Evaluation of Macro Economic Policies of Pakistan (1950 -2008)

Tahir Mahmood, Hafeez ur Rehman and Shahnaz A. Rauf[1]

Abstract

The economy of Pakistan performed quite well until the end of 1980s despite the major shift in policy stance by the economic managers, from a private sector led economy in the sixties to a nationalized economy in the 1970s and a shift towards liberalization, deregulation and denationalization in the decade of eighties. It was in the decade of nineties that Pakistan recorded the lowest GDP growth in South Asia and these were also the years when Pakistan experienced a series of adjustment and stabilization reforms. Towards the end of the nineties there were some signs of improvement in macro economic indicators. However, this improvement did not last long. Thus the economy of Pakistan has always remained under stress due to high fiscal and external sector imbalances, high aggregate demand, unsustainable GDP growth, high unemployment and poverty levels.

Introduction

Ever since independence the economic performance experienced by Pakistan clearly indicate that sustained and sound economic performance is strongly conditional on setting the right policies and priorities for a balanced sectoral growth, supported by social sector and infra structure development policies. Besides that growth is also largely dependent on internal law and order situation, maintenance of governance standards and exogenous shocks to the system.

Among the demand management policies it is surely the sound public finance that is considered to be supporting economic growth by ensuring price stability through minimizing inflationary seignorage; allowing reduction in distortions caused by the taxation structure, yielding positive investment returns induced by low real interest rates. Whereas an unsustainable fiscal position implies that the government will have to take corrective measures in future. Uncertainty about the timing and the form of these measures could harm economic growth by preventing optimal investment decision. Similarly weak public finance is reflected in a weak external sector position in the form of persistent current account deficit and volatile exchange rate position.

[1] Authors are Lecturer and Associate Professor/Chairman at the Department of Economics, University of the Punjab, Lahore (Pakistan), faculty member at Air University, Islamabad (Pakistan) respectively. Corresponding author: drhrehmankhan@yahoo.com

Historically the most distinct and salient feature of the sixties was that economic growth firmly based on the initiatives of the private sector and generally sound economic management. Whereas during the period of seventies economic management shifted towards nationalization and increased role for the public sector. The period of eighties was marked by liberalization, deregulation and privatization etc and during the same period Pakistan also was undergoing structural reforms and stabilization measures. Thus until the decade of 1980's Pakistan's economic performance was characterized by a high rate of growth (GDP), averaging close to 6 percent and it was considered as the most developed country of South Asia. These impressive growth rates were largely based on external capital inflows. The availability of external financing led to a large unaddressed structural imbalance, principally in the fiscal and the external sector accounts.

It was not so in 1990s and the economic performance of Pakistan measured in terms of GDP and sectoral growth was the lowest among the SAARC countries and the sharp decline in capital inflows affected the growth rate. The economic performance during the 1990s deteriorated and failure to contain fiscal and current account deficit led to unprecedented and unsustainable levels of public debt. Besides that other macro economic indicators also worsened including stagnant tax to GDP ratio, double digit inflation, low levels of investment deteriorating infra structure, poor social sector indicators and poor governance of institutions etc. To give a supply side boost to the system , the policies of deregulation, liberalization, and privatization that were initiated in the early half of 1990s were not materialized as this program was not accompanied by demand-side adjustment that were essential for stabilizing the serious macroeconomic imbalances.

This period was also marked by some external shocks including economic sanctions, September 11 event and tension on Afghanistan border area. In other words, 1990s is termed as a lost decade by many analysts. The period of 2000s was faced with the challenge of poverty and unemployment growth, fiscal and external sector imbalances besides external shocks of war on terrorism. Thus the improvement in GDP growth proved to be short lived.

The factual position of Pakistan's growth and development till the sixties and seventies has been reported before by Papaneck (1967), Lewis (1969) and (1970) and Amjad (1984) etc.

The purpose of this paper is to review macroeconomics performance of the economy of Pakistan to date and review the growth, structural change, and policy and non policy determinants of growth and to establish that the policy makers could not develop a sustainable pattern of public finance and external sector balances. Special reference is made to the dependence between the growth of agriculture and industry, domestic savings, investment, fiscal sector, budget deficit, and external assistance, structural adjustment program, financial sector reforms.

2.1 Fifties and Sixties

Table 1 and 2 present the changes in the structure of production and employment that occurred during the period 1950-1988 as well as the sector wise growth rates and GNP.

