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Rethinking Development Policy Choices: Contributions to the Emerging Agenda

In recent years, the World Bank has had the honor and privilege of welcoming incoming administrations with a series of diagnostics studies and policy recommendations. Building on this tradition, the Bank team has put together a Country Economic Memorandum (CEM) focused on job-enhancing growth and 16 sector-specific policy notes for the incoming Pakistan government. This effort is meant to facilitate a dialogue around a menu of policy options and be informative in the spirit of knowledge exchange. The topics were selected from ongoing or completed analytical work and where the World Bank has local and international expertise. This synthesis note aims to provide an overall guiding framework to highlight and bring together some of the critical reform priorities identified in the policy notes and CEM (see Box 1).

The policy notes and CEM aim to help the incoming government achieve its ambitious economic goals. The Pakistan Muslim League Nawaz manifesto—“Strong Economy, Strong Pakistan”—establishes the overarching goal of breaking out of the trajectory of low growth to reach a GDP growth rate of more than 6 percent. To get there, it calls for increasing investment, with particular attention to energy, agriculture, transport, and cities. It calls for placing the energy sector on a solid footing by reducing losses, corporatizing and privatizing energy companies, and rationalizing power tariffs. And it calls for opening markets and encouraging regional trade. It seeks to place Pakistan on a sound fiscal path with increased tax revenues, by reducing subsidies and losses in state-owned enterprises (SOEs) and limiting government borrowing. And it seeks to substantially increase investments in human capital—health, education, and social protection. These are admirable goals, and the policy notes and CEM aim to provide the government with options to meet these objectives.

Challenges are formidable, and a bold approach is needed, focused on growth as well as stabilization.

The past five years represent a historic political achievement with a democratically elected government completing its full term. On the economic front, however, gains have been limited. Economic growth has been modest at best, inflation has been in the double-digits most of the time, and formal unemployment has risen. There is no doubt that Pakistan has had to manage through several exogenous shocks, such as natural disasters and the ongoing conflict in neighboring Afghanistan. Nevertheless, there has also been marked deterioration in many structural areas under government control, such as revenue collection, energy sector, social indicators, governance, and the overall environment for private investment. Moreover, the current level of reserves and the fiscal deficit are unsustainable. They not only constrain
the fiscal space for financing development needs, but also place the economy on the brink of a balance of payment crisis for the second time in less than five years. These macro conditions make solving the structural challenges even more pressing. Simultaneous action on various fronts and a break with the past economic trends will be crucial to putting Pakistan back on the path to prosperity.

Strong leadership with clear vision, and sustained implementation, will be critical for bringing about economic reforms that have eluded Pakistan. Essential ingredients missing in past episodes of reform have been a strong political will and a consensus to implement difficult policy decisions. Unfortunately, “stop and go” policies are the rule rather than the exception in Pakistan’s experience with structural reform. The first few months of the political transition provide a unique window of opportunity. Making a bold start and appointing a competent team responsible for following through with solid and steady implementation will be essential.

Three Central Messages

Accelerating growth in Pakistan has been possible in the past, and it can be again. The country has already enjoyed two previous episodes of sustained rapid growth averaging 7 percent a year (fiscal 1963–67 and fiscal 2004–07). Pakistan needs to come back to that trajectory. At that rate, the economy doubles in size every six to seven years, creating enough jobs for its expanding labor force, but also higher skilled and more productive private sector jobs. There could still be exogenous shocks that can, if unaddressed, derail efforts. But experience has shown that Pakistan’s economy can also be very resilient in preserving growth and poverty reduction despite civil conflicts, natural disasters, and complex political transitions.

Pakistan has many “positives” that can help support accelerated growth and revive the economy. They include the legitimacy of many of its institutions; its capacity to implement national projects when there is a will; the impressive growth of remittances from abroad in the 2000s; its natural resource base and huge potential as a food and mining exporter; its strategic location neighboring some of the fastest growing emerging economies worldwide; and the rapid growth of women in the labor force every year. Pakistan also has a large informal sector serving a sizable domestic market concentrated in rapidly growing large and mid-size cities—and significant untapped potential for export growth in new markets, both regional and global.

