

MANAGING GOVERNMENT BUSINESS-RELATIONS IN PAKISTAN¹²

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At the outset let me submit that empirical evidence for the last fifty years amply demonstrates that the popular binary--- Markets vs Government--- is no longer valid and has become outdated. We need both a strong, capable and effective government and well functioning competitive markets regulated by the government. The successful examples of Japan, Korea, ASEAN, China and more recently India illustrate that when Public and Private sectors work in partnership for common agreed goals, each where they have comparative advantage the country surges ahead. There are both market failures and Government failures and as long as these failures can be redressed the country moves on the right track.

The balance between the two in economic space varies a lot and besides the above countries there are other models such as Nordic, European Social Market, divide the economic space in a wide variety of ways between the private sector and the government. Unfortunately, the US—a citadel of private sector for long--- has retreated Under Trump into a model of active intrusion by the Government in the affairs of the private sector.

Ideally, the division between these two players ought to be based on their respective comparative advantages. Market, if it operates competitively is good at allocating resources and producing efficient outcomes. But it also creates inequalities among households, individuals, regions, gender, urban-rural divide. Government, if it is benign and uncorrupt, can minimize these inequalities through Tax, Transfer, Subsidy schemes, and other policies, investment and regulations. Again it is difficult to find a country which has been able to arrive at this optimal mix of efficiency and equity. The U.S. has 12 percent people living below the poverty line and 4.6 percent unemployment rate. In China, the incidence of poverty has declined considerably and only an estimated

¹ Address delivered at the Competition Commission of Pakistan at Islamabad on January 29, 2026

120-150 million people fall below the poverty line. However, the inequality coefficient has become worse.

I now turn to Pakistan. In my book 'Pakistan: The Economy of an Elitist State' published by the Oxford University Press in 1999 it is argued that in Pakistan, the markets that allocate resources efficiently have been rigged by the elites (about 1 to 2 percent of the entire population included in this category) and therefore produce inefficient outcomes while the state that distribute the gains from economic growth equitably has been captured by the same elite for their benefits resulting in accentuated inequalities. We have therefore got worse of both the worlds – inefficiency and inequity. So there are both market failures as well as Government failures. How can these be redressed to produce desirable outcomes. This requires a delineation of responsibilities between the Government and the private sector.

What should therefore be the appropriate role the Government? In my view, the Government has at least five functions to perform – an Enabler and Regulator, Protector of Life and Property, Enforcer of Rule and Law and Contracts, Provider of Infrastructure and Investor in Human Capital. I would take up each of these roles and dwell on them briefly.

Government as an Enabler and Regulator

Government has no comparative advantage in doing business as proven by the episode of nationalization in the 1970s. . The politicians and bureaucrats in Pakistan are neither equipped with the skills nor have the appetite for risk taking in running businesses. Suffice to say that production, distribution, marketing, trading of goods and services should be carried out by the private sector. What the Government can do is to ensure a level playing field for all market participants. If the market structure is monopoly, oligopoly, Cartel or in other way imperfect the welfare of the public who buy these goods and services will be hurt. The Government through Competition Commission, regulation, legislation and oversight has to protect the consumers from the abuse of market power. A private monopoly, in my view, is worse than a public monopoly and should be shunned.

My study of regulatory agencies and the Competition Commission indicate that there must be greater clarity in their legislations to avoid overlap, duplication and ambiguity in the allocation of functions. Most regulatory agencies have overstretched themselves by excessive intrusion in form of price fixation, licences, permits, clearances, NO objection certificates at various stages of the business cycle shackling the enterprise and initiative of the private sector. Absence of sectoral knowledge and lack of competence among the leadership and senior staff exacerbates the tendency to exert unnecessary controls rather than redress the systemic failures. Multiple agencies working in the same field make pinning of accountability for results difficult. There is a compelling need for a comprehensive review of all the regulatory agencies, their laws, governance, management practices, processes, human resources and expertise. Ad hoc tinkering is no longer feasible.

