Stosunki Międzynarodowe – International Relations ISSN 0209-0961
nr 2 (t. 51) 2015 doi: 10.7366/020909612201505

From Problems to Policy: Sustaining Growth and Public Services after the Global Financial Crisis in India and Pakistan[1]

Matthew McCartney
University of Oxford

Since the global financial crisis of 2008 commentators and activists have been worried about enduring economic recession and the impact of declining incomes on the welfare of the poorest, via both rising unemployment and reduced government spending on social services. This paper examines this debate within the context of contemporary India and Pakistan by reviewing two high-level policy papers; one for India that focuses on the problem of making growth more inclusive and one for Pakistan that focuses on raising the growth rate. The two sampled policy papers are "From poverty to empowerment: India's imperatives for jobs, growth and effective basic services" published by McKinsey Global Institute (MGI) in 2014 and Pakistan: Framework for Economic Growth' published by the Planning Commission (PC) of Pakistan in 2011. Both organisations in general and these two policy papers in particular are concerned with more that stimulating debate and discussion; they are not just academic pieces, rather they actively seek to shape policy. This paper finds that these two policy documents have little practical relevance for policy makers. The reports provide a bewildering list of policy recommendations with no guidance for policymakers on how to prioritise between them. The reports draw on the simple idea of urging policymakers to identify and emulate best practice but fail to draw on lessons and history to gauge what did and what didn't work elsewhere and why. The reports completely ignore issues of political economy; those constraints from the wider social structure on the choice of and the impact of policy. While the reports call for massive, complex and transformative government reforms, they make no reference to the weak and declining capacities of government in both India and Pakistan. In light of these problems this paper argues that policy guidance requires creative thinking structured around a deep understanding of the constraints (and opportunities) of political economy, state capacity, appropriate lessons and history. The careful discussion drawn from detailed context sensitive research by scholars such as Abhijit Banerjee and Ester Duflo provides a good starting point for thinking about policy.

Keywords: India, Pakistan, inclusive growth, economic growth, stagnation, political economy, government capacity, policy, service delivery

---

Matthew McCartney – Professor, South Asian Studies, School of Interdisciplinary Area Studies, University of Oxford.

[1] Grateful thanks to anonymous comments from the peer reviews, the paper was much improved as a result.

1. Introduction: a review of two policy papers

The 2008 Global Financial Crisis has generated two related streams of debate: the first relating to the means necessary to restore global economic growth and the second, to the impact on the poorest of declining incomes and reduced government spending on social services. This debate finds its parallel in contemporary India (less so in Pakistan) where the most newsworthy example has been that between Dreze and Sen who published 'An Uncertain Glory: India and its Contradictions' in 2013 and Bhagwati and Panagariya who published 'Why Growth Matters: How Economic Growth in India Reduced Poverty and the Lessons for Other Developing Countries' in the same year. The former opened their account of India with the claim, '*the growth process is so biased, making the country look more and more like islands of California in a sea of Sub-Saharan Africa*'[2] the latter replied with an equally vociferous claim that '*there is now irrefutable evidence that sustained growth alongside liberalising reforms has reduced poverty not just among the better off castes but across all broadly defined groups*'.[3] Within the context of this broad debate other scholars of India have focused on more specific questions. Firstly, studies focused on economic growth, examining recent declines in investment,[4] potential growth,[5] and the political economy of the growth slowdown[6] and others the impact of economic growth on human development, on education,[7] inequality,[8] nutrition,[9] and employment.[10]

This debate is closely linked with policy recommendations. Bhagwati and Panagariya argue that faster economic growth is the priority, '*the reforms that India has undertaken so far to accelerate growth and to additionally address the plight of the poor through the now feasible redistributive antipoverty programs have gone some way toward pulling the country out of a state of hopelessness that prevailed until 1980*';[11] while Dreze and Sen argue that there is a '*strong case for forceful public*

[2] J. Dreze and A. Sen, *An Uncertain Glory: India and Its Contradictions*, London: Allen Lane, 2013, pix.

[3] J. Bhagwati and A. Panagariya, *Why Growth Matters: How Economic Growth in India Reduced Poverty and the Lessons for Other Developing Countries*, New York: Public Affairs, 2013, p. 37.

[4] R. Anand and V. Tulin, 'Disentangling India's Investment Slowdown', *IMF Working Paper* WP/14/47, Washington, 2014.

[5] P. Mishra, 'Has India's Growth Story Withered?', *Economic and Political Weekly*, 13 April 2013, pp. 51–59.

[6] K. Sen and S. Kar, 'Boom and Bust? A Political Economy Reading of India's Growth Experience, 1993–2013', *IEG Working Paper* No. 342, New Delhi, 2014.

[7] G.G. Kingdon, 'The Progress of School Education in India', *Oxford Review of Economic Policy*, vol. 23 no. 2, 2007, pp. 168–195.

[8] R. Kumar, S. Kumar and A. Mitra, 'Social and Economic Inequalities: Contemporary Significance of Caste in India', *Economic and Political Weekly*, 12 December 2009, pp. 55–63.

[9] Panagariya, A, 'Does India Really Suffer from Worse Child Malnutrition that Sub-Saharan Africa?', *Economic and Political Weekly*, 4 May 2013, p. 98–111.

[10] J.J. Thomas, 'India's Labour Market during the 2000s: Surveying the Changes', *Economic and Political Weekly*, 22 December 2012, pp. 39–51.

[11] J. Bhagwati and A. Panagariya, op.cit., p. 96.

demand for much larger allocations to basic public services (such as school education, health care, nutritional support, and environmental protection), and for much more comprehensive programmes of economic equity and social security, as well as the development of the physical and social infrastructure'.[12]

The bulk of this debate has focused on the case study of India and less so the 200 million people of Pakistan; a comparative analysis of India and Pakistan is a key scholarly contribution of this paper. A second contribution is to the policy debate through a review of two high-level policy papers: one for India, which focuses on the problem of making growth more inclusive and one for Pakistan, which focuses on raising the growth rate.

The sampled policy papers are 'From Poverty to Empowerment: India's Imperatives for Jobs, Growth and Effective Basic Services' published by McKinsey Global Institute (MGI) in 2014 and 'Pakistan: Framework for Economic Growth' published by the Planning Commission (PC) of Pakistan in 2011. Both were written by large teams of consultants and scholars and both are products of an organisation with a specific remit, rationale and goal(s). MGI is the part of the McKinsey Company that does consultancy above the level of single firms, including in its remit '*financial markets, labour markets, natural resources, productivity, competitiveness and growth, technology and innovation and urbanisation*'. The PC is a high level organisation chaired by the Prime Minister of Pakistan, including federal ministers and other members, charged with preparing the National Plan of Pakistan, with '*monitoring and evaluating implementation of major development projects and programmes*' as well as '*evaluating the economic situation and coordinating economic policies*'.

The two policy papers are concerned with more than stimulating debate and discussion; they actively seek to shape policy. The front page of the MGI website states that the organisation aims '*to provide leaders in the commercial, public and social sectors with the facts and insights on which to base management and policy decisions*'. The PC paper variously argues that it '*presents a clear roadmap for developing vibrant markets*'.[13]

The official Indian poverty line is measured against a cut-off level of income that is so low that even those exiting 'official' poverty having a good chance of still being mired in deprivation. MGI introduces a new theoretical-empirical concept – the Empowerment Line – that acknowledges this problem and asks '*whether exiting poverty is enough to guarantee a decent life*'.[14] MGI finds that 56 per cent of India's population in 2011 lacked the means to achieve a minimum acceptable quality of life, which was three times the official poverty line. They show that the prevalence of poor

[12] J. Dreze and A. Sen, op.cit., p. 277

[13] Government of Pakistan, *Pakistan: Framework for Economic Growth*, Planning Commission, Islamabad, 2011, p. 13.

[14] McKinsey Global Institute, *From Poverty to Empowerment: India's Imperative for Jobs, Growth, and Effective Basic Services*, Mumbai, India, 2014, p. 33.

sanitation, malnutrition, and poor primary education is much higher than income poverty measures.[15] The alternative Empowerment Line is instead an expenditure based poverty measure that accounts for a minimally accepted standard of living[16] where each household is 'economically empowered' by having sufficient energy, food, housing, drinking water, sanitation, education, health care, and social security. Affordability MGI is clear is not enough, if for example teachers and doctors are absent from local schools and hospitals. The Empowerment Index is accordingly supplemented by an empirical examination using district level data of the physical availability of services. The MGI estimates that 56 per cent of India's population (680 million people) do not reach the minimum standards indicated by the Empowerment Line and that it would cost 4 per cent of GDP or USD 69 billion to bridge this gap,[17] which provides a measure of the '*economic challenge of alleviating poverty*'.[18]

The PC paper estimates that the labour force in Pakistan will grow by 3 per cent p.a. over the medium term and that the elasticity of employment with respect to GDP growth is around 0.5 so to '*absorb the addition to the labour force and cut into existing unemployment growth of 7-8% is needed*'. PC estimates that '*at the current level of investment and institutional functioning Pakistan potential GDP growth is 5-6% p.a.*'.[19] PC advocates two policy steps, the first to raise growth '*through a combination of measures and reforms for increasing productivity, improving economic governance and developing physical and regulatory space for entrepreneurial and innovative investments*'[20] and the second step is to sustain this growth for a number of years.

