8

State-Society Conjunctures and Disjunctures: Pakistan's Manufacturing Performance

Asad Sayeed

INTRODUCTION

That there has been general disillusionment with the pace, structure, and direction of economic development in Pakistan is recognized across the ideological and political spectrum. Since large scale manufacturing[1] (henceforth LSM) was perceived as an important engine of economic growth and development, the lackluster performance of this sector is regarded as wholly or partly responsible for Pakistan's development failures.

Much has been written on the ebbs and flows of Pakistan's development trajectory over the last fifty years. The LSM sector has also been the focus of inquiry in many scholarly works as well as in reports of international organizations. A running theme in the literature is to analyse the successes and failures in terms of policy instruments used. Moreover, the policy sets are couched in dichotomous terms. Market vs. state, private sector vs. public sector, import substitution vs. export promotion, small vs. large, etc are the usual benchmarks when performance is to be judged. Similarly, political phenomena are explained by dichotomies of democracy vs. dictatorship, centralization vs. decentralization, etc—usually the pattern is that the success of one is pitted against the failure of the other and the way forward is generally shown within this restricted choice set.

The lesson that we learn from Hamza Alavi's scholarship is that economic phenomena are inextricably linked to social and political structures, both nationally and internationally. This is not to deny the role of policy induced failures or of formal political institutions. Methodologically, it is necessary, however, to explain the social processes and more importantly the distributional struggles that underpinned policy failures or changes in formal political arrangements. In this study, we attempt to locate these essentially structural concerns in understanding the fortunes of the LSM sector in Pakistan.

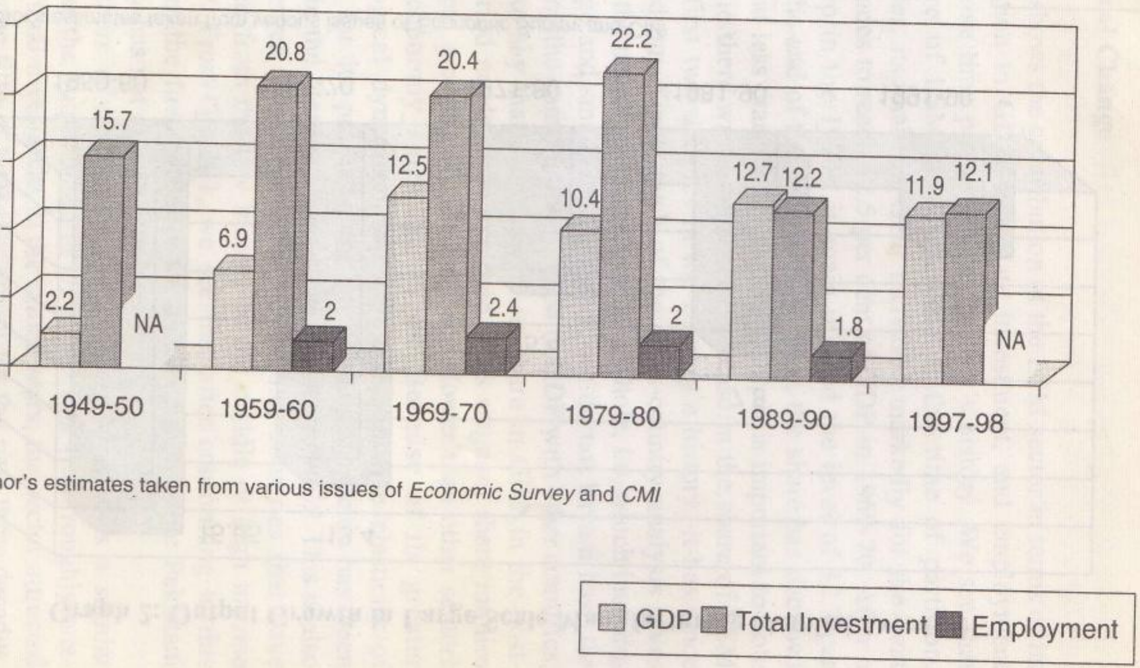
Section I is descriptive and is intended to set the stage for further discussion. It provides a bird's eye view of LSM in Pakistan. Section II puts forth some important theoretical constructs which we will subsequently use in explaining the performance of the LSM sector in Pakistan. Section III forms the main body of the chapter. In this section, we explain the political economy determinants of policy and performance in LSM in different periods of the country's history.

I

Large Scale Manufacturing in Pakistan: A Bird's Eye View

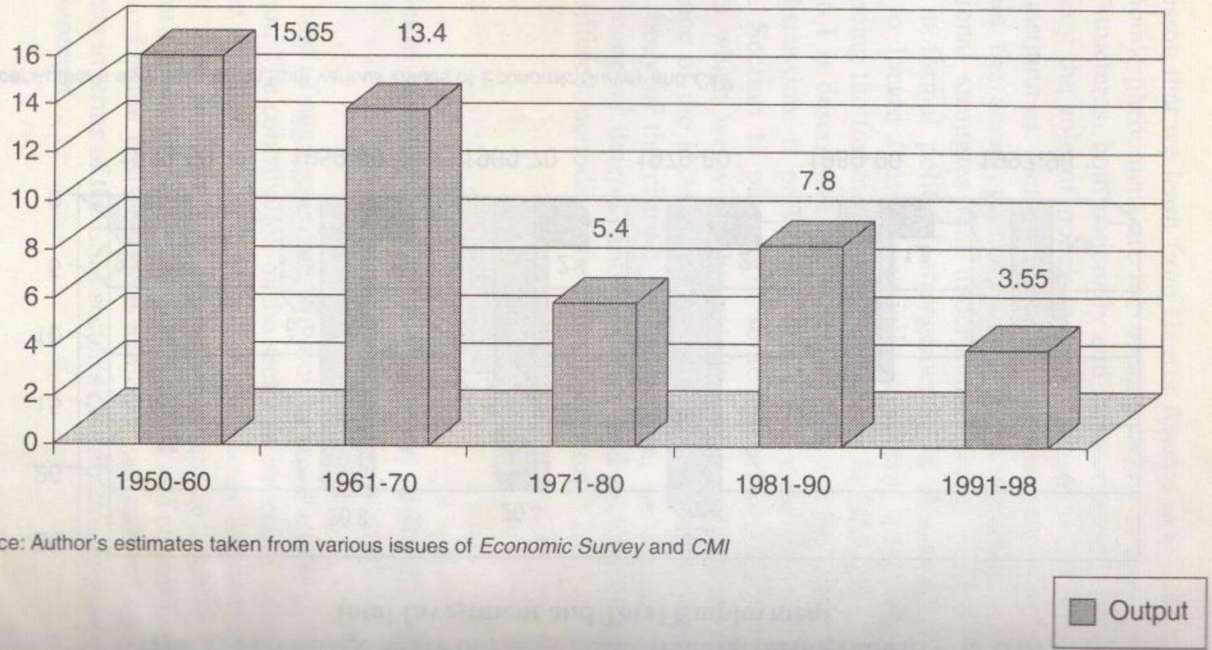
With the help of aggregate data, we look at broad trends in the LSM sector. The contribution of the sector in structural change within the economy as well as within the sector is presented first. We then look at various performance indicators of manufacturing—in terms of growth, efficiency, and employment generation. On the basis of these numbers, we then interpret these results in terms of the LSM sector's contribution to growth and development.

Graph 1: Percentage Share of Large Scale Manufacturing Industry in GDP. Total Investment and Total Employment.



Source: Author's estimates taken from various issues of *Economic Survey* and *CMI*

Graph 2: Output Growth in Large Scale Manufacturing (Annual Average)



Source: Author's estimates taken from various issues of *Economic Survey* and *CMI*

Structural Change

Graph 1 shows the contribution of the LSM sector in terms of its contribution to GDP, aggregate investment, and employment for discrete time periods in the country's history. We see that the share of LSM was miniscule at the time of partition. Thereafter, its share in GDP increased markedly for the next two decades to reach 12.5 per cent of GDP in 1969-70. After a slight dip in the 1970s, it again reached the level of 12.7 per cent at the end of the 1980s. Since then, the share has declined slightly at less than 12 per cent of GDP. It is important to note that while there was a consistent increase in the share of LSM for the first two decades in the country's history, it has since plateaued out. Since much of the cross-country analysis gives data for the manufacturing sector as a whole, i.e. which includes both large and small scale industry, we do not have a base for comparing the contribution of LSM to GDP with other countries. Suffice to say that stagnancy in its share in GDP in the post-1970 period needs to be explored. This stagnant share implies that output growth of LSM has been slower than other sectors in the economy since the 1970s. Because of its greater technological dynamism and increasing income elasticity of demand for its products, the manufacturing sector has been viewed in the literature as the 'engine of growth'.[2] This is also the observed pattern in those developing countries that have graduated from the low income to the middle or high income category. From Graph 1, we see that after conforming to this pattern in the first two decades of its existence, the Pakistani economy has not diverged in later years.

The share of investment geared to LSM follows a similar pattern as the output share in GDP. Starting from roughly one-sixth of total investment in the initial years, the sector attracted roughly one fifth of total investment for the next three decades. Thereafter, its share has declined considerably. In the late 1980s and the 1990s it is only half of that in the late 1970s and most of the 1980s. Much more detail will be required to explain investment patterns. This snapshot picture merely points towards changing policy priorities with regard to the sector. We will see later (in section III) how this lowering in the share of investment has changed the growth pattern in the 1990s.