Protector of Life and Property

The second important function of the government is well known – national defense, internal security and protection of life and property of citizens. While there is no doubt that our national defence organizations have made us proud and performed very well under difficult circumstances internal security is an area where there has been a gradual deterioration over time and the citizens whether in big cities or rural areas, live in a perpetual state of fear for physical safety and protection of property. Terrorist attacks are no longer limited to specific areas but have touched Karachi airport, University and Consulates.. This is a frightening trend. As a consequence the risk premium has risen for domestic and foreign investors.

The whole chain of administration of justice is dysfunctional and unable to prevent crimes or take punitive action against the perpetrators. Police does not entertain the complaints as a matter of routine, investigation is shoddy, prosecution is weak and the courts are overloaded. New agencies and departments are created, safe cities are equipped, forensic labs established but the incidence of crimes against person and property remains unabated.

Enforcer of Rule of Law and Contracts

The third function of the government is to have an impartial system of adjudication of disputes and enforcement of contracts. Private markets cannot function if property rights are not protected, contracts are not honored and disputes are not settled through an open system of the courts of law. If land disputes linger on for over decades in the courts, how can you expect businesses to enter into long term investments. If bank loans worth billions of rupees are stuck because of the protracted litigation how can you expect banks to make loans liberally. There is a plethora of special courts such as Banking courts, tribunals such as Customs, Internal Revenue, and then the high courts, Supreme court and now Constitutional court but the businesses do not get timely relief or speedy adjudication of their disputes. The court system in Pakistan has low approval rating. This does not show an elevated sense of confidence in our judiciary. Alternative Dispute Resolution, which is so common in informal settings, exists on paper but is hardly practiced because of the resistance by the lawyer community. The related issue of competence is equally serious. Legal practitioners and judicial officers who are well versed in Commercial Law, Corporate Law, etc. are few and far between leading to unnecessary adjournments, protracted proceedings, postponed decisions and piling up of cases in the courts. Pakistan's percentile rank in the World Bank's rule of Law Indicator has deteriorated and among the 20 most populous countries Pakistan ranks 19th followed by Nigeria.

Provider of Infrastructure

The fourth area of government responsibility is the provision of physical infrastructure – roads, bridges, highways, ports, terminals, pipelines, railways, power, gas, dams, irrigation water, etc. These are basically public goods whose benefits cannot be appropriated exclusively by any one group of citizens. They are lumpy investments which involve issues of Right of Way, land acquisition, resettlement, compensation that are beyond the reach of the private investors. Therefore, provision of these public goods reduce the unit costs of production and distribution for the private sector and enhance the competitiveness of a country's tradable goods. In Pakistan, the opposite has taken place. Energy pricing has made Pakistani exporters uncompetitive in comparison to their

regional peers. Even the utilization of the existing generation capacity in the private sector is sub-optimal because of the circular debt problem. The Iran Gas Pipeline and TAPI which should have been given urgent attention are stuck putting the future gas availability at serious risk. Railways, Ports, Airports, water reservoirs and dams , etc are all under direct government control and their inefficiencies have raised the cost of doing business and consequently loss of competitiveness.

Other countries have successfully experimented with Public-Private Partnership to meet infrastructure deficiencies and although every government in Pakistan has paid lip service to it nothing of significance has been achieved so far.

Investing in Human Capital

The fifth area of responsibility for the Government is to invest in human development – schools, colleges, universities, technical and vocational institutions. Pakistan has slipped down to low category from middle and now ranks 168th among 193 countries according to the Human Development Index 2009. Adult literacy is dismally low – 40 percent of the population is illiterate. Twenty million children are out of school. 40 percent are stunted. Technical and Vocational training covers only 1 percent of the relevant cohort. Female Labour Force Participation Rate is abysmally low—24 percent compared to 42 percent in Bangladesh. Infant mortality, maternal mortality and child malnutrition indicators are the worst in South Asia. Considering the fact that there is a close connection between human development and overall rate of growth the social returns on these activities are quite high. The private benefits from investment in human development leak out because of what the economists called ‘externalities’. Regrettably Government’s allocation in Pakistan for Education and Health is only 2 percent of GDP while the task of educating 50 percent of the population below the age of 19 is enormous. Government along with the private sector and civil society organizations should have to give top priority to Education, Health, Family Planning, Potable water, Sewerage, Social Protection to make up the lost time.