This paper evaluates the reports according to their own stated aims – to what extent are they useful as policy guides to achieving these goals. This paper uses the following criteria against which to make this evaluation: in section 2 whether the policy advice is linked to some clear practical criteria to help policymakers prioritise; in section 3 whether policy proposals are discussed in terms of useful lessons; in section 4 whether policy advice takes into consideration the political economy constraints and opportunities facing governments in India and Pakistan; and section 5 how the demands of reform match up against government capacity to implement. Section 6 concludes.

2. Prioritise reforms

In 1513 Machiavelli wrote to understand '*how a prince should govern his conduct towards his subjects*...[and argued]...*The fact is that a man who wants to act virtuously in every way necessarily comes to grief among so many who are not virtuous. Therefore*

15 Ibidem, p. 33.
16 Ibidem, p. 34.
17 Ibidem, p. 40.
18 Ibidem, p. 42.
19 Government of Pakistan, op.cit., p. 27.
20 Ibidem, p. 27.

if a prince wants to maintain his rule he must learn how not to be virtuous.'[21] This paper takes as its starting point Machiaevelli's suggestion that Princes cannot be virtuous to everyone and so need to prioritise. To evaluate these two policy reports this paper asks whether their suggestions for policy advice are linked to some clear practical criteria to help policymakers prioritise. Are the policy reforms, for example, prioritised towards reforms that tackle the most significant constraints on growth or poverty reduction, or that generate the least initial political opposition, or perhaps those that will help build a constituency of support for further reforms? The answer with regard to both reports is a resounding negative. This section shows that the reports compile a long list of economic and social problems from which they derive a long list of policy solutions and offer no principle of how to choose from among them.

The PC notes that Pakistan is riddled with rules and regulations that create obstructions and costs for doing business. In response the PC advocates increasing the '*return on investment through measures to improve the investment climate, to reduce the cost of doing business, and to dissolve the impediments to entrepreneurship*'.[22] Government the PC notes has expanded into agriculture, transport and construction and so crowded out the private sector, hence the PC advocates '*with good government devoted to thoughtful, limited and focused regulation, investment space is maximised for innovation and entrepreneurship*'.[23] The ability to '*enforce contracts quickly*' should be addressed by '*strengthening the legal and judicial framework, better training for lawyers and judges in commercial law, strengthening alternative dispute resolution processes and reducing corruption*'.[24] The PC lists for completion in one year or less:[25] a review of rent laws and removal of laws that unjustifiably favour the tenant to establish a regulatory body for the real estate market; the corporate restructuring of Pakistan railways; deregulation of railway fares; drafting a new aviation policy; professional management in energy supply; strengthening coordination between ministries and regulatory bodies; increasing literacy; expanding direct cash transfers to the poor; and improving teacher training. Between one and 3–5 years the PC aspires to improve the legal and judicial environment for domestic commerce, move towards unilateral trade liberalisation, phase out cross-subsidies in energy, establish more rational consumer and producer pricing, and achieve the full cost recovery of public services.

The twin goals for MGI are to raise growth to a sustained 8 per cent p.a. and to make growth more inclusive.[26] This, MGI argue, will require raising aggregate investment to 38 per cent of GDP over the next decade, creating 115 million new non-farm jobs,[27] to raise agricultural yields by 5.5 per cent p.a. (from 2.2 per cent p.a. over the last

[21] Machiavelli, *The Prince*, London: Penguin, 1975, p. 90.
[22] Government of Pakistan, op.cit., p. 37.
[23] Ibidem, p. 36.
[24] Ibidem, p. 92.
[25] Ibidem, pp. 136–144.
[26] McKinsey Global Institute, op.cit., p. 104.
[27] Ibidem, p. 105.

decade),[28] double public spending (from USD 118 billion to USD 226 billion in 2022) on eight key services,[29] improve the efficiency of basic service delivery such that the proportion of spending actually delivering better services rises from 50 to 75 per cent.[30] In practical policy terms MGI concludes these aims will require numerous reforms. There are six priorities to boost investment[31] to improve the execution and productivity of infrastructure by creating a National Infrastructure Delivery Unit[32] to overcome coordination problems between ministries, reducing administrative burdens by '*adopting international best practice*';[33] reduce delays in administration and customs, accelerating implementation of e-governance in relations with business,[34] removing tax and product market distortions, rationalising land markets, and making labour markets more flexible. Other policies include building 35 industrial townships by 2022 to create 1.7 million jobs,[35] investing in roads, hotels, museums, convention centres and theme parks to create 7.7 million new jobs in tourism by 2022,[36] and of course to avoid wasting resources by ensuring the reform process is a '*well considered approach*'.[37]

There is no clear strategy for policy reform in either paper but instead a bewildering and overwhelming list of desirable outcomes. Neither report pays any attention to that staple of economics textbooks – opportunity costs in the context of scarce resources. The capacity of bureaucrats to implement reforms and the political will to build the necessary coalitions in support are both scarce resources. Using such scarce resources to reform education, for example, will reduce their availability to reform state-owned enterprises. Trade liberalisation to promote greater openness is likewise not just about mandating lower tariffs on imports and correcting any overvaluation of the exchange rate. In practice trade liberalisation and trade integration have highly demanding legal and organisational requirements for the relevant bureaucracies. WTO obligations including customs valuation, food safety and animal and plant health measures, and enforcing intellectual property rights were estimated in the mid-1990s to cost a typical developing country USD 150 million.[38]

Once we have accepted the idea that we should prioritise reform, we face the daunting task of selecting those key policies. One method of doing just this was

[28] Ibidem, p. 106.
[29] Ibidem, p. 106.
[30] Ibidem, p. 117.
[31] Ibidem, pp. 129–146.
[32] Ibidem, p. 131.
[33] Ibidem, p. 132.
[34] Ibidem, p. 133.
[35] Ibidem, p. 143.
[36] Ibidem, p. 146.
[37] Ibidem, p. 43.
[38] D. Rodrik, Can Integration into the World Economy Substitute for a Development Strategy, Paper prepared for the World Bank EBGDE European Conference, 26–28 June, 2000.

developed by Hausman *et al.*[39] and is known as 'growth diagnostics'. This method seeks to derive policy priorities from an understanding of the binding constraints on economic activity in specific country case studies. The use of this method would have helped policy makers in Pakistan pinpoint investment as *the* key constraint on growth. Investment rates above 30 per cent of GDP are associated with rapid growth elsewhere in Asia while investment below 20 per cent of GDP characterised Pakistan throughout much of the 1990s and 2000s. After a decade of tax cuts on corporations high taxation was not appropriating those returns by the mid-2000s. Throughout the 1990s and 2000s Pakistan had most of the symptoms of low appropriability of returns –caused by poor property rights and contract enforcement. These can be easily observed from the various Global Competitiveness Reports produced by the World Economic Forum. Launching a small business in Pakistan was a long, expensive and cumbersome procedure. A poorly functioning legal system made banks reluctant to lend as they faced a significant default risk from borrowers. Those borrowers could then continue for years until being declared bankrupt by a corrupt and inefficient court system and be mandated to repay the debt; even then, once assets were scheduled for auction to repay debtors they would typically disappear. Lending for property in Pakistan was hindered by inefficient, unclear and frequently disputed rights to land and land titling. The proximate constraint on growth was low investment and its deeper causes lay in the lack of protection afforded to potential investors.

3. Lessons and history

A second principle is that recommendations for policy reform must be rooted in good lessons what policies have worked in similar countries or contexts. This section looks at lessons relating to both public services and economic growth.

3.1. Lessons: policy reform and public services

In the preface MGI claims: '*we highlight critical reforms that are precursors to achieving these outcomes and draw upon more than 350 case examples to present a host of innovations that can be used to deliver affordable basic services*'. In practice MGI simply exhorts the Government of India to replicate best practice from other case studies. Examples include calls to emulate the best practice of a South Korean government unit that builds infrastructure[40] or the new IT project of the German Federal government or deregulation of laws governing the setting up of a new business in Colombia.[41] There is no attempt to understand either how any of these best practices

[39] R. Hausmann, D.Rodrik and A.Velasco, '*Growth Diagnostics*', Kennedy School of Government, Harvard University, 2005.

[40] McKinsey Global Institute, op.cit., p. 131.

[41] Ibidem, p. 131.

were successful or whether the experience has any practical relevance for contemporary India.

The PC do the same for Pakistan, where the report for example presents Table 1, which demonstrates Pakistan's rank in 2009 on various indicators of doing business and reveals the magnitude of improvement were best practice in Pakistan to become the generalised norm. Again, there is no effort to understand how best practice was achieved nor whether such diffusion would be possible in a country as diverse as Pakistan.

Table 1. Improvement in Doing Business 2009

Indicators	Existing Rank	Improved Ranks with Pakistan's Best Practice
Starting a Business	63	59
Dealing with Construction Permits	105	46
Registering a Property	119	87
Enforcing Contracts	158	138
Paying taxes	143	107
Trading across Borders	78	73

Government of Pakistan, *Pakistan: Framework for Economic Growth*, Planning Commission, Islamabad, 2011, p. 47.