The economy of Pakistan which started with small base could not perform well in 1950s and the composition of GNP showed heavy reliance on agriculture, it was only in sixties and then in seventies that the composition of GNP changed substantially, the share in GDP of agriculture declined, of industry doubled, of construction increased, electricity / gas and that of the services sector also increased. A similar shift though relatively less sharp is observed in the sectoral distribution of employment. The share of agriculture has been declining but it is still the major absorber and the share of manufacturing sector increased slightly. Other sectors providing more jobs were transport, communication, construction and services. Industrial growth was 23 percent per annum in the first plan period (1955-60) and 1 percent during the second plan period (1960-65). Growth of the industrial sector was not accompanied by the agriculture sector that remained stagnant and performed poorly throughout 1950s. The food grain shortage in early 1950s because of the poor performance of the agriculture sector, forced Pakistan to borrow long term credits for imports of food grain. Later in the sixties Pakistan was able to reduce the difference in growth of the two sectors. Agriculture sector grew from 1.0 percent in the first plan period to 3.7 percent during the period 1960-65. This increase in growth of agriculture was the result of green revolution that also brought favorable prices, technology, water and other inputs. Thus, a balance was created in the two sectors and sustained growth of industrial sector was made possible by growth in demand in the rural areas and supply of raw material for domestic industry with out any shortage.

Thus the establishment and expansion of large scale manufacturing sector, predominantly agri-based was the achievement of the decade. Of course the public sector institutions played a vital role for the promotion and development of this sector and huge foreign exchange reserves earned during Korean War were utilized.

During late fifties and early sixties government priorities shifted, i.e. pro-industrial bias diluted and realization to focus on agricultural sector emerged. The result was rapid growth in both the industrial and agriculture sector and consequently significant increase in per capita income. It was a period of sound and disciplined economic management. Strong planning and formal decision-making machinery culminated in the institutionalization of planning process. The era of post war 1965 was featured by marked decrease in foreign loans inflow, slow down in the industrial growth, and increase in defense expenditures and re-imposition of certain controls as foreign exchange constraints. The GDP growth rate remained 6.8% on average per annum. The large deficit in the balance of trade throughout was financed by the increasing flow of foreign loans. In fact big foreign loans inflow helped accelerating the economic growth. The model of economic development during 1960s was featured by pro industrial bias but gradual emphasis on agricultural sector, neglect of social sector and huge contributions of vibrant private sector.

However these trends were reversed by mid 1965 due to the war with India, termination of US grant for military purpose and poor crops in 1966 and 1967 which meant diversion of foreign exchange to import of food grains and the burden of import financing increased at almost 8 % per annum. This led to the revision of development strategy which meant: (a) shift in allocation of resources from capital intensive projects to relatively less capital intensive investments (b) shift in development strategy from industry to agriculture. Given these changes, the overall achievements of the third plan period were not discouraging. The GDP growth was only fractionally less than what it was during the second plan. This was mainly so due to the (1) expansion and growth of the agriculture sector on average by 5.6 percent (2) growth in export of manufactured goods on account of investment in export oriented industries through the export bonus scheme.

However, the biggest disappointment during the third plan period was the performance of the industrial sector. The resource shortage led to limited investment and as a result the manufacturing sector recorded a marked slow down from the 16.9 percent per annum growth rate achieved in the second plan to almost 10.0 percent per annum in the third plan period.

2.2 The Seventies and the Non Plan Period (1971-77)

Political disturbance which had started in late 1960s ended with the crises of 1971 and consequent separation of the former East Pakistan. The new government took over amidst deteriorating economic growth and the country was faced with the challenges of rehabilitation of war shattered economy, high rate of inflation and stagnant agriculture and industrial sector. Finding new markets for the roughly 50% of the exports, that had previously been going to eastern wing, was also a big priority.

The development strategy of the new government identified manufacturing as the major engine of growth, but unlike the previous development strategy of favoring import substitution for consumer goods and export oriented industries, the priorities were changed towards investment in big sophisticated industrial units through public sector expansion , to increase self sufficiency in intermediate and capital goods industries .

In view of the concentration of income and ownership, the main cause of political disturbances of late sixties, the government took some drastic steps in the early 1972 and brought fundamental structural reforms like Land reforms, Labor reforms, Nationalization of key industries , banks and insurance companies, export trade of two major export products i.e. rice and cotton. Termination of the export bonus scheme and devaluation of Rupee resulted in removal of subsidies to the industrialists in the form of over valued exchange rate and improvement in the terms of trade. Although these reforms were introduced to break the link between the industrial and financial capital, improve the efficiency of the manufacturing sector and ensure a fair and equitable distribution of income, instead the percentage share of both the manufacturing and agriculture in GDP declined. Growth rate in large scale manufacturing reached the lowest percent of 4.7 per annum. Agriculture sector slowed down from 5.6 percent per annum in the 1965-70 periods to 2.48 percent during this period mainly due to exceptional weather conditions. Thus decline in the two major sectors of the economy led to decline in GDP growth to 3.6 percent per annum even lower than the growth rate achieved in the period 1955-60. Decline in industrial growth occurred despite large public investment, however this increase was neither accompanied by increase in private investment nor was it accompanied by increase in savings. The inflow of foreign capital reflected the failure to mobilize domestic savings. The major features of 70s are presented below.

