

ECONOMIC SOLUTIONS TO PEOPLE'S PROBLEMS

"Economic Growth & Stabilization"
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Some positive indicators in the fields of macro management, budgetary deficit, debt retirement and increase in foreign exchange reserves do not reveal the true and total state of the economy. Some of these indicators are being used by the government to conceal the overall economic predicament of the people – the painful plight of the common man.

The economic policies pursued by the government have in fact been termed as 'foreign dictated' and a 'total failure'. They have led to serious crisis of confidence of foreign investors, the local investors and overseas Pakistanis. The much trumpeted economic development is mere illusion. GDP ratio remains low. (It had been one of the highest in the first four decades after independence). Domestic savings are in fact being discouraged. Major tax reforms have not been carried out. The Tax-GDP ratio also continues to be low whereas the share of indirect taxes in total taxes has gone up. Instead of improving the performance of Public Sector Enterprises the emphasis has all along been on their privatization at all cost.

Pakistan need enhanced foreign direct investment for achieving sustainable economic growth at an accelerated pace. The acts of terrorism are, however, spoiling the investment climate in the country. It is now the time to review and tone down the foreign policy particularly in respect of Pakistan's over-enthusiastic role in 'fight against terrorism'.

The budgetary deficit of Pakistan is basically a product of corruption. A transparent and effective accountability is an essential prerequisite to curb corruption. The national exchequer is suffering a loss of Rs. 600 billion per year due to financial corruption, tax evasion, inefficiency, mismanagement, poor performance and wasteful expenditure. Additional revenues of billions of rupees can, therefore, be generated by curbing

corruption, which could be utilized for betterment of the common man.

The new economic managers had full authority from the military government to frame economic policies obviously with the twin objectives of securing political and economic support of the western donors for the military government and getting new loans and credits from IFIs. Although both these objectives were duly achieved but as a result of these policies most of the macro economic targets for three years in a row including targets of GDP growth rate, the quantum of trade deficit, exports, tax revenue and budgetary deficit could not be achieved. The unemployment, inequalities between the rich and the poor and miseries of the common man continued to increase during this period. This trend is still continuing. The poverty rate and unemployment rate is now the highest in Pakistan's history.

Tax Revenue:

General Parvez Musharraf in his address to the nation on October 17, 1999 said " There is no way Pakistan can manage without tax survey" and that " if we manage to broaden the tax base, we would be able to reduce the taxes." These commitments have not been honoured and implemented in letter and spirit. The military government was in an ideal position to enforce land reforms but this opportunity has been lost obviously for obtaining political support of the feudals. Similarly the tax survey has already been abandoned without achieving its objectives just to seek support of those traders and industrialists who are engaged in large-scale tax evasions. The quantum of black money, therefore, continues to rise. The tax machinery remains corrupt and inefficient. Practically there is no accountability. The services sector has also not been adequately taxed. The federal Tax Ombudsman in his first report, covering the period from September 2000 to August 2004 observed "In Pakistan the poor are taxed, although they have no ability to pay and the rich enjoy exemption notwithstanding taxable activity". The report also says that the people of Pakistan, who are most heavily taxed in Asia, are being maltreated.

General Sales Tax and Surcharges

Due to low recovery of taxes, government has been increasing the prices of utilities and has also been enlarging the scope of GTS. A sum of Rs. 218.4 billion was recovered as GTS in financial year04 as against recovery of Rs. 38.9 billion in financial year99. The amount recovered as surcharge on petroleum and gas has also increased from Rs. 38.9 billion to 70.1 billion in financial year04. There is no justification for the recovery of these huge amounts from the common man due to the inability of the government to design an equitable taxation system and to check the tax evasion. The major beneficiaries of this state of affairs are few thousand rich and the powerful persons whereas the losers are 150 million people of Pakistan. The Governor SBP has conceded that if taxes are paid honestly, the rates of GTS could be reduced from 15 per cent to 5 per cent and all surcharges withdrawn. There could be no denying the fact that had only tax evasions been checked, all sectors of the economy equitably taxed and taxes recovered accordingly this could have been achieved much earlier. The question that needs to be answered is "Why 150 million people of Pakistan should bear the additional burden of about Rs. 215 billion or so each year due to the inability of the government to levy and recover due taxes at fair rates through an equitable taxation system?"

