Democracy, Autocracy and Macroeconomic Performance in Pakistan

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DEMOCRACY, AUTOCRACY AND MACROECONOMIC PERFORMANCE IN PAKISTAN

By:

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ABSTRACT

Pakistan showed a healthy growth rate of 5.6 percent during the entire history and faced many ups and down in the economic growth due to dramatic changes in the political regimes. The literature shows mixed results regarding the impact of autocracy or democracy on economic growth. The aggregate growth of the economy under the autocracy remained better as compared to democratic period. Financial Indicators show consistent path throughout the history of Pakistan. Different trade policies are designed in different regime to run the external sector and the impact of each policy was different.

<table>
<thead>
<tr>
<th>Keywords</th>
<th>Democracy, Autocracy, Macroeconomic Performance, Pakistan, Growth Financial Sector, Fiscal Sector, External Sector</th>
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<td>JEL Classification</td>
<td>O47</td>
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1. Introduction

The sixty year history of Pakistan is divided into six episodes; those represent different kind of economic policies due to presence of different type of government. The first eleven years, from 1947 to 1958, are the

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years, when the country and economy were trying to settle down, but to
no gain. The first decade (Regime-0) of economic policy and planning
witnessed the attempt of a bureaucracy to kept Pakistan on its feet. All
efforts to move Pakistan as democratic country were unsuccessful. The
failure of democratic experiments from 1949 to 1958 can be attributed to
several specific factors. One was factional conflict and the inability of
the Muslim League to become a well-known national party. Another was
the bitter contest between president and prime minister over leadership
of the central government (Monshipouri, et al. 1995). The failure of
democracy leads to coming out of autocracy imposed by Major General
Iskander Mirza, Field Marshal General Muhammed Ayub Khan and
General Yahya Khan (1958- 1971). Division of regime starts with the
coming out of first military government (Regime-1). This was the
golden era in a sense that economy of Pakistan stabilized, and settles
down. Pakistan achieved highest growth rate in this period. The second
brief and even though highly remarkable era in the Pakistan’s history
was the five and half years of Zulfiquar Ali Bhutto. It was a democratic
government, which turns the Pakistan a democratic country (Regime-2).
The best feature were the nationalization, social reforms and the opening
of the abroad labour migration. His rule ended with the imposition of
Pakistan’s second martial law under General Zia ul Haq in 1977. Second
period of autocracy (Regime-3) also show significant growth

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5 "Regime-0" represent the first eleven of the history of Pakistan from 1947 to 1958,
Governer General, President and Prim Minister: Father of the Nation Quaid-e-Azam
Muhammed Ali Jinnah, Khawaja Nazim ud-Din, Malik Ghulam Muhammed, Major
General Iskander Mirza, Khan Liaquat Ali Khan (Shaheed), Khawaja Nazim ud-Din,
Chundrigar and Malik Feroze Khan Noon.

4 "Regime-1" President, Prime Minister and Chief Martial Law Administrator and
President: represent the era of Malik Feroze Khan Noon, Nurul Amin, Major General
Iskander Mirza, Field Marshal Muhammed Ayub Khan, General Yahya Khan and
Zulfiquar Ali Bhutto (Shaheed) from 1958 to 1971. This is first period of autocracy in
Pakistan.

5 "Regime-2" represents the first democratic government (Democracy) in Pakistan,
which was elected through public voting. This government led by Major General
Iskander Mirza (Chief Martial Law Administrator and President), Nurul Amin (Prim
Minister), Zulfiquar Ali Bhutto Shaheed (President, Chief Martial Law Administrator
and Popular Prim Minister) and President Ch Fazal Ilahi form 1971 to 1977.

6 "Regim-3" start with the second martial law imposed by General Muhammad Zia ul
Haq (Shaheed) from 1977 to 1988. Regime-3 represents the second autocratic period
in Pakistan. Democracy ended in this period. The period also included Prim Minister
Muhammed Khan Junejo period of three year.
performance and stability of economy of Pakistan. There were some similarities between the first and second autocratic period. The main feature that contribute the best performance of Zia era were the opening up of the Middle East, the Afghan war, attempts at the Islamization of the economy and society, and a praetorian democratic system between 1985 and 1988 (Zaidi 2005). The end of era General Muhammed Zia ul Haq in 1988 brought once again democratic government in Pakistan. This starts the second episode of democracy in Pakistan (Regime-4) that shows social and economic performance in Pakistan in all sectors. Pakistan shows similar growth like in 1970s. Another military regime that was third attempt of military was brought by General Pervaiz Musharraf in 1999 by ending the Nawaz Sharif government (Regime-5). The return of military directly in politics does imply considerable change compared to the 1988-1999 period. Economic growth after 90s once again starts moving upward, almost matching the growth of 80s. Furthermore, Pakistan’s creditworthiness has been upgraded and the country has joined the list of few developing countries that have successfully completed the transitions from an IMF program to enter international financial markets.