LSM has consistently attracted a remarkably small share of employment. As Graph 1 shows, its share has never been more than 2.4 per cent of the employed labour force in the country. Moreover, we again see the share to be declining since the 1970s. For the 1980s and 1990s, it needs to be noted that the share of employment in LSM is understated. Contract and irregular employment, which is not reported, has increased considerably since the 1970s, and especially in the 1980s and 1990s. Systems (1989) has estimated that in 1988 as much as 25 per cent of employment in LSM was not reported.[3] Be that as it may, the chart clearly shows that the employment generation capacity of the sector has lagged far behind its share in GDP and investment.

The obvious reason for low employment elasticity in the sector is high capital intensity. While much has been written and argued about how capital intensity is a policy failure in LSM, some important issues need to be highlighted. The nature of some industries in manufacturing are to a great extent capital intensive for technological reasons. Capital intensity in other sectors exists because developing countries import technologies from developed countries where labour rather than capital is relatively scarce. This obviously points to the development of a capital goods industry in developing countries so that such distortions in factor use do not occur. However, it should also be appreciated that technology is often embodied in capital goods and one cannot be had without the other. Also, the structure of demand in developing countries as well as the quality of human resources is such that the pattern of industrialization is sequential, with consumer goods production for purposes of import substitution taking priority over intermediate and capital goods. As such, late developers are to some extent locked in—so to speak—with technological developments that are beyond their control.

The literature on linkages *á la* Hirschman (1958) and others has also argued that dynamic processes unleashed by LSM mean that this sector alone is not the appropriate place to look for employment gains. Through forward and backward linkages, LSM generates employment in small scale manufacturing (through sub-contracting) as well as the services sector. For this process to work, however, it is important that the LSM sector is dynamic with regard to its own internal structure and plays a lead role in growth.

We now move to see what has happened to structural change *within* the LSM sector. The established pattern for structural change within manufacturing is one where there is a steady move away from consumer goods production towards intermediate and capital goods industry.[4] Table 1 vividly draws out the failure of LSM in Pakistan on this very important criterion. We see that very little has changed over a period of thirty-five years in the shares of consumer and capital goods. We see the share of consumer goods to have declined, albeit marginally, between 1970 and 1990. But thereafter there is again an increase in the share of consumer goods, driven largely by increasing output in the share of the textiles and leather sector. This is partly because of increasing exports from this sector, but also because of massive investment that went into this sector in the late 1980s and the early 1990s. The share of capital goods sector has been virtually stagnant. Linking this piece of information with the discussion above, we see that low employment elasticity in LSM over time is not justified because there has been little structural change towards the capital goods industry, which in turn could have contributed in producing machinery which was more in line with relative factor endowments in Pakistan.

The share of intermediate goods, however, has increased from roughly 30 per cent in 1960 to 34 per cent in 1995, after having peaked at 38.6 per cent in 1985. The fact that it peaked in the mid 1980s is explained by the large public sector projects in cement, fertilizer, etc gestating around the mid 1980s.

Table 1
Structural Change in Industry
(% shares in total industrial value added) 1960-95

Industries	**1960**	**1970**	**1980**	**1985**	**1990**	**1995**
CONSUMER GOODS	60.5	60.9	53.8	52.6	54.2	58.1
Food, beverages & tobacco	14.4	23.3	31.2	31.7	23.0	25.4
Textile garments & footwear	42.7	33.7	19.7	17.6	27.4	29.2
Other	3.4	3.9	2.9	3.3	3.8	3.5
INTERMEDIATE GOODS	30.7	32.5	35.6	38.6	35.6	34.0
Cotton Ginning	3.8	3.1	1.8	1.5	1.2	1.1
Industrial Chemicals	6.2	5.9	5.1	8.7	7.3	7.4
Petroleum Refining	-	8.0	6.4	1.4	2.3	1.8
Non-Metallic Mineral Products	6.4	4.3	7.5	6.9	8.0	7.8
Iron & Steel	6.9	2.4	4.0	10.6	6.3	5.0
Others	7.4	8.8	10.8	9.5	10.5	10.9
CAPITAL GOODS	8.8	6.6	10.6	8.8	10.2	7.9
Machinery (including Electrical)	5.0	4.6	4.9	5.5	6.7	5.1
Transport Equipment	3.4	1.4	5.2	2.6	2.9	2.2
Other Capital Goods	0.4	0.6	0.5	0.7	0.6	0.6
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Zaman Associates (1997), p 19.

Growth in Large Scale Manufacturing

Graph 2 gives decade-wise real growth rates in the LSM sector. It is more or less a declining pyramid. Growth in value-added was the highest in the 1950-60 period. This occurrence, however, needs to be contextualised. Areas which constituted Pakistan were devoid of any large scale industry at the time of partition. As such, any investment in manufacturing soon after would result in growth rates to be very high.[5] LSM growth of 13.4 per cent per annum in the decade of the 1960s is, however, different. After having completed the initial phase of import substitution, growth in this decade demonstrated elements of an industrial take-off. A glance at the Table shows that in subsequent years this did not happen. The reasons for aborting this take-off are addressed in section III. The 1970s were marked by an investment strike by the private sector and a concomitant increase in the role of the public sector in LSM. While the early 1980s reaped the benefits of public sector investments made a decade earlier, in the second half of the decade private sector investment confidence was revived and contributed to a fairly respectable growth performance. The Graph also reveals that the first eight years of the 1990s demonstrate the lowest growth on average in the country's history. This is, interestingly, also the period when liberalization and structural adjustment have ruled the roost in the country's economy.

Productivity Performance

To take the cloak off high growth rates, it is important to gauge efficiency of resource use. The most comprehensive indicator to this end is the joint productivity or Total Factor Productivity (TFP) estimate. The virtue of a TFP analysis is that rather than measuring productivity of labour and capital separately, it separates the sources of (in)efficiency from the pure contribution of factor inputs. This 'residual', usually consigned to technical change in the literature, can alternatively be used to explain a host of other factors affecting the efficiency of factor use.

Unfortunately, consistent TFP analyses have only been carried out for discrete time periods in Pakistan. In Table 2, we present data on TFP growth for 1960-70 and 1980-91.

Table 2
Total Factor Productivity Growth: 1960-70 and 1981-90 (% per annum)

Period	TFP Growth
1960-70	5.06
1981-90	0.72

Source: TFP analysis for 1960-70 is taken from Kemal (1978, p. 136) and for 1981-90 from Sayeed (1998a).
Note: TFP is calculated from the growth accounting method. For a description of the method and its relevance in the Pakistani case, see Sayeed (1998a, Appendix 1).

In the table above, we observe the stark difference in productivity growth in the two periods. Efficiency in the LSM sector was far higher in the 1960s compared to the 1980s. In the 1960s, the productivity performance of the LSM is truly impressive, especially when compared to that of other developing countries. TFP growth in Pakistan was higher than that of Argentina, Brazil, Mexico, Thailand, and Turkey.[6] It is important to note that except for Thailand, all the other countries had a much longer history of development, especially in manufacturing.

The depth to which Pakistan had sunk by the 1980s is exemplified by the fact that its productivity performance in this period was worse than all the countries mentioned above.[7] If high output growth is associated with low productivity growth, as it was in the 1980s, it is symptomatic of underlying inefficiencies in resource use. A decomposition analysis of the sources of growth for the 1980s shows that 82.3 per cent of growth in the sector was due to incremental capital input. The share of the capital input is excessively high when compared to that of other developing countries. According to Chenery's analysis, the capital input contributed only on average 39.3 per cent to output growth in the LSM sector for developing countries as a whole.[8]

This is an important result as it draws out differences in the growth regimes of the 1960s and 1980s, which are otherwise considered to have fairly similar growth trajectories. For political economy purposes also, it is important to note that in both periods, the political reins in the country were in the hands of military dictators.

Conclusion

This brief and aggregated foray into numbers demonstrates that the LSM sector has, on the whole, failed to provide the requisite stimulus to growth and development in the country. While its growth for certain discrete periods of time has been high, it stopped assuming the lead role in contributing to overall GDP growth since the late 1970s. More importantly, for much of the country's history, it has consumed a large chunk of the investible surplus in the economy with very little to show in terms of either structural change, employment generation, or efficiency in resource use. We explore the political economy causes for this performance in Section III.

II

Methodological Issues in Political Economy

As mentioned in the introduction, assessments of the LSM sector in Pakistan have centred around the appropriateness or otherwise of the policy instruments used. A critical analysis of the policy tools used and their efficacy in Pakistan's case can be found in Sayeed (forthcoming). The implicit political economy assumption about analyses which focus on policies is that the state is able to formulate and implement policies at its own behest. This implies that the state structure is assumed to be all powerful. The structure and character of the state is thus conceptualized either as predatory[9] or approximating the simple Marxist conception of the state as being a hand-maiden of a single dominant class.

In both these conceptions of the state, society and social forces are putty in the hands of the state structure and state personnel; to be moulded in whichever way it is deemed fit to further the interests of the ruling elite. As Alavi[10] notes, this conception is derived 'essentially from the experience of advanced capitalist countries and are premised on the existence of a single economically dominant class, i.e. the bourgeoisie, as the ruling class.'

