



**TOWARDS A RETURN OF INDUSTRIAL POLICY?  
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# **The Case of Pakistan**

## **Experiments with industrial policy**

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- Brief history of industrial policy in Pakistan
- Industry, trade and growth – Pakistan's experience
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# **Brief history of industrial policy in Pakistan**

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# A brief history of industrial policy

- Pakistan's policies were either formulated in response to a crisis
- Industrial policy has been specific to how each government viewed different productive sectors (sector-picking)
- Pakistan has experienced 5 waves of significant industrial policy changes (next slide)

	Wave 1 Pre-1955	Wave 2 (1955-70)	Wave 3 (1971-73)	Wave 4 (1989-99)	Wave 5 (1999-08)
<b>Based on</b>	Indian trade embargo after partition	Second (1960-65) and third (1965-70) 5 year plans	Nationalization	Privatization	<ul style="list-style-type: none"> <li>• Privatization, deregulation</li> <li>• Macro stabilization</li> </ul>
<b>Policy focus</b>	Consumption goods	Industrial licensing policies (e.g. sugar, textiles, cement) and development finance co's.	Public sector corporations	<ul style="list-style-type: none"> <li>• Deletion</li> <li>• Deregulation</li> </ul>	<ul style="list-style-type: none"> <li>• Automobile</li> <li>• Consumer electronics</li> </ul>
<b>Outcome</b>	Protection from external competition	Spinning mills below optimal capacity and the start of distortion in textiles	<ul style="list-style-type: none"> <li>• deep rooted distortions</li> <li>• projects were chosen on political grounds</li> </ul>	No competitive practices thus privatization did not improve industrial activity	<ul style="list-style-type: none"> <li>• Reversal of trade liberalization post 2008</li> <li>• Inadequate consumer protection and competition</li> </ul>

# Conclusions drawn from history

- Past policies suffered 3 major weaknesses:
  - (1) Lead role of the govt. even during times which stressed upon privatization and trade openness
  - (2) They did not focus on raising productivity (in agri or industry)
  - (3) The structure and incentives of the governing institutions were distortive; corruption increased
- Brecher and Abbas (1972): Import substitution did not cause high industrial growth, it was due to poor initial conditions after independence
  - (i) growth in manufacturing due to excess unutilized capacity
  - (ii) agricultural growth due to favourable weather conditions and not productivity growth
  - (iii) Investment expanded, however productivity growth was stagnant

# Industry, trade and growth – Pakistan's experience

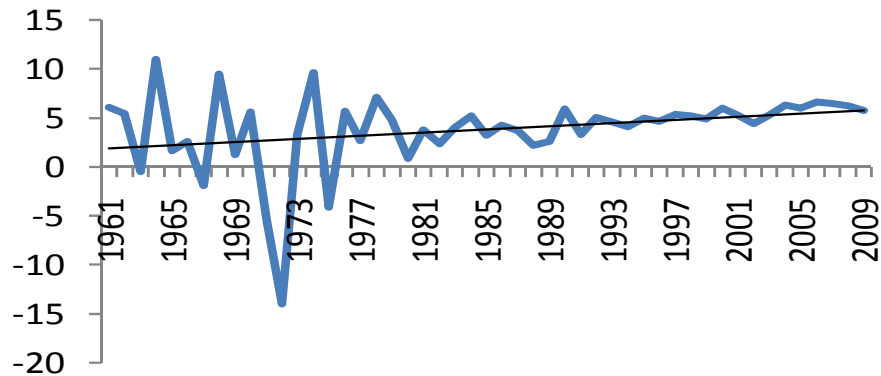
# Industry, Trade and Growth

- Ghani and Musleh-ud-Din (2006) find no strong relationship between public investment and long-run economic growth in Pakistan
- Episodes of stagnating investment rates have been associated with frequent changes of political regimes and balance of payments volatility (Naseem 2008)
- Hausmann and Klinger (2008) show that most factors hindering GDP growth are institutional or policy-based in nature
- Pakistan has seen phases of import substitution, export orientation and now back towards protectionism (PC Growth Strategy)