- Public savings were low largely because fiscal deficit and primary deficit remained at 7.6% and 5.9% of GDP on average respectively, mainly due to large-scale investments in public sector, production subsidies and spending on social program. The huge expansion in public sector was not matched by the off setting rise in revenue which remained stagnant, i.e. 14.2 percent of GDP and subsidies on wheat, fertilizer, plant protection etc increased. The fiscal deficit was financed mostly from external sources, i.e. 50.9 percent, from bank borrowing and non-bank borrowing.
- The current account balance was in deficit of 5.2% of GDP on average. The deficit resulted from huge imports; even the boost in the exports as a result of massive devaluation of 131% in 1972 could not nullify the impact. However the Government succeeded in wining the favor of Middle East countries for accepting Pakistan labor and consequently restrictions on outward migration of workers were eased. The workers remittances enhanced during the decade that helped in improving the balance of payments position.

- Average investment and saving rate remained at around annual average of 17.1% and 11.2% of GDP respectively.

The high inflation throughout i.e. 12.2% was the result of high oil prices, increase in remittances, and enhanced public consumption along with decreased production output.

The positive aspects of the period include setting up of basic industries bringing income redistributions and managing to send a large number of people to Middle East. The policy makers tended to correct the excesses of the previous decades, however increased public expenditures were not matched by increased resource generation in the form of public-private savings, increased tax to GDP ratio and private investment. External sector imbalances were compensated by increase in remittances and increase in export earnings was only 9 percent in contrast to increase in imports of 18.5 percent per annum and the terms of trade were unfavourable due to rise in oil prices. Thus on the whole the new strategy did not bring immediate results in terms of growth rates.

2.3 The Decade of Eighties

The period of 1980s was more focused towards denationalization and the role of public sector was to be reduced. In this context two agreements were made on Extended Fund Facility (EFF) with IMF and Structural Adjustment Loan (SAL) with World Bank. These two agreements were the preconditions of USA for rescheduling Pakistan's $160 millions debt, accumulated over the years. Exchange Rate Policy was revised in 1982 wherein Managed Float System was adopted and Pak Rupee depreciated by 20 percent. The medium term Standby Extended Fund Facility (EFF) agreements with IMF were signed in 1988. It had conditions attached to it regarding devaluation, import liberalization, tariff reduction and financial sector reforms like deregulation of interest rate structure etc.

During this period the agriculture sector was heavily regulated, agricultural commodities were procured by the government at lower than the import parity prices. Moreover, an overvalued exchange rate, export taxes and sale of input and outputs through government owned corporations led to inter-sectoral transfer of resources from rural to urban areas.[2] Big landowners misused their tax exemption status and diverted their earnings to the industrial and the services sectors. These large farmers were also able to get the subsidized loans from ADBP for tractors, farm mechanization and also

[2] Resource transfer from agriculture sector was over 6 percent of agricultural gross product and the growth of agriculture was adversely affected which led to negative impact on poverty and income distribution (Ishrat Hussain, 1999).

diverted water to their land holdings by colluding with the irrigation officials (Janjua, 2004). Thus the era of structural reforms began in late 1980s.
The major features of this decade are summarized below.

- The Growth rate of GDP in 1980's remained at 7.1% on average.
- Fiscal deficit in 1980's remained at about 6.8% of GDP on average where as the primary deficit was recorded about 3.5% on average. Fiscal deficit was financed predominantly by non-bank borrowing i.e. 49.6% of the total. The external financing reduced to 22.6% of total deficit. Bank borrowing financed 27.8 % of the deficit. The non-bank borrowing helped government in avoiding inflationary pressures.
- The inflation rate remained 7.6% on average as compared to 12.2% in 1970s.
- The current account balance remained in deficit at an annual average rate of 2.8% of GDP throughout the decade. It was better than that of 1970s mainly because of decreased imports and enhanced remittances during this decade. Substantial foreign assistance due to Afghan war also helped in improving the balance of payments position.
- The investments constituted 18.7% of the GDP per annum on average whereas savings during the decade fluctuated around annual average of 14.8%. These investments were mostly financed by external resources. The private investment remained very low despite the incentives by given the government for restoring private sector confidence.