The main purpose of this paper is to analyze the performance of macroeconomic indictor in different regimes. How autocratic and democratic policies shows their impact on these indicators. In section 2 different studies are reviewed, that shows empirically and theoretically the impact of democracy or autocracy on the economic growth of any country. In section 3, link between economic growth and type of regime with reference to Pakistan’s data is developed. This section measures the growth performance of the economic indictors regime-wise. This section

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7 “Regime-4” represents the second episode of democratic government in Pakistan from 1988 to 1999. This period is divided into four part, on the basis of tenure of each government. First democratic government established by Prim Minister Benazir Bhutto (Shaheed) from 1988 to 1990, 2nd by Prim Minister Mian Muhammed Nawaz Sharif Regime from 1990 to 1993, 3 by Prim Minister Moin Ahmed Qureshi 4th by again P.M Benazir Bhutto (Shaheed) from 1993 to 1996, 5 by Prim Minister Malik Meraaj Khalid, and 6 by P.M Nawaz Sharif from 1996 to 1999. During the period there were four President namely: Ghulam Ishaq Khan, Wasim Sajjad, Sardar Farooq Khan Laghari and Muhammed Rafiq Tarar.

8 “Regime-5” refers to the third episode of autocratic government in Pakistan led by General Pervez Musharraf from 1999 to 2008. During the period there were three Prim Ministers, Prim Minister Mir Zafarullah Khan Jamali, Prim Minister Choudhary Shujaat Hussain, and Prim Minister Sir Shaukat Aziz.
is subdivided into four parts like economic growth, fiscal sector, financial sector, and external sector. In last section conclusions are drawn.

2. Democracy Versus Autocracy

A political system that allows the citizens to participate in political decision-making or to elect representatives to government bodies is called democracy\(^9\) or a system of government in which power is vested in the people, who rule either directly or through freely elected representatives is named as democracy\(^10\). Political economists have mystified at length about democracy’s effects on economic performance. (Brunetti 1997; Keech 1995; Przeworski et al. 1996; and Remmer 1995). The literature shows that relationship between democracy and growth that are both negative and positive. The negative relation is reviewed by Keech (1995), Alesina and Rodrik (1994) and Persson and Tabellini (1994). In their studies democracies are susceptible to demands for redistribution because they give voice to disadvantaged groups. Redistribution may divert resources from productive investment and thus democracy damage economic growth. Democracy may hurt economic performance in many other ways. Olson (1982) predicts stagnation due to interest group rent seeking. Nordhaus (1975) predicts costly economic manipulation for short run electoral gain. Barro and Gordon (1983) illustrate a "time-inconsistency problem:" Positive views also be plentiful. Wittman and others argue that democratic competition is inherently effective as a mechanism for revealing information (Wittman 1989, 1995; Baba 1997). The more developed the democracy, the more highly developed the institutions that guarantee clearness of policy and policy-making processes. This enables citizens to check voted officials more effectively and reduces the probability of self-serving policies (Dennis, et. al. 2001). Several studies construct on North (e.g., 1989) arguing that institutions critical to growth are enhanced in democracy, thereby encouraging growth (Kormendi and Meguire 1985; Knack and Keefer 1995; and World Bank 1997). Pastor and Sung (1995) argue that private sector actors are more likely to commence investment in settings

\(^9\) Archaeology Dictionary Oxford University Press

\(^{10}\) Political Dictionary, Houghton Mifflin Company
where property rights are better protected, and they find that higher rates of investment are correlated with democratic regimes. Lohmann (1999) proposes that elections serve to select competent leaders and that, over time; democracy should be correlated with higher output. Empirical tests of the link between democracy and economic performance have produced unclear results to match the conflicted theory. Siroy and Inkeles (1990) reviewing fifteen empirical investigations and found that eleven showed either no relationship or a conditional relationship between growth and democracy. Przeworski and Limongi (1993) review eighteen studies, and also find inconsistent results: eight studies reported a positive link between democracy and growth; eight reported a negative link, five others, no link. Following studies similarly disagree on the direct effects of democracy on growth: Helliwell (1994) negative; Keefer and Knack (1997) negative none; Leblang (1997) positive; Przeworski et al. (1996) none; Burkhart and Lewis-Beck (1994) none; and Limongi (1997) report that growth is stabilizing for democracies but do not explore the reverse relationship (Dennis, et al, 2001).

An autocracy is a form of government in which the political power is held by a single person\(^{\footnote{http://en.wikipedia.org/wiki/Autocracy}}\) or a government in which a single leader or party exercises absolute control over all citizens and every aspect of their lives. Similarly different studies show different result, regarding the impact of autocracy on the economic performance of any country. Like Przeworski (1966) by using the data of 57 countries from 1949 to 1963, analyze that dictatorships at medium development level grew fastest and Adelman and Morris (1967) proved that autocracy helped less and medium developed countries in growing faster by using data on 74 underdeveloped countries (including communist bloc) from 1950 to 1964. Kohli (1986) and Landau (1986) also concluded that autocracy is favorable for economic growth than democracy.

After analyzing these studies, it can be concluded that some expert favor democracy, and other favor dictatorship or autocracy, and even it is also discovered that there is no difference of regime regarding there impact on economic growth. Many studies like Marsh (1988) shows that there is no difference between regimes by using data on 47 countries from 1965
to 1984. From these studies one can’t says that democracy fosters or hinders economic growth or autocracy fosters or hinders economic growth or both have positive or negative impact on the growth. All we can offer at this moment are some educated guesses (Przeworski, 1993). Reynolds (1983), having reviewed the historical experience of several countries, concluded that spurts of growth are often associated with major political transformations. Another dimension that captures this link is that politics does matter, but "regimes" do not capture the relevant differences (Przeworski, 1993).

