and privatisation was adopted in the country, which did away with domestic capital control on the advice of World Bank and IMF. They always relied heavily on state support and protection to accumulate, thus were unable to develop independently and stand together as a class. The heavy reliance of state support and subsidies and tax concessions has created endemic system of bribes and nepotism to enrich both bourgeoisies and civil servants. Moreover, having accumulated wealth through the nexus of corruption, many former civil servants and the military officials have set-up businesses directly or through their relatives. As Jalal notes, "The defence trust and foundations run by the army has eight manufacturing units, including sugar, fertilizers, cereals, liquid gas, metals and a gas field as well as transportation companies, schools, hospitals etc.". (Jalal, 1995: 143)

Long-term Structural Constraints

In Pakistan, agriculture is the largest part of the economy, employing 44.2% of the work force. A large gap exists between the potential and realized yield for almost all major crops. The country is the world's fourth largest producer of cotton but output will drop by about 15% in 2010 owing to Pakistan's severe flooding[24]. An estimated 80% of cotton fields in some areas have been

damaged. Industrial growth has slowed compared to recent years owing to a fall in demand for textiles and problems in that industry. The textile industry suffers from power shortages, reduced availability of cotton and lack of competitiveness[25]).

The country has failed to change the structure of industrial output and its export. Pakistan's export share in the GDP has been stagnant for the last 25 years. For example, textiles, leather, agricultural products etc. constitute about 80% of the total export, which are low technology and low value added products. This market is now declining, having failed to penetrate foreign markets, given its narrow and mostly agricultural based export items. The country's textile industries have lost their prominent position of the 1970s and currently hold about 2 % of the world market. It seems that the government has failed to take initiative of industrial upgrading, which could have played an important role in creating jobs in expanding export sectors.

The argument in support of devaluation is that it would make export cheaper in the international market and ultimately export would increase. The experience of successive devaluation shows that exports have increased in volume but the increase was small compared to the fall in value of the *Pakistani Rupee* as most of the country's export seems to be textiles, which faces quotas. An important point of the neo-liberal reforms is to extend the role of the market and reduce the role of the state in economic affairs based on the assumption that the market is always right. 'Getting price right' i.e. having prices as close as possible to what a free market would determine. Patnaik argues that (1994) "Getting prices right as a condition for becoming a successful exporter, and for achieving high rates of viable growth, is belied consistently by actual experience. Virtually every instance of noticeable export dynamism, whether it is Germany in the late 19th century, or Japan and South Korea in the post-war period, has been characterised not only not getting prices right in the neo-classical sense, but by having differential prices for the same commodity between the domestic and foreign markets. Indeed such differential prices are what precisely have helped the export drive: capitalists have made up through profitable domestic sales they have lost in foreign markets by keeping prices low for the sake of export expansion"[26]).

The recurrent balance of payment crisis, which was managed repeatedly by spending cuts on development, has prevented investment in the areas where the private sector has been unwilling to invest. In order to modernise and increase competitiveness of the economy, it is considered vital. Moreover, total neglect of heavy industries, which was briefly prioritised during the Zulfikar Ali Bhutto period, has undermined its ability to change the structure of production from low to high value production, as some south-east Asian economies e.g. Malaysia has done successfully more recently[27]).

The government was unable to mobilise resources. For example, the total tax revenue to GDP declined from about 12 % in 1999 to average 10 % of the GDP at present. While at the same time military spending has been higher than developmental expenditure for the last nearly three decades. Moreover, the military and debt repayment has taken away nearly 60 % of the total revenue over the last ten years.

With the increase in external imbalances, the government opted for IMF led Structural Adjustment Programmes in 1988, taking several measures to reduce budget deficits such as wage restraints, freezing employment in public sector and limiting discretionary grants to provinces. The budget was reduced from 8.5 % of the GDP in 1988 to 6.5 % in 1990. However, in 1991 a sharp fall in the public revenues[28]) resulted in an increase in fiscal deficits to 8.7 % of the GDP. The government spending on social services mainly on education and health, which was already lowest compared to other south Asian countries, declined further as a percentage of GDP from 3.4 % in 1988 to 2.8 in 1991. The literacy rate in Pakistan is one of the lowest in South Asia and is worse than in countries which have per capita GNP close to Pakistan's level. Total government spending on health and education measured as a percentage of GDP remained constant even declined slightly. The existence of a large proportion of illiterate people would simply mean a lower probability that the ruling elite could be displaced.

