

## CHAPTER 5

### SURVIVING ECONOMIC MELTDOWN AND PROMOTING SUSTAINABLE ECONOMIC DEVELOPMENT IN PAKISTAN

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This chapter was originally meant as a comment on Chapter 4 of this book by Shahid Javed Burki, "Pakistan's Economy: Its Performance, Present Situation, and Prospects." However, given the very detailed and comprehensive nature of Mr Burki's arguments, I find myself with few disagreements, if any at all. Mr Burki has laid down a substantive manifesto and policy document with which few economists would disagree. Consequently, my chapter, refers to Mr. Burki's as needed, but does not repeat any of his arguments, or the large amount of his data and facts with which I agree. My chapter builds on Mr Burki's thesis by raising issues that he did not discuss, although he has written about many of them quite extensively in the past. Both chapters should be seen as complementing each other rather than as responses or critiques and should be read in tandem. Where Mr. Burki's chapter provides ample economic data and analysis, my chapter enhances the debate by building on its economic base through the use of a political-economy perspective. While many of Mr. Burki's economic interventions are logical, appropriate, and timely, many will be confronted by vested and institutional interests that hamper any attempt to implement these urgently needed reforms that he proposes. Moreover, I argue that unless some key political issues, no matter how symbolic they may appear to be, are resolved, much of the substantive part

of the economic policy will remain unimplemented, and the economic meltdown will become far worse, perhaps even threatening the democratic transition currently underway in Pakistan.

### **The Structural Transformations of Pakistan's Economy and Social Structure.**

Mr. Burki presents a number of key structural factors that have affected Pakistan's economy over the last 60 years and demonstrates how these shifts are affecting economic and social structures. In this section, I add a number of other factors that have changed over time and are going to affect how Pakistan's economy, its social sector, and politics respond to such dynamic influences.

Perhaps the most important factor that has undergone substantial change and transformation, as Mr. Burki has also pointed out in his chapter, one that, sadly, many other Pakistani social scientists still do not comprehend, is that Pakistan is neither a so-called feudal, agricultural, rural, or even traditional society or economy. Only those social scientists who write their chapters on anecdotal evidence still talk of Pakistan as being feudal. Even a cursory examination of any kind of economic data suggests that this is not so. With the agricultural share of the gross domestic product (GDP) falling drastically from 26 percent in 2000 to 20 percent in 2007, agriculture has lost its predominance in the economy. The share of agricultural labor has also fallen from more than half of the total in 1990 to 43 percent today, and land tenure relationships and landholdings have changed markedly. In terms of social values and behavior, many analysts still refer to them as feudal, perhaps authoritarian, discriminatory,

or undemocratic. However, these adjectives describe the nature of social relations between people, values, and behavior in many highly developed countries as well. Therefore, if we are to understand social change and transformation, it is critical that we look beyond stereotypes, which will only limit our ability to observe and understand.

This is particularly so with regard to stereotypes such as Pakistan is an agrarian economy, and the view that Pakistan is largely rural. Raza Ali's extraordinary research on the 1998 Census<sup>1</sup> clearly showed that Pakistan was an urban country with perhaps 50-55 percent of the population living in settlements that by no stretch of the imagination could be called rural. A decade later, the forthcoming census will most certainly help us define the present social and economic relations of exchange and production and will reveal an even larger urban population. Moreover, with the increasing prevalence of communications technology of all sorts such as phones, electricity, roads, and other social services that are easily accessible, if not available, to so-called rural dwellers, the arbitrary binaries between urban and rural begin to fade. While much data can be shown to emphasize this point, the simple fact is that of the one million mobile phones added to the 81 million in service in Pakistan *every month*, the large majority are rural users, or those outside the geography that is administratively defined as urban. Pakistan is increasingly, if not now predominantly, urban, which engenders far more possibilities and opportunities to build on its economic and social structures. However, one must also recognize that there is the possibility that unless this urban transition is adequately managed, it could implode.

A particularly interesting consequence of this demographic change is how it affects Islamic political parties. Results from the most recent election—probably the fairest in Pakistan’s history—show that for the most part, electoral Islam has been reduced to being primarily a rural phenomenon, Islamic political parties won largely in rural areas—from Balochistan and the Northwest frontier Province (NWFP)—and from the least developed districts in these provinces.