3. Link Between Regimes And Economic Cycle

In Pakistan democracy and autocracy remain in power alternatively in the entire history and macroeconomic performance has been viewed as a process that is initiated and controlled by the state to improve the economy. Existence of different type of empowerment in Pakistan shows great diversification in economic growth. There are two different views regarding the correlation between regime types and development. One group supports autocracy and other in favor of democracy. Economic growth has been successfully achieved in autocracy regimes in Pakistan; but this growth has never enhanced democracy there. No clear pattern has emerged showing the relationship between development and democracy in the country's brief history (Monshipouri, et al. 1995). The lack of such a correlation indicates that economic growth without the expansion of civil and political rights is unlikely to lead to democracy in Pakistan. Economic growth has failed to produce a strong, large middle class in Pakistan; instead, it has created and strengthened only the privileged groups. Significant foreign interest and interference has culminated in external handling of the nation's policies. Pakistan has had governments that were dictatorial and produced good economic results but failed to create sustainable democracy. The economic, political, and social dimensions of Pakistan's history reflect fluctuations between autocratic and more democratic regimes, and the activities of each have created tension between sociopolitical development and economic development.
4. Economic Growth

Comparatively, Pakistan’s economic growth record shows that best growth performance is recorded in autocratic period. Table 3.a.1 gives a useful indication of growth performance during different regime. The first eleven years of Pakistan history, that is contributed as attempt to run country as democratic nation, shows very low growth rate (3.08%), with very low growth rate of agriculture sector (1.43%), less than half of the annual growth rate in Population. Agriculture was allowed to stagnate in the 1950s because the ruling elite believed at that time that it was essential to industrialized at all cost and great speed. The growth rate of manufacturing sector (8.81%) was quite reasonable. Government policies were heavily biased against agriculture and it was only towards the end of the 1950s- when it became clear that growth in agriculture was necessary for the survival of the country (Zaidi 2005). Era of Ayub Khan showed highest growth performance in all sector of economy. Annual average growth rate of real GDP was 6.8% that is accomplished by the excellent growth of manufacturing (9.9%) and agriculture (5%) sector with the impact of green revolution. During this period Pakistan was considered to be a model capitalist economy (Zaidi, 2005). The rapid economic growth created regional and class inequalities and was accompanied with a fall in living standards for substantial sections of the population (Monshipouri, et al. 1995). High growth rate that Pakistan enjoyed in first autocratic is due to the easy access to the foreign aid which increases from 2.5 percent of GNP in mid 1950s to 7.0 percent of GNP in mid 1960s. The decade of ’60s, notwithstanding good growth performance is criticized for increasing income disparities and promoting industrial rent-seeking elite that thrived on the system of Licensing and Protection from competition.

The 1960s has been termed a controversial decade for the type of economic policy pursued, and the resulting economic and political effects. Dozens of economists and social scientists have written about the Field Marshal General Muhammad Ayub Khan’s era and they agree that considerable economic growth and development occurred during this period. They argue that significant positive fluctuations were made in
industrial and the agricultural production, whereas the growth rates in excess of 20 percent per annum were witnessed in the large scale-manufacturing sector. In the first five years of the eras, manufacturing grew by as much as 17 percent, and in the second half of the President Muhammad Ayub Khan’s rule, agricultural growth increased by 6 percent, and the industry grew by 10 percent. Analysis shows that the whole economy performance and the different individual sectors grew by phenomenal rates and World economies Pakistan was considered to be a model economy in the 1960s. Observers have pointed out that this more capitalist development caused serious economic, social, and political tensions. So as concerned the argument that there was an increased disparity in incomes across different regions of the country. Economists know very well that this is a fact that growth with due justice was not possible in a country like Pakistan at initial stages of growth and development, also which was capital poor at that time. Economists and social scientists were so supervised at what had happened during the Ayub Khan’s rule. The consequence of Ayub Khan’s economic policies was that there was growth and development, the forces of production did expand. However, what is most interesting about Ayub’s Khan era is the fact that the economic package was thoroughly illiberal, and was almost the opposite of what is being termed economic illiberal, and was almost the opposite of what is being termed today. It was capitalism, and the private sector did play a significant role, but it was a guided, bureaucratically governed, and directed capitalism. The bureaucracy played an active, influential, and constructive role in the establishment of private sector capital in Pakistan. Dozens of constraints on setting up industry, red tape and numerous hurdles in financial and industrial policy did not stop the impressive growth in this period. The nature of the economy was precisely what it should not have been according to the doctrine of economic liberalism and liberalization. Trade was highly controlled and closed. The exchange rate was overvalued and it distorted local markets. Financial capital was rationed, and the stock market performing was significant. There was government regulation, planning strategy was directing and encouraging the private sector and the market. The government as a vehicle for growth consciously identified the agricultural sector and numerous (governmental) decisions were taken which resulted in growth at times in excess of 11 percent per year. The transformation of the agricultural sector from a precapitalit to a
capitalist one was accelerated by the active involvement and interference of the government. Even public sector projects commissioned by the Pakistan Industrial Development Corporation (PIDC) were ‘gifted away’ to the private sector. The bureaucracy in essence, involved in creation of the private sector capitalist in Pakistan, indeed a very illiberal process according to conventional wisdom. The following table explains the economic performance during different eras from 1960s to 2001 (Khan 2004).