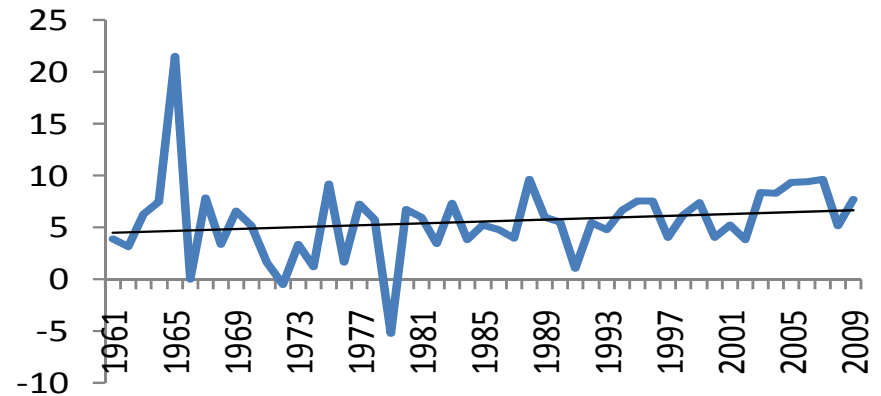


# Falling real growth rates for Pakistan vis-à-vis other South Asian neighbors