The PC calls for various measures relating to land reform to allow the more efficient use of land. These include centralising land title records in one agency, computerising land records and reforming tenancy laws and rental agreements to give protection to small and medium land owners from various urban land mafias.[42] There have been various large-scale efforts to computerise land records in Pakistan and India, none of which is referred to as a lesson in either report. These efforts demonstrate that it is much easier to register land than to reduce conflict over its ownership and transfer between owners. In the early 1990s the Indian Ministry of Rural Development launched a major national effort to register and computerise land records. As a result the system was simplified and the petty corruption traditionally involved in getting access to land records was reduced.[43] In the state of Karnataka 20 million land records held by 6.7 million farmers were computerised. After the registration effort a request for a copy of land records at a rural IT booth took no more than 30 minutes and cost a minimal fixed charge.[44] By contrast, there was no evidence the Karnataka project made land transfers any easier; even after registration the services of the village accountant were needed to inspect land sales, the process could take up to two years to complete and

[42] Government of Pakistan, op.cit.

[43] World Bank, *India: Land Policies for Growth and Poverty Reduction*, Washington, 2007.

[44] M. Ahuja and A.P. Singh, 'Evaluation of Computerisation of Land Records in Karnataka: A Study from Gulbarga District', *Economic and Political Weekly*, 7 January 2006, pp. 69–77.

involve substantial bribes. Conflicts over land ownership showed no decline.[45] In Pakistani Punjab the World Bank supported a five year effort from 2007 and spent USD 50 million to support the management of land records. Land disputes in Pakistan remain prevalent and may take years to resolve through the court system and there are now an estimated one million land cases pending nationwide.

The deep problem is not the registration of land, rather that efforts to transfer land to new owners in contemporary India and Pakistan tend to generate enormous political conflict. In India the law relating to land acquisition was revised in 2005 through the Special Economic Zone (SEZ) Act, which set a framework for state governments to acquire private land for industrial estates. By 2008, 404 SEZs had been approved covering 54,280 acres. Many SEZs then stalled in response to massive political protest. These included the Salim Group's petro-chemical SEZ in Nandigram, West Bengal, the Reliance Group Multi-Purpose SEZ near Mumbai, and the USD 12 billion POSCO steel SEZ in Orissa.[46] In response the central government put together the Policy on Resettlement and Rehabilitation in 2004, which was revised in 2007, after ongoing protests and finally emerged as the National Rehabilitation and Resettlement Policy. The act aimed to quantify the costs and benefits to society at large of land transfer and the impact on affected families and do so in a participatory and transparent manner to enable the payment of proper compensation.[47] In Pakistan land disputes are also prevalent throughout rural and urban areas. A well-studied example is that of the Okara district of Punjab from 2000. The dispute which mobilised up to 40,000 people at any one time was a reaction to new contracts that weakened tenancy rights, turned tenants into wage labourers and dispossessed some tenant families.[48] In Pakistan a National Resettlement Policy and Resettlement Ordinance was drafted in 2002 to provide a legal framework for land acquisition and compensation. The government did not adopt the draft policy. Neither PC nor MGI make any reference to these protests nor to the success or otherwise of the legislative response.

3.2. Lessons: policy reform and economic growth

Both PC and MGI aspire to increase long-term sustainable economic growth but both completely ignore a crucial aspect of economic growth in the contemporary world economy.

---

[45] N.C. Saxena, 'Updating Land Records: Is Computerisation Sufficient?', *Economic and Political Weekly*, 22 January 2005, pp. 313–321 and M. Ahuja and A.P. Singh, 'Evaluation of Computerisation of Land Records in Karnataka: A Study from Gulbarga District', *Economic and Political Weekly*, 7 January 2006, pp. 69–77.

[46] M. Levien, 'Special Economic Zones and Accumulation by Dispossession in India', *Journal of Agrarian Change*, vol. 11 no. 4, 2011, pp. 454–483.

[47] P. Sampat, 'Special Economic Zones in India', Economic and Political Weekly, 12 July, 2008, pp. 25–30.

[48] A.S. Akhtar 'The State as Landlord in Pakistani Punjab: Peasant Struggles on the Okara Military Farms', Journal of Peasant Studies, vol. 33 no. 3, 2006, pp. 479–501.

Long run growth averages are important but miss an important empirical regularity about growth in the modern world economy, its instability and volatility. Using data from 1960 Pritchett found many examples of sudden changes in the pattern of economic growth (or as economists label it 'structural breaks').[49] These included sudden accelerations (steep hills), accelerations followed by growth declines (mountains) and sudden collapses in growth (cliffs). In total Pritchett found more than 80 accelerations in growth between the 1950s and 1980s.[50] These accelerations are widespread; of 110 countries surveyed more than half experienced at least one acceleration, 20.9 per cent two accelerations, Asia had 21, Africa 18, Latin America 17 and the Middle East and North Africa 10.[51] Many of the growth accelerations in Africa have been forgotten; these included Algeria after 1975, Cameroon 1972, Egypt 1975, Guinea-Bissau 1971, Mauritius 1969, Uganda 1998, and Zimbabwe 1963.[52] Many of these growth episodes ran into a series of economic shocks – such as the rapid rise in oil prices in 1979, rise in world interest rates after 1981, sharp falls in world commodity prices and recession in many developed countries. [53] Of the many countries who have initiated a burst of rapid economic growth after 1960 only a small minority of them managed to sustain growth after the mid to late-1970s and most of those were in East Asia. [54]

Efforts to explain these many episodes of growth do not offer support for the vast array of policies listed by the PC and MGI (discussed in section 2). In practice growth accelerations are unpredictable and the vast majority are unrelated to standard determinants such as orthodox economic reform. Hausmann *et al.*[55] find that only 14.5 per cent of growth accelerations are associated with liberalisation and 85.5 per cent of growth accelerations are not preceded or accompanied by liberalisation. Various scholars have found that international trade tends to expand in countries undergoing growth accelerations[56] but this was not linked to greater trade liberalisation increasing the volume of imports and exports but rather to the greater value of exports among resource rich countries as commodity prices increased after 1995.

Evidence linking specific policies to growth accelerations is also mixed but does offer some clearer results. Exchange rate depreciations are typically found in the general

---

[49] L. Pritchett, 'Understanding Patterns of Economic Growth: Searching for Hills among Plateaus, Mountains, and Plains', *World Bank Economic Review*, vol. 14 no. 2, 2000, pp. 221–250.

[50] R. Hausmann, L. Pritchett and D. Rodrik, *Growth Accelerations*, JFK School of Government, Harvard University, 2004; R. Jong-a-Pin and J. De Haan, 'Political Regime Change, Economic Liberalization and Growth Accelerations', *Public Choice*, no. 146, 2011, pp. 93–115.

[51] R. Hausmann *et al.*, op.cit.

[52] R. Jong-a-Pin and J. De Haan, op.cit., pp. 98–100.

[53] Y. Akyuz and C.Gore, 'African Economic Development in a Comparative Perspective', *Cambridge Journal of Economics*, no. 25, 2001, pp. 265–288.

[54] D. Rodrik, 'Where Did All the Growth Go? External Shocks, Social Conflict, and Growth Collapses', *Journal of Economic Growth*, vol. 4 no. 4, 1999, pp. 385–412.

[55] R. Hausmann *et al.*, op.cit.

[56] Ibidem and B.F Jones and B.A. Olken, 'The Anatomy of Start-Stop Growth', *The Review of Economics and Statistics*, vol. 90 no. 3, 2008, pp. 582–587.

literature to have been associated with growth accelerations.[57] Neither PC nor MGI discuss exchange rate management in relation to reviving economic growth. Another common finding is that increased investment is commonly associated with growth episodes.[58] This is not surprising, an earlier generation of growth statistics found out that only investment had a robust link with economic growth across all developed and developing countries.[59] While PC and MGI do call for higher investment, section 2 in this paper showed that they have no clear policy agenda to achieve this goal.

The many growth accelerations uncovered by the empirical literature are not related to deep institutional change. There is thus no evidence to support the view as argued in the PC and MGI that an immediate institutional overhaul is necessary to revive economic growth. This is not surprising when considering the historical record. Now developed countries experienced, according to Chang,[60] a '*long and winding road*' of institutional development, which took 'decades'. It took, for example, a hundred years to establish the sort of modern professional bureaucracy in Britain that PC and MGI are urging Pakistan and India to create immediately. The historical record shows that 'good institutions' have followed rather than being a pre-condition for rapid economic growth. Khan[61] notes that indices of institutional quality based on the quality of the bureaucracy, rule of law, expropriation risk, and contract repudiation by governments in East Asian countries in the mid-1980s were only slightly better than many slow growth countries; they improved alongside not prior to rapid growth. Fast growing Indonesia, for example, scored the same as Burma or Ghana, and South Korea, Malaysia, and Thailand the same as Cote D'Ivoire. There is much broader evidence to show that now-developed countries also had poor institutions during their historical transition to rapid growth.[62]

A good place to start in thinking about devising policies to revive economic growth is the work of Rodrik[63] who has written extensively on '*growth strategies*'. Despite extensive stabilisation, liberalisation and privatisation growth rates in reform countries in the 1980s and 1990s (including Pakistan) were low in absolute terms and also relative to their own historical experience. Successful growth performers, notes

---

[57] R. Hausmann *et al.*, op.cit.

[58] Ibidem and B.F.Jones and B.A. Olken, op.cit.

[59] R. Levine and D. Renelt, 'A Sensitivity of Cross-Country Growth Regressions', *American Economic Review*, vol. 82 no. 4, 1992, pp. 942–963.

[60] H-J. Chang, '*Kicking Away the Ladder: Development Strategy in Historical Perspective*', Anthem Press, London, 2000.

[61] M.H. Khan, '*State Failure in Developing Countries and Strategies of Institutional Reform*', Paper for ABCDE Conference, Oslo, 24-26th June, 2002.