To perform the above mentioned multiple roles there are two essential prerequisites that the Government should possess. The bureaucracy administering laws,

rules and regulations, protecting life and property or building infrastructure or running schools and health centers should be efficient, and free from large scale corruption. Inefficiency and corruption cause heavy damage to the economy and stifle growth of businesses. Pakistan's rank in Transparency International Perception Survey has fallen to 135th out of 180 countries. Second, there should be continuity and consistency in public policies. Sharp twists and turns with each change in the government erode the credibility of the country. With every incoming government reversing the policies, projects and programs of its predecessor, uncertainty about the country's long term commitment has enhanced.

Having described the catalogue of government's responsibilities I now turn as to what private businesses should do in return. I would argue that private sector should act as a good corporate citizen, promote good corporate governance, invest in Research and development, be prepared to face competition and pursue social mission.

Good Corporate Citizen

First, the private businesses have to diligently and honestly apportion a part of their profits to the Government in form of direct taxes, pay all indirect taxes and duties without concealing misrepresenting, understating, misclassifying under-or over-invoicing. No government, however capable it may be, can ever carry out all the responsibilities that we expect from it in absence of adequate revenue base. Lower Tax-GDP ratio is a manifestation of the tendency on the part of our businesses to make huge windfall profits at the expense of the government. Underlying this behavior lies our desire to become rich overnight and amass fortunes by hook and crook. We all condemn corruption but we conveniently forget that it takes two to tango – the bribe giver and the bribe taker. Pious pontifications on TV shows against corruption are no substitute for the crooked behavior on the part of some of our private businesses. The financial bottom line is not good enough. Was it achieved through unethical practices, degradation of environment and destruction of natural resources or did it promote tenets of sustainable development? Both financial and environmental bottom lines are desirable. But were they accompanied by social dislocation, violation of property of the weak and the vulnerable, gender

discrimination or child labor. These are the questions each of the firm has to answer if it wishes to demonstrate that it is a good corporate citizen. To be a good corporate citizen you have to be answerable to multiple stakeholders in the society rather than to your shareholders only.

Corporate Governance

Second, the private businesses do not realize the great opportunity for attracting other people's money into their businesses. Open, transparent public disclosure of their performance and finances would help bring in other people's money into their businesses while the ongoing sponsors continue to exercise control over the operations of the businesses. The myopic tendency to keep two or three sets of books, doctor the accounts, understate the balance sheets, siphon company's earnings off through criss cross of related transactions may bring some short term gains. But in the long run such companies are unlikely to survive. Good corporate governance that ensures disclosure, transparency and accountability of the management, independence of Directors, and the Board keeping a watchful eye on Managers would not only result in enhanced credibility of the companies but also in better performance.

Investing in training of their employees makes a good business case as it would raise productivity translating into higher profit per unit for the shareholders, reduce unit cost of production, stepping up on the escalatory ladder of scale and raising market share.

Competition

Third, Pakistan's manufacturing industries have yet to realize that they are still operating behind tariff and non-tariff barriers. Trade barriers raise domestic prices by depriving consumers of the benefits of competition, while also artificially limiting their consumption options. These barriers also stifle productivity boosting measures. India lowered its outrageously high tariffs to a level of about 10 percent. East Asian countries and China have average tariff rates of around 5 percent. The results of this liberalization are simply astounding. Cross-country studies suggest that openness of the economy is important for raising growth and attracting technological innovations and spillovers.

Lower trade barriers unleash the competition that forces domestic industries to become more efficient or they would not survive. Anti-export bias of Pakistani industries is quite high and that's why export is limited to only a few items. Selling in domestic market under protectionist barriers is easy and lucrative. Why should the businessmen spend time and energy in finding new markets for their products, reduce the level of high profits they are used to and abide to the rigor and discipline of international trade. Pakistan's maximum tariff rates have to be brought down further and manufacturing industries have to prepare themselves to become competitive or move on to some other line of business in which they can excel. Perpetuating the present set of inefficient industries artificially does not augur well for the future of Pakistani economy situated in a fiercely competitive world market.