Privatization

The privatization of Public Sector Enterprises was not part of the agenda announced by the Chief Executive on October 17, 1999. It was on December 15 that under pressure of International Financial Institutions (IFIs) and on the advice of the country's economic managers, General Musharraf expressed his intention to go ahead with the sale of Public Sector Enterprises (PSEs). Privatization in Pakistan has been a failed experience. This process has been a big source of corruption in many cases. The privatization programme has not been transparent in the past and many PSEs were sold at throwaway prices allegedly even for wrongful personal gains. This amounted to criminal breach of trust and should have been dealt with accordingly. Many independent economists have termed privatization as "the single most important factor fuelling the growth of unemployment and asset distribution related inequalities.

General Musharraf in September 2004 disclosed that he was at one time advised by his Finance Minister (Shaukat Aziz) to

privatize Pakistan International Airways, Pakistan National Shipping Corporation and Pakistan Steel Mills, but these organizations are now showing profit.

Inflation

The fact is that during last seven years or so the low inflation was mainly due to lack of purchasing power of the common man and not because of increased flow of goods and services and enhancement in productivity. The military government practically inherited an inflation of 5.7 per cent. All indications are that at the end of financial year 2005 the inflation would be over 8 per cent. To tame inflation Pakistan must, among other policy measures, stimulate productivity, exercise money restraint, enhance revenues by broadening the tax base, design an equitable taxation system, curb corruption – both financial and intellectual- and recover the money looted from the national exchequer by attaching the assets created in the country out of such money. This practically is not being done in Pakistan. The steps for taming inflammation should be a part of the over-all economic policy, which in any case needs a complete change – altogether different from the existing economic policies.

Interest Rate Regime

The State Bank of Pakistan (PSB) had been persisting with the policy of lowering interest rates. The Governor SBP had some time back conceded that: "Interest rates were lowered by four percentage points, Despite this domestic investors remained shy, private sector demand for credit was insignificant and the overall pace of economic activity did not pick up." The lower interest rates, however, immensely helped the government in reducing the debt servicing liability on domestic debt thereby containing the budget deficit. Although this policy has brought hardship to millions of depositors of banks but the worst sufferers of this policy have been the pensioners, widows, handicapped and small savers who have been investing in National Saving Schemes. The policy of lowering interest rates has benefited mainly a few thousand borrowers at the expense of millions of depositors. of banks. It will

be recalled that on November 17, 1993 the then Governor SBP had termed the payment of negative real rate of return to depositors by banks as exploitative. He had also said that such a system provides a subsidy on lending to the rich, who usually are the main borrowers and that this process is injurious from welfare and growth point of view. He also advocated the need of paying a rate to depositors of banks minimum one per cent above the inflation rate.

Freezing of Foreign Currency Accounts

This may not be a mistake as it may have well been done to comply with the advice of IMF aimed at fulfilling the hidden agenda of the imperialist powers to conquer the economic frontiers of Pakistan. This is supported by the following facts:-

- (i) A former Finance Minister of Pakistan said that the then Governor SBP, being a former employee of IMF and the then Secretary Finance (who was reemployed by military establishment) had played a vital role in the finalization of the decision of freezing FCAs. It was also alleged by him that Pakistani officials having links with IFIs leaked confidential information to IMF.
- (ii) At least since 1993 SBP was then being dominantly managed by former IMF officials. The SBP vide F>E> Circular No. 17 Of 1998 directed the FCA holders to convert their FCAs in to Pak Rupees by a specified date, even before maturity of fixed deposits. It was this mysterious circular and not the mere decision of freezing FCAs that created serious crisis of confidence. The fact that this circular was subsequently withdrawn under public pressure did not repair the damage.

Public Sector Development Programme

The development expenditure as a percent of GDP was 7.3 percent (average annual) in 1980, while in the so-called lost decade of 1990 it was 4.4 percent. In 1999 it was 4.4 percent which further declined to 2.1 percent in 2001 but rose to 3-5 percent in FY2002 and to 4.1 percent in FY2003. The SBP Annual Report 2003-04, also noted that that development expenditures showed under utilization of Rs. 5.6 billion during the year.

