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Sustaining Development in South Asia

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Sustaining Development in South Asia¹

Thinking South Asia is very difficult despite many commonalities and a geographic reality of a subcontinent. In keeping with expectations, countries within the region have their own successes and failures and are now seemingly progressing at different rates. Yet there are some common themes that can be seen. For example, identity politics and nationalism have divided the region like no other in the last sixty years. In many areas (countries) of South Asia, civil strife prevails. Extremism and fundamentalism are leading to terrorism especially in Pakistan. Institutional and political stability has yet to be reached in most of south Asia..

While constituent countries have shown some divergence in their economic policies and their ensuing successes and failures, none of them have broken into the ranks of the middle income group. Sri Lanka has achieved more on social indicators, India is beginning to show strong growth, strong exports, accumulation of reserves, and an attraction for FDI, Bangladesh and Pakistan have both had their patches of strong growth though never has it been sustained at levels that would elevate these countries out of the low income group. Meanwhile, outside Sub-Saharan Africa, South Asia is only region where persistent poverty is widespread. The latest World Bank numbers show that about 600 million people (40 percent of total population) live on less than \$1.25 a day.²

Economically, the biggest development challenge that South Asia faces is the elimination of poverty. This paper will use many fresh currents in economic thought to argue for developing fresh strategies in all South Asian countries to try to achieve this goal. This goal cannot be achieved unless South Asia rethinks identity, religious and nationalistic politics to be more inclusive and allows peace to be achieved in all communities. There is a need to rethink our

¹ Although I will try to talk about South Asia in general but I do so mindful of the considerable heterogeneity in the region. However, I hasten to add that my most immediate and detailed knowledge is that of Pakistan. Hence I will only make strong claims on my own country. In drawing commonalities, I have tried to be soft on my conclusions on other countries in the region but I will be ready to accept any corrections by those from other countries.

² While talking of poverty numbers we must not forget Surjit Bhalla's critique of the World Bank. He has contended that the World Bank has an incentive to overestimate poverty

institutions to align them with globalization and opportunity. Much needs to be done to end this fragmentation of hard borders and little trade (especially between India and Pakistan).

I will argue that we need to understand the process of policymaking to see if it is sufficiently informed of new thinking and to see if agents in that process are motivated to take ownership of new ideas and see them implemented. This analysis will lead us in the direction of interventions that align the incentives of key players with reform and others that are perhaps more appropriately targeted to affecting the processes that affect change and growth.

Path-dependence: Understand South Asia's Political Economy

South Asia's colonial heritage included on the one hand people educated well in the English tradition of welfare and Keynesian Fabianism and on the other a colonial civil service that was resistant to change, was suspicious of the market and saw innovation and openness as a risk to public order.

South Asia retained the paternalistic colonial policy where the state was seeking to develop the economy through state planning and deep state interventions seeking to eliminate the market's role everywhere. This overbearing role of the government in the economy has changed and evolved but not completely revised in most parts of South Asia. The civil service guards this role but the local intellectual provides the justification for it. Even today, very few South Asian intellectuals argue for a market based economy.

It was not surprising that South Asia resisted opening out the economy till the 90s when even the communist world had accepted it. Market deregulation is still deeply resisted. While there is some variation on deregulation, most of South Asia shows up very low on global rankings for ease of doing business. Even today ADB and the World Bank are talking about labor laws being outmoded and various other market enhancing legislation being either outmoded or not being in place.

While economic thought moved on, communism collapsed, the Reagan and Thatcher revolutions happened, South Asia resisted a market state and gave in to small doses of liberalization very grudgingly. Even today, the Banking sector is liberalized and privatized

only in Pakistan and there is a fair amount of engineering industry that remains protected in both India and Pakistan. Central Bank independence has not been achieved anywhere in South Asia. At the cost of giving up the regional hub to Dubai, airline and airport deregulation has been glacial. Nowhere has the land or real estate market been developed. Agricultural productivity remains below potential in Pakistan for example, because the state continues to lead activities such as market development and storage.