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>GDP</td>
<td>6.77</td>
<td>4.84</td>
<td>6.45</td>
<td>4.70</td>
<td>3.9</td>
</tr>
<tr>
<td>Agriculture</td>
<td>5.07</td>
<td>2.37</td>
<td>5.44</td>
<td>4.09</td>
<td>6.1</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>9.93</td>
<td>5.50</td>
<td>8.21</td>
<td>4.95</td>
<td>1.4</td>
</tr>
<tr>
<td>Commodity Producing Sector</td>
<td>6.83</td>
<td>3.88</td>
<td>6.49</td>
<td>4.67</td>
<td>3.0</td>
</tr>
<tr>
<td>Service Sector</td>
<td>6.74</td>
<td>6.26</td>
<td>6.65</td>
<td>4.75</td>
<td>4.8</td>
</tr>
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</table>


The aggregate growth of the economy under the PPP 12 (Regime-2 “Democratic Episode”), as measured by the annual average of GDP was 3.9%. There was a decline in per capita income. The growth rate of all other sector also decline. Industry and educational institutions were

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12 Pakistan People Party: The PPP was launched at its founding convention held in Lahore on November 30, 1967 and Zulfiqar Ali Bhutto was elected as its Chairman. Goals for which the party was formed were the establishment of an “egalitarian democracy” and the “application of socialistic ideas to realize economic and social justice”. A more immediate task was to struggle against the hated dictatorship of Ayub Khan, who was at the height of his power when the PPP was formed. The Party also promised the elimination of feudalism in accordance with the established principles of socialism to protect and advance the interests of peasantry. During its Government from Dec. 20, 1971 to July 5, 1977, the PPP government made significant social and economic reforms that did much to improve the life of Pakistan’s impoverished masses. Bhutto was symbol of Reform and Reconstruction.
nationalized, the efficiency of industry declined (Burki et. al 1991). The Government tried to make up for this deficiency by larger investments in the public sector. But these investments were mainly in social over-head capital projects, which were used for production, and had not yet gone into production (Khan 2004). The PPP government reforms agenda main objectives was to achieve socio-economic growth and development through increased production: agricultural, industrial and other etc. The main goal was an improvement in the standard of living of the people by increases in per capita incomes, by the provision of employment opportunities, by equitable income distribution, by eradication of poverty, by providing basic needs, by the provision of educational facilities to raise the cultural and intellectual levels of the people, by the extension of health facilities, by geographically balanced development to remove regional disparities and by promoting rural development to remove rural and urban inequalities. The economy was to be made viable and self reliant by the diversification of production, by improvement of the recognized but reliance on it was to be reduced over time. In short, the development was intended to raise the quality of life of the people in its broadest sense and to bring he economy to a stage of self-sustaining growth. There have been occasional shifts in emphasis form time to time, but the above have remained, by large the main objectives of development till the present time. So the varying degrees of success in the achievement of these objectives (Khan 2004). Bhutto's nationalization measures, which later badly affected small-scale entrepreneurs and several private industrial firms, led to an deal between religious elites and the entrepreneurs that proved to be a major force in removing him from office in 1977 (Kemal et. al. 1987). Secondly, regional tension, floods, pest attacks, and external shocks including hike in petroleum prices and recession in the world market, also contributed in low growth performance. Industrialists faced a number of governmental restrictions, including fixed prices. These measures created a considerable uncertainty, resulting a fall in the private investment and flight of capital (Haq, et. al. 2007). Third reason of low growth was that overall deficit increased from 2.1 percent of GDP to 5.1 percent of GDP. Second episode of autocracy was also followed by an excellent growth performance. The average annual GDP growth rate was 6.6% during this period. The manufacturing growth rate was 9.3%,. During the Zia regime, although growth in the agriculture sector remained sluggish, around 3.6% due to unfavorable weather conditions, the industrial sector posted a healthy average annual growth of more than 9% substantially above the 3.73% average during 1971-77. The services
sector also grew strongly in the 1980s, led by ownership of dwellings, transportation, storage and communication and wholesale and retail trade. On the demand side, Din (2007) shows that growth in the 1980s, particularly during the 1983/84-1987-88 period, was ‘fuelled by an upsurge in both private and public consumption expenditure, which grew on average respectively by 5.5% and 9.3% in real term’. This significant growth performance showed that economy clearly started to revitalize after the Bhutto government was overthrown.

Table 4.1.1 Regime-wise Economic Growth

<table>
<thead>
<tr>
<th>Growth rate (%)</th>
<th>Regime</th>
<th>Regime-1</th>
<th>Regime-2</th>
<th>Regime-3</th>
<th>Regime-4</th>
<th>Regime-5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>3.08</td>
<td>6.8</td>
<td>3.9</td>
<td>6.6</td>
<td>4.5</td>
<td>5.0</td>
</tr>
<tr>
<td>GDP Per Capita</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capita</td>
<td>1.72</td>
<td>4.3</td>
<td>0.35</td>
<td>3.93</td>
<td>1.50</td>
<td>2.90</td>
</tr>
<tr>
<td>Agriculture</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sector</td>
<td>1.43</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sector</td>
<td>9.9</td>
<td>3.73</td>
<td>9.16</td>
<td>4.30</td>
<td>6.40</td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sector</td>
<td>6.7</td>
<td>5.65</td>
<td>7.31</td>
<td>4.46</td>
<td>5.71</td>
<td></td>
</tr>
</tbody>
</table>

Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation

The period after the President General Muhammad Zia ul Haq in 1988 resulted in the return of second episode of democratic regime. Pakistan has four general elections, with both Benazir Bhutto and Nawaz Sharif begins returned to power twice. Once again the era of democratic regime showed negative growth in all sector. The average growth of real GDP was 4.5% with almost negligible growth of agriculture (1.50%) sector and also very low growth of manufacturing (4.30%) sector. Beside political instability, many other factors contributed in the low economic performance, including deteriorating law and order, economic sanctions.

