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**POLITICAL AND INDUSTRIAL GROWTH REGIMES**

**BY**

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**To**

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# **INTRODUCTION:-**

A major economic transformation in or towards modern economy requires a state which can effectively perform the roles of the ultimate entrepreneur and the conflict manage. Rapid industrialization for economic and social development needs coordinated encouragement of desirable activities. The state plays a critical role in this process. Many researchers have argued that a primary role of the state in envisioning structural change as well as establishing viable coordination mechanisms, during different phases of industrial development, has been a key feature of the ‘late industrializers in East Asia.. However, since the early 1980s, many economies have been structurally adjusted and the role of the state shifted from interventionist industrial and economic management towards liberalization. In fact, the neoliberal idea system behind this shift assumes the institutional primacy of the markets for economic change and emphasizes reforms in other institutional arrangements in line with the theoretical assumptions of free market economy.

On the other hand, since late 1980s, there is a reinvigoration of academic interest in the role of the state and designs of industrial policy which contradicts the basic assumptions of neoliberal orthodoxy. The debate discusses effectiveness of interventions by the state in industrial development as well as technological capability enhancement. A growing body of knowledge has also argued that direct interventions by the state has played a critical role in the growth of industrial capability of many economies of Western Europe and the USA in the past. The Political Economy of Industrial Policy in Pakistan is visibly inconsistent and shows episodes of rise and fall of the manufacturing sector fortunes. Starting from the classical Import Substitution, Industrialization period to reach export led growth strategies. The history of the political economy of industrial policy development is divided into decades starting from the birth of Pakistan in 1947 and also compares Pakistan’s strategies with other countries specially South Korea. Pakistan adopted industrialization as a main pillar of development. Severe deficiencies in economic, industrial, and human resources, characterized Pakistan in 1947 at the time of independence from the British raj. Structural transformation of a predominantly agricultural, inefficient and low performing economy was needed and the early economic managers decided to favour processes of industrialization in the early 1950s..The most compelling reason for industrialization was falling export prices of raw agricultural commodities and deterioration of the balance of payment situation. Therefore, the government developed trade policy instruments, economic incentives, and profits which facilitated industrial activity and discouraged other investment alternatives.. Broadly speaking, Pakistan’s industrial orientation of imports substitution industrialization possibly shows some similarities with Brazil’s pre World War II industrialization efforts under Getulio Vargas. However, unlike isolationism of Brazil, under the influence of dependency theorists, Pakistan was emerging from its unique post colonial experience and breakdown of custom union with India in 1949 which massively influenced on composition of foreign trade.. The state took a lead role in industrialization as was the case in Brazil and later in South Korea. In Pakistan, however, the basic strategy for industrialization was to use the public sector for capital accumulation and investment and then transfer the productive resources to the private sector.. In the absence of any significant large scale industry, the early industrial policy identified cotton and jute as the main primary exportable commodities along with the development of local consumer goods sector. Interestingly, Pakistan was producing 75% of the world’s production of jute without having a single jute mill and 1.5 million bales of cotton with a few textile mills. The strategy worked and the country started making progress towards industrialization. Between 1947-58, Pakistan achieved around 3% of economic growth rate while industry grew at the rate of 23.6% between 1949-54 and maintained growth rate of 9.3% by 1960.

The strategy for Industrialization and Performance in Pakistan, during the first decade, used the policy of Import Substitution industrialization, here in after called ISI, which has been called a classical and fairly successful period of ISI. The strategy laid the basis for rapid growth in manufacturing sector for the subsequent decades and helped create exportable surplus as well. The state intervened for creation and distribution of rents as well as tried to influence investment decisions in line with industrial priorities through licensing system, facilitating import of capital and intermediate goods with overvalued exchange rates. Policies such as protection against import of consumer goods along with provision of fiscal subsidies and availability of credit provided an environment in which high profits in industrial sector were possible in the early 1950s.