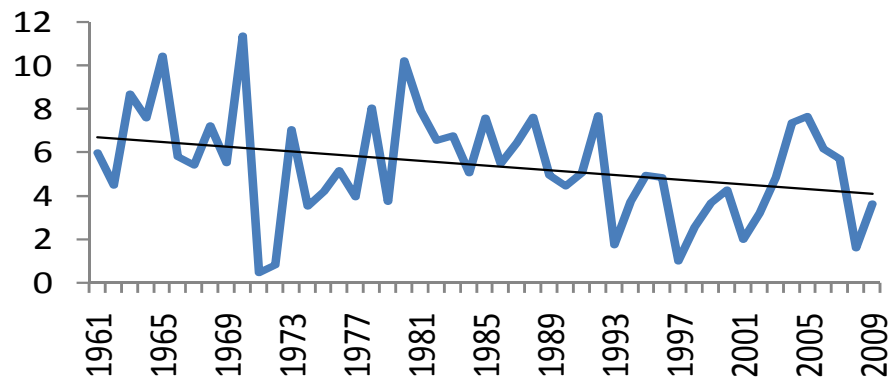
**Bangladesh**



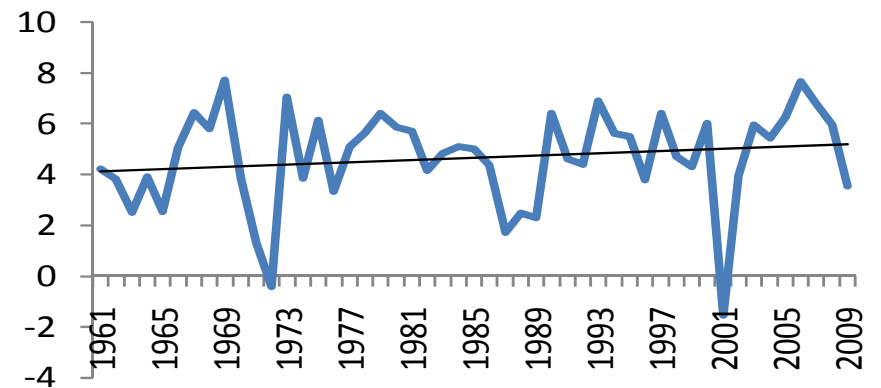
**India**



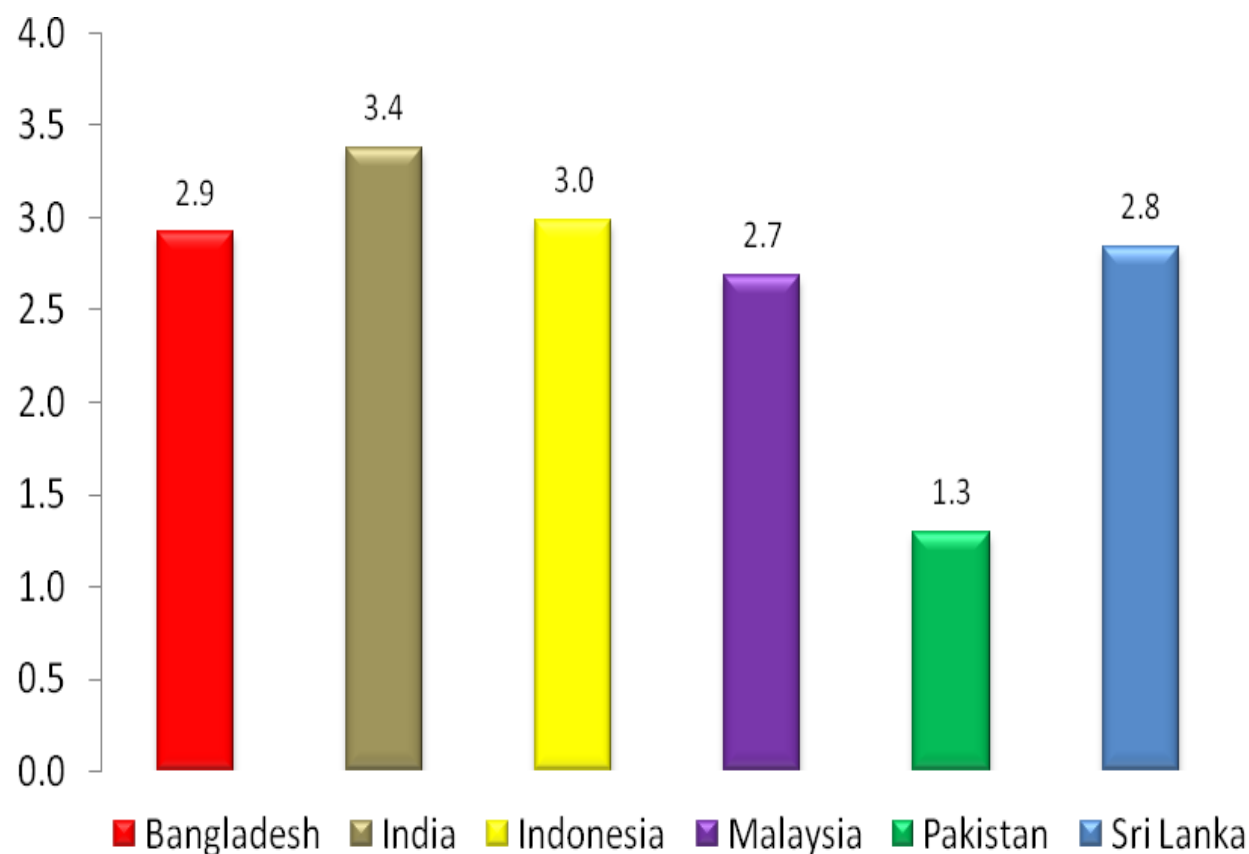