As Niall Ferguson argues, we have a lot to thank British Colonialism for—not the least of which are the legal, judicial, administrative, communication and education systems that they left us. But all systems must be maintained and developed in line with technology and globalization. Yet the story of South Asia is largely that of resisting reform and letting the outmoded colonial structures become a distortive drag on the economy.

The years of independence have not been kind to the Civil Service in varying degrees in the countries of South Asia. In general, they have been politicized and lost their sense of service and reward. The prevailing egalitarian mood has eroded their real salaries dramatically over the years. The services retaliated through managing their perks, creating rentseeking opportunities and letting their ethical standards deteriorate. They have realized maintaining a large and controlling state has its advantages. This is now very apparent in the corruption indicators for South Asia: the civil service and organs of government have learnt how to use the large role of state to their advantage.³

The key question to ask is why does reform remain slow? And what is the process of making policy and reform?

South Asia was one of the early regions to achieve independence and thus was one of the early favorite of the emerging world of donors. The role of donors has been increasing over the years and now in some countries they are major actors and even the principal source of policy. The motives of donors and their relationship with the civil service, civil society and academia needs analysis for an understanding of the political economy of reform.

³ See Transparency International and IRIS rankings.

Box 1

Global Ranking Ease of Doing Business 2007

Region	Average of Regions' Country Rankings
OECD	22
Eastern Europe and Central America	76
East Asia and Pacific	77
Latin America and Caribbean	87
Middle East and North Africa	96
South Asia	107
Sub-Saharan Africa	136

OECD = Organisation for Economic Co-operation and Development.

Note: South Asia comprises Afghanistan, Bhutan, Bangladesh, India, Maldives, Nepal, Pakistan, and Sri Lanka.

Source of basic data: World Bank. 2007c. *Doing Business 2008: Overview*. Washington DC. Available: <http://www.doingbusiness.org/documents/DB-2008-overview.pdf>

Global Ranking Ease of Doing Business by Country 2007-8

	2007	2008
Afghanistan	156	159
Bangladesh	102	107
Bhutan	122	119
India	132	120
Maldives	58	60
Nepal	104	111
Pakistan	73	76
Sri Lanka	100	101

More and more policy initiatives in many parts of South Asia (especially Pakistan) over the years have come from donors. Planning, DFIs, public utilities, industrialization, banks first, stock markets later, developing education in stages, opening out, Washington consensus, SME and later development of governance all came from donors.⁴

Donors are now probably senior partners of the civil service. The policymaking process is as follows:

- Donors define projects, policies and programs based on their own lending needs and the whims of their bureaucracies.

⁴ India shows more policy independence than others.

- They then hire consultants (cheap local academics and bureaucrats, led by high priced foreign consulting firms or Technical Assistance Advisors) to develop projects, policies and programs.⁵
- The project is accepted by the government because of the expected inflow of aid. When accepted in most cases, a Project Implementation Unit (PIU) is set up with some civil servant in charge and some foreign consultants. The PIU has funds to spend and gives several civil servants special allowances.
- Special evaluation procedures are set up and a large number of consultants are employed to continuously evaluate the project.

This process needs careful review and discussion as it has several ramifications for development. Some of these are.

- *A donor led policy agenda where the local expert and official is at the bottom of the thinking process.* The process generates a large amount of paperwork benefiting consultants especially foreign consultants.⁶ Local officials and local intelligentsia is held responsible to donor consultants and donor agendas. For example, almost all donors have commissioned extensive work on measuring poverty in Pakistan; many studies on rural credit have been done and at some more are underway; rural development is frequently studied; many studies on agriculture are repeated frequently. The result is that millions of dollars annually are spent on these consulting studies employing most educated individuals in the country. The consulting studies when completed are seldom reviewed or evaluated except at donor head quarters. No local peer review is done.⁷
- *A steady erosion of human capital and thinking institutions:* All local academia is involved in this donor consulting work at the cost of their teaching and research. Given the poor quality bureaucratic nature of the work, most of these academics do not develop a portfolio of research and lose their skills over time.

⁵ See Haque and Khan (2007) for an interesting analysis of how there is a choice between brain drain repatriation and technical assistance.