Alavi has contributed substantively to reject these simple formulations of the state by introducing the concept of the 'relative autonomy of the state'.[11] He has argued that in post-colonial societies, and in South Asia in particular, there are contending proprietary classes, but none powerful enough to dominate the state. As a consequence, state policies are not formulated at the behest of any one class, and in that sense are autonomous. The autonomy of the state is, however, *relative* and is constrained by the need to 'preserve the social order in which their (the contending proprietary classes') interests are imbedded, namely the institution of private property and the capitalist mode of production as the dominant mode of production'.[12] While an important methodological advance in state theory, this approach also appears static. This is because it falls short of introducing the notion of relative power balances, both within dominant classes and between the state structure and other social forces that exist in society.

A new stream in state theory—broadly labelled as the 'state in society' framework—uses the conceptual apparatus of the embeddedness of the state within society as a dynamic phenomenon. The work of Migdal as well as that of Kohli, Migdal, and Shue does away with the assumption of the omnipotence of the state by introducing the concept of the state-society power relations as determining social, political, and economic outcomes.[13] This methodological framework enables us to understand the shifting power balances between the state and society as well as within society. This approach thereby provides the necessary analytical tools to understand the social bases of policy formulation at different times in Pakistan's history as well as the increasing gap between policy formulation and implementation.

In the state-society approach, not only is it necessary to specify the particular state structure that exists but also the changing power balances among different groups and classes within society. At any given point in time, the state-society balance can be conceptualized as the existing political settlement. The political settlement is defined as:

> The political balance which constitutes the alignments and mobilizations behind an existing structure of economic rights—once a major political settlement is arrived at, the rights its supports are not infinitely variable, though marginal changes can and are attempted.[14]

The political settlement, in turn, is conceptualized as setting precise limits to the relative autonomy of state personnel to pursue any given set of policies. Obviously, a serious economic or political crisis can compel state functionaries (both civilian and military) to take autonomous action in changing the political settlement. But, as we shall see subsequently in this chapter, their success in doing so is again deeply conditioned by the inherited political settlement.

We further conceptualize political settlements leading to conjunctures and disjunctures in state-society relations. A *conjuncture* in the state-society interface refers to a political settlement where the state structure reflects the balance of power that exists in society. In such a political settlement policy formulation by the state will reflect the interests of those groups in society who are economically and politically powerful. Moreover, the relative power of these groups *vis-à-vis* other social groups in society is such that, with the help of the repressive machinery of the state, they can successfully ward off challenges emanating from others. Where such a political settlement exists, *ceteris paribus*[15], the gap between policy formulation and implementation will be narrow.

In a political settlement, where a *disjuncture* between state and society exists, the dominant groups in society may still be powerful enough to influence state policy. But relative power in society will be disbursed to the extent that in order to maintain their property rights, the dominant groups have to make pay-offs to other social groupings or engage them in a patron-client relationship. To make pay-offs, the state requires resources. The long-run sustainability of a disjunctural settlement is unlikely as resource dole-outs for pay-offs will lead to a precarious fiscal situation. Moreover, in a disjunctural settlement, the state will continue to use repressive measures against social forces that challenge its writ. But this is not sufficient to ward off challenges emanating from society.

III

State-Society Interface in Pakistan and Industrial Performance

The Conjuncture Years: 1947 to the late 1960s

Pakistan's inheritance in terms of both state and social structures was typical of the trend in de-colonization witnessed elsewhere. The state, in terms of its administrative structures, was a mirror image of the colonial state.[16] An elaborate and centralized bureaucratic network, where there was little room for democratic governance, formed the substance of the post-colonial state in Pakistan.

The other important arm of the colonial state was the army. That one of the major recruiting grounds of the British Indian army was central and northern Punjab is well documented. These two arms of the state—commonly referred to as the military-bureaucratic oligarchy—were able to establish their authority in post-partition Pakistan simply because their institutional structures were intact and merely needed 'some minor revamping.'[17]

Perhaps the most unique feature of West Pakistan was that the political party which had successfully rallied for carving British India along communal lines landed in power in a country where it hardly had an indigenous support base.[18] The import of this phenomenon can be fully understood if the social structure in West Pakistan at that time is understood.

The social structure of West Pakistan at the time of partition was unique in the sense that neither did a substantial and a politically mobilized middle class exist, nor did the country inherit an industrial bourgeoisie. The only dominant class at that time was the landed and tribal elite. Since an important element of the landed elite was aligned with the pro-British Unionists, fissures and distrust between them and the Muslim League hierarchy were palpable.[19]

This equation meant that the bureaucratic-military oligarchy gained the upper hand in running affairs of the state. The ascendancy of the oligarchy had important implications for industrialization. Both the bureaucracy and the army were convinced that unless the country industrializes swiftly, the very survival of the nation state is in jeopardy.[20]

Industrialization was deemed necessary by what Lewis describes as the structural disequilibrium inherited by Pakistan.[21] The first phase of industrialization thus concentrated on import-substituting goods that were manufactured in what was now India. After the break-up of the customs union, this was no longer possible.

We saw in section I that growth rates of LSM during the period were high. There were three important policy decisions on which this high growth regime hinged. The first was to maintain an overvalued currency. This policy also served to turn the terms of trade against agriculture as a large component of exports came from agriculture while imports were mostly for industry. The second policy decision was to protect industry through tariff and non-tariff barriers. Protection was kept highest for agro-based industry and consumer goods and progressively lower for intermediate and capital goods. The third element was import licensing. Initiated earlier on to monitor scarce foreign exchange outflows from the country, it became an important tool for chanelling industrial investment. As a result, the state not only succeeded in affecting industrial growth but also influenced the decisions on what sort of industry should be put up.[22]

There is ample evidence to suggest that these policy instruments were implemented and the growth that ensued can be causally linked to them. If we look at these policy instruments from the lens of the above enumerated political economy framework, we see that the bureaucratic-military oligarchy was able to ride roughshod over the interests of the only dominant class at the time, i.e. the landed interests. The maintenance of an overvalued currency as well as the sharp bias in terms of trade against agriculture went directly against the economic interests of the landed elite.

Though the existing political settlement was able to launch large scale industrialization in Pakistan, it led to numerous other destablizing forces in the economy and polity. In the economy, the agricultural sector had been badly neglected and was unable to meet the food and raw material needs of a burgeoning population. On the political front, power struggles within the elite were rife. Struggles for domination between the eastern and western parts of the country, between the oligarchy and the politicians, and between the largely migrant political elite and the landlords were central features of this process.

The first phase of praetorianism in Pakistan sought to stablilize the political settlement. The first impact of martial law was that the space for Muslim League politicians was foreclosed. As a result, one of the elements, largely urban and migrant, was eliminated from the power equation at the stroke of a pen. However, the regime needed legitimacy. Since the strength of numbers at that time was in the rural hinterland, the most effective channel for achieving this goal was to develop a constituency for itself among this group. This was the area where the erstwhile Muslim League politicians had no support base and any mobilization of urban groups could be effectively challenged by a numerically larger and hitherto economically more powerful agglomeration. However, to develop a broad-based and numerically strong constituency, the Ayub regime needed the support of the numerous medium and small peasants, especially in the Punjab. By mobilizing the middle peasantry, the regime could not only checkmate the designs of urban-based politicians but could also check the large landlords from acquiring inordinate political power in the dominant coalition.

Two important decisions of the military regime in 1959 were to serve the purpose of creating a rural constituency for itself. One was land reforms and the other was the institution of Basic Democracies (BDs). Given that land reforms were a rallying cry among the non-landed elements of the dominant coalition, the reforms sent the signal that the landed elite was being cut down to size. However, not only were the land ceilings rather liberal and implementation of reforms slack, but there were enough loopholes in the land reform order to ensure that the land holdings of the large landlords remained intact. This decision of the regime meant that the economic rights of the landed elite were not a bone of contention for some time to come.

Similarly, the BD system mobilized a large part of the middle peasantry in areas where its numbers were substantial. The incipient mobilization of a rural middle class can be identified through this particular institution. The mobilization of a rural middle class should, however, be seen as a balancing act on the part of the regime. The dominant partners from the hinterland in the settlement continued to be the landed elite. The third important element in the equation of the Ayub settlement was the incipient industrial bourgeoisie. By bringing about a settlement in the rural areas and repressing industrial labour, the regime could divert resources towards a small group of merchant capitalists for developing the industrial sector.

So far as the middle class in urban West Pakistan was concerned, it was bereft of groups with much political weight. The urban petty bourgeoisie was largely un-mobilized. The Ayub regime for some time was able to circumvent their organization by using both the carrot and the stick. With healthy economic growth and the increasing role of the state in both the economic and social aspects of life, the Ayub regime was able to co-opt the immigrant petty bourgeoisie, mainly based in large cities, through jobs in government departments and the numerous public and semi-autonomous institutions that were created during the period. Since the numbers were relatively small in the earlier decades, the absorption of this class was manageable. On the other hand, through a series of repressive legislations, organizational rights of the urban middle class were restricted.[23]

This was the high point of conjunctural politics in Pakistan. A political settlement was created where all opposition to the dominant groups in the state structure was successfully contained by the state. It was on this edifice of economic and political rights, or the lack thereof, that the high growth industrial regime of the state should be interpreted. It should also be noted that the political strategy of the time was in consonance with the social structure that existed on the ground.[24]

The industrial policy of the regime consolidated on the gains made in the first decade of the country's history. Based on a political edifice where the state found enough autonomy to allocate resources, the industrial policy of the state was based on unabashed capitalist premises. Articulated in the Second Five Year Plan (1960-65) the cornerstone of this policy was that industrial growth will be private sector and large scale industry based and that the now (in)famous doctrine of functional inequality *à la* Mahbubul Haq[25] will mean that resources will be diverted to a small base of industrialists rather than be spread out more broadly. The policy also articulated the need to diversify the industrial sector towards exports and higher stages of import substitution.