External Debt, Foreign Investment and Overseas Pakistanis

Qa'id-e-Azam Muhammad Ali Jinnah in 1948 said: "Because of our addiction to living beyond our means and borrowing money we lost our sovereignty over this subcontinent". Unfortunately the focus of the economic policies of the successive governments has all along been on securing external loans and credits at all costs ignoring domestic and overseas Pakistanis is fraught with risks.

Notwithstanding the accelerated pace of privatization, lower interest rates, write-off of a portion of Pakistan's external debt and cash grants, the external debt rose by \$3.5 billion from #31.3 billion in June 1999 to #34.8 billion in December 2004. The domestic debt during this period also rose by Rs. 640.6 billion to Rs. 2033 billion.

During the last few years incentives have been given to foreign investors but due to series of acts of terrorism in the country, the investment climate continues to deteriorate. However the government should be careful in transferring the privatized industrial and financial institutions to foreign investors because they might emerge as a new East India Company.

Pakistani nationals living in Pakistan and abroad have deposits/liquid assets aggregating to more than triple the total quantum of country's external debt. It is estimated that over three million expatriate Pakistanis are earning about #15 billion per annum while their total savings are to the order of @15 billion per year. These Pakistanis remitted to their homeland a sum of over \$12 billion in post-9/11 era up to March 2005, while Pakistan received only about \$5.5 billion from IMF during last 16 years and that too after implementing dozens of their conditionalities. No steps worth mentioning have been taken either to win over the hearts of overseas Pakistanis or to design a meaningful strategy for attracting their investments and deposits. If only a part of their savings of overseas Pakistanis could be invested in Pakistan in profitable projects, Pakistan would not only receive accelerated economic growth but could also reduce its dependence on foreign loans and credits.

A massive (at least ten fold) increase in public investment is required to give real boost to the manufacturing sector and availing of technological advances needed to enable Pakistan to

compete in the world markets. In order to participate in the global knowledge economy we have to invest heavily in the capital goods and intermediate good industry. Public investment is also needed for increasing the learning capabilities of the leading manufacturing enterprises. Multinational investments (direct and portfolio) has rarely contributed to technological upgrading anywhere in the world. Neglect of the public sector is one of the major failures of economic policies pursued during the last five years.

Banking

The rates of return paid by banks to the depositors in the half year ended June 30, 2004 were in fact lowest in the 57 years history of Pakistan. The SBP Annual Report 1995-96 had observed: "The first prerequisite of an efficient banking system should be to provide a positive real rate of return to savers". The then Governor SBP said in 1993 that: "A banking system that gives a rate of return to small savers which is negative in real terms is an exploitative one as it taxes the savings of the poor who keep them in banks."

The list of defaulters promised to be published in November 1999 has not been published. The indicators are that the powerful lobby of chronic and willful defaulters has prevailed upon the military rulers and the economic managers to indefinitely postpone the publication of the list of defaulters. On the contrary the pace of re-scheduling and write-off has been accelerated. The pace of cash recovery of stuck-up advances during the term of military government has slowed down after December 1999

SOME CRITICAL ISSUES AND CHALLENGES

After a broad review of the economy as developed by the military regime an attempt is being made to briefly touch upon some upon some other critical issues and challenges.

Poverty, Unemployment and Human Development Index

Independent economists have come to the conclusion that "ours is an elitist economy, taking care of elite and not the common man.". Unemployment and poverty has continued to rise, income and

assets distribution have become more unequal – inter-personally and inter-regionally – and access to housing, health and education for the poor has tended to stagnate. There is the extremely unequal distribution of agricultural land in Pakistan. The government has not taken effective steps to curb corruption and tax evasion, and has followed rich-friendly economic policies due to which additional burden has been imposed on common man. Poverty has continued to increase.

The special focus should be on agriculture, small enterprises and cottage industries. Budgetary allocation for education and health should be significantly enhanced, allocated funds are [prudently utilized and it is ensured that 150 million people of Pakistan equitably share the fruits of economic growth.

Transparency and Crisis of Confidence

Failure in achieving the objective of economic revival, as laid down in the agenda announced by General Musharraf on October 17, 1999, is being camouflaged by distortion of facts and circulation of dubious statistics. This has led to a crisis of confidence.