[62] H-J. Chang, op.cit.

[63] D. Rodrik, 'Development Strategies for the Next Century', prepared for presentation at the conference on 'Developing Economies in the 21st Century,' Institute for Developing Economies, Japan External Trade Organization, January 26-27, Chiba, Japan, 2000b. D. Rodrik, '*Growth Strategies*', John F.Kennedy School of Government, Harvard University, 2003. D. Rodrik, '*Rethinking Growth Policies in the Developing World*', Harvard University, October, 2004.

Rodrik, followed heterodox policies. In China, for example, small scale *state* (not private) owned enterprises (township and village enterprises, TVEs) were the most dynamic sector of the economy for the first twenty years of reform. In India rapid economic growth began in the early 1980s and did so in an environment of *increasing* trade protection. Others, such as South Korea and Taiwan experienced rapid economic growth with extensive use of trade and industrial policies. All successful growth stories have adhered to some basic principles; macroeconomic stability, avoiding high inflation or unsustainable debt, prudential regulation of the financial system, providing investors with effective protection of property rights and maintaining a degree of social cohesion and political stability. While the PC and MGI urge the rapid emulation of US and European models, in reality these principles of macroeconomic policy do not map onto unique policy agendas. There are multiple ways of achieving them. China, for example, protected property rights not through immediately reforming their legal system to duplicate those in developed countries (as advocated for Pakistan by PC) but by partnerships between entrepreneurs who ran business and local government officials who protected their property rights in return for agreed revenue payments to support local public spending. South Korea and Taiwan did not re-orientate their economies to exporting in the 1960s through liberalising imports but rather through subsidising exports. Chile, despite its commitment to the free market, retained its largest export industry (copper) under state ownership and retained controls on capital outflows throughout the 1990s. The work by Rodrik shows that policy, diversity, experimentation, and scaling up successful local experiments where feasible is desirable, not the search for 'best practice' and urging its immediate replication in Pakistan or India.

4. Political economy

There are three types of economic analysis. Positive Economics purports to show what will happen in the advent of a change in any economic policy? The PC claims that higher investment will raise the rate of economic growth in Pakistan. Normative Economics adds to this a value judgement: what policies or goals of economic change should be pursued? MGI argue that improving education for the poorest in India is a desirable policy goal. The third type is Political Economy, which seeks to answer the questions: '*Who owns what? Who does what? Who gets what? What do they do with it?*'[64] Of political economy both reports are strangely quiet. This section reviews examples from the PC showing that their suggested policy reforms in education flounder when situated in the political economy constraints of contemporary India or Pakistan.

---

[64] H. Bernstein, *Class Dynamics of Agrarian Change: Agrarian Change and Peasant Studies*, Nova Scotia: Fernwood Publishing, 2010.

4.1. Education

In education PC uses a range of evidence, such as Table 2 below, to show that Pakistan and India have made some progress in increasing average years of schooling over the 2000s but remain a long way behind other developing countries. In both countries the low average years of schooling are reflected in low enrolment rates, large drop-out rates from primary school, and a low transition from primary to secondary school. Alongside this the PC notes that the private education sector in Pakistan has expanded and now accounts for about 40 per cent[65] and in India over one-third of total enrolment.

Table 2. Average Years of Schooling

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

Government of Pakistan, *Pakistan: Framework for Economic Growth*, Planning Commission, Islamabad, 2011, p. 52

The PC supplies a long list of reasons to explain these poor educational output indicators in Pakistan. PC notes, for example, the overly centralised education system where distant ministries determine what is to be taught, post and transfer teachers, and manage budgets, the weak accountability of teachers and educational administrators to parents, the limited capacity for monitoring, and the lack of clarity regarding policies for private sector participation in education.[66] The problem with the PC is that there is absolutely no appreciation of how to move from problems to solutions.

There is little evidence to support the arguments in MGI and PC that more resources to education can provide a solution. Using data from 21 developing countries, Filmer[67] found a significant but only very small link between school availability and the probability of children being enrolled. Moreover there is a recent and disastrous case

[65] Government of Pakistan, op.cit., p. 52.

[66] Ibidem, p. 53.

[67] D. Filmer, 'If You Build It, Will They Come? School Availability and School Enrolment in 21 Poor Countries', *Journal of Development Studies*, vol. 43 no. 5, 2007, pp. 901–928.

study of failed efforts to reform education in Pakistan. The Social Action Programme (SAP) was launched in Pakistan by the World Bank in two phases, from 1993 to 1997 and then to 2002. The SAP was a massive (USD 8 billion) and sustained effort to tackle the same problems in education as noted by the PC and MGI. There was only a marginal improvement in education indicators between 1991 and 1996 and a decline thereafter until 1999. Not surprising. Pakistan has had ten National Education Policies since independence and none of them have succeeded in raising standards. PC ignores this record and instead only repeats a well-worn call for better education.

The sort of solutions structured around supplying more public services as advocated by PC and MGI may fail because policy makers do not consider the demand for those public services. Family planning services have often failed because they do not address the reasons why people want children, such as high rates of child mortality or the need for children to work in subsistence agriculture. Easterly argues that governments should stop pushing services onto the poor but instead empower the poor to demand health and education through their own actions.[68] Local residents cannot demand better services until they have sufficient information about the quality and availability of existing services. Neither PC not MGI makes any reference to this crucial problem. While education commissions and NGOs are well aware of poor education standards – the 2005 ASER study, for example, found that 67 per cent of Indian children in grades 3 to 5 cannot read a simple text – parents are often unaware. Parental literacy rates are likely to be a proxy measure for parental awareness of the quality of their children's education or health status. There is good empirical evidence to support this argument. In India teachers are more frequently absent in schools where the parental literacy rate was low.[69] In Pakistan at the household level the health knowledge of the father is a positive determinant of child immunisation and the health knowledge of the mother has a positive impact on child height.[70]

In India decentralised participation has been given central importance in primary education through a huge government effort to achieve universal primary education (Sarva Shiksha Abhiyan or SSA). As part of this effort Village Education Committees (VECs) were set up as the mechanism through which village level planning, implementation and monitoring of public funds was to be coordinated. Banerjee *et al*.[71] reports on a survey from 2005 in Uttar Pradesh of parents, teachers and members

---

68 W. Easterly, *The Elusive Quest for Growth: Economists' Adventures and Misadventures in the Tropics*, Cambridge: MIT Press, 2001.

69 N. Chaudhury, J. Hammer, M. Kremer, K. Muralidharan and F. Halsey-Rogers, 'Missing in Action: Teacher and Health Workers in Developing Countries', *Journal of Economic Perspectives*, vol. 20 no. 1, 2006, pp. 91–116.

70 M. Aslam and G.G. Kingdon, 'Parental Education and Child Health – Understanding the Pathways of Impact in Pakistan', *World Development*, vol. 40 no. 10, 2012, pp. 2014–2032.

71 A. Banerjee, R. Banerji, E. Duflo, R. Glennerster, D. Kenniston, S. Khemani and M. Shotland, 'Can Information Campaigns Raise Awareness and Local Participation in Primary Education?', *Economic and Political Weekly*, 14 April, 2007, pp. 1365–1372.

of VECs. A large fraction of children in the surveyed villages could not read simple texts or do basic arithmetic operations and were unable to write a simple sentence correctly. Parents, teachers, and VEC members were not aware of the magnitude of the problem and had given little consideration to the role of local committees or local participation in improving outcomes. 92 per cent of parents said they were not aware of the VEC Committee and only 2 per cent could name members of the VEC. Such information failures are prevalent even among the urban elite. One study directly observed doctors engaged in clinical practice in middle-class areas of Delhi, India. The study found that only 52 per cent of private-sector 'doctors' sampled held the required Bachelor of Medicine and Bachelor of Surgery (MBBS) degree. In observation tests only 30 per cent of public-sector doctors were able to ask the appropriate questions to gauge a medical condition from the symptoms declared by a patient, but less than 10 per cent then did so when observed interacting with actual patients. Private doctors who are directly accountable to the patient, make more effort but tend to over-prescribe medicines that are not effective to please the patient.[72] The example shows that again service users lack the information necessary to demand good services.

Providing information can help empower parents demand better education. A study in three Indian states tested whether school outcomes improved if the community had detailed information about the control it has over schools and what services parents were entitled to from schools.[73] A follow up two to four months after a community level information campaign found some positive impact on reading, writing and mathematics and on teacher attendance. Such interventions are not generally successful. In government health clinics in Rajasthan, India, a member of the community was paid to check once a week on unannounced days whether the nurse-midwife assigned to the health sub-centre was present or could be easily found in the village. During those four months the absence rate turned out to be nearly exactly the same in the programme and in comparison facilities (44 and 42 per cent respectively). Better information was not used by service users to try and improve public health services.[74]

A problem with the assumption that information empowers is that often people have long-established low expectations about public service provision so they prefer to exercise an exit option rather than invest voice in a seemingly hopeless effort to improve public services. In India and Pakistan many people have long ago opted out of public service provision and turned instead to the private sector. In India between 1993 and 2002 24.4 per cent of the increase in total primary school enrolment

[72] J. Das and J. Hammer, 'Money for Nothing: The dire straits of medical practise in Delhi, India', *Journal of Development Economics*, no. 83, 2007, pp. 1–36.