These structural shifts in economic and consumption patterns have finally given rise to the emergence, substantial growth, and consolidation of a Pakistani middle class. The consumer boom that has taken place in Pakistan over the last decade or so would not have been possible without the existence of a sizeable middle class. The exact size of the middle class is difficult to estimate or measure, and one hopes that some approximation of its size will emerge through research. On account of easy availability of credit, an argument can be made that supports the claim that a consumer-based middle class is the true stimulus of the economy. For instance, the numbers of cars and of motorcycles doubled in Pakistan between the period 2001-07; mobile phones, which had a density of just 5 percent of the population in 2004. By 2008, that percentage skyrocketed to 51 percent of the Pakistani population. Moreover, despite growing regional and income disparities, per capita income has almost doubled since 2000.

While an economic middle class clearly exists, one can perhaps surmise that along with the substantial growth in the news and information media, this class has also become more aware of its rights and perhaps even responsibilities. Perhaps it was these new emergent and assertive groups who participated in, and gave

direction to, the political and civil society movements of 2007, of which Pakistan's media revolution played a key role. When the last elections were held in 2002, there was only one private TV channel in the country; today there are perhaps more than 30 private news and information channels broadcasting in all major languages. With constant information, analysis, and chatter about even miniscule political issues and developments, much of Pakistan's society has become involved and informed about what is happening throughout the country. While there are numerous rumors and justifications concerning a host of political stories, no one can any longer claim to be uninformed.

However, one must add a word of caution here. If the economic transformations from the agrarian, rural, and feudal structures have given rise to these new groups or the middle class, it is important to state that the political role of such classes need not be progressive, as is often incorrectly assumed and romanticized. The category of the middle class has no particular moral or ideological mooring. This group or class, can be as democratic and revolutionary as it can be fascist.

Another factor that is affecting society and its relations is the increasing visibility of women in public, and not merely in Parliament. While the largest number of women have been elected from the General seats in the last elections, evidence from most urban population centers suggests that women are more visible at higher tiers of education, in the media, and in the growing service sector. It is not just that young women predominate in liberal arts and humanity colleges, but rough estimates suggest, for example, that in the case of Karachi University and the Government College University, women dominate the campuses by a huge margin, perhaps four-to-

one. While many observers point out that while on university and college campuses more women are certainly more visible, they immediately add that most wear some version of the hijab, suggesting a form of growing conservatism. These visual descriptions perhaps confirm the view of some that Pakistani society has become far more socially conservative, yet obscure the liberating element experienced by many of these women who have escaped from their oppressive, traditional, patriarchal, and familial bonds, if only for a few hours in the day. Clearly, just the fact that women are being educated in growing numbers and that they are working is a revolutionary transformation, which has multiple and diverse social, demographic, and economic repercussions that many would consider highly progressive.

A dramatic shift that has occurred in the last 6 years, and this might be the only benefit from the consequences of September 11, 2001 (9/11), is the substantial change that has taken place in India-Pakistan relations. On the one hand, little seems to have changed, with an inhospitable visa regime still in place, with bureaucrats trained in older schools of thought still determining relations between the two countries. While on the other, an astonishing set of figures paint a completely different picture. For example, *India is today Pakistan's seventh largest trading partner as a source of imports*, and the first three in this list primarily supply oil to Pakistan. Pakistan imports more from India than it does from France, Germany, Canada, Switzerland, Iran, Turkey, or even Thailand! Overall, *India is Pakistan's ninth largest trading partner*. In 2000, the official trade between the two countries amounted to approximately \$235 million. Today, that number has grown to over \$1.4 billion. And this despite

challenging travel and visa restrictions for both traders and businessmen. One of the few positive policy actions taken by the new democratic government was the extended set of measures outlined in the Trade Policy for 2008-09 announced on July 18, 2008, in which trade with India was encouraged and a number of new concessions given. Early estimates suggest that if these opportunities are taken, trade with India will cross the \$3 billion mark, an astonishing turnaround from just 8 years ago. In this case, India may become Pakistan's third major nonoil trading partner. The consequences of such a positive development is that it could substantially change Pakistan's political economy.<sup>2</sup>