These positives can be unlocked in three ways:

- **Message 1.** Pakistan must aim to achieve higher growth linked to more and better jobs—especially among women and youths. Perhaps the most powerful and dramatic reason for Pakistan to change course is demographic. With the sixth highest fertility rate in the world, the country’s population is projected to double by 2025. The youth labor force is rising fast, and Pakistan needs to create about 1.5 million new jobs a year—about twice its present rate—to prevent rising formal unemployment. Growth and employment, inextricably linked, can feed off each other in a mutually reinforcing manner. But unless growth accelerates, employment required to absorb a demographic bulge will not materialize and inequality will increase—aggravating the risk of conflict and social divisions. While the country is already creating lowproductive jobs, formal and informal, they are not enough to sustain growth in the medium term. To sustain growth, Pakistan needs to create more productive jobs.

- **Message 2.** Pakistan must strive for inclusion and improving human capital as a cornerstone of rebuilding productivity. Pakistan is making progress in reducing poverty and improving social indicators, but not as fast as other countries in the region. Sustainable growth can best be achieved by pulling people out of poverty and into a growing middle class. In this sense, inclusiveness is not merely about fairness—it is about creating a more educated and healthy middle class that is employable and more productive and that, as consumers, can drive economic growth. Inclusiveness should therefore be a central objective-reaching marginalized groups
and promoting equal access to economic opportunities and government services. Special focus is needed for the conflict-affected regions of Khyber Pakhtunkhwa, Federally Administered Tribal Areas, and Balochistan, where strengthening human capital is harder but, if achieved, can yield transformational results.

- **Message 3.** Pakistan can sustain its growth, jobs, and inclusion agenda only by enhancing governance and accountability. Good governance is fundamental to accelerating growth and attracting private investment—by setting simple minimum rules and regulations that can govern key economic activities with greater accountability and transparency. It can also increase the efficiency of service delivery, particularly for the poorest people, especially if equity is a major goal. In the last decade, indicators of many dimensions of governance have deteriorated, with weaknesses in the rule of law and control of corruption—and with few gains in government effectiveness and regulatory quality. Even with some improvements in public financial management, revenue collection has deteriorated and shrunk the already small fiscal space to finance development needs. A significant reversal of these downward trends is essential, as are improving the quality of public administration and completing the decentralization process to promote a more accountable and efficient system of service delivery.

> It is important to emphasize that implementing these reforms ad hoc and piecemeal will not yield results.

The CEM and 16 policy notes can be grouped under these three main messages (Figure 1). Each area of reform will reinforce the others—but, if not pursued, will undermine the others. For example, the current approach to taxes and subsidies not only distorts business activities and creates avenues for corruption—it also reduces the government’s ability to supply electricity. A lack of energy in turn reduces business competitiveness, reduces trade, and slows growth and job productivity. Similarly, governance issues cross sectors, from education and health to trade policy. Partial implementation will therefore undermine desired results. For instance, if prompt solutions are not found to

![Figure 1. Three central messages](image-url)
reduce SOE losses, they will continue to constrain the fiscal space and keep jobs unproductive. Or if a solution is not found to reduce corruption in tax collection, overcoming taxpayer unwillingness to register and file will remain an uphill battle. And unless social protection builds effective insurance mechanisms to protect vulnerable populations against natural events, households that climb out of poverty will likely fall back following the next natural disaster. In this sense, the whole would be far greater than the sum of the parts.

The Overall Agenda: Why a Piecemeal Approach Will Not Work

For details in each area of reform, readers are directed to the CEM and individual policy notes of most relevance to their concern. Each note provides a short analysis of a few key issues, a menu of priority actions, and their potential sequencing in the short to medium term. But it is also critical to look at the benefits of implementing reforms as a whole and see how they interrelate. Simultaneous and persistent efforts will have higher probabilities of changing the dynamics required on most fronts.

Jobs and growth

To accelerate growth, Pakistan needs to address its interrelated binding constraints. The key constraints are for the most part well known, and addressing them is indeed at the core of the Pakistan Muslim League Nawaz manifesto. They include poor access to steady electricity, macro fiscal vulnerabilities, low access to finance and credit (especially for small and medium-size enterprises, or SMEs), trade restrictions, business-unfriendly cities to service growth and green manufacturing, excessive business regulations, poorly performing SOEs, and gaps in infrastructure financing. Some of the main interlinkages are as follows.