**Pakistan**



**Sri Lanka**

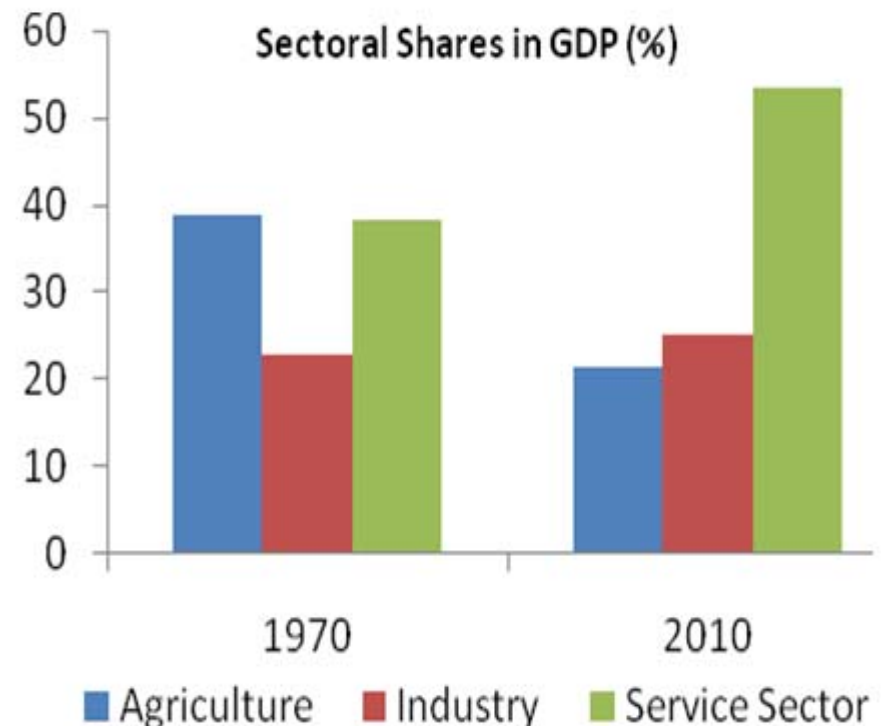
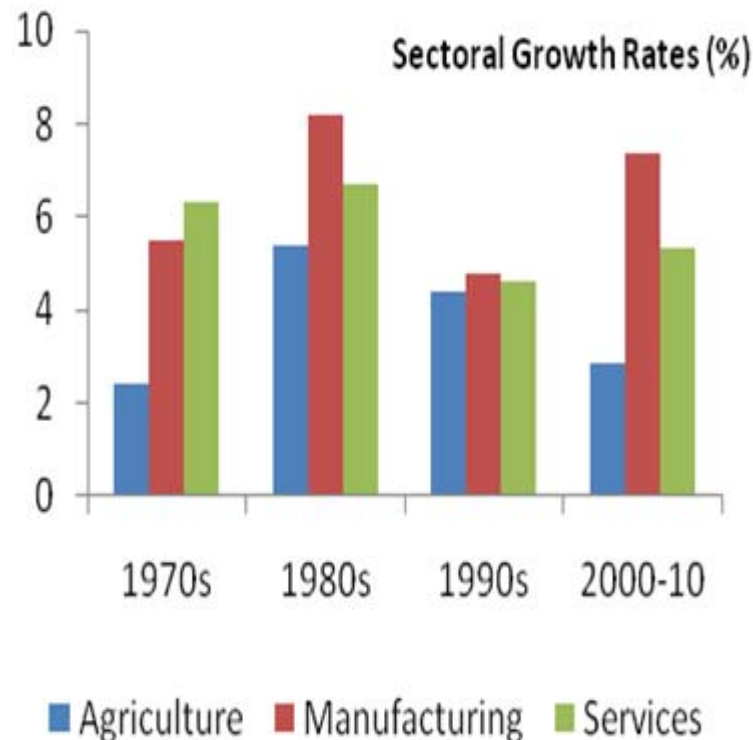