Economic Policies – Home Grown or IFIs Dictated?

The conditionality imposed on Pakistan included imposing of GTS on retail trade and services, deregulation of petroleum imports, linkage of domestic POL prices to international prices and increase in consumer prices of gas and electricity etc. The economic managers of the military government have at numerous occasions been conceding that they had little choice but to accept these harsh and unpopular measures.

The government of Pakistan, prior to September 11 incident, was in a very weak position being under tremendous pressure from US for “restoration of democracy” – a weapon for compelling Pakistan to implement its tough economic and political agenda. After 9/11 the political agenda of US was also embraced. It thus again led to further dependence on IFIs and surrender to their conditional ties. The IMFs rarely allows sufficient time for broad consensus building or even widespread consultations with either parliament or civil society. It only dictates the conditions on the borrowing country.

Time has now come to have broad-based consultations for achieving sustainable economic growth at an accelerated pace and

for passing the fruits of this growth to the common man. This requires total re-designing and restructuring of the economic policies and the system. Thus a home-grown economic agenda developed in consultation with the home-grown professionals is the need of the hour.

Good Bye to IMF – Restoration of Political Sovereignty

The Governor SBP after 53 years of independence conceded "While I am independent of the government (interference) I am not independent of International Financial Institutions."

In this connection Dr. Javed Iqbal said in The News International on April; 15, 2002 "An autonomous State Bank is an instrument for depriving Pakistan of its economic sovereignty. The State Bank has become an imperialist agency disciplining Pakistani markets and governments and forcing them to serve America. For all intents and purposes the State Bank of Pakistan is now a minor regional sub-office of the US Federal Reserve System."

While saying goodbye to IMF, Pakistan has simultaneously enhanced reliance on World Bank and ADB. This means that the exit from IMF Programme may well simply be symbolic.

It is time to perceive that no country on the globe has achieved sustainable economic growth by enhancing reliance on others particularly the IFIs. Mr. Adolfo Perez Esquivel, the Noble Prize winner for peace said "The world's indebted nations, unfortunately known as "Third World" transfer capital to the rich nations by paying interest on their foreign liabilities. This generates a vicious, untenable cycle of poverty and social exclusion for the South. The northern countries, unfortunately known as "First World", used the hunger and poverty of southern nations to ensure a better life for themselves.

It is a sad part of the history that for the last 16 years i.e., between December 1988 and December 2004, Pakistan remained under IMF prescriptions.

U-Turn: A Word of Caution

The Governor SBP recently said that no economy could be on sound footing unless strong middle class is there. During the last few years due to persistent rise in the cost of petrol,, electricity, gas, daily consumption items and payment of negative real rates

of return to depositors by banks/DFIs, the middle class has practically been crushed.

Pakistan need enhanced foreign direct investment for accelerated economic growth, as the present level is too low. The British High Commissioner has said that corruption, attitude of bureaucracy and uncertainties due to security problems are the reasons, which are contributing to low foreign investment in Pakistan.

Pakistan lost a rare opportunity to get a significant portion of its external debt written-off by the bilateral creditors before committing to assume the role of front-line state. The developments after nine-eleven have provided only a breathing time to Pakistan to bring sustainable improvements in the economy and take the country to the path of self-reliance. This breathing time is practically being wasted which may have serious consequences for Pakistan in coming years.

It should be kept in view that many gains in post-nine-eleven era including rise in GDP growth rate, remittances, reserves and stability in the value of Rupee against US Dollar etc., may not be sustainable in coming years and that the economy has not been made strong enough to absorb any major external shock. The fact of the matter is that much trumpeted economic development is a mere illusion.

It is time to rethink the whole economic strategy and pursue a new path leading to the evolution of national consensus based on wide ranging and across the board consultations as regards future policy options in respect of foreign, political and economic issues. This is essential for safeguarding national interests, strengthening the economy and saving the nuclear programme.

REVIW OF THE ECONOMY – A SUMMING UP

- Most macro-economic targets for three years have not been achieved.
- Existing economic policy has pursued low wage-low productivity growth strategy. Virtually a de-skilling and de-technologizing industrial growth strategy is being pursued.
- Instead of checking tax evasion, curbing corruption and securing recovery of the looted money, the economic managers have (a) repeated enhanced rates of petrol,

electricity and gas (b) imposed GTS at exorbitant rates and (c) persistently lowered the rates of interest on NSS and other government securities. The miseries of the common man have thus been tremendously enhanced.