The decade was featured by high public consumption without matching rise in tax revenue, change in deficit financing mix, i.e. domestic non-bank borrowing replaced bank borrowing and external financing and controlled inflation rate because of high growth rate and huge non-bank borrowing.

2.4 The Decade of Nineties

Structural reforms in the agriculture sector were meant to remove bias against the agriculture sector by removing the protection given to the industrial sector. Thus agriculture prices were liberalized and the subsidies given to the sector, the price support and procurement system were all discontinued. Reforms in the agriculture sector targeted four areas, including: (A) enhanced availability of water and its efficient use. (B) Providing market based environment for input and output prices. (C) Provide physical infra structure and support for research and extension work, and also provide better farm to market links (D) provide access to good land for cultivation. The response of the farmers to these changes and incentives were reported to be positive (Ishrat Hussain, 2003).

Industrial sector of Pakistan has been faced with excess capacity, particularly due to huge investments in the 1990s in thermal power projects, cement, sugar, automobiles and electronic durables. Thus capacity utilization has been ranging between 60-70 percent. However, industries such as fertilizer, steel, chemicals, paper and paper board operated at full capacity. In the textile sector there was some expansion of capacity, and efforts were made for the balancing, modernization and replacement of existing capacity.

Further, in the early period of 1990s, a number of measures were undertaken to create a better business environment to attract foreign inflow of capital. It included allowing of foreign equity participation up to 100 percent, liberalizing foreign exchange regime, liberalizing import policy, convertibility of rupee on current account and a number of fiscal incentives in the form of quantitative and non tariff barriers were also removed.

In addition to that agriculture, services, infra structure and the social sector were also opened to foreign investors. Thus FDI inflows and portfolio investment took place in PTCL, private power projects, and oil and gas sectors. However these investments did not show any marked impact on increase in employment as most of these investments were highly technical and skill specific.

All these efforts failed to attract significant inflow of foreign capital and investment in Pakistan. The main reason behind this failure was poor law and order condition, inadequate infra structure facilities and inconsistent policies of the changing governments of that time. Moreover, inflow of foreign investment to stagnant economies can hardly be attracted by offering attractive policy incentives (Niazi and Javed, 2000).

During the period of 1990s, monetary management was reformed and changed to a market based system that included abolition of credit ceilings and credit deposit ratios, phasing out of directed and concessionary credit, removing of caps on interest rate and initiation of auction of public debt. The market based system of monetary and credit management meant management of monetary and credit expansion through indirect market oriented instruments like open market operations, along with changes in the discount rate and cash reserve requirement. Moreover the multiple exchange rate system was abolished and a unified exchange rate system was introduced thus integrating the exchange rate with the monetary policy.

On the fiscal sector, it is observed that despite several attempts to raise revenue and reduction in development expenditures the fiscal deficit that was significantly high in 1980s continued to remain high in the period of 1990s. Whatever fiscal adjustment was achieved it was mainly done by reducing development expenditure and compromising on the growth of the economy. However fiscal deficit as a ratio of GDP remained above

6%. The revenue generation efforts failed on account of weak structural base with low buoyancy of the taxation system and tax to GDP ratio as low as 13% to 14 % of GDP.

Large and persistent fiscal deficit since 1980s has resulted in fast growth of public debt and debt burden. Debt as a percentage of GDP was as high as 106 percent of GDP in 1999-00. Domestic debt was almost 50 percent of total debt and so was the external debt.

Similarly the exchange rate misalignment rose significantly during the period of 1990s and its volatility was very high. Besides that the current account remained high throughout the1990s, i.e. 5.9 percent of GDP compared to 2.7 percent of GDP in 1980s. The current account was largely negative due to persistent trade deficit caused by economic sanctions and substantial decline in exports. Foreign exchange reserves have never remained sufficient and hardly covered six weeks imports during 1990s.

On the social sector development it is generally argued that rural poverty increased and income distribution deteriorated during the 1990s. As the social indicators were poor, a Social Action Program was initiated in two phases to improve the social sector indicators of health, education, clean drinking water, sanitation etc. However, little progress was made in improving the social sector indicators as growth was itself deteriorating averaging to hardly 4 percent. According to UN Human Development Index 1991 Pakistan was ranked higher than India and Bangladesh, whereas towards the end of 1990s Pakistan was placed far below these two countries. All the social sector indicators thus deteriorated with the exception of adult literacy rate and family planning.