The most important policy tool used during the period was the Bonus Voucher Scheme (BVS). The BVS created an incentive structure for export promotion at a time when the tariff structure was still protectionist. Thus, the goals of both export promotion and import substitution were pursued simultaneously.

There is a common misperception in Pakistan that the Ayub government had 'liberalized' the industrial sector. Looking at other policy tools prevalent at the time, we can see that this was not the case. Although the Ayub government did away with the import quotas imposed in the mid 1950s, import licensing and industrial sanctions remained intact. These two instruments coupled with high tariff barriers meant that resource allocation remained firmly in the hands of the state.

That the industrial policy of the state succeeded in achieving the goals it set for itself was demonstrated in section I. Not only was high output growth maintained, but high productivity growth meant that efficiency in resource use was also present. Moreover, export growth during the period was significant. Who could believe in 1999, that in 1965 Pakistan's manufactured exports were greater than that of South Korea, Turkey, Thailand and Indonesia put together!

The ability of the state to control resource allocation is exemplified by its response to the foreign exchange crisis that occurred in the wake of the 1965 war and the drought that followed in 1966. Investment schedules were revised, industrialists were directed to enhance exports while foreign exchange availability through the state-controlled financial institutions (PICIC and IDBP) was reduced. These developments go to show the dynamic nature of industrial policy at the time as well as the control the state had in such maneuverings.

It goes without saying that unbridled capitalism bears a huge social cost. It is now well documented and analysed that industrial growth was concentrated in the hands of the (in)famous '22 families'. Moreover, industrial labour was repressed and the process of industrial development in the 1960s was based on a profit-share strategy—a logical outcome of the doctrine of functional inequality. As Ahmed[26] shows, the profit share strategy meant that wages of industrial workers remained stagnant during the period and price reductions that should have occurred as a result of increasing productivity were retained as profits rather than passed on to consumers. These logical consequences of capitalist development should, however, not be seen as containing in them an inherent instability. Elsewhere, we have shown that arguments of instability based on the above mentioned factors do not stand up to close scrutiny.[27] The important point to note is that in the 1960s, the Pakistani state was able to achieve what it set out to do.

The Disjuncture Years: 1970 to the Present

The end of the 1960s marked a radical shift in Pakistan's economy and polity. So far as industrial policy and performance is concerned, as we saw in section I, the LSM sector has never reached the heights it attained in the previous period. Nationalization and increased public sector involvement in the 1970s, a high growth spurt in the 1980s, and a prolonged recession in the 1990s under a regime of liberalization have broadly marked the fortunes of this sector ever since.

It is but natural that the political determinants of this shift need to be explained. Below we briefly trace factors which resulted in transforming the political settlement from a conjunctural course to a disjunctural one. Analysis of industrial performance in subsequent years hinges on this explanation. We then analyse industrial performance in the Bhutto, Zia, and the present democratic era.

The Transformation from Conjunctural to Disjunctural Politics

The mass movement against the Ayub regime which finally culminated in its overthrow in 1969 and the coming to power of the Pakistan People's Party in the 1970 elections were critical indicators of the transformation of politics in Pakistan. These events were also indicative of an important shift in the balance of power in society.

What were the factors which led to this transformation? Our own work,[28] as well as that of others[29] link this development with changes that took place in the agrarian economy in the 1960s. The importance of the BD system in mobilizing a rural middle class was mentioned earlier. When this was coupled with mechanization and introduction of the Green Revolution technologies, this middle class gained economic power to complement its albeit restricted political clout.

The swelling in the numbers of the middle class was manifested by a swift increase in the growth of small towns. The population growth rate of towns[30] both large and small, was 4.7 per cent per annum between 1961 and 1972 whereas that of the cities was 4.1 per cent during the same period.[31] The 'elite farmer strategy'—as Alavi has called it[32]—which materialized as a result of the Green Revolution, filled these small towns with a large number of out-migrating middle and small landowners.[33]

The towns also consisted of a large number of the kindred of the small and medium landowners in search of upward mobility through education. As a result of fragmentation of land over time, particularly in the older settled districts of Lahore and Rawalpindi, those with enough cash to send their children to school and then for higher education also increased.[34] This factor accounted for a precipitous increase in the number of lawyers, the salariat and students, whose base was the small and large towns in the Punjab.

It was this class, created both as a result of the push and pull of agrarian transformations as well as the ambitions for upward mobility among the small and medium landowners that swelled the ranks of the middle classes primarily in the Punjab and to a lesser extent in Sindh and the North West Frontier Province.

The critical issue, however, is not the existence of a class 'in itself', but its mobilization to become a class 'for itself'. As we saw earlier, the rural middle class was given political voice through the BD system and the basic democrats diversified their economic activities in collusion with the bureaucracy. A similar outcome was sought by the agitators in towns to challenge the existent structure of property rights, though their impact was much greater than that of the basic democrats or even the landed elite because of the larger size of this class.

A conjuncture of events contributed to the mobilization of this class in the second half of the 1960s which eventually led to the demise of the Ayub regime. The first was a drought that afflicted the agrarian sector. This affected the agricultural service sector as well as the small time lawyers in the areas.[35] The drought also coincided with aid cut-off as a result of the 1965 war. The combined effects of these two phenomena created a severe economic downturn. The regime also lost a considerable amount of legitimacy as a result of Ayub Khan's perceived capitulation to India through the Tashkent agreement after the 1965 Indo-Pakistan war. The most important catalyst, however, was the resignation of Zulfiqar Ali Bhutto from Ayub's cabinet and his active search for a populist base for politics subsequently. In 1967, Bhutto travelled through the length and breath of the Punjab to seek the support of the middle classes, especially in smaller towns.[36]

The hitherto unmobilized middle class in the larger cities, dominated by the migrants from India, forged an alliance with the emerging middle classes in the towns of the Punjab to concretize the class formation of a group which could exert political pressure on the state to challenge the existent property rights structure.

It is important to note that the transformation to disjunctural politics in Pakistan actually initiated in the countryside. This is in consonance with Barrington Moore's thesis[37] that processes of accumulation in the industrial sector are often determined by transformations in the countryside.

Specific to the LSM sector in Pakistan, it is clear that the industrial strategy of the Ayub regime fell into disrepute only as part of the increasing contention of economic rights endowed by the state. However, much of the rhetoric employed against the Ayub regime during the agitation centred around the beneficiaries of industrial rights. This class was particularly vulnerable to such an onslaught because of two inter-related reasons. One, that it was the only proprietary class that the state had created and as such did not have any autonomous political base. Secondly, given that it was composed largely of migrants, it was not rooted within the country. This further eroded its legitimacy, particularly since the contention of rights initiated due to convulsions in the countryside. With the rise of this disjuncture between state and society, the resources which could be devoted to a small class of industrialists were no longer possible.

The Bhutto Years (1971-77): The First Phase of State Resurrection

The PPP had emerged as the majority party in the western wing of the country in the 1970 elections. As discussed above, Bhutto and the PPP played an important catalytic role in the mobilizations against the Ayub regime. In the more prosperous and urbanized provinces of Sindh and the Punjab, the hitherto dormant middle and lower middle class quickly turned to Bhutto to gain organizational impetus. This mobilization was maintained through the 1970 elections. The PPP government formed in December 1971, thus inherited a highly mobilized middle class as its central constituency.[38]

Among a number of other radical changes initiated by the new government, nationalization of key industries and the financial sector were most critical so far as the industrial sector is concerned. In its election manifesto, the PPP had pledged to nationalize key industries to break the stranglehold of a handful of industrialists on the means of production, as well as to promote certain capital and intermediate goods industries in accord with national planning imperatives. The Economic Reforms Order of 1972 fulfilled this electoral pledge of the party. Nationalization brought roughly 20 per cent of the value-added of large scale manufacturing under public ownership. While the employment index in these industries increased from a base of 100 in 1972-73 to 142 in 1976-77, the labour productivity index moved from 100 to 120 in the same period.[39] The nationalization of the entire financial sector on New Year's day 1974, however, had more profound implications. While there can be a number of economic justifications for a state-owned financial sector,[40] the context in which such a policy is undertaken determines its political economy outcomes. There were two considerations that prompted this move. First, it was used to break the monopoly hold of this class of entrepreneurs, since virtually all commercial banks and insurance companies were owned by the '22 families'. Second, and more crucially, keeping the financial sector under the wings of the state was also necessary if state resources were to be used as pay-offs to important constituencies.

The impact of the new policy regime on the economy was initially favourable. In the 1971-73 period, economic performance picked up after the events of the civil war in East Pakistan. Industrial output grew by 7.3 per cent and GDP grew at 6.9 per cent. Industrial growth during the period was export-led because of the devaluation of the rupee in May 1972. The devaluation was undertaken to correct the imbalance created as a result of the loss of markets for some industries because of the separation of East Pakistan. Coupled with a bumper harvest and favourable conditions in the world market, exports of cotton, cotton yarn, and cotton cloth in particular increased.[41] While a one-off increase in exports will be expected in the immediate aftermath of a significant devaluation, Ahmad and Amjad[42] show that another important factor for high export growth was the significant excess capacity which was created as a result of the loss of markets in East Pakistan.