- Reduction in budget deficit has been secured not by significantly enhancing tax revenues as percentage of GDP but by further burdening the common man and securing concessions/grants from donors and IFIs on political considerations for which heavy price is being paid by the nation.
- Home-grown structural reforms for achieving sustainable economic growth, alleviation of poverty, reducing unemployment, improving human development index, removing distortions and improving the quality of governance have not been introduced in the real sense.
- Poverty and unemployment continue to rise. Economic stability (though unsustainable) is claimed to have been achieved by the economic managers due to their prudent economic policies. But the growth rate of the economy has been slowed down for a number of years and the welfare of the common man has been sacrificed as reflected from the rise in the percentage of persons living below the poverty line as also rise in the rate of unemployment
- Agricultural sector has not received due attention. Land reforms, declaring landless tenants / *haris* as owners of the land they cultivate, have not been introduced. The agricultural sector recorded a negative growth.
- No meaningful strategy has been developed to motivate people for the canalization of the remittances from expatriate Pakistanis into productive channels. The remittances of over \$12 billion have been received from expatriates since July 2001 up to March 2005. A significant portion of these remittances has gone into conspicuous consumption, the real estate sector and in stock market.
- Investment in National Savings Schemes has shown a negative growth in financial year 2004.
- The taxation system remains regressive and exploitative. This system discourages the honest tax payers and rewards the tax evaders.
- There is excessive reliance on external loans and credits while the domestic and overseas Pakistanis are not being effectively motivated to invest in their own country.

- National assets are being sold at an accelerated pace, even at throwaway prices, just to comply with the demand of the World Bank notwithstanding that it is not in the national interest to sell profit-earning public sector units and some other assets particularly to the foreigners.
- The economy has not been made strong enough to sustain any major external shock. In such an eventuality, there are apprehensions that foreign exchange reserves could evaporate instantly.
- Crisis of confidence between the government and common man has deepened
- The poverty rate, unemployment rate and the quantum of trade deficit is now the lowest in Pakistan's history.

RECOMMENDATIONS

It is important not only to design a new economic policy with national consensus but there is also an urgent need to formulate a new foreign policy so that the root cause of series of acts of terrorism in the country is removed. In the meantime revolutionary measures must be taken to significantly enhance government revenues without further burdening the common man and to bring significant and sustainable improvements in the economy.

The national exchequer is suffering a loss of about Rs. 600 billion per year due to financial corruption, tax evasion, inefficiency, mismanagement, wasteful expenditure and poor performance of some public sector enterprises. The losses due to intellectual corruption are, however, of much larger magnitude. To curb a significant portion of these losses is a must for enhancing government revenues which could be utilized for the betterment of the common man.

It needs to be perceived that the budget deficit of Pakistan is basically a product of corruption. To overcome the menace of budgetary deficit, we need to curb corruption rather than imposing taxes and surcharges on 150 million people of Pakistan. A transparent and effective accountability system is an essential pre-requisite for curbing corruption.

It is important to note that if only 50 percent of the losses of Rs. 600 billion per year are checked, the fiscal deficit would be converted into surplus and additional revenues of billion of rupees

generated. These additional revenues will enable the government (a) to refrain from taking domestic debt for consumption purposes and (b) to significantly enhance funds needed for human recourse development and for improving the quality of life of the common man.

The measures to enhance revenues and to bring improvement in the economy should include:

- (i) enhancing revenues by curbing corruption, checking tax evasion and attaching the assets available in the country created out of the plundered money.
- (ii) Utilizing funds judiciously and reducing unproductive expenditures by 30 percent.
- (iii) Designing a new strategy for attracting foreign investment mainly from overseas Pakistanis.
- (iv) Setting high standards of austerity and economy in expenses and stress on professionalism of the highest order in personal conduct and corporate behaviour at all levels.

Pakistan's aggregate debt to GDP ratio still remains among one of the highest in the world.