# **FINDINGS AND DISCUSSION**

# **Decontrolling and Early Liberalization**

During 1960s, the government changed a number of control mechanism and took pro-business measures. Imports were made easier with relaxed foreign exchange pressure due to foreign aid. The decontrolling and facilitation of industrial growth possibly generated surplus which led to increase in manufactured goods and in 1965 exports from Pakistan were more than South Korea, Turkey and Indonesia combined.

According to another estimate, in 1968, Pakistan’s export to OECD countries were more than Indonesia, Thailand, Turkey and Malaysia put together.. However, owing to various lingering issues of governance and institutional atrophy export growth could not keep pace and lagged behind other countries.

The government made attempts to strengthen ISI for intermediate and capital goods and export oriented industrialization (EOI) for primary and secondary goods. The Bonus Voucher Scheme (BVS) helped maintain two exchange rates for controlled imports and incentive for exports. And within three years of introduction of BVS in 1959, rapid increase in exports of jute and cotton was reported. Nevertheless, this intervention of the state was held responsible for derailing the long term industrialization processes.

# **Political Fallouts of Industrial Policy:**

Contrary to the government’s claim of ‘decade of development, some researchers call it ‘controversial sixties’. Therefore, owing to a popular perception about increase in inequality, low priority to social justice, social exclusion, and sugar shortages, a political labour movement against the regime caused downfall of the Ayub regime in 1969.It appears that the policy instruments and emphasis on ISI which Pakistan adopted were surprisingly similar to what South Korea and Brazil later designed after the military coups in 1961 and 1964 respectively.. However, the results, owing to the role of the state and political economic fallouts were different in the subsequent decades. South Korea kept on moving up the industrial ladder and Brazil had to change the policy orientation in the late 1970s. Pakistan underwent political upheavals in 1971 which affected the structure of economy in a fundamental way. In 1972, after dismemberment of Pakistan in 1971, the 'otherwise successful’ industrial policy and growth strategy was abandoned.

**Nationalization and Investing in Public Sector - The Third Decade:**

The independence of East Pakistan, in fact, created a new Pakistan as well. The primary reason was significant shifts in patterns of trade and industrial development. Before December 1971, around 50% of West Pakistan’s products were exported to the East Pakistan and 18% of its imports were from the Eastern wing . The Eastern wing was no longer part of Pakistan. On the political front, a civilian and democratic setup settled in power which promised to address the issues of inequality

# **Response to Concentration and Nationalization:**

The revelation by Dr. Mahbub ul Haq that 22 families and business houses have accumulated 66% of industrial assets owing to the wrong economic policies of the previous decades had created a charged environment against the private capital. In another estimates it was revealed that around 65% of loans from Pakistan Industrial Credit and Investment Corporation (PICIC) were given to thirty-seven monopoly houses while 70% of this disbursement was siphoned off by thirteen big business houses.

Therefore, the civilian regime while acting on its election manifesto against inequality, nationalized the industrial and financial sector. Industries related with capital and intermediate goods were the first targets and by the middle of the third decade banking and insurance sector were also brought under public sector. The regime strategically tried to break the nexus between financial and industrial capital. As result of such policies, with some exceptions, it is popularly believed that socialist populism under nationalization schemes precipitated a long term downturn in the economy and retarded the pace of industrialization. Others dispute such claims since decline in private investment had already started before 1972.

# **Economic Performance:**

During 1970s, bad luck factors such as bad harvest, floods, and oil shock10 of 1973-74 were significant reasons behind a perceived economic decline. Economic performance of the regime in comparison with 1950s was not dismal. It is argued that contrary to popular perception, growth rate of overall GDP were higher than 50s, agriculture growth was almost equal, though there was some decline in the manufacturing sector. In the case of Brazil, the oil shock is also cited as bad luck factor precipitating balance of payment crisis and industrial decline after the ‘miracle’ between 1964-74.

The growth rates during this period are given below. An interesting point is that the rate of growth in small scale sector increased from previous decade average of 2.7% to more than 7% during 1970s.