This hiatus was, however, short-lived. The oil price shock and the floods in 1973 proved onerous exogenous shocks. Specific to LSM, private sector investment took a massive nose dive during the period. If anything, this was symptomatic of the assault on capitalist rights unleashed by the populist government. The government attempted to compensate for this phenomenon through increasing the rate of public sector investment.[43] However, as public sector investment was largely in capital and intermediate goods industries, the gestation lag of this investment meant that its dividends would not be forthcoming in the short-run.

The change in economic policies ushered in by the PPP government was the direct outcome of this, the first phase of disjunctural politics in Pakistan. It was reflective of changed political alignments and balances of power, both within society and thereby in state-society relations. As a result of the Anti-

Ayub demonstrations and the subsequent liberation of Bangladesh, the military—a central component of the oligarchy—as well as other elements of the dominant coalition had received a serious setback. On the other hand, other social forces, generally belonging to the middle class had seen their relative power increase. In this situation, it was an important window of opportunity on the part of the new government to restructure the state. Instead, it chose to resurrect the forces that had controlled the state earlier. The military operation in Balochistan in 1974 resurrected the military. The purge of the left from the government in 1974, and subsequent re-appointment of large landlords in the party were important signals in this direction.

The industrialists, however, did find their relative power reduced in the aftermath of the events in the late 1960s and early 1970s. The question to be asked, however, is relative power with regard to whom? There is evidence that with regard to middle class groups, the relative power of the industrial class did reduce. Nationalization, which explicitly benefited middle class groups in terms of employment as well as greater access of the emerging bourgeoisie in the distribution of credit demonstrates that the relative power of industry had reduced *vis-à-vis* this group. But in comparison to industrial labour, in spite of the rhetoric of the government and Bhutto himself, the state came to the rescue of the industrialists whenever there was a conflict between the two groups.[44]

The disjuncture between the state and other social forces under populism was unsustainable for the simple reason that pay-offs required to maintain stability were not there. The Bhutto government, therefore, resorted to ration these resources by attempting to appease some groups and coercing others. Important social groups—notably the *mandi* merchants, and those elements of the small scale bourgeoisie who were affected by the nationalization of small rice and cotton ginning units coalesced to launch a mass movement which subsequently resulted in the overthrow of the regime and the induction of another and more brutal martial law regime.

The Zia Years (1977-88): Exogenous Windfalls and High Industrial Growth

Referring back to section I, we see that LSM growth in the period was high. While figures in section I are for the 1980s, if industrial growth during the Zia years, i.e. 1977-88 is taken, it was slightly higher at 9.6 per cent per annum. We also saw in section I that productivity growth in the period was low and that this high growth regime was essentially driven by large capital inputs.

The most pertinent issue, therefore, in explaining industrial growth during the Zia regime is two-fold: one, to specify the sources of investible capital during the period and second, to see the manner in which this capital was allocated.

High stocks of investible capital in the period are largely explained by exogenous factors. As we see in the table below, although the role of foreign aid and loans in investment declined considerably during the 1980s, still credit lines from multilateral institutions were an important source for financing industrial investments.[45]

Table 3

Total Investment, Gross Domestic and National Savings

	Total Investment (% GDP)1	GDS* (% GNP)2	GNS** (% GNP)3	Loans and grants (1-3)
1960-61/1964-65	18.04	10.02	10.06	7.98
1964-65/1969-70	16.09	12.42	12.38	3.71
1970-71/1976-77	15.05	11.04	12.04	3.11
1977-78/1985-86	16.03	7.09	14.26	1.77

Source: Amjad (1986, p 763)

*GDS= Gross Domestic Savings = Total Investment - (Net Factor Income from Abroad+Loans &Grants)

**GNS = Gross National Savings = GDS+Net Factor Income from Abroad

In Table 3, we see that the share of domestic savings as a proportion of GDP had also declined to roughly 7 per cent of GDP during the period. The gap between savings and investment was filled up by Gross National Savings (GNS). As the GNS identity shows, this difference comes from an increase in Net Factor Income from abroad during the period. The source of the increase in NFI is foreign remittances from overseas Pakistanis. As we see in the Table, roughly 50 per cent of investments in the period were financed through remittances.

Foreign remittances were not only important in plugging the savings-investment gap, but they also proved instrumental in tiding over the perennial Balance of Payments problem that the Pakistani economy faces. Remittances from Gulf migration increased from a paltry $133.77 million in 1972-73 to peak at $2.98 billion in 1982-83. These remittances accounted for financing roughly 50 per cent of the trade gap during the period and financed 50 per cent of the total investment through the 1978-88 period.[46] This windfall enabled the regime to maintain trend levels of investment and imports.

This investible surplus accrued through remittances was then allocated primarily through the state-owned banking system. Interest rates for long-term finance as well as working capital were kept below their market rates.[47] There is no indication in policy documents of the time to provide specific sector subsidies save for exports and locally manufactured machinery (LMM). For LMM, the government provided subsidized credit at a nominal value of 1 per cent during this period. The beneficiaries of the LMM policy have been the cement and sugar industries whose machinery has been locally produced.

An important aspect of credit through the nationalized financial sector during the 1980s was a sharp increase in the leverage ratios. In the early 1980s, the debt-equity ratio was fixed at 60:40, but in cases where the banks would underwrite supplier's credit and for LMM credit, the ratio was fixed at 70:30 and 80:20 respectively. In many cases the debt-equity ratio is also known to be as high as 90:10.[48]

High leveraging during the period meant that the liability of the capitalist was kept minimal. The usual channels of over-invoicing on machinery and equipment meant that the capitalist would recover a portion of the cost even before the project would begin. But this phenomenon would be a one-off rent that would accrue to the credit recipient and does not necessarily imply inefficiency in the production process. Inefficiency through the financial sector in the 1980s also came about through the ability of loan recipients to continuously reschedule their debts and to acquire more loans in spite of not having cleared their former arrears. In this case, there is little incentive on the part of the capitalist to enhance the profitability of the project as rents can be accrued through a seemingly unlimited access to resources through the state-controlled financial sector. The most vivid manifestation of this phenomenon is the increasing degree of 'sickness' in Pakistan's manufacturing sector. Although industrial sickness has come to the fore as a major issue in the 1990s, its roots can be found in the credit disbursal system of the 1980s.[49]

There were three categories of industrialists who received credit on easy terms from the financial sector.[50] The first category were some of the erstwhile '22 families' who had survived the tremors of the Bhutto regime. The other category consisted of a set of former traders who entered industry because of loosened entry barriers as a result of credit availability through the nationalized financial sector. The third category was of a large number of new entrants who carried direct or indirect political clout. The Chaudhrys of Gujrat, the Sharif group of Lahore, and others were politically important personalities who were liberally provided with loans from the state-controlled financial sector in order to neutralize opposition to the regime. These personalities are, however, only the tip of the iceberg. There were many others, who either because of their direct political clout or because of attachment to influential lobbies, entered the industrial fray.

On the surface, however, the industrial elite regained much ground that it had lost during the Bhutto period. To lure the private sector to invest in large-scale manufacturing, new public sector investments were frozen, industries which were made the exclusive preserve of the public sector under the Bhutto government were opened up for private industrial investment and a martial law ordinance ensured against any further state take-overs of industry. In addition to subsidized credit from the nationalized banking sector, a plethora of incentives were provided to the private sector for investment.[51]

The regime also moved to decisively curb labour militancy. The general curb on organizational rights meant that unions were constrained to bargain only for specific demands at the firm level, and national level union leadership was either intimidated or bought off.[52] While the labour laws enacted in 1969 remained intact, the government turned a blind eye to the practice of employing labour on contract in circumvention of the law. Both these steps played an important role in reducing labour militancy in the 1980s.

The economic—and one must concede—political success of the Zia regime needs to be explained, especially since we have termed it as part of a disjunctural political settlement. Obviously, a severe curb on organizational rights—in the form of suspension of the constitution and a ban on political parties—was important in containing dissent against the regime and preventing it from gaining momentum. However, the fact that the regime inherited a highly mobilized polity would imply that a lot else was afoot to bring about this outcome.

The example of the LSM sector illustrates the ability of the regime to make pay-offs to a number of social groups. The resources to make pay-offs, in turn accrued through fortuitous exogenous circumstances. The remittances from migrant workers, mentioned earlier, was only one avenue through which Gulf migration helped in easing constraints on the state. The migration also meant that large sections of the urban and rural middle class migrated to the Gulf in search of upward mobility. The fact that the Movement for the Restoration of Democracy

(MRD), launched in 1983, remained largely confined to rural Sindh, has been attributed by a number of analysts to both the direct effect of many 'enterprising' sections of the workforce leaving the country[53] or to the ensuing prosperity of the families of these migrants.