In terms of investment interests, a new phenomenon is the emergence of business interests from the United Arab Emirates (UAE) and other Gulf States. Awash with excessive amounts of revenue from the rise in oil prices, Arab sheikhs have been buying up key sectors in Pakistan. They have invested in real estate, banking, telecoms, information technology, and in other service sector tie-ups. While it is still too early to judge, there are indications that the UAE is getting involved in Pakistan's economy and politics to the extent that it can influence decisions. Both Nawaz Sharif and Asif Zardari have had very close ties—business and personal—with many of the rulers in the Emirates, and both have lived in Dubai for long periods of time. Moreover, the November 3, 2007, closure (following General Musharraf's Martial Law) of the private channel Geo News which was based in Dubai, UAE, suggests that numerous arms of the Pakistani state also have close connections with the Emirates' sheikhs. If UAE business interests grow, and given the overlapping business, personal, and

political relationships, one can be sure that financial capital from the Gulf will influence, or keenly follow, developments in Pakistan.

These are just a few of the many changes that are transforming Pakistani society, its economy, its politics, and its social relations of exchange and production. There are many reasons for these changes, from excess capital liquidity to globalization, to the media boom, to women's education, and similar trends. Some of these, such as trade with India, are reversible, but many suggest a more permanent state. There is a need for scholars to interpret and further explore such trends to examine and understand what, if anything, they mean for political transitions and transformations, and for economic development. One must understand that while there have been substantial and noticeable transformations, some institutions and some forms of politics have still not changed.

### **The Politics of Economics: The 2008-09 Budget.**

Mr. Burki gives a comprehensive assessment and critique of the 2008-09 federal budget announced on June 11, 2008, the first from the new government of Prime Minister Yousuf Raza Gilani. Mr. Burki ends his chapter by saying that while the new government had an opportunity and perhaps the responsibility to undertake a number of reforms, some of them urgently needed, the opportunity to do so was lost. One cannot agree more with Mr. Burki's assessment, and many economists have criticized the new government for not dealing with many of the critical issues that Mr. Burki has highlighted, ranging from exorbitant food prices, the rising price of oil, the cost of doing business, stabilizing the rupee, etc. In this section, I examine

how the politics of the new government affected its ability to act, and I argue that it first had to address some important political issues before economic management could become the primary focus.

If the economy is in as bad a shape since March 2009 as the two Finance Ministers have maintained, then the budget presented in Parliament in June 2008 failed to address issues to turn the economy around. In fact, by not addressing pressing problems at this juncture, the government has made things far worse for itself within a very short space of time. This lost opportunity to move forward on the economy is symptomatic of the way this government has functioned, a fact displayed in the two other critical arenas with regard to the president and the judiciary, where it was unable to act and to move forward with deliberate speed. Its failure to act clearly, forcefully, and timely on the economic front will, in all probability, only add to causes that will result in its own undoing.

Of course, the present government is in no way responsible for the numerous problems that afflict Pakistan's economy, yet the fact that it is in power assumes that it must take responsibility if it fails to address these problems. While we celebrate the return of the democratization process, albeit one that continues to be partial and interrupted, we also expect the government to fulfil its responsibilities.

As Mr. Burki's chapter indicates, the main economic indicators show that a deteriorating trend has been in process for some months now. The GDP growth rate, expected to be 5 percent, is still considerably higher than the average for the 1988-2003 period, but is lower than the trend seen over the last 5 years. While perhaps this slowing of the growth rate was to be expected, given adverse international commodity prices

and because previous growth was built on a weak foundation, expectations suggest that growth is going to be lower for some years to come. With the growing fiscal deficit which is approximately 7.8 percent of GDP, the highest in over a decade and that worsened as oil prices rose, all estimates for GDP growth seem to be overly optimistic. While these three key indicators need to be immediately addressed by the government, inflation is the single most important issue affecting all citizens, and this problem demands action from the current democratic and popular government.

With inflation at approximately 28 percent, the highest in the last 3 decades, any government would have had a major task dealing with causes that are not under its control. The global rise in food and oil prices are the main reasons why inflation is so high, although a number of poor decisions and an equal number of indecisions by the Shaukat Aziz government and the caretaker government have made things far worse. Moreover, the economic policies of the previous government were responsible for creating an artificial bubble, which resulted in a substantial deterioration in income distribution.

The Finance Ministry must realize the scale of the issues it must confront and quickly deal with them if it is to make a difference on the economic front and stop the economy from deteriorating further. However, the budget represents a substantial attempt to turn the economy around, and, although a couple of measures have been taken, they are insignificant compared to the nature and scale of the problems. The imposition of import duties on luxury goods was long overdue, and the attempt to provide an income support program for the poor is welcomed. Development expenditure has also been raised, and one can only hope that better

and effective targeted provision of all government expenditures will take place. However, a number of measures that were announced in the budget are troubling, and many are conspicuous by their absence.