The fundamental Structural and institutional reforms were initiated and pursued during this decade. The Privatization program started and institutionalized under Protection of Economic Reforms Act 1992. SBP Act 1956 was amended; Trade liberalization started in 1990 along with Tariff reforms. The external environment did not remain favorable as USSR disintegrated and Western Allies backed out; and the USA aid also ceased completely. Nuclear Test conducted in May 1998 led to further economic isolation of Pakistan as sanctions were imposed. The Freezing of Foreign Currency Accounts and consequently drastic decrease in workers remittance was another severe blow to the stagnant economy. The pursuance of deflationary policy and structural changes in the economy in pursuance to Structural Adjustment and Stabilization Program (SASP) were implemented during 1990s. The persistently high budget deficit and balance of payment worsening in 1980s and its then management through external financing and non bank borrowing had resulted in rising debt servicing expenditures in 1990s. The major features of the 90s decades are highlighted below.

- The GDP growth rate remained about 4.4% on average throughout;
- The budget deficit and primary deficit[3] remained 7.3% and 1.3% of GDP on average respectively in this decade. Thus the revenues remained stagnant; the non-developmental expenditures especially non-discretionary i.e. debt servicing expenditures rose considerably resulting in high fiscal deficit throughout. The deficit was financed by borrowing from banks i.e. 28.5% of overall deficit, from non-bank borrowing, i.e. 40.8% and external resources, i.e. 30.7% of total deficit. The reliance on non-bank financing was reduced a little bit and other resources were resorted to.
- The current account balance remained in deficit from an annual average of 4.1% of GDP. Removal of non-tariff barriers, tariff rationalization and exchange rates reforms during 1990's have implications for imports and exports. The significant decline in remittances and foreign grants were the main factors behind this high current account deficit.
- High fiscal deficit accumulated over time resulted in sharp growth of public debt. Increasing reliance on short/medium term financing, the sanctions imposed after nuclear blasts and the freezing of foreign currency accounts compounded the problem.
- The investment rate remained around annual average of 18.3% of GDP despite investment friendly policies in the early years. The foreign investment was encouraged through many incentives & measures like removal of restrictions on maximum holdings of equity by foreigners, remittance of dividend proceeds without the interference of State Bank of Pakistan, removal of restrictions on raising loans from domestic markets, relief from double taxation, however inconsistent economic policies, political uncertainties, ongoing process of structural adjustment and finally post explosion sanctions caused decrease in investment rate in later part of the decade.

The decade witnessed vigorous pursuance of privatization/deregulation policies, implementation of Structural Adjustment and Stabilization Programs and the reliance on more stable, less volatile and sustainable sources of external capital inflows. The structural reforms, though initiated and pursued vigorously, failed to achieve the objectives like low fiscal deficit and viable balance of payments situation during the decade.

---

[3] **Fiscal Deficit:** When expenditure (including interest payments on public debt) exceeds the fiscal revenue, the fiscal deficit results that may be financed in a variety of ways.
Primary Deficit: The primary deficit is the difference between government expenditure exclusive of interest payments on public debt and revenue.

2.5 The 2000s

The 2000s was featured by continuation of a more liberal outward oriented economic strategy aiming at enhancing exports and to get integrated into world economy. The structural reform programs designed and initiated in 1990s, was continued and pursued during 2000s to put the economy on the path of recovery. Unpopular decisions like imposition of sale tax, raising prices of petroleum, withdrawal of subsidies were taken for bringing fiscal discipline. These were in fact conditions attached with IMF standby agreement executed in 2001 and three years Standby Poverty Reduction and Growth Facility (PRGF) were implemented during 2001-2004. Certain structural reforms, i.e. financial sector restructuring, privatization, liberalization and deregulation of economy and bank reforms leading towards market led economy were under taken.

The privatization process was pursued; main focus was on banking, telecommunication, oil and gas and energy sector. Liberalization of Foreign exchange regime and macro economic stability helped boosting investor's confidence. Stock markets became extremely attractive for foreign investment. Huge public sector investment, especially in water and power sector, housing and physical infrastructure were undertaken in last 4-5 years. Economic governance also improved significantly and losses of public sector enterprises diminished dramatically.

The event of September 11, 2001 and Pakistan's alliance with coalition forces in the fight against terrorism helped its economy in many ways. The rescheduling of $12.5billion bilateral and multilateral external debts resulted in about $1.5 billion annual relief in shape of decreased debt servicing charges. Lifting of sanctions brought handsome foreign grants about $1 billion to $1.5 billion per annum during last four five years. Some external debt were written off. The remittances amounting to $18.5 billion during last five years helped in building foreign exchange reserves, easing BOP position and in achieving good growth rate of economy. The greater access to the markets of USA and EU countries helped achieving significant upsurge in Exports. The major features of 2000s are given below.