[73] P. Pandey, S. Goyal and V. Sundararman, *Community Participation in Public Schools: The Impact of Information Campaigns in Three Indian States*, *Policy Research Working Paper* No. 4776, Washington: World Bank, 2008.

[74] A. Banerjee and E. Duflo, 'Addressing Absence', *Journal of Economic Perspectives*, vol. 20, no. 1, 2006, pp. 117–132.

(95.7 per cent in urban areas) occurred in private schools.[75] In Delhi investment in private wells, cisterns, and rooftop storage tanks has enabled middle class households to get 24 hour water and so reduced motivation to campaign for improved public water supply.[76] In Pakistan by 2000, 35 per cent of children enrolled in education were in private schools, the ratio having nearly doubled over the previous decade.[77] Another deep problem for improving public services are the incentives faced by politicians. It is generally much easier for a politician to take credit for constructing and opening a new building than to take credit for 'health status' or 'teaching quality'. The former is visible and requires a single visit from a politician at an opening ceremony; the latter depends on the sustained efforts of many different actors. The resulting impact on the allocation of resources means that too little effort is expended on improving the functioning of public-service facilities, and too much on building facilities and employing education / health care workers.[78] In Pakistan over the 1990s there was a stagnation in educational outcome measures such as net primary enrolment despite a huge increase in the number of teachers employed and schools constructed.[79]

Focusing on incentives to service providers, rather than information to users is another potential policy reform; again one not mentioned by either PC or MGI. There is no evident shortage of health facilities in Rajasthan, India, where a 1.4 km walk separates the average village from the closest public health facility. A significant problem is the functioning of those facilities; absence rates for teachers in India are over 24 per cent and for health providers over 40 per cent. A randomised experiment was implemented in rural Udaipur, Rajasthan, India, that gave teachers a salary bonus related to the number of days they actually attended (verified by photos on specially designed cameras). The absence rate of teachers was cut by half in the treatment schools, which represented a one-third increase in the number of child-days of actual teaching. This study indicated that small incentives (around USD 6) could motivate a significant extra effort from teachers.[80] However, a similar effort to change incentives for nurses failed. Here time-clocks were used to monitor the attendance of nurses at small rural health clinics, also in Udaipur. The government used the attendance data with a schedule of fines and penalties (introduced for this programme) to determine the wages for any nurse. In the first six months the incentives led to dramatic improvement in attendance (doubling by some measures). After the first six months the local health

[75] G.G. Kingdon, op.cit., p. 186.

[76] L. Pritchett, op.cit.

[77] T. Andrabi and J. Das and A.I. Khwaja, 'A Dime a Day: The Possibilities and Limits of Private Schooling in Pakistan', *Comparative Education Review*, vol. 52, no.3, 2008, pp. 329–355.

[78] P. Keefer and S. Khemani, 'Why Do the Poor Receive Poor Services?', *Economic and Political Weekly*, 28 February 2004, pp. 935–943.

[79] Z. Hasnain, 'The Politics of Service Delivery in Pakistan: Political Parties and the Incentives for Patronage, 1988-1999', *The Pakistan Development Review*, vol. 47, no. 2, 2008, pp. 129–151.

[80] A. Banerjee and E. Duflo, op.cit.; and E. Duflo R. Hema and S.P. Ryan, 'Incentives Work: Getting Teachers to Come to School', *American Economic Review*, vol. 102, no. 4, 2012, pp. 1241–1278.

administration deliberately undermined the incentive system by allowing more exempt days for nurses and not sanctioning them for absences. After sixteen months there was no difference between the absence rates in treatment and comparison centres, both reaching around 60 per cent. These results show that public service providers can be responsive to incentives but also show that ensuring attendance among public sector employees is often a low priority for the local administration. Incentive systems can be quickly distorted where there is no countervailing pressure working through the political system to actually deliver better-functioning primary health care.[81]

Neither PC nor MGI acknowledge the enormous difficulties in generating any such countervailing pressure. India and Pakistan have highly centralised systems for recruiting teachers and health workers; it is to the central administration not to local parents that teachers are accountable. Recruitment, salaries and promotion are generally determined by educational qualifications and seniority, giving little scope for performance-based pay. Disciplinary action is rare and teachers and doctors are almost never fired. The main sanction is transfer to an undesirable location, though one study found that only in 18 of 3,000 cases was a teacher transferred for repeated absence.[82] In India there is substantial teacher representation in state-level parliaments and district level political leaders are often from the teaching community. Teachers have been able to use this political muscle to subvert policies aimed at improving standards. The state government in Uttar Pradesh in 1991, for example, deployed police in examination centres to prevent cheating and the pass rate in high schools dropped from 57 per cent in 1991 to 15 per cent in 1992. The measure provoked massive opposition from teachers, no countervailing pressure from parents, and was removed. The pass rate increased in subsequent years.[83] Teachers have consistently campaigned on issues related to pay and rarely for broader improvements in the schooling system. The overall result is that public spending on education has been increasingly captured by high pay. Wage costs as a proportion of total public expenditure on education increased from 74.7 per cent in 1960/61 to around 94 per cent by 2006/07.[84]

5. Government capacity

This section shows that while both PC and MGI have compiled long lists of complex policy reforms, neither report has paid any attention to the capacity of the government to implement those reforms.

---

[81] Banerjee, A.V E.Duflo and R.Glennerster, 'Putting a Band-Aid on a Corpse: Incentives for Nurses in the Indian Public Health Care System', *Journal of the European Economic Association*, vol. 6, no. 2–3, 2008, pp. 487–500.

[82] N. Chaudhury *et al*., op.cit.

[83] G.G. Kingdon and M. Muzammil, 'A Political Economy of Education in India: The Case of Uttar Pradesh', *Oxford Development Studies*, vol. 37, no. 2, 2009, p. 130.

[84] Ibidem, p. 140.

Both reports have big aspirations for the state to implement transformative policy changes. The MGI, for example, urges the Indian state (by 2022) to double investment in key public services and increase the share of public resources than reaches the poorest from 50 to 75 per cent.[85] The PC is full of much wider goals for the state: to promote investment, innovation, industrialisation and creativity. While urging massive and complex reforms onto the state, both reports acknowledge the weakness of the Indian and Pakistani states. The PC, for example, argues that in order to better oversee the process of reform the Planning Commission itself needs radical reform. The Planning Commission, they declare, should create mechanisms and consultation processes necessary for conception, analysis and implementation of national reforms, concentrate its planning functions to define/analyse directions for the whole nation, provide stronger guidance to the ministries and departments[86] and '*establish and maintain a system of monitoring and evaluation of the results…and…formulate processes to enhance accountability for results*'.[87]

There is a well-established body of literature that explores the criteria necessary for a state to be 'developmental', these criteria include: that leaders have a politically driven desire to promote growth, that state institutions are autonomous, the bureaucracy is competent and insulated from politics, that civil society is weak, and that the state enjoy widespread legitimacy, whether of the democratic variety or other.[88] There is a widespread agreement that neither India nor Pakistan has a state with the capacity to be developmental. Herring instead argues that '*India must be the most dramatic case of a failed developmental state*'[89] and that India's state was '*too democratic, soft and embedded, to govern the market*'[90]. It is not easy to measure state capacity but proxy indices relating to power supply and law enforcement as well as more general indices show that state capacity is actually declining in India and Pakistan. Losses in electrical power (from theft and non-payment) in India have been increasing over time. In 1971, such losses were about 9 per cent (lower than Brazil, Mexico, and Indonesia and about same as Malaysia and China) and by 2003 losses in India were 27 per cent higher than any of the other five. Since 1973 there has been a sharp decline in the disposal of murder cases in India from 35 per cent in 1973 to about 15 per cent in 2005.[91] The Global Competitiveness Reports compile indices, ranging from 1 to 7

---

[85] McKinsey Global Institute, op.cit., p. 57.

[86] Government of Pakistan, op.cit., p. 129.

[87] Ibidem, p. 129.

[88] A. Leftwich, 'Bringing Politics Back In: Towards a Model of the Developmental State', *Journal of Development Studies*, vol. 31 no. 3, 1995, pp. 400–427 and A. Leftwich, *States of Development: On the Primacy of Politics in Development*, Cambridge: Polity Press, 2000.

[89] R.J. Herring, 'Embedded Particularism: India's Failed Developmental State', in M.Woo-Cumings (ed.), *The Developmental State in Historical Perspective*, Ithaca: Cornell University Press, 1999, p. 1

[90] Ibidem, p. 3.

[91] A. Subramanian, 'The Evolution of Institutions in India and Its Relationship with Economic Growth', *Oxford Review of Economic Policy*, vol. 23 no. 2, 2007, pp. 196–220.

(7 being the best) to measure various aspects of governance. Table 3 compares the reports from 2006/07 and 2014/15, which reveals a widespread deterioration in state capacity, across the quality of institutions, judicial independence (Pakistan excepted), favouritism in government decision making, wastefulness in government spending and an improving if low measure of the reliability of the police.

Table 3. Declining State Capacity in India and Pakistan

Measure of Governance	2006/07	2014/15
Quality of Institutions		
India	4.5	3.8
Pakistan	3.5	3.2
Judicial Independence		
India	5.9	4.2
Pakistan	3.3	3.8
Favouritism shown in decisions of government officials		
India	3.6	3.4
Pakistan	3.1	2.6
Wastefulness of Government Spending		
India	3.6	3.5
Pakistan	3.5	2.6
Reliability of Police		
India	2.9	3.6
Pakistan	3.1	3.1

World Economic Forum (2006), *The Global Competitiveness Report, 2006-07*, Geneva, Switzerland and World Economic Forum (2014), *The Global Competitiveness Report, 2014-15*, Geneva, Switzerland.