The cut in subsidies might help to marginally lower the fiscal deficit, but will probably result in higher prices for oil, power, fertilizers, and food items for consumers, especially the poor. Similarly, an increase in the proportion of indirect taxes will also have a disproportionately higher impact on lower income earners. Neither of these two measures will help the poor and will further challenge their ability to survive under worsening economic conditions mostly related to rising inflation.

With a tax-to-GDP ratio of a mere 10 percent and with a fiscal deficit of 7.8 percent of GDP, one would expect the government to be considerably more imaginative on the revenue generation front. It is unforgivable that the government has allowed the exorbitant profits from the stock market to go untaxed for another 2 years, a concern also raised by Mr. Burki. There is no reason why profits from speculation should be untaxed under stable and normal circumstances, and under conditions where the economy is facing serious crises, such generosity is criminal.

The government should have gone out of its way to give inflation and food shortages its highest priority. It should have taken a short-term, immediate focus, which would have meant compromising on other issues at the moment, and a medium and longer-term economic agenda. One would have expected that the Peoples Party election manifesto, launched with much fanfare, would have had more substantive issues addressed with regard to the economy, some of which would have found expression in its first budget.

The democratically elected government in power today is struggling with an economic meltdown and economic crisis affecting its own constituency, but also a crisis of legitimacy, effectiveness, and political control. The disappointment one has with regard to the budget is just another indication of the democratically elected government's failure to act on a number of critical issues, both economic and political. Although a new president has been elected, it is quite clear that the new government in Pakistan seems vulnerable and weak. The war on Pakistan's borders seems to be getting out of hand, and differences with Pakistan's main ally, the United States, bode ill for any economic aid or rescue package that was envisioned. Economic and financial issues—such as the continuing deterioration of the rupee, the lack of foreign direct investment, the stock market unable to reflect any bullishness—are all linked to political stability in Pakistan.

### **Political Stability and Development.<sup>3</sup>**

The arguments made in the previous section need to be reemphasized; without political stability in Pakistan, economic development will not take place. Political stability is a prerequisite for economic development. There are three arenas where political stability needs to be managed and resolved. First, there is the need for the newly elected democratic government to deal with the regime, institutions, individuals, and power structures in place since 1999, and to establish its writ. Second, there is a need to resolve provincial, domestic, and local political issues, such as the National Finance Commission (NFC) Award mentioned by Mr. Burki, inter- and intraprovincial disputes and inequalities, and issues about devolution and local government. In

this category, there also is a need to develop a level of consensus between the different political parties vying for power in a more accommodative political framework. Finally, and equally importantly, there is a need to address and resolve issues related to Pakistan's neighbors, the war on terrorism, and in particular, the relationship between Pakistan's newly elected leaders and the U.S. administration. This last point is probably the most important and affects the other two, hence, it is to this I now turn.

It took the previous U.S. administration under President George W. Bush several months to come to accept the new reality in Pakistan after the 2008 elections and that its old and trusted ally since 2001 was not acceptable to the new government in Pakistan. For 6 months, it seems, the United States put pressure on Pakistan's new elected leaders to accept General (Retired) Pervez Musharraf as President of Pakistan, even after he and his political allies were resoundly defeated in the February 18, 2008, elections. The U.S. administration under President Bush, because of its own agenda and need in the region to fight and win the war on terrorism, had not been able to move beyond its political arrangements in Pakistan since 2001. By supporting General Musharraf after 9/11, almost unconditionally, the Bush administration was seen as the most powerful force propping up a military dictator in Pakistan. While political parties were equally to blame for not working for democracy and for being the General's collaborators and ensuring his longevity, it would be fair to say that General Musharraf continued to stay in power largely because of U.S. support for him. While the U.S. position was understandable, perhaps until the February 18 elections, the victory of democratic forces since then, and most importantly,

the rejection of Musharraf's policies by the Pakistani electorate, not only delayed the democratic transition, but was also the main reason for political instability in Pakistan.

