

ELITIST ECONOMY: How to Dismantle It?

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It is now well established in theory and practice that developing countries which were successful in raising the living standards of their population were characterised by a strong and capable state and efficient competitive markets. The binary 'State' versus 'Market' debate has outlived its utility. Pakistan has lagged behind others because a small class of elites has rigged the markets and captured the state to their advantage keeping the majority of the population deprived of the benefits of growth. The phrase 'elite capture' was not so widely rampant when my book, *The Economy of an Elitist State* was published twenty-five years ago. This word has now gained currency and has become congruent with the decline of the Pakistani economy and hypothesised as a major explanatory factor for this decline. There is a widely held belief: the elites in Pakistan have expanded in number and are getting stronger in influence in matters of public policy and unless this model is dismantled Pakistan would continue on its downward trajectory.

How does the elitist model work in actual practice? A clear understanding of the dynamics is essential for the measures required for the dismantling the elitist system of governance.

At present a common citizen without any connections or ability to offer bribes cannot access any of the basic public services for himself and his family. Political leaders use this helplessness of the common citizen to their advantage by acting as the intermediaries between government functionaries and the poor citizen. The dividends he collects this way are cashed on the day of elections. The grateful beneficiary exercises his own, his family and kins' votes in favour of their benefactor. Elected this way the political leader asserts his weight and gets the thanedar, patwari, tehsildar, Irrigation SDO, school teachers and other government functionaries of his choice appointed/posted in his constituency. As they are beholden to him these officials carry out his

wishes favouring the elected MPA/MNA's supporters and penalising those who oppose him. This vicious cycle keeps on moving irrespective of the changes in the political parties in power. Only the cast of character changes. The old defeated leader is replaced by the newly elected one but the tactics remain the same. The grant of millions of rupees out of Public Sector Development Funds allocated to each MNA/MPA for spending in their own constituencies further fortifies their hold as they are able to demonstrate the public works they have carried out or the gas and electricity connections they have been able to secure. The elites continue to keep their firm control intact.

The mechanism of rent seeking and wealth accumulation by the elites is through the distortions created by the crony capitalism widely practiced in Pakistan. Concessions, exemptions and bank loans that are subsequently written off, preferential allocation of land at subsidised rates, import duty slab changes through SROs to favour some to the exclusion of others, invoicing and over voicing of international traded goods, misdeclaration and undervaluation of goods, unrealistic tender awards for contracts subsequently padded up for large cost overruns have made the business elites, their families, the bureaucrat friends and political allies fabulously rich. The deadweight loss to the economy by higher end use prices, loss of international competitiveness, elimination of the genuine competitors has led to poor and inefficient economic outcomes. The machinery of state to enforce these malpractices participates in the rents so garnered.

Where markets fail to perform their function of clearing prices by equilibrating supply and demand a wedge is created between the 'observed prices' and their fundamental determinants ending up in inefficient allocation of resources. Investors shy away from sectors and activities that the economy really needs for growth and sustenance and shift to those unproductive ones

where quick, short term gains can be achieved in an environment of market distortions and imperfections.

Private profits keep accumulating at the cost of widely shared benefits to the society. Overall low economic growth coexists with excessive returns pre-empted by selected market players. There are some 'rent thick' sectors such as real estate, construction, railways, ports, airports, highways, media and telecommunications, mining, oil and gas, food procurement in which the government enjoys disproportionate powers in determining the financial health of a company through administered prices, award of contracts, concession agreements, spectrum allocations and grant of licenses, tariff determination, permits, no objection certificates, allotment or leasing of land. These sectors have been the principal source of wealth accumulation.

Elite classes have also become rich through acquisition of state land at below the market prices, getting these housing societies and estates developed through public exchequer, securing public utilities on priority basis, then disposing them off at prevailing market prices. The ratios of acquisition costs and sale proceeds run into 1:100 depending upon the city, location and years the plot or property is held. The sale price at which the transaction is recorded is only a fraction of the actual market price. The balance amount at which no tax or registration fees are charged becomes available for conversion to other assets: real estate, stocks, equities, gold, foreign currency or cash. The currency in circulation ratio in Pakistan is one of the highest in the region. As the money changers are allowed to freely buy and sell foreign exchange and foreign currency deposits in banks for residents are permissible a lot of money thus earned is transferred abroad to safe havens.

The question that needs to be addressed is: what are the ways in which the elitist model can be dismantled and the economy freed from the stranglehold of the elites? At least five major reforms can be offered for this purpose.