As noted, the developmental state theorists argue a key criteria for a state to be developmental is a bureaucracy that is autonomous and so empowered to take a long run growth-promoting view of the economy that is not side-tracked by the populist and short-term demands of politicians. The reality is very different both in India and Pakistan. A key component of the weak state read which undermines the likelihood of any transformative policy reform is the decline of the civil service of which (in India), Appu says**,** the '*once superb administrative structure lies in ruins, reduced to a shambles*'.[92] The Indian Administrative Service (IAS) has long been subordinate to the short term demands of politicians. The reforms outlined in the PC and MGI are not compatible with a civil service who face the immense uncertainty of rapid and often arbitrary transfers. During the 1980s over 60 per cent of IAS officers in

[92] P.S. Appu, 'The All India Services: Decline, Debasement and Destruction', *Economic and Political Weekly*, 26 February 2005, p. 826.

Haryana, Andhra Pradesh and Rajasthan, India served in their post for less than one year. The power to transfer is a tool used by politicians in India and Pakistan to extract obedience and enable compliant civil servants to be placed in key positions, where they can demonstrate loyalty by focusing resources on schemes of benefit to supporters and potential supporters of the ruling party.[93] The resulting impact on public service delivery is best illustrated by the seminal work on canal irrigation in India by Wade.[94] Canal officials have great discretionary power in allocating resources for maintenance contracts and for rationing water between competing users at below market prices. By established convention Wade found that 8.5 per cent of each contract for annual maintenance work was returned to officers and clerical staff with a fixed allocation based on seniority. There were also savings from construction work where inflated charges for raw material and labour can mean that at least 25 per cent of what is meant to be built and sometimes as much as 50 per cent is returned to state officials resulting in sub-standard physical infrastructure. During times of water shortage officers run a kind of water market and '*the use of a rotational delivery can provide a pretext for highly discretionary, predatory behaviour by irrigation staff towards farmers*'.[95] Engineers may actually help create scarcity and uncertainty by diverting water and cutting off villages, which creates lucrative space for political intervention where the '*essential business of a state Minister is not to make policy. It is to modify the application of rules and regulations on a particularistic basis, in return for money and/or loyalty.*'[96] Any honest irrigation engineers refusing to participate in these institutionalised norms will find themselves quickly transferred.

This picture is broadly characteristic of the contemporary state in India and Pakistan. Pritchett[97] characterises India as a '*flailing state*'; the head (elite institutions at the national and sometimes state level), he argues, is functional and has even been rejuvenated in recent years. The Election Commission since the 1980s, for example, has increased its independence and presided over many difficult elections[98] but the head is no longer reliably connected to its own limbs. Of India Pritchett has noted that in the police, tax collection, education, health, power supply, and water supply there is rampant absenteeism, indifference, incompetence and corruption. The civil service from top to bottom has been personalised, politicised and corrupted.[99] The

---

[93] D. Banik, 'The Transfer Raj: Indian Civil Servants on the Move', *The European Journal of Development Research*, vol. 13, no. 1, 2001, pp. 106–134.

[94] R. Wade, 'The System of Administration and Political Corruption: Canal Irrigation in South India', *Journal of Development Studies*, vol. 18, no. 3, 1982, pp. 287–328 and R. Wade, 'The Market for Public Office: Why the Indian State is Not Better at Development', *World Development*, vol. 13, no. 4, 1985, pp. 467–497.

[95] R. Wade, 'The System of Administration and Political Corruption…', op.cit., p. 299.

[96] R. Wade, 'The Market for Public Office…', op.cit., p. 480.

[97] L. Pritchett, op.cit.

[98] A. Subramanian, 'The Evolution of Institutions in India…' op cit.

[99] L. Pritchett, op.cit., p. 4

daily practise of teachers, nurses, police officers and others deviates significantly from desirable professional norms and this has become institutionalised among the state and its employees.

Even Wade's view of well-institutionalised corruption may no longer reflect the realities of the local state in India and Pakistan. The declining capacity of the contemporary Indian and Pakistani state (as shown in Table 3) means that their monopoly powers to create an informal market around privatised state property under their own control is likewise declining. The boundaries between the state and civil society and between the state and markets are becoming increasingly blurred. Recall that theorists argue that for a state to be developmental civil society needs to be weak. In India and Pakistan an ever stronger civil society is increasingly encroaching into the state. Reform efforts need to recognise the reality of this starting point. Lieven writes that since independence there have been one civilian and three military efforts to radically change Pakistan. Presidents Ayub in (1958–1969) and Musharraf (1999–2008) both promoted a kind of secular nationalism, President Zia (1977–1988) a stricter form of Islam mixed with Pakistani nationalism and Prime Minister Bhutto (1971–1977) who combined populism and nationalism. They all failed, and '*every one of them found their regimes ingested by the elites they hoped to displace, and engaged in the same patronage politics as the regimes that they had overthrown. None was able to found a new mass party staffed by professional politicians and ideologically committed activists rather than local "feudals" and urban bosses and their followers*.'[100] And in India, calls for the radical privatisation of the state '*ignore the effective radical privatisation, informalisation and now mafianisation that south Asian states have been undergoing for much longer than the era of liberalisation of the 1990s*'.[101]

The PC documents the failures to extract or mobilise resources through taxation in Pakistan and while not referring directly to resource mobilisation, the MGI has compiled a large number of new spending priorities for the Indian government. A case study of tax collection in Pakistan illustrates how efforts at policy reform will be undermined by the weak and declining capacity of the state and its weakness in relation to local civil society. The PC makes a comprehensive list of the main technical-policy reasons for the low level of tax mobilisation. Pakistan, PC argues, has a narrow tax base, high enforcement costs and complex compliance procedures. Agricultural incomes, exports and workers remittances were not taxed so rising prices of commodities over the 2000s did not translate into tax revenue; likewise, income from rising exports and workers remittances were missed by taxation. Property owners find it easy to evade taxes as the official value of urban property are usually much less than actual market value.[102] The PC runs through a list of potential policies to mobilise more revenue:

---

[100] A. Lieven, op.cit., p. 23.

[101] B. Harriss-White, *India Working: Essays on Society and Economy*, Cambridge: Cambridge University Press, 2003, p. 101.

[102] Government of Pakistan, op.cit., p. 63.

improved compliance with tax laws, a broadening of the tax base, a more efficient tax administration and stronger auditing and enforcement procedures.[103] While the PC did note that recent reform efforts have been unsuccessful, the report made no attempt to understand or explain why. This call ignores the long and ignominious history of the IMF has had with tax reform in Pakistan. The following gives some examples of occasions on which the IMF has loaned money to Pakistan between 1995 and 2010 together with an extract from the IMF website of the tax related conditionality (a fuller list is contained in an appendix to this paper). After this list is the result – what happened to tax revenue?

1996 IMF Approves Extension and Augmentation of $231m Stand-By Credit to Pakistan

'*These policies will be supported by far reaching actions on the structural front, with emphasis on an improvement in the operations of Pakistan's major banks, broadening of the tax base, and rationalization of government expenditures.*'

2000 IMF Approves US$596 Million Stand-By Credit for Pakistan

'*The program envisages a reduction in the overall budget deficit in 2000/01 to 5.2 percent of GDP, from 6.4 percent in 1999/2000, with further consolidation over the medium term. The budget target is to be achieved through increased tax collections with a widening of the tax base, improved tax administration, and strict expenditure controls*'.

2003 IMF Executive Board Completes Sixth and Seventh Reviews of Pakistan's PRGF-Supported Program, Grants Waivers and Approves Disbursements Amounting to US$247.54 Million

'*In this regard, Pakistan's request for waivers for the non-observance of three structural performance criteria was approved by the Executive Board……In the fiscal area, this will include efforts to broaden the tax base through an expansion of the general sales tax to services, a reduction of tax exemptions, and an improvement in the capacity of local governments, which administer most poverty-related expenditures*'.

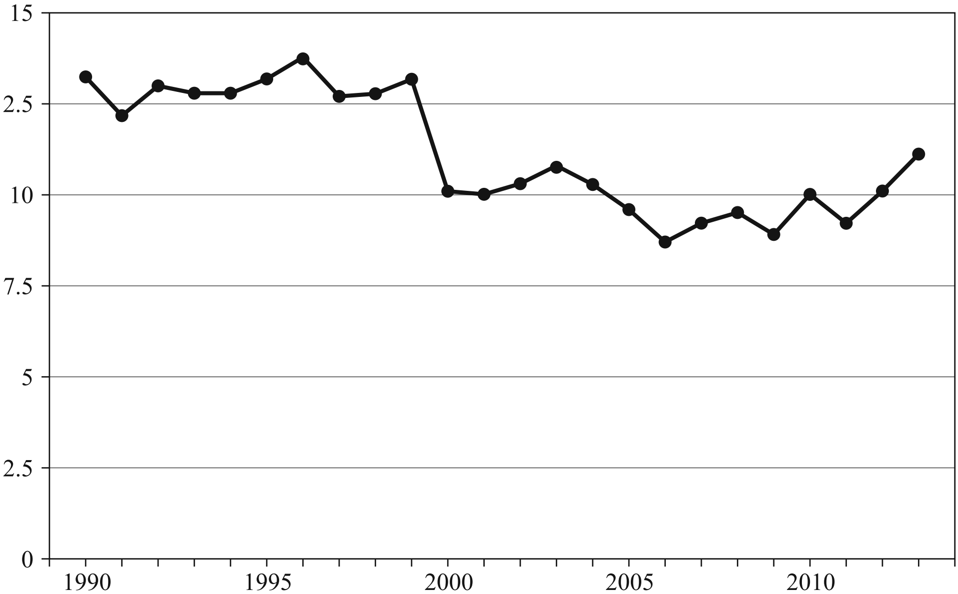
2010 IMF Completes Fourth Review Under Stand-By Arrangement for Pakistan and Approves US$1.13 billion Disbursement

'*Achieving the 2009/10 fiscal target will require strong efforts, including from the political leadership. Resolute continuation of tax collection efforts, tax administration reform, and expenditure restraint, together with timely disbursement of the pledged foreign financing will be critical to facilitate fiscal management*'.