Another exogenous windfall that helped the Zia regime to ward off pressures emanating from disjunctural politics was the Afghan war. The war in Afghanistan once again transformed Pakistan into a front-line state in the geo-strategic calculus of the United States. Not only was aid revived, but Pakistan received both military and economic assistance at more favourable terms. Husain shows that the grant component in net foreign resource inflows increased substantially in the 1976-85 period.[54] Being a frontline state also enabled Pakistan to receive loans and grants without any significant conditionality attached to them. This is best reflected by the fact that in 1981, Pakistan signed a structural adjustment agreement with the IMF. However, the government did not fulfil most of the conditionalities attached to the package, yet continued to receive balance of payment support from the Fund.

Resource inflows were, however, not the only positive fallout for the regime so far as the Afghan war was concerned. With a covert guerrilla war being fought on Pakistan's north-western border, drug smuggling, gun running, and other criminal activities that typically accompany such wars, also had an important impact on the country's political economy. These illegal channels opened up by the Afghan war were, therefore, an important, perhaps crucial, mechanism through which demands on the state from potential political lobbies were contained as long as the state was willing to turn a blind eye on these activities.

These two phenomena as well as the drive towards Islamization during the Zia regime created a number of strong factions within society. These factions and mafias, with dense and complex networks constantly demanded pay-offs from the state. A regime bereft of all political legitimacy could make these pay-offs because of the resource windfalls available to it.

The fact that industrial growth (as well as overall GDP growth) increased over the period on the basis of an exogenous windfall provides an important pointer towards the sustenance of the Zia regime for a period of eleven years. It also goes to demonstrate that if the resource constraint is relieved, then a disjunctural political settlement can also deliver high growth rates. However, the growth regime will be fragile as it cannot ensure sustained productivity growth simply because it has to continue to appease a number of different groups by making pay-offs.

The Second Phase of State Resurrection: Democracy and Economic Liberalization

Going back to section I, we see that growth in the LSM sector has reached its lowest ebb in the 1990s. Moreover, we also see that investment in the manufacturing sector has also declined from an average annual growth rate of 10.3 per cent per annum in the 1980s down to 2.3 per cent between 1991-98. While productivity of investments was low, yet positive, in the 1980s, aggregated and partial evidence suggests that the Incremental Capital Output Ratio (ICOR) increased substantially in the 1990s.[55]

Other indicators for LSM in this decade further indicate that the present decade so far is turning out to be the worst in the country's history. Growth in manufactured exports is down from an average of 9.08 per cent in the 1980s to roughly 5 per cent in the 1991-98 period. Industrial sickness has reached a point where more than 4000 industries are either closed or in serious financial doldrums by the end of 1998.

The central villain in this downturn in Pakistan's economy in the 1990s and in the LSM sector in particular has been the intense and wide-ranging dose of liberalization that the Pakistani economy has been subjected to since 1991. The instruments of liberalization used in Pakistan are usual neo-liberal prescriptions to an ailing economy. We briefly describe some of these instruments as they pertain to the LSM sector:

i) Interest Rate Liberalization: The economic reforms of 1991 ushered in an almost complete deregulation of interest rates.[56] Lending rates to industry, in nominal terms, increased from an average of 12 per cent in 1990 to 20-23 per cent in 1997.[57]

High interest rates crowd out new investment. This is clearly manifested in the sharp decline in manufacturing investment mentioned earlier. High rates on working capital—ranging from 25-35 per cent per annum nominally in 1997—is another reason for low rates of capacity utilization in the 1990s. The phenomenon of industrial sickness, which was earlier entirely due to wilful defaults is now compounded by the fact that no genuine, long gestation manufacturing project can yield returns commensurate with prevailing interest rates. As a result, borrowed money is either diverted to short-term, often speculative activities or if invested in industry, the project soon becomes financially insolvent.

ii) Exchange Rate Liberalization: The rupee has depreciated by roughly 100 per cent since 1991. In the neo-liberal schema, the rationale for devaluation is simple enough: nominal devaluations improve the real exchange rate and thereby remove the anti-export bias in the economy. The fact that growth in manufactured exports has decelerated in the 1990s shows that this has not happened.

Regardless of whether one accepts the first neo-liberal premise that relative prices should be used as a tool to increase exports, the point is that the real exchange rate does not automatically improve as a result of nominal devaluations. In Pakistan, a reduction in the nominal exchange rate has been a prime factor in increasing the cost of inputs and machinery. Moreover, Pasha et al.[58] also show that devaluations usher in inflationary expectations in the economy. The entire economy, including the LSM sector has suffered a great deal as a result of this particular instrument of liberalization.

iii) Tariff Reduction: Import tariffs have been steadily reduced in Pakistan since the early 1980s. The maximum tariff rate was reduced from 225 per cent in 1983-84 to 65 per cent in 1995-96 and in March 1999, it was further reduced to 35 per cent, resulting in obvious disincentive for the domestic manufacturing industry. The protagonists, on the other hand, argue that reduction in tariff rates is welfare enhancing for consumers and it also reduces the anti-export bias in the economy. It is further argued that reduction in import tariffs induces inefficient industries to rise from their slumber and move towards greater efficiency. That tariff reduction has not resulted in either efficiency gains or export growth is evident from the aggregate information given above.

The fact that tariff reduction has both a positive and negative impact is clear. What has to be ascertained is which affect has dominated in Pakistan. There is some information to show that the intermediate goods industries have lost as a result of tariff reductions. Khan did a decomposition analysis of manufacturing growth and found that the component of import substitution for the intermediate goods industry was negative for the post structural adjustment period.[59]

The above evidence is, however, not exhaustive. To gauge the impact of tariff reduction on manufacturing performance, average tariff rates are a better indicator than maximum tariffs. According to Kemal, the average tariff rate has declined only marginally between 1983-84 and 1994-95 from 27.5 per cent to 24.2 per cent.[60] This brings into focus the important point that average tariffs in Pakistan have always been low, principally because of special exemptions given to specific industries and firms through Standing Regulatory Orders (SROs). Thus, in spite of high tariff rates a large number of goods that were imported in Pakistan by-passed statutory tariffs. This is an important result for it demonstrates that contrary to popular belief Pakistan has never been an over-protected economy. Therefore, to expect large efficiency gains accruing from tariff reductions is misplaced to start with.

iv) Reduction in the budget deficit: Reduction in the budget deficit has been an important conditionality of multilateral agencies in Pakistan. As a result, the budget deficit as a percentage of GDP has come down from an average of 7.8 per cent in the 1985-91 period to 6.3 per cent in the 1991-98 period.

With the revenue base virtually stagnant, this reduction has been achieved entirely from reducing government expenditure. But due to the inelasticity of current expenditures, the brunt of deficit reduction has fallen on public investment, primarily in infrastructure. In the case of Pakistan, public sector investment—in roads, communications, electricity, etc—have traditionally crowded-in public investment.[61] Deceleration in public investment has also been one important reason for deceleration in overall LSM investment.

v) Privatization: In line with its conception of the minimalist state, neo-liberalism particularly emphasises privatization of state-owned enterprises. The argument for privatizing industry is straight forward: public sector enterprises face a 'soft budget constraint'. As such, allocative efficiency is distorted and inefficient outcomes in the form of low productivity, low profitability and over-employment ensue. Obviously, it is assumed that the opposite outcomes necessarily prevail in the private sector. Hence the need to privatise.

At the time of privatization in 1991, the share of public sector in total industrial investment was 17.9 per cent, whereas its share in total value-added is indeterminate. In the mid 1980s, however, its share was roughly 11.8 per cent of value-added. Although the public sector was by no means pre-dominant in either investment or value-added, certain industries in the public sector had a large market share.[62] Between 1991 and 1996, 88 out of 109 industrial units in the public sector were privatized.[63] There is very little information on the post-privatization performance of these industrial units. However, judging by overall deceleration in performance indicators for the sector, it can be safely asserted that privatization has not ushered in an era of efficiency gains in the sector.

This is not a surprising result for two reasons. First of all, the total factor productivity and profitability performance of public sector industries was no worse (or indeed better) than that of the private sector in the 1980s—the heydays of public sector presence in the LSM sector.[64] Second, the 'soft budget constraint' was, if anything, equally prevalent in the private sector as exemplified by the large bad debt portfolio and industrial sickness.

The question to be asked is why did the country's industrial bourgeoisie not resist these obvious negative impacts of liberalization.[65] In our perception there are two reasons for this. As such it is welcomed. The other policies are not comprehended as constituting the liberalization package outlined above. Second, the incentive structure of liberalization in Pakistan has been such that finance capital becomes more lucrative than industrial capital. Playing the stock exchange, investing in real estate or simply transferring money abroad (or keeping it in dollar deposits at home) are avenues which enable them to multiply their assets without taking the requisite risks that accompany industrial investment. This also goes to show that the relative power of the industrial bourgeoisie has not necessarily declined, only that it has simply enabled their industrial capital to be switched over to finance capital. The relative power of the industrial class is best exemplified by the fact that to date there has been no serious attempt to liquidate their bad debt. This is in spite of the fact that the bad debt situation has been the most serious crisis that faces the banking sector in Pakistan.

Was the Economy Liberalized to Resurrect the State?