⁶ Donor bureaucracies have been increasing in size at a rapid pace in recent years as have consulting firms to take advantage of increasing funding. More needs to be done to understand incentives here.

⁷ Donor reports do not even make a pretense of using domestically generated research or ideas. Very little domestic thinking or research is referenced in donor work. In any case most of donor work is based on their own work.

- *No local ownership*: Local intelligentsia and local officials are reduced to minor colleagues often filling in the blanks with little control over the agenda of reform or policy. Local academics and bureaucrats who are poorly paid survive only on donor consulting. Often they can spend a lifetime doing these projects while not believing in them. In private they are all critical of this approach citing a policy and project agenda that is out of synch with local needs. The result is that there is *no local ownership* of the policies, projects and programs.
- *The local official loses interest in his core task in search of funding*: For example, the Chief Secretary of Punjab became a development chief secretary and had lost interest in his primary function of maintaining law and order. The Punjab Chief minister seems to think that the eventual delivery of economic development over the longer term has priority over law and order and rights.

The Problem with Development Economics or What is required to end poverty and break into the Middle Income Group?

All South Asian countries are following similar policies---struggling to maintain macro balance while putting in place projects that seek to address sectoral and development issues. World Bank and ADB websites reveal that the ongoing projects are in the areas of capacity building, governance, health and education in almost all South Asian countries. These are all sector-wide and nation wide approaches.⁸ And these have been repeated many times and evaluations have not been very complimentary of these programs. Yet they are repeated and often by the same teams.

The model underlying this approach of some capacity building, some governance interventions and seeking some sectoral improvements seems to be based on a simplistic growth model with exogenous productivity improvements. None of these interventions are informed of the incentives of agents involved in the various sectors. Nor are they informed of the inter-linkages. Nor does the unreformed colonial structure and its rentseeking factors in.

⁸ Donors and current development policy also expends a lot of money and effort in trying to achieve a uniform development and economy wide egalitarian policies.

But there is more! Economic research continues to move at a fast pace. Research has opened out several new areas that are beginning to improve our understanding of how society, economy and the individual interact. Could this improve our understanding of development? Very briefly some of these are:

- *Endogenous growth* research has emphasized the productivity enhancement and innovation that ensues from intangible items such as governance, institutions and social capital. Innovation happens with entrepreneurship which happens in markets and environments of trust and law.
- *Experimental economics* has shown that the rational atomistic representation model may need to be revised to include social aspects of humans and the limited knowledge environment that they operate in. People live in communities and their communal side can have productivity impacts. This relates to social capital (trust) aspects that the endogenous growth models are also emphasizing.
- *New Institutional Economics* notes how exchange and trade requires the development of devised constraints to structure human interaction. Consequently, beliefs, norms and ideas lead to institutions that will shape the efficiency of human action. As North notes “In such a world ideas and ideologies play a major role in choices and transaction costs result in imperfect markets.”
- *Game theory* combined with information economics points to incentives and strategic plays that underlie behavior of groups. Policy must seek to align the incentives of these groups with reform for developing institutions and social capital that will produce innovation and growth.
- *Complexity* suggests that development may itself be an emergent phenomenon. Underlying behavioral mechanisms that determine how society and community is configured will lead to the emergence of development or the lack of it. Consequently, policy interventions need to understand the various aspects of societal and communal development that will affect productivity growth and eventually development.
- *Economic geography* contradicts the sector-based, nation-wide approaches that donors are taking. Recent work has shown that productivity growth, skilled work force and innovation happens in human clusters known as cities. Historical evidence recalls how cities can be configured for the emergence of productive, innovative, enlightened and modernized individuals. This literature also argues against uniform nationwide approaches. A systems-wide integrated approach rather than of isolated

and independent sectors. National egalitarian policies that seek to develop regional equality need to be reconsidered in light of cities and cluster development.⁹

What do we learn from this. We need to think of the connectedness of people. We need to think of how they can develop trust and community. We need to think of cities being configured to be engines of growth and modernization. Enlightened and modernized individuals, with a feeling for community living in productive and liberal cities will lead to the emergence of development.