---

103 Ibidem, pp. 62–63.

After this hugely expensive 15 years of cajoling, assisting, pressurising, enticing, persuading, inveigling, flattering, coaxing, and wheedling Pakistan to reform its tax system what happened? Nothing happened. Graph 1 shows that tax revenue remained stagnant or even declined between 1990 and 2013.



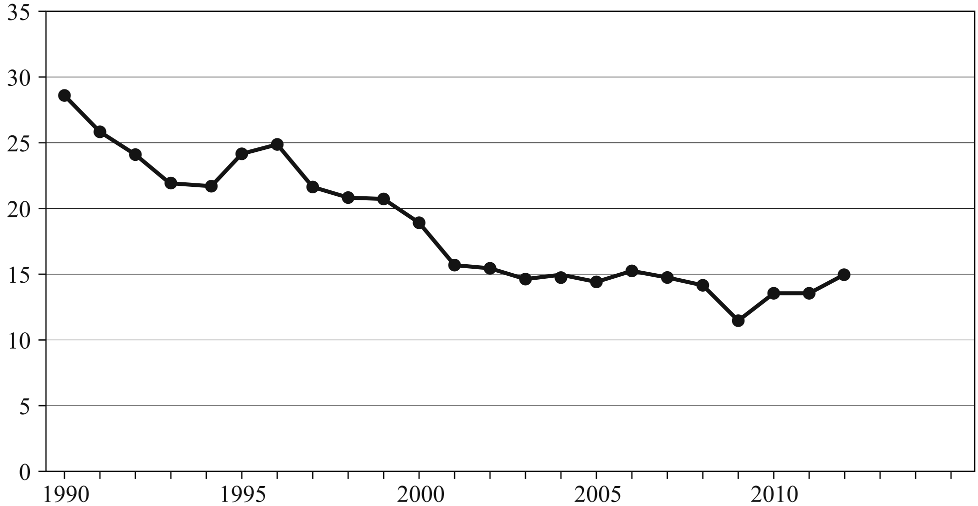
Graph 1. Tax Revenue in Pakistan (% of GDP) 1990–2013

World Development Indicators, World Bank, Washington, 2015.

The proximate reason for falling / stagnant tax revenue was trade liberalisation; this directly reduced government tax revenue. Graph 2 shows the sharply declining share of trade taxes in total revenue in Pakistan, which occurred alongside the fall in overall revenue in the late 1990s. This was not surprising; the structural features typical of a developing country (such as Pakistan) include the large dispersed, low-income subsistence sector in agriculture and small-scale informal sector in urban areas, the weakness of the tax administration, and the lack of good accounting systems which together make raising tax revenue from income and consumption taxes very difficult. Imports mainly enter Pakistan through a few ports, airports and highways so trade taxes are easier to collect than taxes on the millions of income earners or consumers or thousands of (small) businesses.[104] During the 1990s the phenomenon of trade liberalisation leading to declining overall revenue was widespread across developing countries.[105]

[104] M. McCartney, 'Competitiveness and Pakistan : A Dangerous, Distorting and Dead-End Obsession?', *Lahore Journal of Economics'* 17:SE, 2012, pp. 213–241.

[105] B. Khattry and J.M. Rao, 'Fiscal Faux Pas?: An Analysis of the Revenue Implications of Trade Liberalisation', *World Development*, vol. 30, no.8, 2002, pp. 1431–1444 and B. Khattry, 'Trade Liberalisation



Graph 2. Taxes on International Trade, Pakistan (% of revenue)
World Development Indicators, World Bank, Washington, 2015.

The deeper question seeks to explain why the IMF efforts to promote policy reform over 15 years failed to overcome these constraints on revenue. The answer, as this section has made clear, is that state capacity is declining and the state has become increasingly subordinate to the demands of civil society. The relationship between state and society in Pakistan is one of patronage relations between politicians and supporters or dependents, '*people gain access to patronage by using their position within a kinship network to mobilise support for a politician who then repays them in various ways in office, or by using kinship links to some policeman or official to obtain favours for relatives or allies*'.[106] The process can be likened, argues Leivin,[107] to state fiscal resources being '*nibbled by a plague of mice*'. The state fails to provide public services such as water, education and power because it is too weak to raise tax revenue and to control patronage relations between state officials and civil society.

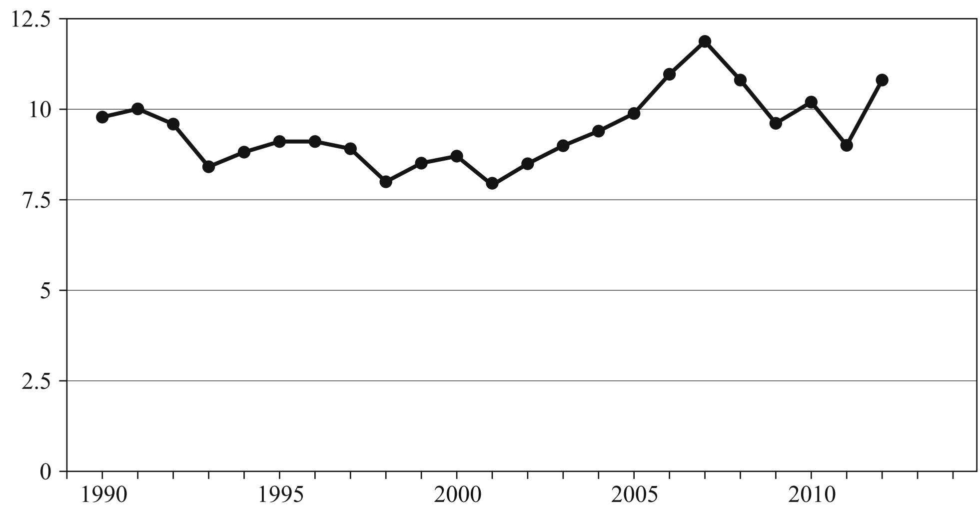
A good example is the case of property taxation in Pakistan which raises no more than 0.03 per cent of GDP. To boost property tax revenue reform proposals (echoing the PC and MGI) have called for more regular and reliable updating of property valuations, a shift to electronic billing and payment, more discipline among better trained staff and simplifying the valuation-taxation schedule. In principal taxes can and should be levied on objective, quantifiable factors such as income, business turnover,

and the Fiscal Squeeze: Implications for Public Investment', *Development and Change*, vol. 34, no. 3, 2003, pp. 401–424.

[106] A. Leivin, op.cit., p. 213

[107] Ibidem.

size of property, value of assets, import volume, or profit levels. In 2012 fieldwork in Karachi studying property taxation Piracha and Moore[108] found that in practice taxable criteria are based on physical (rather than accounts-based) verification and subject to conflicting interpretation which creates opportunities for collusion between the tax collector and the tax payer. For example, whether a property is classified as rented or owner occupied, or residential or commercial makes a significant difference to assessments for taxation. Piracha and Moore found that informal earnings from tax collection were substantial and were derived from the enormous discretion given to field staff in evaluating tax assessments. There is a well-institutionalised procedure for sharing these earnings among the field staff that collect them and the more senior officers. Other than transfers there is no disciplinary action initiated among departmental staff. In practice it would be near impossible to enforce discipline and performance targets on field staff because the ground level knowledge of field staff means that they monopolise the relevant information on the building of new property and usage of existing property. The regular rotation and transfer of senior level offices and the potential for politicians to manipulate this process makes any long term efforts at building knowledge or raising collections difficult. The incentives of tax collection staff and allocation of information make any of the standard reform measures unlikely to be of success in boosting revenues.



Graph 3. Tax Revenue in India (% of GDP) 1990-2013

World Development Indicators, World Bank, Washington, 2015.

[108] M. Piracha and M. Moore, *Understanding Low-Level State Capacity: Property Tax Collection in Pakistan*, *International Centre for Tax and Development Working Paper* No. 33, IDS, Sussex, 2015.

Graph 3 below shows a very similar pattern of long term stagnation in tax yields in India. Apart from a brief surge during the early part of the economic boom after 2003 tax revenues have remained stuck at below 10 per cent of GDP. A recent IMF working paper[109] repeats for India those long-standing failed intervention efforts in Pakistan. The paper notes these long-standing failures to raise revenue, repeats the call to remove tax exemptions, improve tax compliance and widen the tax base and yet again makes no mention of the underlying political economy constraints on tax mobilisation.

