Pakistan's Economic Strategy for 1980's — Financing Development

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Financing of development should call for marathon efforts to generate domestic savings. The objective would not be to completely eliminate dependence on foreign resources but to minimize it. Given the overall financial constraint, I would suggest a different approach for financing the development. This is with regard to who should finance the development within the country. In other words, whether the development should be financed by the federal government, or by the provincial governments. Development reflects the aspirations and instincts of the people, hence the strategy for development needs a complete reorientation for restructuring the society, for ensuring social justice and for reducing regional disparities. As such it would be desirable to have it through the provincial governments as it would give them an opportunity to determine the expenditure priorities. In the past the financing of the development had been through federal government.[1]

It is not the contention of this paper to minimize the importance of the efforts done by the federal government in financing the development but to suggest a new approach to finance the development which if tried may achieve the objectives of development successfully.

At present financing of development is done by the federal government and the new approach of financing of development by the provincial governments has significance because of following reasons.

The development expenditures have to reflect the aims and

aspirations of the people of the area concerned. Any single state or province or group of states or provinces which can gain political dominance of the federal government can use the power to withhold revenues to force the governments of other states or provinces to pursue expenditure policies which are in the interests of such dominant province or provinces. This may lead to inefficient expenditures in the sense that they reflect the aims and aspirations of the outsiders.

2. Even when there is no actual attempt of one group or groups within the federation to dictate expenditure policies, the financing of development by the federal government may be undesirable. This is because where inter-provincial differences exist all unpopular decisions are likely to be blamed on the dominance of the centre.

3. The situation is made worse by the possibility that provincial politicians may use the financing of development by the centre cynically so as to further their personal political careers. Under such conditions it is possible for the provincial politicians to make extravagant promises to the people of their area so as to gain offices. When they fail to make good their promises they can blame failure on the centre which failed to grant funds or would only grant funds for other purposes.

4. Provinces are not going to plan their eventual disappearance as economic regions.[2]

In Pakistan the financing of development is done by the federal government, as such it has to dictate the expenditure policies. The trend suggests that the provinces have to depend for 3/4 of all the funds on the federal government.[3] It is, therefore, suggested that not only more resources be transferred to provinces, so that they could pursue the expenditures according to their own priorities to reflect people's aspirations, but the distribution among the provinces should also take into consideration not only population which is the criterion at present, but also such other criteria as collection of revenue, per capita income and area. Considering the importance of these criteria, a brief description of them is given here.

Population is considered to be a neutral basis. But it alone is

not a satisfactory index of needs. There is a paramount difference among the provinces, with respect to area, physical nature of the land, distribution of the population over area, and inequality of per capita incomes. Populous provinces are not necessarily below the average. For example the province of Punjab is the most populous of all the provinces of Pakistan, but its per capita income stands second only to Sind.[4] On the contrary a less populous province like Baluchistan with a low standard of living and vast area with scattered population, would qualify for more funds as it would need more expenditure for the provision of social services. Moreover, population does not reflect the relative stage of development of particular province.

Collection as a basis of distribution means that the revenue assigned to each state or province should be in proportion to collections from that particular state. The major collection of revenues normally comes from the industrialized provinces or states as their taxable capacity is higher. The higher rungs of society in commercial and industrial fields are disproportionately richer. Incidentally these classes are the ones which pay the direct taxes at higher rates. If it is made the only basis, the bulk of the revenues would go to such province, hence instead of bridging the gap between the provinces or states, it would widen it.

There are certain cities which are the main entrepots of import and export trade—Karachi for example in Pakistan. The main offices of the companies and other concerns, which operate all over the country are located in such cities. In such cases it would be undesirable to adopt collection as a basis. However, there is no gainsaying that throughout the country basically there is a certain part of income, particularly in the range of personal and small business which would be treated as of local origin. Apart from that the provinces which basically find that more has been collected from their areas in the pool, feel inclined to have more of revenues from it on political grounds too. Therefore, collection as basis cannot be ignored in toto.

Per Capita income as a basis for allocation of funds to provinces means that the provinces with a higher per capita income may

receive less and vice versa. The analogy is derived from the fact that even on international level, the philosophy of present day aid and investment programmes is the conscious desire and attempt to raise the standard of living of the less developed countries to that of the advanced countries, least the existence of a wide gap between the very rich and the very poor nations should create undesirable political and social complications.