## Pakistan has the lowest total factor productivity growth (%) between 1995 and 2006 in a sample of Asian economies



Source: Asian Productivity Organization 2007

# Structural Transformation 1970-2010

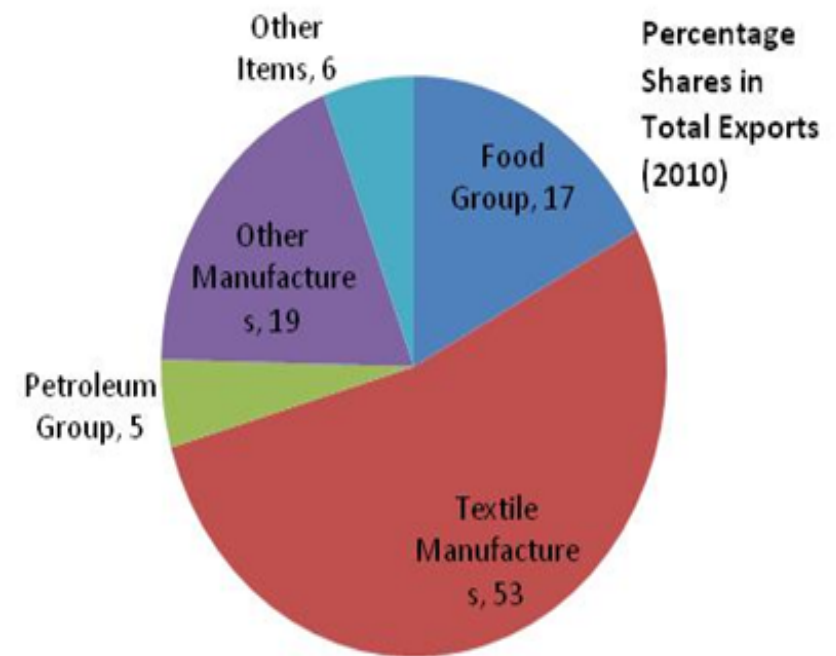
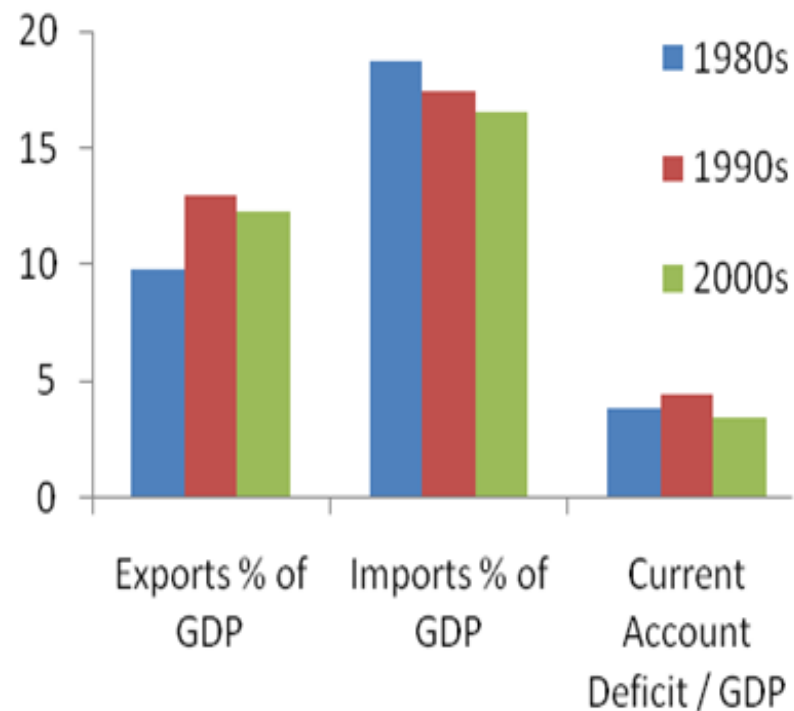


Source: *Economic Survey of Pakistan*, various issues

Manufacturing sector has been the fastest growing sector since the 1980s. However this progress has not translated into a rising share of industry in the overall GDP