Our sector-wide and national approaches seem to forget community, city, trust and human connectedness. With the state apparatus focused on development, and law and order starved of resources and the law enforcers poorly paid and turned to corruption, the infrastructure of trust that so depends on contracting and associational law, has been eroded. The result is that people in Sialkot one of South Asia's largest sports and surgical goods exporters are now seriously suspicious, hiding their mail and their buyers even from their managers. People in Lahore find it difficult to live in apartments because they cannot trust their neighbors with the common areas and their up keep.

Most South Asian cities lack the infrastructure and the configuration of a modern city. Lahore, an important South Asian city has no public libraries or community centers. Most South Asian cities lack culture: museums and art galleries seldom exist. Inspiring architectural landmarks, memorable town squares with beautiful art or stirring sculptures are all missing. Shopping centers, theaters and other leisure activities have been regulated away. Cities in Pakistan have all adopted a barren suburban approach to development with no mixed use development or dense city centers. The poor have no room in these cities; nor does culture and modernity. Is it a wonder then that fundamentalism and intolerance is on the rise and productivity declining?¹⁰

⁹ For example in a sparsely populated area like Baluchistan should policy seek to have a school and health center in every district? Or should the state commit to provide utilities in remote mountainous areas of the same quality in more settled areas?

¹⁰ "Aid is broken" Ashraf Ghani Former Finance Minister of Afghanistan Ted talks http://www.ted.com/index.php/talks/ashraf_ghani_on_rebuilding_broken_states.html

Understanding Change and Reform

To make things happen in these countries we also need to invest in understanding how change and reform happen.

The nineties saw a spate of studies to understand the Reagan/Thatcher Revolutions, the fall of communism, and how success happened in several reforming countries like Chile. What do we learn from these? Studies like the Commanding heights, Smith's Idea brokers, Easterbrook's "Ideas Move Nations" and several others have noted the role of think tanks and academic debate in shaping locally owned policies. In Chile Valdes notes how the Chicago boys and their debates were ultimately owned by Pinochet to create the reform that happened. Grindle studies the reform process to see how it is shaped by its design teams and policy elites that champion it. Domestic debate and research develops the local ownership for reform while also influencing its final outcome.^{11 12}

Change and reform has also happened in South Asia. We have followed the donor in setting our priorities: liberalizing our economies, attempting export led growth, attempting macro stabilization, developing health and education in sectors, and developing infrastructure, while leaving our communities, property rights, institutions, cities and social capital for a later date. Nowhere has this ordering been debated! Nor have we even begun to understand the ordering or what is required to make holistic development.

Unfortunately, in South Asia, professions, professional associations, think-tanks remain largely undeveloped. Foundations do not exist and are replaced by aid-giving institutions that are run from far off capitals with little vision. Whatever public policy debate takes place is conducted in the relatively closed groups comprising mainly of these aid institutions, their professionals and consultants. In such discussions the only group that has a marginal participation is the government-- marginal because the government has neither the capacity nor often the political time to concern itself with longer term implications of public policy.

¹¹ Debate is not one conference or publication. Donors often mistake a carefully contrive conference with the usual suspects to be this domestic debate.

¹² This point seems obvious if one casts back in history to see the relationship between enlightenment philosophy and the rise of democracy, openness, markets and the unprecedented growth that ensued.

We need to rethink the position of academia in our society and their incentives (See Box 2). Currently they only have room at the bottom of the public policy pyramid as junior consultants. Many of them fuel the brain drain because they feel that they are not empowered at home.^{13 14}

Should we build think tanks, colleges or universities? Yes we do but differently than before. Paternalistic approaches to build think tanks universities and various other institutions without domestic intellectual debate and empowerment have failed. The key lesson to learn is that **Capacity building is more than technical assistance: it is more than human capital development; it is empowerment of local talent!**¹⁵ If we build anything, it must be a profession. Whatever needs to be developed must be managed in the main by a *plurality of* local professionals with a minimum of (or no) bureaucratic or sponsor demands. This is an important area and all of us concerned with development must debate and understand it.