The per capita income approach looks fair index of devolution, as it attempts to remove the disparity in per capita incomes of the different provinces. But this too cannot be the only criterion. Firstly, per capita income data especially in under-developed countries is not reliable. Secondly, this would be unacceptable to those high per capita income provinces, where the intra-provincial income differences are great. Thirdly, a pure per capita income approach would ignore other important factors like density and location of population. Sparsely populated province with large areas will qualify for more funds for the provision of basic social services, though its per capita income may be higher due to a few rich areas, which would mean that it may not be allotted more funds on the per capita income basis.

The distribution on the basis of Area would mean that provinces or states with vast areas would qualify for more funds as large amount would be needed to meet the basic requirements of scattered population. Where the provinces differ appreciably in respect of their areas, the formula for distribution of revenues should therefore carry weightage for the relative area of the provinces.

None of these methods alone can, therefore, form a basis for division of revenues among the provinces or states. Due consideration will have to be given to all relevant factors, which include the total population, its density and location, collection of revenues, per capita income and area of the provinces. Consideration of these factors will give a reasonably satisfactory index of a basis of distribution of revenues among various provinces. The proper weighting of these factors would depend largely on the circumstances prevalent and can be changed from time to time to obtain satisfactory results.

Shortage of funds is an overall constraint, as such to make

effective dents to improve the socio-economic condition of the people, some drastic changes are to be made about the functional responsibilities of the provinces and also some elastic sources of revenues are allotted to them. In this regard as a policy measure (a) initially the agricultural sector should be completely provincialized as it is only at the provincial level that the aspirations of the people could be met. The key to more rapid and equitable development lies in policies to stimulate agricultural growth and to confront rural poverty.[5] The provinces administer only 39% of the total expenditure on agriculture.[6] (b) Both sales tax and excise tax be transferred to provinces, which will give them adequate resources of their own. Firstly because the tax specifically sales tax, originally a provincial source of revenue, was taken over from the provinces after Independence, with a special arrangement to meet the immediate financial difficulties faced by the central (federal) government due to dislocation caused by the partition. But since then, and by now the Centre's financial position has improved greatly. Secondly, the economic conditions of the provinces would differ from time to time which would necessitate different rates in the various provinces. The level of tax, therefore, would be determined by the provincial government concerned, which would keep in view the prevailing economic conditions and its need of revenues.[7] Thirdly, the complete transfer of any other major central tax apart from other considerations, would mean asking the provinces to contribute to the Centre. However, there may be a view that it is easier to collect sales tax and excise tax at the centre (federation) and its proceeds returned to the provinces, but the provinces having full control over the rates and conditions. Administrative convenience, therefore, would not be an overriding ground for retention by the Centre. (c) Distribution among provinces should take into consideration various criteria, including population, pet capita income, collection of revenue and area.

CONCLUSION

Assuming that the availability of funds will remain overall constraint during the eighties, as such the strategy of achieving various developmental objectives should be empowering the provinces to determine their expenditure policies and the financing thereof. In this regard initially agriculture may be completely provincialized.

More funds may be transferred to the provinces preferably sales tax and excise tax, to bring structural changes in the socio-economic status of the people, and the distribution of funds among provinces should not be alone on the basis of principle of population but other principles such as collection of revenues, per capita income and area may be taken into consideration.

References

1. Government of Pakistan Finance Division Islamabad, Annual Budget Statement 1980-81.

2. Anthony Scott, "The Goals of Federal Finance", *Public Finance*—International Quarterly Journal, Vol. 19 of 1964, p. 241.

3. Michel M. Sherman with the assistance of Faqir Hussain Shamsi, Division of Economic Analysis USAID/Islamabad—"Pakistan Fiscal Sector and the Economy" 1971-78, p. 9.

4. The estimated per capita income in 1968-69 is as follows :—

Province	Population (In million) (Estimate 1968-69)	Per Capita Income (In Rupees)
Sind	11.5	852.6
Punjab	34.8	613.7
Baluchistan	1.7	452.4
N.W.F.P.	10.3	360.6

Source : The Fourth Five Year Plan 1970-75, Planning Commission Government of Pakistan, July 1970, p. 547.

5. The World Bank 'World Development Report', 1979, p. 1.

6. Michel M. Sherman with the assistance of Faqir Hussain Shamsi, *op. cit.*, p. 12.

7. See Hicks, J.R., "*Essays in World Economics*", Oxford, 1960, where he recognizes a need for giving provinces some revenues of their own, which they can control, and adjust to their own

needs. And also see Hicks, U.K., "*Development Finance—Planning and Control*", Oxford, 1965, where she recognizes the necessity of independent taxes for state in a federation and by independent she means the governments concerned can choose the rates and conditions.