- The GDP growth rate remained around annual average of 4.9% during 2000s.
- The Fiscal deficit remained around annual average of 4.5% of GDP while the primary balances remained surplus. The fiscal policy remained expansionary during 2000's i.e. huge PSDP during these years; however, reduction in debt servicing charges as a result of debt rescheduling did help in reducing this fiscal deficit. This deficit was financed by bank borrowing i.e. 5.8%, non-bank borrowing i.e. 62.4% and from external resources i.e. 31. 8%.

- The current account balance remained surplus around an annual average of 1.9% of the GDP. The exports fluctuated around 18.4% of the GDP per annum where as the imports remained liberal and grew at a faster rate i.e. 40% annually. The rising oil prices also raised the import bill. The trade gap resulted but ever-rising remittances since Sep11, 2001 onward kept the current account balance in surplus.
- The external debt has increased to $37 billion in 2005 that is 36.6% of the GDP as compared to 50.2% of GDP in 2000. In fact public Debt to GDP ratio has declined from 102.8% of the GDP in 2000 to 74.6.3% of the GDP in 2005 mainly because of healthy GDP growth rate and premature retirement of expensive debts to ADB. Some debts were also writt2 ff.
- Inflation rate remained below 4% in early years but later on has an upward swing to double-digit level in 2004-05 but annual average was 5.7% per annum.
- The period recorded investments around annual average of 17.3% of GDP where as saving rates remained around 17.8% of GDP on average.

Broad based recovery in the form of improvement of macro economic indicators since 2001-02 did not last long and the economy started flattering in some areas i.e. inflation rate was on the rise and so was the trade deficit and current account deficit. Fiscal deficit was also on the rise. Soaring aggregate consumption necessitated demand management through tighter monetary policy.

2.6 Conclusion:

The economic history of Pakistan further reflects the Government's inability to establish a sustainable pattern of public finance relying first on foreign grants, supplemented by non-bank borrowing and of late, even by borrowing from short-term private sectors. High current expenditures forced cuts in development expenditures thus retarding the infrastructural development. Similarly the resource mobilization had been much short of our requirements. An inelastic, non-progressive tax structure with narrow tax base and a big size ever developing black economy are the main structural weaknesses in the fiscal policy.[4] The tax to GDP ratio remained around 12.5% of the GDP over the last 3-4 decades, despite massive tax system reforms, in sharp contrast to industrial countries where this ratio is between 25% and 40% per annum on average.

[4] A recent study conducted at LUMS revealed that the current tax collection accounts for 38% of the total tax potential; remaining 62% is being pocketed by the tax payers, tax collectors and tax practitioners [The daily Dawn]

The fiscal imbalances i.e. highly buoyant current expenditures but insufficient resource generation always resulted in budget deficit and it has been financed throughout from domestic borrowing and external finances instead of focusing on cut in expenditures and raising more tax revenues. The easiest recourse of monetizing the budget deficit and financing the expenditures by borrowing from abroad was adopted. The result was an ever-rising public debt and expenses on debt servicing.

The policy makers have always been attracted by the idea of maximizing foreign assistance for financing budget deficit and big investment lay out to achieve high growth. The domestic savings were too low to finance it. The persistent high Current Account Deficit, ever larger than the rapidly growing economies of East Asian countries further worsened when the percentage of concessional loans started decreasing in 1990's and the percentage of market based loans increased. External sources at concessional terms were not available in 1990s as these were in 1960's. These big inflows of concessional foreign aid facilitated the policy makers in avoiding the restructuring of economy and taking steps for correction of imbalances in fiscal and external accounts.

Instead of relying upon stable and sustainable sources of external financing like exports, FDI, portfolio investments and foreign assets of Pakistan for stimulating growth of economy, the policy makers remained dependent on unstable and less sustainable sources of external financing like loans, foreign aid, and remittances. Thus the marginal saving rate has been at about 15% of GDP over the last three decades whereas it was 25% in India and 35-40% in East Asian Countries in 1973-93 periods. Short-term foreign exchange liabilities in 1990s were a major reason behind debt crisis in that decade.

The privatization process was pursued vigorously and was considered as the dominant factor of our economy in 2000's, however it has slowed down in the second half of the 2000s. The rising FDI and portfolio investments are the encouraging signs for Pakistan's economy.