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13 These are all annual average growth rate
14 First Democratic Attempt or Period of Democracy-0
15 Autocracy-1 (Ayub Khan)
16 Democracy-1 (Zulfiqar Ali Bhutto)
17 Autocracy-2 (Zia ul Haq)
18 Democracy-2 (Bazir Bhutto and Nawaz Sharif)
19 Autocracy-3 (Pervez Musharraf)
in the wake of nuclear testing, persistent drought conditions, and infrastructure bottlenecks such as inadequate power supply with frequent power outages in the industrial area, and also lack of many public facilities at optimal levels (Haq, 2007). Failure in enhancing revenues consistent with growing expenditure requirements, stagnation in exports and in overall foreign exchange earnings exacerbated these imbalances and vitiated a stable macroeconomic environment (Din, 2007). The consequences of the policies designed by this democratic regime have been serious economic crises at the macroeconomic and individual level throughout the period (Zaidi, 2005). During this regime the volume of foreign aid was relatively low and that too was available only under IMF's strict Conditionality. It seems more than a coincidence that the growth performance during the this period was not very encouraging, though a significant part of the blame can also be attributed to political instability within the country. The persistence of large fiscal and current account deficits and the associated build up of public and external debt emerged as the major source of macroeconomic imbalances in the 1990s. Failure in enhancing revenues consistent with growing expenditure requirements, stagnation in exports and in overall foreign exchange earnings exacerbated these imbalances and vitiated a stable macroeconomic environment (Din, 2007).

**Figure 3.a.1: Regime-wise Real GDP and GDP per Capita growth rate**

Source: GoP, Economic Advisor's Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation
Growth performance during third episode of autocratic regime has been impressive, 5% per annum on average, matching the growth of 80s. Several factors contributed in this performance. Growth performance of manufacturing (6.40%) sector and services sector (5.71%) is quite impressive. The overall share of values added industry in GDP is 26.2% in 2005-06 (Economic Survey, 2005-06). Fiscal deficit has been reduced to around 4 % of GDP, debt ratios have witnessed significant improvement, exchange rate has been stabilized and international reserves have reached an all time high level.

These results suggest that economic growth in Pakistan shows excellent performance in autocratic period then the democratic period. All sectors grew rapidly in autocratic regime. This Growth pattern of other sectors is also shows the similar behavior, which is shown by the real GDP. Figure 3.a.2 shows the trend of growth of agriculture, manufacturing and services sector in different regimes.

**Figure 3.a.2: Regime-wise Sectoral Growth Rate**

*Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation*
a. Fiscal Sector

Regarding public finance indicator there is no difference that indicates which type of government is better. In first autocratic period the overall fiscal deficit remain quite low (2.10 % of GDP (mp)) and in first democratic period it remain high (5.30 % of GDP (mp)). During the 2\textsuperscript{nd} autocratic regime the fiscal deficit in Pakistan averaged over 7.10% of GDP and was financed largely through extensive controls on financial markets, relatively strong monetary growth and external borrowing; growth also averaged 6% a year in the 1980s. But in the early 1990s adverse supply conditions increased the fiscal deficit to over 9% of GDP and the growing external debt burden eventually led to a financial and exchange market crisis. Again with the arrival of Musharraf government, overall deficit again fall to very low rate (3.2% of GDP (mp)). Total revenue has not grown substantially over the entire history and ranged around 17 or 18 percent of GDP.

**Figure 3.b.1: Total Revenue, Expenditure, and Overall Deficit as \(\%\) of GDP (Market Prices)**

![Graph showing revenue, expenditure, and overall deficit as % of GDP](image)

**Source:** GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, 2005-06, Self Calculation

Expenditure side shows significant changes over the entire history. These changes are closely related with the debt position of Pakistan. Analysis shows that change in external debt/GDP ratio can be attributed to the
increase in non-interest current account deficits and capital losses on external debt due to real exchange rate depreciation. The pattern of change in the external debt/GDP ratio differs fundamentally between the regimes. In first autocratic period, external debt to GDP ratio increase (18.75). The highest ratio of external debt to GDP was found in first democratic period (60% of GDP). In 1980s, the Period of Zia also show high debt to GDP ratio with high debt servicing. Unlike Zia’s period, the ratio has fallen in the 2nd democratic period largely because of the difference in the rate of real exchange rate depreciation during the two periods and not due to the difference in non-interest current account deficit (Pasha, 1995). Ratio falls in the period of Musharraf period.