Research and Development

Fourth, like government the private sector has been equally amiss in promoting Research and Development and investing in high quality manpower. Short term profit considerations have blinded them to the virtue of investment in their long term survival. The future of the companies and Pakistan's place in the global market is highly dependent upon innovation, export diversification, integration into Global Value chains, high quality reasonably priced products delivered on time , the quality of human resources, leadership of its Corporates and adapting to the changing dynamics of the global market. China now is the largest exporting nation of the world and produces 30 percent of global manufactured goods higher than the US and many European countries combined because it spent on Research and Development, first rate scientific manpower , invested in emerging technologies. Productivity increased by 80 percent and average real wages for middle and low income workers rose by 12 percent. Korea today is taking an edge over other advanced countries as its private sector has learnt the art of constantly renewing and revitalizing itself. With 3.5 percent of GDP spent on R&D and 60-70 percent tertiary education enrolment rate Korea is the fastest growing source of Intellectual Property Rights. And as you know most of this is coming out of largely a result of the efforts of private sector. It is never too late although we have a lot of catching up to do. Private sector firms in Pharmaceuticals, Chemicals, Agro-Food, Electronics, IT ought to

step up their R&D activities and all firms should support and set up higher educational institutions in Science Technology and Engineering.

Social Mission

Finally, let me make a distinction between Social Mission of the Corporate and the Corporate Social Responsibility (CSR). It is gratifying that the notion of Corporate Social Responsibility (CSR) has gained a lot of currency in the recent years and that indeed is the right move. But CSR should not be construed in a narrow sense but must be part of a broader social mission. In a country that so proudly professes to be an Islamic State there should not be stark inequalities among different segments of the population. But we know there is plenty of inequality in this country – we have backward districts, rural poor, vulnerable groups, ethnic minorities and geographically disadvantaged areas. Our sensitivity to human misery should not be awakened only at the times of floods or earthquakes. We should serve and help these groups in many different ways. Companies, for example drilling or producing oil or gas in the backward areas of Balochistan and Sindh or southern districts of KPK, exploring and exploiting minerals in Gilgit Baltistan or merged districts or developing Gwadar port should help those communities by providing education, health, drinking water, housing, employment opportunities, service contracts, etc. Similarly other companies should help in adopting a few rural areas and implementing integrated area development programs and paying special attention to education. It also makes business sense that latent purchasing power of 60 percent of underserved population at the bottom of the pyramid is offered innovative, low cost products and unconventional, inexpensive marketing channels such as use of the mobile phone. Those who are already embarked upon such a path will enjoy the First Mover advantage and gain a significant presence in this market. Bottom-of-the pyramid marketing is taking a life of its own in many parts of the world. There is no reason as to why Pakistani companies cannot reach out to this large but unexplored market of 100 million people.

All the above changes will neither happen automatically nor overnight. They would require visionary leadership, coherent strategy, credible execution plan, and a competent

team which buys into these changes, a motivated work force and something else that is beyond the control of any business leader. That is a benign external environment and a set of sensible and predictable government policies. The challenge for the corporate leaders become even more formidable if the external environment is hazardous and the government policies and practices are unreliable and erratic.

Let me share the evidence as to what kind of leadership will have fairly good prospects of success. A cross national study of some 16,000 middle managers of 825 companies in 64 countries, ranging from Albania to Zimbabwe, found for instance, that the most valued attributes of company leadership, regardless of country, are dynamism, decisiveness and honesty; a capacity to motivate and negotiate with others; and a focus on performance. The company managers also universally agreed on several unfavorable traits; autocratic, egocentric and irritable. The same study also found that the successful leaders were also humane, compassionate and generous.

To sum up, the appropriate model of Government – Business Relations in any country has to emerge from the country's own historical, cultural, social and economic milieu. Transplanting other models without testing their suitability and acceptability is not going to work. Nor the outright rejection of everything foreign is something we should take pride in. There is much better understanding today as to what Government can and ought to do and in return how the private sector should behave and operate. If the Government sticks to things which nobody else but the Government itself can only do and the private sector focuses on activities for which only it is equipped and capable then a lot of air can clear up and the country can march forward. The interface between the two is not always so clear cut as I have sketched out. In India, since 1991 the business and Government have worked together in unison leading India on the path of prosperity despite the presence of a bureaucracy that clings to its legacy. There is no reason that Business Leaders and Government of Pakistan should not be able to put their act together and turn the corner in spite of much more difficult challenges. . Thank you.