That liberalization of the economy has been generally negative for the economy and specifically for the manufacturing sector is established. The important question is, why did the government decide to liberalize the economy at the time when it did and the extent to which it did? The first documented commitment to liberalization came three years before liberalisation was actually initiated. On 1 December 1988—significantly, the day before Benazir Bhutto took oath of office as Prime Minister—the care-taker Finance Minister, Dr Mahbubul Haq signed a Structural Adjustment loan agreement. Commenting on the need for this programme, Zaidi says:

> ...Pakistan's economy, at the time of the initiation of the 1988 programme was in relatively good shape and did not suffer from the problems faced by most African or Latin American countries, with rampant inflation, low or negative growth, large external debts, etc.[66]

On the surface, there was no need for an IMF agreement when it was signed in 1988. Interestingly, when liberalization started in earnest in 1991, the 1988 Agreement with the IMF was defunct. Liberalization was, thus, very much the initiative of the politicians in power at the time. The answer to the above question has elicited three possible responses in Pakistan. The neo-liberals term it as the 'step in the right direction' with the only complaint that its implementation has been slack. At most, their criticism goes so far as to challenge the sequencing of reform efforts.[67] Ideological and intellectual persuasion of neo-liberal economic thought, especially in the absence of coherent indigenous thinking on the issue is one argument. Yet another explanation is that of the acquiescence of the local elite to global imperialist pressures.[68] While all these arguments may have some grain of truth, they do not explain how and why the structure of the state had changed so radically at the turn of the decade to accept these prescriptions when it had resisted them throughout the 1980s.

Seen in the context of disjunctural politics, we conceptualize liberalization as the response of politicians of different hues who have been at the helm of affairs as well as the 'establishment' in Pakistan to resurrect the state structure at a time when the windfalls that kept the ship afloat were no longer available. In 1988, the Afghan war ended and in 1991, the US government invoked the Pressler Amendment. As such, the US was no longer willing to provide economic and military aid to Pakistan. In the 1990s, and particularly after the Gulf war remittances plateaued out to the US $1.0 to 1.5 billion mark, down from US $ 1.8-2.2 billion mark in the 1980s. The ability of the state to constantly make pay-offs to powerful factions and lobbies was becoming increasingly onerous. In the perception of state decision-makers, the best strategy, therefore, was to minimize the role of the state and thereby divert demands from these lobbies towards the private sector. In this way, state personnel and those groups who have greater access to state-generated resources can maintain their privileges.

Liberalization of the economy, however, is one attempt in the economic sphere towards this direction.[69] There are no signs that this strategy has been successful. Pressures on the state have increased manifold as the resource crunch deepens. This is best exemplified by corruption occupying the centre stage in political-economic discourse in the country.[70]

Conclusion

In this study, we have used secondary data and information in a political economy framework. The main thrust of the study is, therefore, methodological. The framework of conjunctural and disjunctural politics in explaining the underlying contours of economic phenomena should, however, be seen as an initial attempt in treating political economy issues analytically.

Rather than using dichotomies of democracy-dictatorship (so often used in explaining Pakistan's economic developments), dynamics within society and between the state and society have been the operative concept. We have argued that as long as the structure of the state reflected the interests of dominant groups in society, the state could formulate and implement policies—whether these policies were good or bad is a moot point—successfully. Since the relative power distribution in society was highly unequal, the pattern of economic development that ensued was reflective of that.

We have also conceptualized disjunctures in state-society relations occurring essentially as a result of dynamic changes that have occurred in society. The state, on the other hand, has remained ossified in its colonial trappings and has not developed formal mechanisms to grant economic or political rights beyond the narrow elite. But since it is embedded in a mobilized polity, it has to either resort to oppression in various forms or informally make pay-offs to a number of social groups and lobbies. Economic performance (demonstrated through the performance of the LSM sector) in such a political settlement is bound to suffer. While exogenous windfalls can bail out the economy for some time, the pattern of growth and development that develops is not sustainable.

Within the realm of disjunctural politics, we have alluded to the role of the middle class and factions within this class as having been the key players in altering the balance of power between state and society. The role of the middle class in politico-economic transitions has been generally seen as taking the polity towards a more democratic and equitable pattern of socio-economic development. Our analysis shows that in the case of Pakistan, this has not happened yet and there are no tangible signs of it occurring in the near future also. This is simply because one cannot ascribe a teleological role to any class without tracking the actual process of its evolution and development in a specific context. Much of the lament against the middle class[71] or hopes pinned on it are based on such pre-determined historical roles that classes are supposed to perform. The analysis that follows, therefore, ends up viewing classes 'in terms of *what they are not*, instead of *what they are*.'[72]

As for the LSM sector, in the near to medium future, its role in Pakistan's economy will continue to diminish. Liberalization and globalization have created an incentive structure where finance capital will continue to replace industrial capital in developing countries generally and Pakistan particularly. We have already seen Pakistan's industrial bourgeoisie adjusting to this incentive structure. Moreover, Pakistan's macro-economy will become increasingly incapable of supporting LSM activity as physical infrastructure decays (and is not rehabilitated) and improvements in human capital are painfully slow. Whether we will witness substantial growth in productive employment generation and real incomes—some minimal indicators of economic development—in spite of LSM taking a back seat remains to be seen.

NOTES

1. Large scale manufacturing is referred to as that segment of manufacturing activities that are in the 'formal sector' in Pakistan. Rather than the size of the establishment it is their registration status which is the defining characteristic. Thus those industries registered under sections 2(j) and 5(i) of the Factories Act, 1934 are included in the large-scale manufacturing sector. While the definition is not strictly one of large-scale in terms of size, the general observation is that registered 'formal' enterprises tend to be large scale while unregistered firms, by and large, tend to be small scale.
2. For a review of the literature on the theme, see Weiss (1991).
3. The reason why we have given official figures and not updated them is for the sake of consistency with previous data.
4. See Chenery (1986) for a cross-country study on this pattern among successful developers.
5. See Lewis (1969) for a detailed account of industrial performance in the 1950s.
6. Elias, 1992, and Ahluwalia, 1985.
7. This is in spite of the fact that the Latin American countries as well as Turkey had gone through a severe macroeconomic crisis in the 1980s.
8. See Chenery, 1986.
9. The most articulate exposition on this theme is Lal (1983).
10. Alavi, 1990, p. 21.
11. Alavi, 1972, 1983, and 1998.
12. Alavi, 1972, p. 62.
13. Migdal, 1987, 1988; Kohli, Migdal, and Shue, 1994.
14. Khan, forthcoming.
15. The *ceteris paribus* clause would include factors such as exogenous shocks or external imperialist influence and technological developments.
16. See Laporte Jr., 1992; and Kennedy, 1988.
17. Jalal, 1990, p. 297.
18. Of the three provinces in West Pakistan at the time, the Muslim League had control only over the Sindh legislature. The Frontier and Punjab assemblies were in control of the Congress and the Unionists respectively.
19. Jalal, 1985.
20. See Jalal (1990) and Alavi (1983) for the predominance of this view among the military and bureaucratic personnel.
21. By structural disequilibrium it is meant that for a country with Pakistan's per capita income and the demand pattern that level of income engenders, the share of manufacturing in GDP was abnormally low. See Lewis (1969) for a further elaboration of the concept.

22. Kibria (1999) has argued that this decision resulted in nipping in the bud the thriving capital goods industry that Pakistan had inherited from the colonial state.
23. See Ali, 1970.
24. The political strategy of the time, which was compatible with the social structure of West Pakistan was also extended to East Pakistan. That it was largely unsuccessful in a region where the social structure was markedly different is documented in Alavi (1972) and Khan (forthcoming).
25. See Haq, 1963.
26. Ahmed, 1980.
27. Sayeed, forthcoming, chap. 3.
28. Sayeed, 1996.
29. Burki, 1980; and Zaidi, 1999.
30. The size classification used for urban areas is as follows: Large cities with a population of 500,000 or more, medium cities between 100,000 and 500,000, large towns between 50,000 and 100,000, and small towns with a population of more than 5000 and less than 50,000 inhabitants.
32. Alavi, 1983.
33. A survey done on rural out-migration between 1967 and 1969 reveals that 72.2 per cent of the out-migrating landowners preferred to go to the towns rather than large cities while a larger proportion of landless workers (58.3 per cent) went to the larger cities (Burki, 1974).
34. Alavi, 1976, pp. 325–26.
35. Burki, 1971, p. 475.
36. For some accounts of Bhutto's mobilization of the middle classes in towns, see Burki (1980) and Syed (1992).
37. Moore, 1966.
38. Although workers and peasants were also part of the populist platform which voted for the PPP, as we saw in the previous chapter, the dominant element in the new settlement was the middle class.
39. Ahmad and Amjad, 1984, p. 221.
40. A state-owned financial system is important for disbursing credit according to plan imperatives, as is evident from the experience of successful East Asian economies.
41. 1972-73 was the first year since the early 1950s that a current account surplus was realized.
42. Ibid., p. 94.
43. By 1976-77, public sector investment in LSM reached a high of 78 per cent of total investment in the sector.
44. See Ali, 1970.
45. The World Bank has maintained a direct credit line to all the four major Development Finance Institutions (DFIs)–PICIC, NDFC, IDBP and BEL–

for the foreign exchange component of industrial investments (UNIDO, 1990, pp136-37).