# **Industrial Performance in 2000s:**

Interestingly, since the start of liberalization under structural adjustment programmes in 1988, no government in Pakistan has been able to develop a viable and independent industrial policy framework. The policy emphasis has been on developing the World Bank and International Monetary Fund (IMF) compliant policy framework papers. As mentioned in the previous section, 1990s witnessed unambiguous decline in the manufacturing sector which possibly had linkages with the sequencing and structure of reforms.

Under the World Bank and IMF inspired growth strategy, the sixth decade is the period which witnessed more reforms and commitment of the Government of Pakistan in the direction of liberalization, deregulation, and privatization. However, paradoxically, the manufacturing sector did not pick up as it was thought to take off as a result of neoliberal reforms. In fact, as the table 3.8 shows, the growth rate increased but then contracted from 2005-06 onwards. As Zaidi (2005, p. 122) pointed out, the growth in manufacturing appeared to be short lived. However, the small scale industry shows some recovery after growth reversal which dipped to negative (-20%) in 2003-04.

# **Liquidity and Private Investment Situation:**

A key feature of the 2000s is the availability of liquidity in the market. However, Pakistan has not been able to benefit from this opportunity in terms of robust gains of private investment in manufacturing (Bengali, 2008). It has been argued by researchers that the state intervention has been dismal as compared to regional competitors in overall strategy of Pakistan’s industrial development. In addition, macro economic liberalization since 1988 has persistently removed many rents for the manufacturing sector, and did not usher any significant efficiency or accumulation gains (Nadvi and Sayyed, 2004). Empirical evidence shows that during the fiscal year 2007-08, gross fixed investment by the private sector grew by 0.9% in real terms while manufacturing received only 8.1% of the private sector investment. Foreign Direct Investment showed decline of 16.7% during the first ten months in comparison with the last year, it is, on the other hand, concentrated (67%) in financial, communication, and oil and gas sector. More than half (57%) of the total FDI comes from three strategically important countries i.e., UAE, USA, and the UK (MOF, 2008). Pakistan decided to industrialize and transform the economy soon after coming into existence. The main strategy of industrialization in Pakistan has historically been ISI13 with some interest in EOI. During the first decade the state deployed policy instruments to generate push for industrialization. The second decade encouraged and supported the private sector to accumulate and invest for industrial development. However, responding to the political pressure on the issue of economic inequality, the state brought public sector to prominence through nationalization during 1970s. In 1980s, the state could not rectify the inherited structural issues of the economy and the resource waste resulted in a near-failure of the second round of industrialization. The 1980s ended with the start of neoliberal ascendency under various forms of Structural Adjustment Programmes in Pakistan.

So far, no unambiguous breakthrough has been made in the manufacturing sector growth under the export-led growth strategy. In fact, the controversial growth spurt which started between 2004 and 2006 is fast declining. Pakistan seems to have reached a point where the state must try to understand industrial decline without losing the sense of history, institutions, and social and political processes. It must capacitate itself to provide vision, institutional arrangements, and coordinate structural transformation for industrial growth. The next chapter explores the role of the state as entrepreneur and conflict manager.

# **The Role of the State as**

Entrepreneur and Conflict Manager: The role of the state for rapid industrialization is central since it is a process of structural transformation and needs effective institutional arrangements to coordinate and encourage certain economic activities (Chang, 2004). Therefore, in industrialization the role of the state must be of entrepreneur who can conceptualize and also create institutional arrangements to coordinate resource allocations and growth strategies. The other role must be of conflict manager who can provide governance structures to execute public policy agenda while harmonizing the social and economic disequilibrium (Chang and Rowthorn, 1995b; Stein, 2003).

Industrial Development and the Role of the State: An important lesson of the dismemberment of Pakistan in 1971 is that when state fails to coordinate and execute industrialization for equitable economic change, social unrests become difficult to manage even with authoritarian military regime. It appears that without consciously building ‘meta-institutions of participatory politics’, the effectiveness of the state in managing conflicts is sufficiently weakened (Rodrik, 2007, p. 166). Therefore, imposition of military and civil oligarchy in multiethnic societies seldom creates national integration and developmental dynamism. In fact, repeated military coups d'etat challenge the legitimacy of the state’s existence itself and the country suffers (Noman, 1988).