Financial sector reforms resulted in a vibrant banking sector in Pakistan with improved regulatory and supervisory capacity of the central bank. Deregulation of interest structure, like auctioning of government securities through bids, discount rates and increased market share of foreign banks has made the banking sector competitive and capable of supporting growing economy. The decreased borrowings by public sector have made credits available for consumer financing, micro financing and SME's resulted in healthy GDP growth rates in 2000's, but this phenomena has slowed down and government borrowings have increased in the second half of 2000s.

In sum, the evaluation of macro economic policies reveals that the growth rate of GDP remained quite high except in 1990s but lacked sustainability and equitable distribution of growth benefits. The fiscal imbalances always resulted in budget deficit. The economic managers failed to establish a sustainable pattern of public finance relying first on foreign grants, supplemented by non-bank borrowing and, even by borrowing from short-term private sectors to meet these deficits. The domestic savings were also low to meet these gaps. The twin deficits have been financed throughout from domestic borrowing and external finances instead of focusing on cut in expenditures and raising more tax revenues.

Table 1

MACROECONOMIC ENVIROMENT				
Variables/Years	1970s	1980s	1990s	2000s
	Growths rates			
Gross Domestic Product	5.0	7.1	4.4	5.3
Agricultural	2.4	4.1	4.2	2.8
Industry	5.5	8.2	4.6	8.2
Services	6.3	6.7	4.5	5.3
Inflation(GDP deflator)	12.2	7.6	10.0	5.7
	Percent of GDP			
Saving	11.2	14.8	13.8	17.8
Investment	17.1	18.7	18.3	17.3
Budget Deficit	7.6	6.8	7.3	4.6
Current Account Balance	-5.2	-2.8	-4.1	0.0

Sources*: CD _ ROM IFS [2006], and Economic survey of Pakistan various issues*

Table 2

FISCAL INDICATORS: REVENUES

Variables/Years	1970s	1980s	1990s	2000s
	Percent of GDP			
Tax	11.4	13.2	13.0	12.5
Non-Tax	2.3	3.6	4.2	4.0
Revenues	13.7	16.8	17.2	16.4
Grants	0.6	0.7	0.3	0.9
Total Revenues +Grants	14.3	17.6	17.6	17.4

Sources *CD _ ROM IFS [2006], and Economic survey of Pakistan various issues*

Table 3

FISCAL INDICATORS: EXPENDITURE

Variables/Years	1970s	1980s	1990s	2000s
	Share in Current Expenditure			
Interest payments	12.5	18.3	30.2	36.6
Defense	43.9	36.0	29.5	22.1
Others	43.6	45.8	40.3	41.3
	Percent of GDP			
Interest payments	1.7	3.3	6.0	6.6
Defense	6.0	6.3	5.8	3.9
Current Expenditure	13.7	17.8	19.8	17.8
Development Expenditure	3.3	2.9	3.4	3.7
Net Lending to PSEs	4.9	3.7	1.7	0.4
Grand Expenditure	21.9	24.3	24.8	22.0

Sources *CD _ ROM IFS [2006], and Economic survey of Pakistan various issues*

Table 4

FISCAL INDICATORS: GAPS & FINANCINGS

Variables/Years	1970s	1980s	1990s	2000s
	Percent of GDP			
Primary Deficit	5.9	3.5	1.3	-2.0
Overall Deficit	7.6	6.8	7.3	4.6
	Percent of Overall Deficit			
External Financing	50.9	22.6	30.7	26.5
Domestic Financing	49.1	77.4	69.3	73.5
Bank borrowing	21.2	27.8	28.5	12.0
Non-Bank borrowing	28.0	49.6	40.8	57.5

Sources *CD _ ROM IFS [2006], and Economic survey of Pakistan various issues*

Table 5
EXTERNAL SECTOR INDICATORS

Variables/Years	1970s	1980s	1990s	2000s
		Percent of GDP		
Trade Gap	-8.14	-10.46	-6.53	-4.43
Interest payments	1.00	1.63	1.80	1.33
Remittances	3.13	7.40	2.96	3.82
Current Account Balance	-5.19	-2.79	-4.07	-0.002
Foreign Direct Investment	0.05	0.31	0.85	1.36
Portfolio Investment		0.14	0.52	-0.08
Reserve (Stock in $m)*	970	1188	2410	13415
Reserve (Growth %)	26.9	4.3	10.7	35.7

*Stock values pertain to the end of decade

Sources *CD _ ROM IFS [2006], and Economic survey of Pakistan various issues*

Table 6
MONETARY SECTOR INDICATORS

Variables/Years	1970s	1980s	1990s	2000s
			AS Percent of M2	
Government Borrowing	44.9	44.8	49.7	22.4
Private Sector credit	49.7	55.3	54.6	99.4
Domestic Credit	94.7	100.1	104.3	255.7
M2 as % of GDP	44.4	47.4	46.8	23.7
Reserve (Growth %)	26.9	4.3	**10.7**	35.7

Sources *CD _ ROM IFS [2006], and Economic survey of Pakistan various issues, various issues of Annual reports of State Bank of Pakistan*

References

Ahmad, M. and Khalida, G. “Pakistan Prospects and Perspectives”, Royal Book Company, Karachi

Ahmad, V. and Rashid, A. “the Management of Pakistan’s Economy: 1947-82”, Oxford University Press, Karachi.