**Table 3.b.1: Regime-wise Fiscal Sector of Pakistan**

<table>
<thead>
<tr>
<th>Fiscal Sector</th>
<th>Regime-0</th>
<th>Regime-1</th>
<th>Regime-2</th>
<th>Regime-3</th>
<th>Regime-4</th>
<th>Regime-5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Price Level of GDP</td>
<td>53.72</td>
<td>51.56</td>
<td>38.16</td>
<td>33.15</td>
<td>24.24</td>
<td>20.11</td>
</tr>
<tr>
<td>Total Debt Growth Rate</td>
<td>11.9</td>
<td>12.87</td>
<td>20.9</td>
<td>17.15</td>
<td>17.88</td>
<td>4.35</td>
</tr>
<tr>
<td>External Debt Growth Rate</td>
<td>-</td>
<td>11.50</td>
<td>6.38</td>
<td>6.35</td>
<td>4.40</td>
<td></td>
</tr>
<tr>
<td>As percent of GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Revenue</td>
<td>10.99</td>
<td>13.1</td>
<td>16.8</td>
<td>17.3</td>
<td>17.1</td>
<td>15.1</td>
</tr>
<tr>
<td>Expenditure</td>
<td>10.87</td>
<td>11.6</td>
<td>25.1</td>
<td>24.9</td>
<td>24.1</td>
<td>19.0</td>
</tr>
<tr>
<td>Overall Deficit</td>
<td>0.11</td>
<td>2.10</td>
<td>5.30</td>
<td>7.10</td>
<td>6.90</td>
<td>3.2</td>
</tr>
<tr>
<td>Total Debt</td>
<td>28.37</td>
<td>32.75</td>
<td>63.69</td>
<td>59.54</td>
<td>78.99</td>
<td>90.2</td>
</tr>
<tr>
<td>External Debt Servicing</td>
<td>-</td>
<td>18.78</td>
<td>46.78</td>
<td>34.73</td>
<td>38.28</td>
<td>35.0</td>
</tr>
</tbody>
</table>

Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, Self Calculation
**Figure 3.b.2: Regime wise Total Debt, External Debt and External Debt Servicing as % of GDP**

![Chart showing regime-wise debt and servicing](chart.png)

*Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, 2005-05*

**b. Financial Sector**

It is a generally accepted belief that a sound financial sector is a prerequisite for macroeconomic stability.

**c. Growth of Financial Indicator**

Total monetary assets in the economy consist of currency in circulation, which is issued by the State Bank of Pakistan, minus the amount held as cash by the banking sector. Adding demand deposit and other deposit constitute the M1 and adding time deposit in M1 define the M2. Growth of M1 and M2 show consistent path throughout the history of Pakistan. There is little impact of regime on the growth of monetary assets. Pakistan’s inflation rate over the years has been enigma to the most analysts. Inflation rate is quit low in Regime-0 and in first autocratic period (4.74% and 3.52% respectively). It rises to 13.97% on the average in Bhutto regime, and again it falls to an average of only 7.2% in the Zia regime. Once again it rises in second democratic period up to 9.55% on average and again falls in the current autocratic period on average of 5.56%. From 1961 to 1988, the bond financed government expenditure has negative effect on the acceleration of inflation and real money balances are found to contribute the inflation during this period (Hossain, 1990). Instead a high fiscal deficit of the late 1980s, however the high inflation was considered to be the key consequences of the irresponsible policies of government (Hossain, 1990). Some people said that inflation is purely a monetary phenomenon in Pakistan. High inflation of second
democratic period is mainly due to procurement prices especially of wheat and the administered prices of fuel, gas and electricity (Pasha et al, 1995). The reason why inflation fall rate started to fall after the 1998 are probably related to the considerable slowing down of aggregate demand following the nuclear test, General Mushraff’s cop and 9/11 (Zaidi, 2005).

Table 3.c.1: Regime-wise Growth of Financial Indicator

<table>
<thead>
<tr>
<th>Financial Indicator</th>
<th>Regime</th>
<th>Regime-0</th>
<th>Regime-1</th>
<th>Regime-2</th>
<th>Regime-3</th>
<th>Regime-4</th>
<th>Regime-5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth Rates</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>M1</td>
<td></td>
<td>7.32</td>
<td>10.27</td>
<td>14.91</td>
<td>16.27</td>
<td>11.98</td>
<td>16.21</td>
</tr>
<tr>
<td>M2</td>
<td></td>
<td>7.89</td>
<td>13.16</td>
<td>14.20</td>
<td>16.18</td>
<td>15.22</td>
<td>15.06</td>
</tr>
<tr>
<td>GDP Deflator</td>
<td></td>
<td>3.03</td>
<td>3.49</td>
<td>13.65</td>
<td>7.17</td>
<td>9.52</td>
<td>5.32</td>
</tr>
<tr>
<td>Inflation</td>
<td></td>
<td>4.74</td>
<td>3.52</td>
<td>13.97</td>
<td>7.2</td>
<td>9.45</td>
<td>5.56</td>
</tr>
<tr>
<td>As percent of GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>M1</td>
<td></td>
<td>32.61</td>
<td>29.47</td>
<td>24.02</td>
<td>26.07</td>
<td>23.12</td>
<td>21.99</td>
</tr>
<tr>
<td>M2</td>
<td></td>
<td>36.30</td>
<td>41.70</td>
<td>35.55</td>
<td>39.10</td>
<td>42.51</td>
<td>41.56</td>
</tr>
</tbody>
</table>

Source: GoP, Economic Advisor's Wing, Finance Division, Economic Survey, FBS, SBP, IFS, Self Calculation

Figure 3.c.1: Regime wise Inflation rate

Source: GoP, Economic Advisor's Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation
d. Financial Sector Development Indicators