**Trade Patterns have not  
changed much in the past 3  
decades**

**Little diversification away  
from textiles**



Source: *Economic Survey of Pakistan*, various issues

# Global best practices

# Evolution of Industrial Policy recommendations

Phase	Key ideas
1940s - 1960s	<ul style="list-style-type: none"> <li>-Industrialization is necessary for development, market failures would prevent this from happening automatically.</li> <li>-IP is needed, particularly infant industry protection, state ownership and state coordination.</li> </ul>
1970s - 1990s	<ul style="list-style-type: none"> <li>-Practical obstacles to IP are considered significant.</li> <li>-Government failure is worse than market failure. IP is invitation to waste and rent-seeking.</li> <li>-Trade liberalization (exports), privatization and attracting FDI together with macroeconomic stability and minimum government interference are the basic requirements for growth and industrialization.</li> <li>-The era of the Washington consensus, especially after the debt crisis of the early 1980s and the ubiquity of structural adjustment programmes (SAPs).</li> </ul>
2000s	<ul style="list-style-type: none"> <li>-Market and government failures are persistent.</li> <li>-The 'how' rather than the 'why' of industrial policy is important.</li> <li>-Innovation and technological upgrading should be a central objective of industrial policy.</li> <li>-Promoting national innovation systems should be an important objective</li> </ul>

# Different views of Industrial Policy

**Selective;** Industrial policy guides govt. interventions to selectively promote certain sectors

Industrial policy should be **broad-based**, promoting the 'competitiveness' across entire manufacturing sector (Lall 2004).

# The current consensus (Naudé 2010)

- The solution is not to abandon industrial policy altogether but to realize that the design of the interventions is more important and innovation and technological upgrading across the board should be the objective of industrial policy
- Industrial policy in the context of
  - rise of global production sharing
  - recent crises in food, fuel and financial markets
  - climate change
  - the rise of China and India
  - the rise of the 'entrepreneurial economy'



# **Need for Consensus-building in Pakistan**

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# **The Need for Consensus**

## **Draft National Industrial Policy (NIP)**

- Favors protection of; steel, fertilizer and chemicals and sub-sectors (distortive approach of the past)
- Based on the premise that liberal trade policies have weakened the manufacturing sector (not rigorously proven)
- Assign a central role to the state in incentivizing local manufacturing and discouraging the import of finished goods and/or export of raw materials through the placement of non-tariff trade barriers.