- The key institutions of state such as civil service, police, judiciary responsible for delivery of basic services such as education, health, water supply, traffic control, housing, protection of property etc. have become increasingly dysfunctional. The apathy, indifference and lacklustre performance of these institutions have deprived the non-elites from access to justice, grievance redressal, resolution of daily life problems and basic social services. Corruption and sifarish rampant in these institutions have actually intensified the power of the well-to-do and influential. The devolved local government structure under which the elected officials were empowered to deliver the basic public services to the communities at the grass root level has been abolished and the provincial governments have centralised powers and control over financial resources. The poor remain at a distinct disadvantage from the current system as they have no direct access or control and have to seek the assistance of powerful intermediaries i.e. the elites to obtain

relief and obtain services such as filing an FIR, registering a document, getting mutation of land, obtaining a passport etc. An effective, devolved, responsive and empowered Local Government system (directly elected) would dilute the powers of the narrow and entrenched elite classes.

- The judicial system remains clogged with hundreds of thousands of cases of frivolous litigation that crowd out legitimate and serious cases of contract enforcement, property and land disputes, crimes to life and person and threats to public order. As there is no perceptible penalty against frivolous litigation the existing system is being grossly misused by the vested interests to their advantage by indulging in protracted proceedings that unnecessarily prolong the determination of the cases. The multiple appeal system add fuel to the fire and act as a further deterrent to the efficient functioning of the process. The relationship between the Judiciary and Executive branches has become adversarial hindering the process of law enforcement. An open, transparent system of selection of judges and their accountability by which the corrupt and incompetent are removed, frivolous litigants are heavily penalised and an inexpensive alternate dispute resolution system are the most important steps in breaking the back of elitism.
- Education has proved to be a great leveler providing opportunities to the children from poor and disadvantaged classes to acquire skills and training and reach the highest pinnacles of success in their respective professions of choice by dint of hard work, merit and performance. Unfortunately, the fragmentation of the educational system in Pakistan right from the beginning of a child's life cycle has made it quite difficult to use education as a source of upward mobility and improvement. Although several well-meaning individuals and organisations are providing quality education to the children from the poor segments of the society their numbers and reach are still quite limited. A further expansion of public private partnership would have a beneficial effect with the government providing infrastructure and stipends to the poor and disadvantaged and girls. At present the public school system with a few exceptions, is jammed with mediocrity and inefficiencies and needs to be completely reoriented and revamped to meet this objective.
- The taxation and public expenditure system can be another potent instrument in transferring some part of private incomes beyond a certain acceptable threshold from the well-to-do and the rich to the poor and disadvantaged. But unfortunately, the number of actual tax payers in relation to potential tax payers in Pakistan has remained small restricting the ability of the state to promote equity. The wind fall gains made by the elite classes in the real estate, trading, agriculture have escaped taxation dwindling the tax collection and also generating a sense of lack of fairness in the society. The sooner the agriculture incomes, service incomes and capital gains are taxed and then

used for spending on pro-poor services through local governments and social safety nets the better off the distribution of income will be. The elite class will be prevented from deploying public finances for intensifying their hold.

- The financial sector has failed to address the credit needs of the small farmers, small businesses, salaried individuals and the poor. The coverage so far, among the agriculture households is only 15 percent. Similarly, microfinance institutions (MFIs) have penetrated about 10 percent of the potential beneficiaries. Financial inclusion can be achieved by expanding digital financial services. The availability of credit to such a sizeable number of households belonging to lower income groups will empower them socially and financially reducing their dependence on the elite class as intermediaries. The outreach of MFIs to the women clients in particular will have many collateral advantages in form of education, nutrition, better health, cleanliness etc.

To sum up it is fair to say that the elitist capture of Pakistani economy during the last twenty-five years has become accentuated as the agenda for reforms particularly in the institutions of the state, judicial system, educational system, tax and public expenditure system and further coverage of the financial sector has remained unattended. The incoming elected government should devote its tenure to bring about these reforms and begin uprooting the tentacles of the elitist economy and make institutions of governance inclusive, strong and effective. Resetting the direction of the economy rather than the immediate electoral gains should be their motto. They must realise that an impartial system in which all citizens have equal access to opportunities on the basis of hard work, rather than connections and class, has a much better chance of achieving shared prosperity in the long run. In a polarised multiethnic, multilingual society extra efforts have to be made to ensure that the markets work openly and competitively and the state distributes the gains from such an economy by taxing the rich and building the capacity of those who are less well endowed, marginalised, residing in remote areas, etc. and to help those who require social safety nets and transfers to sustain themselves.

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