Financial sector development can be assessed on the basis of the level and extent of financial sector depth and efficiency\textsuperscript{20}. The one of the most commonly used indicator for financial development is “M2 (broad money)\textsuperscript{21} to GDP ratio”. The higher the M2/GDP ratio, the more developed and efficient financial intermediation is perceived to be. M2 to GDP ratio is high in autocracy period (41.0, 38.45, and 42.31) as compared to democracy period (37.06, 35.2 and 42). This implies that financial sector develop more in autocracy. M2/GDP shows a fluctuating pattern over the period of analysis, with instance of a sharp decline in FY75. From FY79 to FY90, it averaged around 40 percent with little evidence of volatility. There was another drop witnessed at the end of the 1990s. Since FY01, it has exhibited an increasing pattern, FY04 registering the highest level ever over the period of observation. Another most common quantity (Quantity indicators are based on monetary and credit aggregates and are the traditional measures of financial deepening.) measures used for analyzing the financial sector development is the money (liquid liabilities) to GDP ratio, which assesses the degree of monetization in the economy. High value of this indicator shows that financial sector grow positively. This again is better in autocracy period.

<table>
<thead>
<tr>
<th>Financial Development</th>
<th>Indicator</th>
<th>Regime-0</th>
<th>Regime-1</th>
<th>Regime-2</th>
<th>Regime-3</th>
<th>Regime-4</th>
<th>Regime-5</th>
</tr>
</thead>
<tbody>
<tr>
<td>M2/GDP</td>
<td></td>
<td>37.06</td>
<td>41.0</td>
<td>35.21</td>
<td>38.45</td>
<td>42.45</td>
<td>42.31</td>
</tr>
<tr>
<td>M1/M2</td>
<td></td>
<td>89.71</td>
<td>70.8</td>
<td>67.57</td>
<td>66.70</td>
<td>56.76</td>
<td>52.80</td>
</tr>
<tr>
<td>(DD+TD)/M2</td>
<td></td>
<td>39.06</td>
<td>59.2</td>
<td>69.61</td>
<td>68.44</td>
<td>71.65</td>
<td>76.10</td>
</tr>
<tr>
<td>TD/M2</td>
<td></td>
<td>10.26</td>
<td>29.0</td>
<td>32.4</td>
<td>33.3</td>
<td>34.4</td>
<td>39.9</td>
</tr>
<tr>
<td>LRM</td>
<td></td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>7.96</td>
<td>5.20</td>
<td>19.19</td>
</tr>
</tbody>
</table>

Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation

\textsuperscript{20} Efficiency of financial sector (analyzing through NPLs, interest rate spread, bank spread, and NIM) is discussed extensively in SBP report ‘Banking System Review 2003

\textsuperscript{21} Broad money best captures the saving function of money
Figure 3.c.2: Regime wise M2/GDP

Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation

e. External Sector

Pakistan’s external sector has been evolved over the last fifty nine years, where from producing and exporting agriculture primary commodities in 1947, Pakistan is today exporting manufacturing, and semi-manufacturing goods. External sector is also influenced by the type of government inaction. Different trade policies are designed by the different government. High growth that is calculated in first autocratic period is mainly influenced by the high growth rate in industry due to the trade policies adopted by the Ayub Khan. A study by the Asian Development Bank summarizes the external sector policies adopted by Ayub Khan era “The martial law government dismantle the system of direct control on imports, prices, profit margins, and investment. One important component of this program was to the adoption of the Export Bonus Scheme in 1959. This scheme was essentially a floating multiple exchange rate for exports. The gradual liberalization of the import controls continued with the Open General Licensing System and the repeat and Automatic Licensing Scheme introduced in 1961 and reached a peak with the introduction of the Free List for the selected raw materials in 1964\(^2\). This liberalization process was unfortunately

\(^2\) Selected raw material are: Consumption goods (Essential, Semi-luxuries, Luxuries), Raw material for consumption good (Unprocessed), Raw material for capital good
reversed in order to meet the foreign exchange shortage which arose after the war with India in 1965, the Government once again opting for direct control.” Average growth rate of export (5.71%) was very low, with almost very low import (2.86%) growth rate. Exchange rate remains stable throughout this period. Trade openness as a percent of GDP was 0.91. After this Bhutto came in power in 1971. He completely revised the trade policies, and a prominent feature of the Bhutto era was the absence of an explicit export policy (Adam et.al, 1987) and between 1972 and 1977, Pakistan lacked the formal, organized export policy in which clear objectives was laid. Bhutto trade policies were summarized as “except for a few items reserved for industrial users, all registered importers could obtain licenses for any number if importable items. The import trade was thus thrown wide open and imports were again liberalized after having gone through restrictive phase. The liberalization trend continued during the seventies and Free List was extended to 407 items in 1976 and 438 in 1978-79.” Exchange rate grows (11%) very quickly. Export (growth rate 12.81%) and Imports (growth rate 16.83%) also grow, with the increase of trade openness (2.44). Zia regime made a series of steps to liberalize the trade regime, particularly imports, by reducing the number of banned goods and lifting others restrictions (Zaidi, 2005). A little improvement in export growth (14.85) is calculated, with little decline in imports growth (12.93%). Trade openness (7.01) increase is to some extent. Share of import (4.6) and export (2.54) in GDP also increase. After this the second democratic period also adopts those trade policies that show fever control import and export. Trade policy pattern is continuously moving toward the lower tariff, and more openness. No tariff barriers have been replaced by tariffs, and tariff rate have come dropping down (Zaidi, 2005). Fifth and last regime introduced many reforms regarding the trade policies. The World Bank has categorized trade policy of Pakistan as one of the least restrictive in South Asia. This policy has gradually reduced the anti-export bias to strengthen exports in existing markets and explore new markets around the globe. The liberal trade policy is complemented by a market-based exchange rate regime. As a result of these policies, not only the exports of the country picked up, the imports also surged manifold. Total exports increased from US$5587 million in 1990 to US$14058 million in 2005 whereas total imports rose from US$7383 million to

(Unprocessed, Processed), and Capital goods (Consumer durable, Machinery and Equipment).