The following are some more suggestions for various other segments which may also be kept in view while formulating a new economic policy:

Taxes:

- (i) A survey of properties should be arranged initially in important cities. This will bring into limelight large number of properties, which have been acquired out of the income concealed from tax authorities. The properties acquired from the plundered money should be confiscated while the taxes as per law should be recovered on the tax-evaded income.
- (ii) Agricultural income above a reasonable limit should be subjected to income tax, in the real sense, like income from other sources.
- (iii) The number of income taxpayers must be enhanced to at least six million within a set time frame.
- (iv) The NTN numbers should invariably be required to be quoted in all transactions of sale / purchase of shares

- exceeding specified amount and immovable properties. The income on these transactions should be taxable
- (v) All *benami* transactions of whatsoever nature must be prohibited.
 - (vi) The rates of GTS should be a maximum of 5 percent from financial year 2006 and all surcharges should be withdrawn.
 - (vii) Equitable System of Taxation within the framework of Islamic economic system should be introduced.

Poverty, Unemployment and Human Development Index

- (i) The imprudent consumer scheme of banks should be reviewed. Cultivators / *haris* instead of launching a campaign for granting more and more loans for purchase of luxury items under this scheme (a) more financing should be provided by banks to landless *hari* for agricultural production. They should be declared owners of the land they cultivate. (b) the share for financing of small and medium size enterprises should be bifurcated and separate targets for financing of small enterprises should be given by SBP to banks and (c) more financing should be provided to housewives for cottage industries. The government should establish at least 100 technical education and vocational institutes for providing training to young men and women. This would also encourage private sector to establish such institutes.
- (ii) A target, to begin with Rs. 25 billion, should be given to banks for disbursing advances only to small enterprises for trade and industry under the guarantee of federal government during the next financial year.
- (iii) An allocation of 6 percent and 2 percent of GNP should be made for education and health respectively while development expenditures should not be less than 5.5 percent of the GDP. in financial year 2006.
- (iv) The rate of return on National Savings Schemes should at least be 3 percent more than the inflation.
- (v) All government officials should be required to get their children educated only in government schools.

- (vi) The chancellors, vice-chancellors and pro-vice chancellors should be appointed from amongst the senior educationists only.
- (vii) A meaningful strategy should be developed for realizing the millennium development goals in the social sector.

External Debt. Investment

- (i) A law must be framed prohibiting officials and economic managers representing Pakistan in negotiations with the IFIs from accepting jobs / assignments offered by these IFIs at least after five years of their retirement from service or relinquishing the charge.
- (ii) The government of Pakistan should propose to the powers in North America, Western Europe and the IFIs to freeze the accounts of corrupt persons of the developing countries and to directly utilize the misappropriated funds for the adjustment of external debt of the respective countries after completing legal and other formalities.
- (iii) Pakistan should appeal to the good conscious of western powers for not opening in future any ban account of a resident Pakistani without prior clearance from the government.
- (iv) The acts of terrorism including bomb blasts, and their wide coverage at local and international media, have been spoiling the investment climate in the country. It is now the time to review and tone down Pakistan's foreign policy particularly in respect of its over-active role in "fight against terrorism".
- (v) A meaningful strategy should be developed to motivate people for the utilization of the remittances received from overseas Pakistanis into productive channels.

Privatization

- (i) The privatization programme should be deferred.
- (ii) A commission should be appointed to, look into various aspects of privatization process during the last 14 years as also the performance of privatized units.
- (iii) Privatized unit acquired by fraud, misrepresentation and mal-practices should be taken back and all those involved

in the non-transparent process of privatization should be held accountable.

- (iv) Unrestricted participation of foreigners should not be allowed in the privatization process. The commission proposed above should also make recommendations in this respect.
- (v) Some of the Public Service Enterprises running into losses, instead of being placed on the privatization block, may be given on management contract.

Setting Standards

- (i) Members of Parliament, civil and military officers, economic managers and ban borrowers of Rs. 1-0 million and above should be required to give a declaration that they and their dependent family members are not maintaining a bank account abroad.
- (ii) All public figures, including members of the parliament and central, provincial and local government functionaries who got their advances re-scheduled / written off since 1985 should be required to repay the same with reasonable penalties wherever necessary.
- (iii) The president, prime minister, provincial governors and provincial chief ministers should not reside in official residences exceeding 1000 sq. yards.