

## Inaugural Address

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It is a matter of great pleasure and privilege for me to inaugurate the Eighth Annual General Meeting of the Pakistan Society of Development Economists and to address such a distinguished group of professional economists and policy-makers.

Many of you will recall Lord Keynes famous remark, "Every politician is a slave of some defunct economist". Perhaps the only way for a politician to escape that Keynesian trap is to remain an economist. That is what I am trying to do, but I have begun to realise that the principles of good economics cannot always be reconciled with the requirements of politics. Similarly, a Finance Minister cannot always be both popular and patriotic at the same time. Often he has to make a deliberate choice of taking unpopular decisions in the national interest.

This meeting of development economists is being held at a time of momentous changes in World history. The post-war debate between capitalism and socialism appears to have suddenly ended, in favour of the former. Some writers have even called it 'the end of history'.

This debate was a very important part of the cold war, in which throughout the past 40 years, theoretical and academic discussions of the merits and demerits of the two systems became a parallel battleground, along with the geopolitical struggle on spheres of influence.

Many of us have argued passionately in this debate on one issue or the other. It will be very opportune to look back on this debate in Conferences like this, and draw some lessons for future policy. If I were to offer my own version of this obituary, I could highlight the following:

- The debate between capitalism and socialism was essentially about the inherent conflict between the objectives of freedom versus the objectives of equality. The ultimate utopia of human existence must be to find a system that can combine both these objectives but so far the choice has to swing from one to the others every 10 to 20 years;
- Under a socialist system citizens are required to work hard without many material incentives, for the good of the community. For short periods,

under charismatic leaders, some countries did achieve outstanding results. But as these economies grew more complex, it became more and more difficult to maintain discipline or to generate enough motivation for enterprise, technological innovations or sustained hard work without commensurate material rewards;

- Over centralisation of decision-making through central planning and regulated prices, have been the most significant causes of the failure of these systems;
- Basically the demise of socialism shows that man as a whole has not yet evolved to a level of maturity or selflessness that he would sacrifice individual rewards for collective benefit. Also the political system that determines collective priorities may itself be less than legitimate;
- What has succeeded in relation to socialism is not capitalism in its narrow economic meaning, but liberalism with its broad political implications. A free-market-oriented system can succeed only if there is democratic pluralism and a political framework based on the rule of law;
- One crucial set of lessons of what is happening in what was once the Soviet bloc pertains to economic policies. The collapse of economic and political systems in that part of the world serves to dramatically emphasise that in a world of increasingly rapid changes and technology, in business organisations and methods and in economic conditions, there is a growing premium on the syndrome of competitiveness, flexibility and openness – openness not just to trade but equally to ideas, and foreign investment and business methods; and
- The emphasis on freedom of speech, choice, mobility and action does not mean that such a system will automatically achieve the objective of greater equality. The government will have to continue to intervene, through fiscal policy and public expenditures in favour of the weak and the less privileged.

### PAKISTAN'S EXPERIENCE

Pakistan has always had a mixed system, with changing emphasis on the roles of the public and private sectors. In the 1960s the country was moving towards greater liberalisation of investment and imports with notable success but the debate about growing inequality started prematurely in the early 1970s leading to large-scale nationalisation and greater regulation of private sector activities. Since we did not have even the minimum political prerequisites for a socialistic system, we got the worst of both the systems namely bureaucratic socialism.

Now after almost 2 decades, we are again moving towards a deregulated and market-oriented system through wide-ranging reforms. The reform programme aims

to create a much more open, liberalised and privatised economy. An economy in which private savings, investments and energies will be stimulated and diverted from activities of dubious economic merit such as real estate speculation and seeking favour and privileges – what economists call “rent seeking” – to more productive areas and more efficient uses. Relatedly and as importantly we seek to create an economy in which by reducing its reach, the public sector will be more effective in undertaking activities which it can more usefully accomplish. This is perhaps an aspect of the Government’s reform programme which has received rather less attention than the other side of the coin, viz liberalisation and privatisation. It means in addition to the right incentives and a supportive policy framework, such tasks for the public sector are the development of human resources and alleviation of poverty as well as the provision of infrastructural support and environmental protection.

But we must be careful not to go to the other extreme and let the debris of the erstwhile Soviet bloc bury the concerns about unbridled capitalism that inspired socialism and its various experiments nor some of the successes of these experiments. One of these concerns, of course, was about equity or social justice. Another set is subsumed by the recognition of the need for an appropriate regulatory and legal framework for the private sector. These are the two sets of issues that I shall focus upon in the rest of my remarks.

### **THE SOCIAL AGENDA**

The accelerated economic growth that will ensue from the economic reforms programme that we have launched, will of course, help in improving the living conditions of the poor. However, we must not take that for granted. Economic growth is not a sufficient condition for poverty redressal. Not only must we ensure that the less privileged fully participate in the process of growth but also receive a significant share of public sector programmes and expenditures. This is not only an ethical issue but the very sustainability of economic policies is unlikely, if their benefits are not in fact, and in perception widely distributed.

There is another aspect of the complementarity between growth and distribution and here I refer to the mutually reinforcing relationship between economic growth and human resource development. Education, especially of females, health, population growth and economic progress are bound together in a seamless web. An important objective of improved progress in the social sectors must be a lower rate of population growth. This is absolutely necessary for ensuring that per capita growth be sustained.

### **RULE OF LAW IN ECONOMICS**

The other set of issues concerning the role of the State in a more “liberal”,

market oriented is to use a more recent and fashionable phrase “market friendly” – economy that I would like to talk about today is pertaining to the State’s functions in enunciating and enforcing rules. This is not merely an issue of enforcement of contracts. It encompasses something wider and something I will call the “rule of law in economics”.

Whenever, we refer to the rule of law in society, the issues commonly raised include the country’s judicial system, the role of the police and other law-enforcing agencies and respect for the Constitutional laws of the country. The concept of the “rule of law” in the realm of economics has not received much attention in Pakistan, so far. The evolution of the deregulated economy that we are trying to create and its successful operation require that the concept and its practical implications are fully explored and implemented.

The framework for the rule of law in economics should have the following basic elements:

1. Evolution of a legal framework under which all economic transactions are conducted and adherence by the financial sector to sound criteria for lending based on the merits of the case, and to prudential regulations and recovery of loans;
2. Avoidance by policy-makers of consideration of personal gain and of granting favours at the expense of the national interest in the formulation of policies.
3. Transparency in the design and implementation of rules and regulations which should apply without discrimination and a process of accountability which is based on objectivity and fairness.
4. Curbing tax evasion and other such practices in the private sector e.g. violation of safety and environmental regulations or consumer protection regulations; and
5. Preventing the creation or operation of monopolistic practices and relatedly rewarding those economic activities which benefit society rather than the acquisition of rents.

These elements of the rule of law have profound implications for the system of incentives, including trade policy and the regulatory function of government. They also imply responsibilities for the private sector and a social compact under which it operates.

In the coming weeks, we hope to formulate and implement policies in both these areas: namely more balanced social and economic development, and evolving a framework for the rule of law in economics.