# **Conclusion**

The present study tried to analyse the political economy of industrial policy of Pakistan. The analysis used the Institutionalists Political Economy framework which was developed to explain major economic changes involving institutional arrangements. Therefore, the role of the state as entrepreneur and conflict manager in Pakistan’s industrial development was scrutinized. Historical analytical perspective which is embedded in the framework provided the design of the study. The state has historically been an important player in economic change and structural transformation. For rapid industrial development both the late industrializers and now developed countries have used the institutional arrangements of the state. Most important role of the state has been in providing support systems for structural transformation of the economy from agricultural to manufacturing which has ultimately resulted in industrialization of almost every sector.

The state of Pakistan has also played an important role in industrialization efforts since it made the decision to structurally transform the economy through the ISI strategy. In pursuit of the goal, the state created organizations and financial institutions to fuel the ‘engine of growth’ and provided protection to domestic manufacturers against the foreign competition. It also provided subsidies and cheap foreign exchange for input imports. Despite these efforts, the early industrialization strategy exacerbated the development differentials between the East and West Pakistan. The state which was dominated by the civil and military bureaucracy could not establish participatory democracy credentials in a multiethnic and fragmented body politic of Pakistan.

The ramifications of inequitable industrial and economic growth were enormous. Before 1971, despite visible industrial growth, authoritarian state dominated by the military and civil bureaucracy failed to act as entrepreneur who could visualize and create choice sets for higher levels of equilibrium in the allocation of economic resources. The state failed to act as a trust worthy conflict manager who could address social, political, and economic grievances of the people. The state, however, partially succeeded in addressing the needs of a small group of people who could politically align themselves with the military regime. The small group of people included big business houses, top brass of the military and civil bureaucracy, landlords, and to a certain extent opportunistic politicians who were either industrialists or landlords. However, the small group could not ensure the continuous growth in the manufacturing sector as the state might have wished earlier.

Immediately after 1971, there was change in the balance of power in favour of the middle class but it remained for a very short period of time. The nationalization, land reforms, and administrative reforms programmes could not establish the credentials of Pakistan as entrepreneurial state which some countries of East Asia did manage to get. The post-1971 Pakistan is structurally the same Pakistan which was created in 1947. It still has a very low level of human development, it is still dominated by the civil military bureaucracy, and it is still trying to achieve industrial growth which could drive its society towards a sustained level of high growth path. Most importantly, the meta institution of participatory democracy is still weak and therefore the institutions of dispute settlement and management are fighting for survival.

The neo liberal reforms have added little to the growth of manufacturing sector and technological capability. Big push in the private and public investment in the manufacturing sector is still awaited though foreign direct investment has increased in oil and gas as well as telecom and financial sector. The state must understand that the ultimate saviour of the state is the state itself but weapon of the first and last resort are its people. They are human capital when skilled and an expression of population explosion when unskilled. They serve as engineers and doctors when trained and cause social unrest when deprived and illiterate. They are entrepreneurs when respected and fodder for antisocial canons when excluded from mainstream economic activities. The post-1971 state of Pakistan needs to understand that "industrialization is a necessary but not a sufficient condition for development" (Nixson, 2002). Perhaps, more than that Pakistan needs to learn from the experiences of its own past. However, for rapid industrialization the first important step is to develop a coherent development vision and industrial policy. The other policies such as labour, competition, and FDI policy should follow the logic of industrial policy. A key component of the industrial policy may be the re-distribution side of the economy to address rapidly increasing spatial and income inequality which has produced socially and politically inefficient results. In this sense, the state should not only be a facilitative agent for change, it should move ahead and become an entrepreneurial and institution builder which can provide viable governance structure for an equitable structural change.

To conclude, it may be said that the theoretical and empirical evidence presented in this study possibly built a case to argue that:

‘A major economic transformation in (or towards) modern economy requires a state which can effectively perform the roles of the ultimate entrepreneur and the conflict manager ‘

(Chang and Rowthorn, 1995b, p. 46)

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