Most importantly, donors need to be sensitized to the possibility of “intellectual crowding out’ just as much as they are sensitive to the “crowding out of private investment.” Domestic intellectuals must fight for intellectual space by subjecting themselves to the painful discipline of discourse. For long term development donors must allow the domestic intellectual to rise to a position of equality and get a seat at the table through dialog and debate regardless of funding and its sources.¹⁶

¹³ While Pakistan has been in the throes of an inner struggle where the entire judicial system collapsed, democracy was killed, terrorism was rising, most donor economists (see WB, ADB and IMF assessments) were treating the economy as if it were divorced from these developments. They failed to examine the possibility that the causes of the joint failure of economics and politics may be the failed institutions and lack of social capital.

¹⁴ Donor interventions are leading to brain drain. In return donors are supplying technical assistance. This strategy has been shown to be welfare reducing. (See Haque and Khan (2007)).

¹⁵ When donors build domestic capacity they are so busy doing it and controlling it that they forget to empower domestic talent. *As an aside, I will add a hypothesis that the fundamentalist donor has been more enlightened (talent based, fewer controls, more objective oriented) in his capacity building and consequently more successful.*

¹⁶ Interestingly enough the current donor approach of constant external monitoring and evaluation also reveals a certain lack of trust.

Rethinking Development Strategy

Given the persistence of poverty and weak success with development and reform in South Asia, we must entertain the hypothesis that development strategies and policy formation and reform-making strategies need review and should change in the coming period. Clearly, funding, sector based strategies, poverty reduction programs, projects and project implementation units, technical assistance, training, consultants reports and evaluations are not working. A fundamental rethinking is necessary!

The above analysis suggests that development is an emergent phenomenon the outcome of which is not totally controllable or determinable.¹⁷ It also suggests that development is not a funding or a mere capital accumulation problem. It has a lot to do with how society and politics is configured. And configuring society for development is a challenge that requires considerable thought and research. Policy and donors must work on the various underlying structures the outcomes of which can lead to development.

This paper argues that the current policymaking process needs to be revised. Current reliance on donor consultants and technical assistance need to be reviewed. Design needs to be informed of recent research. Success is more likely if reform ideas have been generated through local debate and the underlying research has been subjected to peer review. Local academia, its professionalism, its research and forums of debate can be an agency of change as well as a source of good ideas. Competitive and independent universities and think tanks will house these agents of change and offer a platform for their debate.

Policy design needs to take into account new developments arising from recent research. Earlier approaches of sector-based national interventions developed through a technical assistance and consultants with the bureaucracy as a junior implanting partner are clearly not working very well. Instead perhaps it is worth considering how local academia and civil

¹⁷ The positions here is closer to the Easterly solution to development; Easterly has argued for searching and seeking solutions that place less emphasis on funding while Sachs and others seem to think that development is a funding problem.

society can be motivated to develop more community, social capital and human cluster approaches.

The city is a typical human cluster which should form the unit of analysis and implementation. Much research these days is available on the creative cities and many cities around the world are dressing themselves as such.¹⁸ South Asian cities and development work is not thinking on these lines. Current economic work thinks of atomized individuals instead of people in a community. Many communal social capital building aspects such as community centers and libraries are ignored.

Good reform design must also account for the motives and incentives of policymakers and other stakeholders to see what will make them take ownership and responsibility for that policy or reform. The civil service and various state functionaries must become an agent of reform. This would mean moving them away from their current rent-seeking and corruption. This line of reasoning would suggest that Civil Service reform should have priority and must include incentive reform breaking them out of the system of low salaries and corruption.

As Ghani and Lockhart (2008) argue, efficient exchange, functioning markets and a vibrant society all demand an effective state as a foundation. State institutions need to be modernized and aligned with community and social capital development. An effective state needs to be built in many parts of South Asia (in particular Pakistan) and this should be a priority item in any reform agenda. The results of not giving state effectiveness priority it deserves are now being seen!¹⁹

¹⁸ Obvious examples are Dubai, Singapore, Las Vegas.

¹⁹ Again development of state effectiveness varies in South Asia. However, there is a long way to go and perhaps Pakistan has the longest journey ahead.

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