46. Amjad, 1986.
47. The rate of interest for fixed investments as disbursed by the DFIs, ranged between 6 and 14 per cent per annum. In real terms, the range varies from slightly negative to moderately positive rates.
48. UNIDO, 1990.
49. See World Bank (1988) as the first indicator of this problem arising in the 1980s.
50. See Sayeed, 1990.
51. These included tax holidays, duty drawbacks and duty exemptions through a number of Standing Regulatory Orders (SROs).
52. See Sayeed, 1980, pp. 179–181.
53. Waseem, 1989, p. 383.
54. See Husain, 1992.
55. Zaman, 1997, p. 23.
56. Regulated or subsidized interest still continues only for the export refinance scheme and agricultural credit. Although for these two categories interest rates are subsidized, their rates have also increased considerably in the last seven years or so.
57. In 1998, interest rates on long-term lendings have been reduced to an average of 18-20 per cent for the private sector, Zaman Associates, 1997.
58. Pasha et al, 1995.
59. Khan, 1997.
60. Kemal, 1997.
61. See Zaidi, 1999; and IMF, 1993.
62. Cement, vegetable oil, automobiles and fertilizer industries in the public sector had a market share of 70, 65, 60, and 50 per cent respectively (Aziz, 1996, p 19).
63. Zaman, 1997.
64. For productivity results, see Sayeed (forthcoming, chap. 6), for profitability analysis, see Naqvi and Kemal (1991). A synthesis of this view is presented in Zaidi (1999).
65. None of the Chambers of Commerce or other industry associations have been critical of the total package of liberalization, although there are muted voices that one hears of criticism on one policy or the other.
66. Zaidi, 1999, p. 324.
67. Husain, 1998.
68. The latter two arguments are quoted in Zaidi (1999, p. 327).
69. Other measures taken to ward off these pressures have manifested themselves in the form of increasing repression from state authorities.
70. Elsewhere (Sayeed, 1998b) we have attempted to show that pay-offs from the state to maintain the political settlement of disjunctural politics is interpreted as 'corruption'.

71. See Kibria (1999) as one example of a lament of the middle class not performing its historical role.
72. Kohli and Shue, 1994, p. 310.

Bibliography

Ahluwalia, I.J. (1985). *Industrial Growth in India*, University Press, Delhi.

Ahmad, V. and Amjad, R. (1984). *The Management of Pakistan's Economy: 1947-82*, Oxford University Press, Karachi.

Ahmed, M. A. (1980). 'Productivity, Prices and Relative Income Shares in Pakistan's Large Scale Manufacturing Sector, 1958-70', unpublished D.Phil dissertation, University of Oxford.

Alavi, H. (1972). 'The State in Post-Colonial Societies: Pakistan and Bangladesh', *New Left Review*, No. 74.

______, (1976). 'The Rural Elite and Agricultural Development in Pakistan', in Stevens, R.D., Alavi, H., and Betocci, P. (eds.). *Rural Development in Bangladesh and Pakistan*, The University Press of Hawaii, Honolulu.

______, (1983). 'Class and State in Pakistan', in Gardezi, H. and Rahid, J. (eds). *Pakistan: The Unstable State*, Vanguard Books, Lahore.

______, (1989). 'Politics of Ethnicity in India and Pakistan', in Alavi, H. and Harriss, J. (eds) *Sociology of Developing Societies: South Asia*, Macmillan, London.

______, (1990). 'Authoritarianism and Legitimation of State Power in Pakistan', in Mitra, S. (ed). *The Post-Colonial State in South Asia*, Harvester-Wheatsheaf, London.

Ali, T. (1970). *Pakistan: Military Rule or People's Power*, William Morrow and Co., New York.

Amjad, R. (1986). 'Impact of Worker's Remittances from the Middle East on Pakistan's Economy: Some Selected Issues', *Pakistan Development Review*, Vol. 25, No. 4.

Aziz, S. (1996). *Privatization in Pakistan*, Development Centre Studies, OECD, Paris.

Burki, S.J. (1971). 'Social and Economic Determinants of Political Violence: A Case Study of the Punjab', *The Middle East Journal*, Vol.25, Autumn.

______, (1974). 'Development of Towns: The Pakistan Experience', *Asian Survey*, Vol. 14, No. 8.

______, (1980). *State and Society in Pakistan: 1971-77*, Macmillan, London.

Chenery, H. (1986). In Chenery, H., Robinson, S. and Syrquin, M. *Industrialization and Growth: A Comparative Study*, Oxford University Press, New York.

Elias, V.J.(1992). *A Study of Economic Growth of Latin America*, International Center for Economic Growth, San Francisco.

Federal Bureau of Statistics, *Census of Manufacturing Industries*, various years, Karachi.

GOP, *Economic Survey*, various issues, Economic Adviser's Wing, Ministry of Finance, Islamabad.

Haq, M. (1963). *Strategy of Economic Planning*, Oxford University Press, Karachi.

Hirschman, A. O. (1958). *Strategy of Economic Development*, Yale University Press, New Haven.

Husain, I. (1992). 'External Debt and Foreign Aid to Pakistan', in Nasim, A. (ed.). *Financing Pakistan's Development in the 1990s*, Oxford University Press, Karachi.

______, (1999). *The Economy of an Elitist State*, Oxford University Press, Karachi.

IMF, (1993). 'Developments of Private Investment in Pakistan', IMF Working Paper, Washington D.C.

Jalal, A. (1985). *The Sole Spokesman: Jinnah, the Muslim League and the Demand for Pakistan*, Cambridge University Press, Cambridge.

______, (1990). *The State of Martial Rule: The Origins of Pakistan's Political Economy of Defence*, Vanguard, Lahore.

Kemal, A.R. (1978). 'An Analysis of Industrial Efficiency in Pakistan: 1959-60 to 1969-70', unpublished Ph.D. dissertation, University of Manchester, Manchester.

______, (1997). Employment and the Manufacturing Sector of Pakistan, mimeo, Planning Commsion, Government of Pakistan, Islamabad.

Kennedy, C.H. (1988) *Bureaucracy in Pakistan*, Oxford University Press, Karachi.

Khan, M.H. (forthcoming). *Corruption, Clientilism and Capitalist Development*, Oxford University Press, Oxford.

Khan, S.R. (1997). 'Do IMF and World Bank Policies Work?', Sustainable Development Policy Institute Monograph Series, #6, Islamabad.

Kibria, G.(1999). *A Shattered Dream: Understanding Pakistan's Underdevelopment*, Oxford University Press, Karachi.

Kohli, A., Migdal, J., and Shue, V. (1994). *State Power and Social Forces: Domination and Transformation in the Third World*, Cambridge University Press, Cambridge.

Lal, D. (1983). *The Poverty of Development Economics*, Institute of Economic Affairs, London.

Laporte Jr, R. (1992). 'Administration', in James, W. and Roy, S. (eds.). *Foundations of Pakistan's Political Economy*, Sage Publications, New Delhi.

Lewis, Stephen R. (1969). *Economic Policy and Industrial Growth in Pakistan*, George Allen and Unwin Ltd., London.

Migdal, J. (1987). 'Strong States, Weak States: Power and Accommodation,' in Weiner, M. and Huntington, S. (eds.). *Understanding Political Development*, Little, Brown and Company, Boston.

______, (1988). *Strong States and Weak Societies*, Princeton University Press, Princeton.

Moore, B. (1966). *Social Origins of Dictatorship and Democracy*, Beacon Press, Boston.

Naqvi, S.N.H. and Kemal, A.R. (1991). 'The Privatization of the Public Industrial Enterprises in Pakistan', *Pakistan Development Review*, Vol. 30, No. 2.

Noman, O. 1988 *The Political Economy of Pakistan: 1947-85*, KPI, London.

Pasha, H., Khan, A., Hasan, A. and Rashid, E. (1995). 'What Explains the Current High Rate of Inflation in Pakistan?', *Pakistan Development Review*, vol. 34, No. 4.

Sayeed, K.B.1980 *Politics in Pakistan: The Nature and Direction of Change*, Praeger, New York.

Sayeed, A. (1990). 'The New Breed', *Herald*, June.

______, (1992). *The Discourse and Politics of Zulfikar Ali Bhutto*, Macmillan, Basingstoke.

______, (1996). 'Growth and Mobilisation of the Middle Classes in West Punjab: 1960-70', in Singh, P. (ed.) *Globalization and the Region*, Oxford, 1996.

______, (1998a). *Growth and Productivity in Pakistan's Large Scale Manufacturing Sector: Implications for Competitiveness and Employment.* Study Conducted for ILO- South Asia Multi Disciplinary Advisory Team (SAAT), New Delhi, 1998.

______, (1998b). 'Political Economy of Corruption in Pakistan: Locating Structural Features', in Tahir, N. (Ed). *The Politics and Economics of the Market Economy in Post Cold War Europe: Lessons for South Asia*, University of Karachi Press, Karachi.

______, (forthcoming). *Political Alignments, the State and Industrialization in Pakistan*, unpublished thesis Cambridge University.

Systems (1989). *Survey of large Scale Manufacturing: A Study of Contract Labour*, Vol. 1. Systems (Private) Limited, Lahore.

UNIDO. (1990). *Pakistan: Towards Industrial Liberalization and Revitalization*, Basil Blackwell, Oxford.

Waseem, M. (1989). *Politics and the State in Pakistan*, Progressive Publishers, Lahore.

Weiss, J. (1991). *Industry in Developing Countries: Theory, Policy and Evidence,* Croom Helm, London.

World Bank. (1988). *Pakistan Industrial Regulatory Policies*, Volumes 1 and 2, Washington DC.

Zaidi, S.A. (1999) *Issues in Pakistan's Economy*, Oxford University Press, Karachi.

Zaman, A. (1997). *Pakistan: Industry and Trade Sector Study*, for Asian Development Bank.