In the period between early February to the end of June, U.S. State Department officials had more meetings with the two most important unelected Pakistani civilians—Asif Zardari and Nawaz Sharif—than they probably had with Pakistan's quasi-civilian leadership between 2002-07. These meetings were held not just in Pakistan, but apparently in London, United Kingdom, and the Gulf States as well, whenever the two Pakistani leaders were abroad. Moreover, more substantive quantitative research would also support the impression that the number of meetings the two leaders had with the U.S. Ambassador to Pakistan and their excessive public presence in the media has seldom been as high as it was in the last 5 months before, during, and after the February 18 elections. Public announcements by senior State Department officials seemed to suggest that these meetings and the pressure put on the Pakistani leadership was to garner continued support for the U.S. war on terrorism in the region and to ensure that President Musharraf was not removed.

Rather than support the process of further democratization and Pakistan's emerging democracy to a more sustainable level, the United States continued to support the one man who was unpopular and probably illegally in power. The needs and requirements of the previous Bush administration and the desires of the Pakistani people were seen to be at odds. Eventually, however, President Musharraf was replaced by the leader of the Pakistan Peoples Party (PPP), Asif Ali Zardari, who was sworn in as Pakistan's democratically

elected President. Only time will tell if President Zardari is able to gain the same trust and confidence of the new U.S. administration under President Barack Obama, as the man he replaced enjoyed with the Bush administration. With the United States playing such a crucial role in the region and particularly in Pakistan, and with democracy still emerging and establishing itself in the country, the relationship between Pakistan's elected leaders and the new U.S. administration under President Obama will be crucial. Moreover, it is also important for President Zardari and his new government to diversify and expand their diplomatic relationships with other regional powers, such as China and India, and to build alliances that look beyond too much reliance and dependence on the United States.

It is important to point out that U.S. intrusion in the region and on Pakistan's borders in military terms does not bode well for Pakistan's government and its democracy. Military attacks by U.S. drones on the border region with Afghanistan have already caused a great deal of resentment in Pakistan and help to increase anti-U.S. sentiment. Moreover, statements by Pakistani leaders, both civilian and military, seem to be at odds with those of U.S. military leaders, and clearly, differences of opinion, priority, and tactics have emerged. This relationship between the present U.S. administration and the new democratically elected leadership in Pakistan, and its relationship through the war on terror, may determine far more than just the future of democracy in Pakistan. Much more is at stake, and a misreading or mishandling of the situation will have multiple consequences, most of them ugly, on numerous actors and relationships in the region.

## Conclusions.

In agreement with Mr. Burki's suggestions of how Pakistan should exploit its many positive economic trends, my chapter has only added to the debate, suggesting that some key political and diplomatic issues need to be addressed quickly, alongside issues related to the economic meltdown affecting the economy and the Pakistani people. Political instability and factors related to the war on terror will hinder economic development. It is in the interest of the new U.S. administration under President Obama to support and strengthen the civilian democratic setup in Pakistan and to show a longer-term commitment to stability in the country. The longer any uncertainty lasts, the greater the economic meltdown. The blow-back of an economic crisis, along with a political one, will benefit neither the people of Pakistan and nor the U.S. administration in its war on terrorism in the region. Continuing instability and the unravelling of the Pakistani economy and the state are likely to have consequences far beyond Pakistan itself.

## ENDNOTES - CHAPTER 5

1. Raza Ali, "Underestimating Urbanisation?" in S. Akbar Zaidi, ed., *Continuity and Change: Socio-Political and Institutional Dynamics in Pakistan*, Karachi, Pakistan: City Press, 2003.

2. For domestic linkages and political-economy consequences of trade with India, see Chapter 20 of my *Issues in Pakistan's Economy*, Second Ed., Karachi, Pakistan: Oxford University Press, 2005; my *Pakistan's Economic and Social Development: The Domestic, Regional and Global Context*, New Delhi, India: Rupa and Co., 2004; and *South Asian Free Trade Area: Opportunities and Challenges*, Washington, DC: U.S. Agency for International Development

(USAID), 2006. I must also acknowledge that Mr Burki was one of the first Pakistani economists to talk and write publicly about improving Pakistan's economic relations with India.

3. See my unpublished background paper presented at the International Debate Education Association (IDEA)/Centre for Security and Defence Studies (CSDS) Conference entitled "Democracy, Development, Dictatorship and Globalization: The Complicated Histories of Pakistan," held in New Delhi, India, June 17-18, 2008.