Arby, M.F. (1997), “Major Issues and Remedies with Regard to Public Debt in Pakistan”, Journal of the Institute of Bankers in Pakistan.

Asian Development Bank (2002),”Escaping the Debt Trap: An Assessment of Pakistan’s External Debt Sustainability”, Working Paper No. 1.

Easterly, W, and Klaus. S.H, “Fiscal Deficits and Macro Economic Performance in Developing Countries”, the World Bank Research Observer, Vol.8, No 2 (July 1993).

Fatima, M. and Qazi, M.A., “Political Economy of Fiscal Reforms in the 1990s”, The Pakistan Development Review 40: 4 part II (winte2001) pp.503-518.

Government of Pakistan, “Pakistan Economic Survey”: (various issues).

Hassan, P. “Learning from the Past: A fifty Year Perspective on Pakistan’s Development”, The Pakistan Development Review, Vol.36:4 part I (winter 1997) pp.355-402.

Hassan, P. “Pakistan Economy at the Crossroad” Oxford University Press, 1998

Husain, I. “Current Issues in Pakistan’s Economy”, State Bank of Pakistan, 2005

Husain, I. “Pakistan, the Economy of an Elitist State”, Oxford University Press, 1999

Ishrat, H., Governor’s Speeches 1999- 2005 ‘Economic Management Policies”, www.sbp.org.pk

International Monetary Fund, International Financial Statistics (CD-ROM and various issues), Washington, DC.

International Monetary Fund, Government Finance Statistics Yearbook (various issues), Washington, DC

Janjua, A, ‘History of the State Bank of Pakistan, Printing Press State Bank of Pakistan

SBP-BSC (1988-2003) ‘, (2004)

Kemal, A.R. 2002, “Macro Economic Policies and Poverty in Pakistan” Pakistan Institute of Development Economics.

Kemal, A.R. “Pakistan’s Economy: Performances and Future Prospects”, South Asian Journal, No. 4 (April-June 2004).

Lewis, S.R., and Guisinger , S,C, Measuring Protection, in a Developing Countries: The Case of Pakistan, Journal of political economy, LXXVI (December 1968).

Lewis. S.R., ‘Economic Policy and Industrial Growth in Pakistan ’, London, George Allen and Unwin, (1969).

Lewis, S. R., ‘Industrialization and Trade Policies’, London, Oxford University Press, (1970).

Nasim, A. “Financing Pakistan’s Development in the 1990s”, Oxford University Press, Karachi.

Pakistan, Government of (2001), “A Debt Reduction and Management Strategy, Summary Report of the Debt Reduction and Management Committee. Islamabad: Finance Division.

Papaneck . G., ‘Pakistan’s Development: Social Goals and Private Industries ‘, Cambridge, Harvard University Press. (1967)

Pasha, H.A. and Aisha, G.,” Fiscal Policy in Pakistan” Social policy and Development Centre, Research Report No. 1 (January 1992)

Qazi, M.A.,” Structure of Public Finances: Historical Perspectives and Future Prospects”, Pakistan Journal of Applied Economics, Vol. 14, No. 1&2 1998, pp. 89-105.

Raghbendra, J. (2001), “Macroeconomics of Fiscal Policy in Developing Countries”, Australian National University, Canberra, Australia

Raza, R., “Pakistan in Perspective 1947-1997”, Oxford University Press, Karachi.

Social Policy and Development Center, “An Overheating Economy”, Annual Review June 2005.

State Bank of Pakistan, Annual Reports (Various Issues).

Standard and Poor’s. Available: http// www.standardandpoor.com

World Bank, Global Development Finance (CD-ROM and Various Issues), Washington, DC

World Bank, World Development Indicators (CD-ROM and Various Issues), Washington, DC

Zaidi, S.A., "Structural Adjustment Program and Pakistan: External Influences or Internal Acquiescence", Pakistan Journal of Applied Economics, (1994), Vol. X No. (1 & 2) pp. 21-46.