Conclusion

Returning to the debate about growth and its inclusivity with which we opened this paper. Bhagwati and Panagariya were correct in arguing that growth matters. Where PC failed in turning this observation into practical policy was not distinguishing between starting and sustaining growth. Starting growth is relatively easy, section 3.2 showed that a large number of developing countries have experienced growth surges during the last sixty years. This records show that initiating growth does not require the vast array of policy reforms exhaustively catalogued by the PC. The enduring problem has been rather in sustaining growth, and on this the PC had much less to say. At the heart of sustained growth is an investment strategy; section 2 showed that investment is too low in Pakistan and this is related to weak institutions. Unfortunately, section 3.2 showed that rapid institutional change is unlikely in a developing country such as Pakistan which, as demonstrated in section 5, has only weak existing state capacity. The trick is to find, as Rodrik discussed, a way of protecting the property rights of investors that is compatible with the underlying political economy and state capacity. Rodrik discussed several very country-specific heterodox examples. Such creative thinking about appropriate growth strategies requires more than calling for better education or copying Korea. A good start here could be Ahmed and colleagues who examine the paradox of rapid export growth and weak governance in contemporary Bangladesh.[110]

Dreze and Sen were also correct in showing how all too often the benefits of economic growth are harvested almost entirely by the already successful and prosperous. How to leverage the benefits of growth towards the poor and marginalised requires more than exhorting policy makers to magnanimously distribute public services as a form of largesse. There are good examples of interventions (teachers in Rajasthan) that dramatically improved service delivery. But even success cannot be necessarily then scaled up as the entrenched political influence of teachers in Uttar Pradesh showed.

---

[109] R. Mohan and M. Kapur, 'Pressing the Indian Growth Accelerator: Policy Imperatives', *IMF Working Paper* WP/15/53, 2015, pp.20–28.

[110] A.F. Ahmed, A. Greenleaf and A. Sacks, 'The Paradox of Export Growth in Areas of Weak Governance: The Case of the Ready Made Garment Sector in Bangladesh', *World Development*, vol. 56, 2014, pp. 258–271.

Again, creative thinking is required, structured around a deep understanding of the constraints (and opportunities) of political economy, state capacity, appropriate lessons and history. The careful discussion drawn from detailed context sensitive research by Banerjee and Duflo is a good starting point here.[111]

This paper has analysed two policy papers that according to their own remit seek to influence policymaking in India and Pakistan. They are rooted in a contemporary global economy concerned with the twin dilemmas of slow economic growth and intensive pressures on public services; unfortunately that is where any practical use of these documents ends. The reports provide a bewildering list of policy recommendations with no guidance for policymakers on how to prioritise between them. The reports draw on the simple idea of urging policymakers to identify and emulate best practice but fail to draw on lessons and history to gauge what did and what didn't work elsewhere and why. The reports completely ignore issues of political economy; those constraints from the wider social structure on the choice of and the impact of policy. While the reports call for massive, complex and transformative government reforms, they make no reference to the weak and declining capacities of government in both India and Pakistan. In view of the tremendous effort by so many highly qualified people that went into researching and writing these reports perhaps the last words are best left to that noted social commentator Groucho Marx:

'*Politics is the art of looking for trouble, finding it everywhere, diagnosing it incorrectly and applying the wrong remedies.*'

Appendix: IMF Programmes and Tax Reform in Pakistan, 1995–2010

1995 IMF Approves $596m Stand-by Credit for Pakistan

'*the program is designed to cut the budget deficit in relation to GDP through a combination of revenue and expenditure measures*'.

1996 IMF Approves Extension and Augmentation of $231m Stand-By Credit to Pakistan

'*These policies will be supported by far reaching actions on the structural front, with emphasis on an improvement in the operations of Pakistan's major banks, broadening of the tax base, and rationalization of government expenditures.*'

1997 IMF Approves Combined $1,558m ESAF/EFF Financing for Pakistan

'*In the public sector, the domestic tax base will be broadened; tax administration strengthened; government expenditure shifted towards the social services and human capital formation; and key public enterprises restructured*'.

[111] A.V. Banerjee and E. Duflo, '*Poor Economics: Rethinking poverty and the ways to end it*', Random House, New Delhi, 2011.

1999 IMF Approves $575m Second Annual ESAF Arrangement
'*The budget deficit is targeted to decline from 5.5 percent of GDP in 1997/98 to 4.3 percent of GDP in 1998/99, and to 3.3 percent in 1999/2000. To achieve this target, the government has already taken or intends to take several fiscal measures: an increase in the GST rate to 15 percent from 12.5 percent...*'

2000 IMF Approves US$596 Million Stand-By Credit for Pakistan
'*The program envisages a reduction in the overall budget deficit in 2000/01 to 5.2 percent of GDP, from 6.4 percent in 1999/2000, with further consolidation over the medium term. The budget target is to be achieved through increased tax collections with a widening of the tax base, improved tax administration, and strict expenditure controls*'.

2000 IMF Approves Release of US$133 Million Credit to Pakistan
'*Another challenge will be to boost revenue collections, a key pre-condition for containing the fiscal deficit while increasing social and pro-poor spending. This will require resolute action to broaden the tax base and strengthen tax administration. The extension of the sales tax coverage, and steadfast implementation by the Central Board of Revenue of the recently adopted short-term action plan to improve tax administration, will be critical*'.

2001 IMF Completes Last Review Under Pakistan's Stand-By Arrangement, Approves US$135 Million Disbursement
'*At the same time, the broadening of the tax base and a fundamental reform of tax administration are urgently needed*'.

2001 IMF Executive Board Approves US$1.3 Billion PRGF Credit to Pakistan
'*The strategy centers on sustained fiscal adjustment supported by a major reform of tax administration and a widening of the tax net, while increasing public spending for poverty alleviation*'.

2002 IMF Completes First Review of Pakistan's PRGF Supported Program, Approves US$107 Million Disbursement
'*the Executive Board approved two waivers for the non-observance of performance criteria on tax revenue and credit to public enterprises, and modification of the tax revenue performance criterion for end-March 2002 and of one structural performance criterion on tax issues......On the fiscal side, a significant improvement in tax revenue remains a key challenge. The recent tax measures taken by the authorities are welcome, but looking ahead, a significant improvement in the fiscal position will be needed to ensure debt sustainability, while raising allocations for basic social services. This will require the further reduction of tax exemptions, subsidies, and unproductive*

expenditure, and improved tax administration, in particular through a vigorous reform of the Central Board of Revenue'.

2002 IMF Completes Second Review of Pakistan's PRGF-Supported Program, Approves US$114 Million Disbursement
'*This will, however, require strong determination in enforcing tax collection, the continued timely implementation of reforms to enhance tax administration, and improved tracking and effective monitoring of social expenditure and related outcomes. The authorities should also stand ready to undertake appropriate corrective fiscal measures, if needed, to achieve the budgetary targets*'.

2003 IMF Completes Fourth Review of Pakistan's PRGF-Supported Program, Approves US$118 Million Disbursement to Pakistan
'*In approving the disbursement, the Executive Board granted a waiver of Pakistan's non-observance of the continuous structural performance criterion regarding tax exemptions and regulatory import duties... The removal of a significant number of tax exemptions with the next budget should lead towards a tax system where the burden is more fairly distributed across income earners*'.

2003 IMF Completes Fifth Review of Pakistan's PRGF-Supported Program, Approves US$123 Million Disbursement
'*This will require forceful pursuit of reforms aimed at simplifying the tax system and broadening the tax base, including through the elimination of a number of tax exemptions, to reduce distortions and the potential for corruption*'.

2003 IMF Executive Board Completes Sixth and Seventh Reviews of Pakistan's PRGF-Supported Program, Grants Waivers and Approves Disbursements Amounting to US$247.54 Million
'*In this regard, Pakistan's request for waivers for the non-observance of three structural performance criteria was approved by the Executive Board... In the fiscal area, this will include efforts to broaden the tax base through an expansion of the general sales tax to services, a reduction of tax exemptions, and an improvement in the capacity of local governments, which administer most poverty-related expenditures*'.

2004 IMF Executive Board Completes Eighth Review Under Pakistan's PRGF-Supported Program and Approves Disbursement Amounting to US$253 Million
'*It will be essential to press ahead with the ongoing reforms to simplify the tax system and broaden the tax base*'.

2008 IMF Announces Staff Level Agreement with Pakistan on US$7.6 Billion Loan
'*This fiscal adjustment will be achieved primarily by phasing out energy subsidies, better prioritizing development spending, and implementing strong tax policy and administration measures*'.

2009 IMF Completes Second Review Under Stand-By Arrangement for Pakistan and Increases Financial Support to US$11.3 billion
'*A durable solution to the problem of low tax revenue should start with the early implementation of VAT and the ongoing tax administration reform*'.

2009 IMF Completes Third Review Under Stand-By Arrangement for Pakistan,Approves US$ 1.2 Billion Disbursement
'*The introduction of the VAT and associated administrative reforms, scheduled for July 1, 2010, is key to strengthening revenue, crucial for reducing poverty and financing needed investment in human and physical capital. Prompt submission of the VAT law to parliament and its passage will therefore be important*'.

2010 IMF Completes Fourth Review Under Stand-By Arrangement for Pakistan and Approves US$1.13 billion Disbursement
'*Achieving the 2009/10 fiscal target will require strong efforts, including from the political leadership. Resolute continuation of tax collection efforts, tax administration reform, and expenditure restraint, together with timely disbursement of the pledged foreign financing will be critical to facilitate fiscal management*'.