Since the late 1980s, the evolution of Pakistan's economy is closely linked with international financial institutions and strategic interests of western countries, especially the United States. As a result,

the economy has moved into dependent development, which appears to be an important reason for the on-going economic crisis and any attempt to build self-reliance is sidelined. The structural economic weaknesses are associated with the structure of production, items of exports and skills and education levels of the working people and the nature of the country's economic integration with the global economy[29]. As Tariq Ali argues that, "Throughout the 1990s, the IMF had scolded civilian governments for failing to keep their restructuring promises. Musharraf's regime, by contrast, won admiring praise from 1999 onward for sticking to IMF guidelines "despite the hardship imposed on the public by austerity measures". Improvement and desperation in the burgeoning city slums and the countryside – still home to 67.5 % of the population – were exacerbated further. Some 56 million Pakistanis, nearly 30 % of the population, now live below the poverty line; the number has increased by 15 million since Musharraf seized power"[30]

Conclusion

Capitalism has failed to remove poverty and inequality despite its long history of penetration in South Asia under colonial and neo-colonial regimes and in spite of being backed by the new technology and increased amounts of credits clearly illustrated by the experience of Pakistan. It is not simply a question of growth rates. As Pakistan's dependence on foreign loans increased, there was little effort by the government to broaden the industrial base to encourage diversification of its exports. At the same time, with the adoption of neo-liberal economic reforms imports rose, largely financed through the foreign borrowings. As a consequence, the balance of payments crisis has deepened. Though the growth rates picked up for a short period after 2000, it impaired the country's long-term capacity to mobilise domestic resources for long term investments and obstructed the achievement of sustainable and equitable development. The existence of high illiteracy rates and the neglect of social sectors have also undermined the overall productivity growth in country.

The failure to break the monopoly of landownership from the rural elites is the root cause in the continuing atrocities against vulnerable sections of rural inhabitants. Moreover, this proved to be a major constraint against the expansion of rural middle classes. Thus, the existence of large landowners did represent a hurdle to increasing agricultural output and income of the small farmers and tenants. As agricultural surplus remained with the small proportion of rural elites, this further narrowed the markets towards luxury goods rather than investments in capital goods sectors to improve the overall productivity of the manufacturing sectors and competitiveness. The rural rich are now much more connected with the urban rich through their investment diversification within the family, benefits from urbanisation of land and social interaction and in the current situation the old rural-urban divide does not have much relevance.

In recent years crony capitalism flourished, while local industries that were once the backbone of the economy were left to decline. Pakistan's export is based on primary commodities, with a heavy dependence on cotton and textile industry and neo-liberal economic reforms since 1988 and this did not alter the situation. Successive governments have neglected the industrial upgrading necessary for economic development, and have thus failed to diversify economic activities and build a successful manufacturing sector.

Notes

[1] For more discussion on ISI policies see Raul Prebisch (1961) "Joint Responsibilities for Latin American Progress", *Foreign Affairs*, Vol.39, issue, 4, New York.

[2] For more detail on the impact on neo-liberal economic policies in Central America see Kalim Siddiqui (1998) "The Export of Agricultural Commodities, Poverty and Ecological Crisis: A Case Study of Central American Countries", *Economic and Political Weekly*, Sept. 26, 1998, vol. xxxiii, No. 39, pages A128-A137

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[11] S. Akbar Zaidi (2005) *Issues in Pakistan's Economy*, second edition, Karachi: Oxford University Press

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[14] However, during the 1980s and 1990s the developing countries of sub-Saharan Africa and Latin America under enormous external pressure carried out 'neo-liberal' economic reforms. The result was a decline in living conditions for the majority of the population. During the post-reform period, the income and wealth of the rich increased, while the incomes poor witnessed dramatic fall. These countries were growing much faster in the pre-reform periods i.e. 1960s and 1970s when their economies were not liberalised.

[15] S. R. Khan (2007) "Pakistan's Economy Since 1999: Has There Been Any Real Progress?", *South Asian Journal*, Vol.8, No.2, pp.317-34.

[16] For a village level study in India see Kalim Siddiqui (1999) "New Technology and Process of Differentiation: Two Sugarcane Cultivating Villages in UP, India", *Economic and Political Weekly*, 25th December, 1999, No. 52, vol. xxxiv (pp A39-A53), Mumbai: India.

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[18] I mean to say with the implementation of land reforms and involvement of middle and poor farmers, the agricultural outputs and incomes of these rural groups would have increased. Thus, it would have created extra demands for domestic industrial products. For example, Germany in the late 19th century and South Korea and Taiwan in the late 20th century support this point.

[19] 'Green Revolution' technologies are another product of government intervention. This was carried out through subsidisation of inputs - new seeds, chemical fertilizers, credits and irrigation.

[20] I bid, A. Hussain (1988:178)

[21] Kalim Siddiqui (1995) "Role of the State in South-East Asia", *The Nation*, May 27th.

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[28] In Pakistan the public revenue declined as a percentage of GDP as custom duties revenue fell from 5.9 to 4.9 % of the GDP. For more detail see T. Anwar (1996).

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