80
US$26296 million during the same period. Growth Pattern of import, export, openness and exchange rate is given in the table, regime wise.

**Table 3.d.1: External Sector at Glance**

<table>
<thead>
<tr>
<th>External Sector</th>
<th>Exchange rate</th>
<th>Export</th>
<th>Imports</th>
<th>Openness</th>
<th>As percent of GDP</th>
<th>Annual Average</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Growth Rate</td>
<td>Regime-0</td>
<td>Regime-1</td>
<td>Regime-2</td>
<td>Regime-3</td>
<td>Regime-4</td>
</tr>
<tr>
<td>-----------------</td>
<td>---------------</td>
<td>---------</td>
<td>---------</td>
<td>----------</td>
<td>------------------</td>
<td>------------------</td>
</tr>
<tr>
<td>Exchange rate</td>
<td>3.38</td>
<td>0.0</td>
<td>11.02</td>
<td>5.59</td>
<td>9.63</td>
<td>2.79</td>
</tr>
<tr>
<td>Export</td>
<td>8.18</td>
<td>5.71</td>
<td>12.81</td>
<td>14.85</td>
<td>12.88</td>
<td>14.43</td>
</tr>
<tr>
<td>Imports</td>
<td>1.15</td>
<td>2.86</td>
<td>16.83</td>
<td>12.93</td>
<td>10.62</td>
<td>16.43</td>
</tr>
<tr>
<td>Openness</td>
<td>-1.83</td>
<td>0.91</td>
<td>2.44</td>
<td>7.01</td>
<td>18.99</td>
<td>36.70</td>
</tr>
<tr>
<td>As percent of GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Export</td>
<td>9.87</td>
<td>0.37</td>
<td>0.97</td>
<td>2.54</td>
<td>8.61</td>
<td>17.78</td>
</tr>
<tr>
<td>Imports</td>
<td>10.17</td>
<td>0.54</td>
<td>1.47</td>
<td>4.46</td>
<td>10.38</td>
<td>18.92</td>
</tr>
<tr>
<td>Trade Deficit</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>8.33</td>
<td>4.34</td>
<td>2.74</td>
</tr>
<tr>
<td>Worker's</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>7.70</td>
<td>3.12</td>
<td>2.95</td>
</tr>
<tr>
<td>Remittances</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-3.69</td>
<td>-4.80</td>
<td>0.08</td>
</tr>
<tr>
<td>Current account</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deficit</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Annual Average</td>
<td>3.94</td>
<td>4.76</td>
<td>9.01</td>
<td>13.33</td>
<td>32.11</td>
<td>58.26</td>
</tr>
</tbody>
</table>

*Source: GoP, Economic Advisor's Wing, Finance Division, Economic Survey, FBS, SBP, IFS, Self Calculation*

**Figure 3.d.1: Regime-wise External Sector Growth Rate**

*Source: GoP, Economic Advisor's Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation*
5. Conclusion

After analyzing the macroeconomic history of Pakistan, regime wise, we conclude that, the nature of relations between regime types and development defies the established finding that economic growth fosters progress toward democratic performance. Under Pakistan's unique circumstances, the relationship between development and democracy is unclear and indeterminate. Economic growth in Pakistan has been more compatible with dictatorial political regimes than with democratic ones and the causal relationship between economics and democracy, as outlined by Huntington, cannot be demonstrated in the case of Pakistan. Economic growth is high is all episode of autocracy with high GDP per Capita growth rate. All sector that contribute in GDP also grow with high rate is autocracy. Fiscal sector indicator like government expenditure, revenues, overall deficit, and debt show increasing behavior despite the nature of regime. Financial sector development is measured by M2 to GDP ratio. M2 to GDP ratio is high in autocracy period as compared to democracy period. This implies that financial sector develop more in autocracy. External sector also depict the similar behavior, reforms were introduced with the passage of time, trade openness increase gradually. Keeping in all these facts and figure we can’t predict the either autocracy is feasible or democracy is good for Pakistan, only external shock, and long tenure of government which follow consistent policies can contribute high growth. Reynolds (1983), having reviewed the historical experience of several countries, concluded that spurts of growth are often associated with major political transformations. It means that politics does matter, but "regimes" do not capture the relevant differences. Same finding is true for Pakistan, only Politics matter instead of the nature of the regime. So Pakistan can achieve high growth by adopting consistent policies.
References


6. APPENDIX

Figure 1: Regime wise M2/GDP and M1/GDP

Source: GoP, Economic Advisor’s Wing, Finance Division, Economic Survey, FBS, SBP, Self Calculation