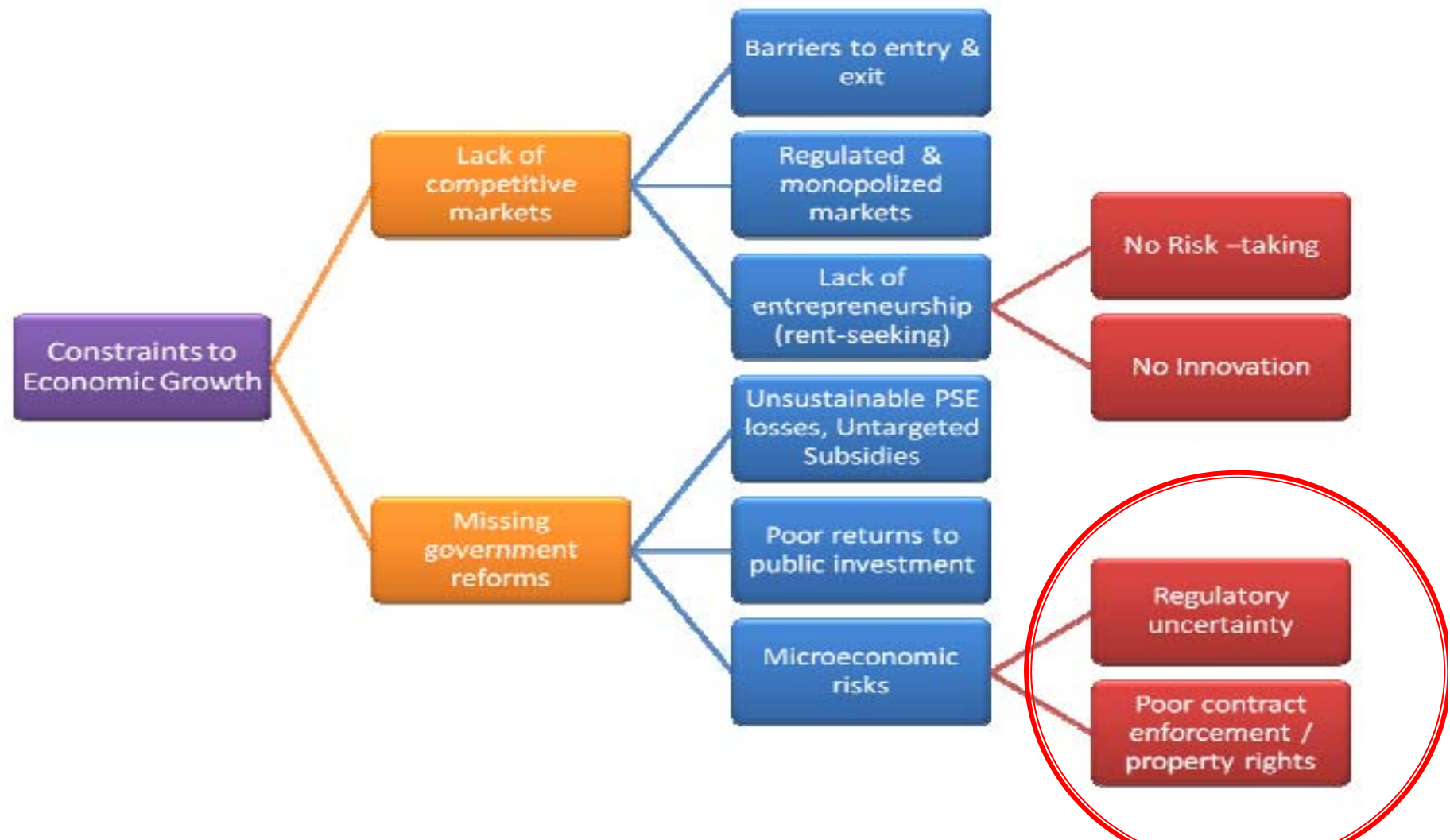
# **The Need for Consensus**

## **Framework for Economic Growth**

The Planning Commission's new framework for economic growth (2011); opposes the NIP and proposes:

- Lower barriers to entry
- Refrain from sector-picking
- Further reduction in tariffs
- Abolishment of regulatory duties
- Enactment of pending national competition act
- Corporate rehabilitation and bankruptcy laws to allow exit of sick industries

# Pakistan: Binding Constraints



# Critical Reforms Required (Industry)

## Diversification

- Support should be time-bound and linked to performance
- Promote industries with global dynamic demand (textile sector has not shown learning spillovers)

## Investment Climate

- Simply tax procedures
- Reduce barriers to entry & exit
- Corporate Rehabilitation and bankruptcy law

## Competition Policy

- Government exit from market
- Industrial licensing and financial sector policies lead to monopolistic markets
- Enforce Competition Act 2010

## Institutions (EDB and NTC)

- Abolish SRO system
- Reduce discretionary role of Engineering Development Board
- Tariffs should have economic rationale and published by NTC

# Coordination between Industrial and Trade Policies

## Required Trade Policy Measures

- Abolish import licensing
  - Revisit role of Engineering Development Board
- Uniform tariffs structure
- Review justification for protection and subsidies
  - Revisit role of National Tariff Commission
- Transparency in tariff evaluations
  - The reports not publically disseminated
- Neutral real exchange rate policy
- Stronger trade relations with India
- Accelerate potential of FTAs, e.g. China and Malaysia.

**Thank You**