Reliable energy is the cornerstone of a strong business environment. It is not an understatement to say that energy is the top constraint to growth and jobs. If the country had solved the power load-shedding crisis, GDP growth would have been 1.5–2.0 percentage points faster. Without a reliable and efficient source of energy, businesses simply cannot be competitive. And many businesses have either to invest in captive power generation capacity or face closure and possible bankruptcy. But just as significant is the inverse—the importance of the business environment in resolving the energy sector governance dysfunctions. An important goal is to develop lower cost sources. But the amount of investment needed suggests that—without private financing and a strengthened overall macro, business, and trade environment—this will not be an easy task.

An efficient energy sector is necessary to achieve fiscal consolidation and improve human capital. It clearly is not possible to make the fiscal situation sustainable without a dramatic reduction in power subsidies. This then feeds into strengthening human capital in two ways. First, without reducing power subsidies, Pakistan will not have the fiscal space to make the increased investments in education, health, and social protection it so desperately needs. Second, targeted protection to the most vulnerable low-power consumers is in turn critical to creating the political space to reduce subsidies—most power subsidies go to the well off.

Fiscal consolidation will help improve access to finance by SMEs. The large and rising fiscal deficits of the past four years have to be financed. This financing adds to a public debt burden that exceeds the 60 percent of GDP ceiling allowed by the country’s Fiscal Responsibility Bill. More important, the skyrocketing domestic financing of the deficit has contributed to a private sector credit crunch—severely crowding out the private sector. Heavy SOE losses and guarantees for about 2.5 percent of GDP are also worsening the fiscal situation. While large businesses can often obtain nonbank financing, the most vulnerable are the SMEs, ironically the most dynamic and job-creating portion of the business community. Bank lending to SMEs is only 6.6 percent of total advances. But just as important is the reverse flow. The growth of businesses and SMEs is critical not just for growth and jobs, it is also necessary for the government to increase the tax revenues needed to bring down the deficit.
Fiscal consolidation is necessary to improve the perception of reduced country risk and raise private investment. A clear sign of this linkage is the Emerging Markets Bond Index, which rose above 1,000 basis points in March 2013 (later falling, following the election). Coupled with a downgrade of Pakistan’s sovereign bond ratings in 2012, this has made external finance extremely expensive for Pakistan, resulting in a sudden stop in external flows and requiring excessive government borrowing domestically. Bringing the macro stance into greater sustainability would help improve the perception of an investment-friendly country with much lower risk—and to bring down interest rates and inflation for businesses.

To unlock the manufacturing potential, attention needs to be devoted to urban development, green manufacturing, and infrastructure financing. Current urban development strategies and zoning regulations do not foster productive or commercial activity. As a result, there is a lack of multifunction urban areas that emphasize density and commerce. Manufacturing continues to be heavily concentrated in low-value-added consumer products that attract little investment. To take advantage of the important benefits that agglomerations produce for job generation, cities should become growth-friendly clusters that foster both competition and learning. This should in turn help introduce new more competitive technologies, including those that meet basic environmental and social standards increasingly required for exports. Equally important is that cities be linked to each other to get the most out of agglomeration, connecting industrial clusters. This requires upgrading, extending, and rehabilitating transport infrastructure to build trade corridors (within Pakistan and between Pakistan and its neighbors).

Improved trade policy is necessary to foster export (and rural) diversification, business competitiveness, and revenue. The trade regime is plagued with privileges: 9 out of 10 manufactured products granted statutory regulatory order (SRO)—based tariff exemptions benefit a single local monopoly producer. And contrary to the most-favored nation (MFN) declared tariff rates, there are myriad tariff slabs. Simplifying the tariff and trade regulation regime and reducing SROs would help reduce Pakistan’s anti-export bias and create a level playing field for competition—without which Pakistan businesses will fall behind. While some businesses would surely face stronger competition, the sooner Pakistan integrates into the regional market, the faster its businesses will become competitive overall and benefit from the high growth rates of its large neighbors. Businesses would also benefit from the greater availability of trade finance. Trade logistics businesses such as trucking, rail, roads, ports, trade finance, warehousing, and storage would also benefit. And farmers would gain greater access to advanced technology and new markets. But just as important, increased trade and a simplified tariff regime should increase government revenue, enabling the government to invest in further trade-enhancing improvements, and contribute to expanding agricultural productivity.

In all these efforts, it is important to focus on youths and women. Overall economic growth and even high levels of education have not translated into high levels of employment for these two vulnerable groups. Similarly, skills training and temporary jobs are not widespread enough to transition them into the workforce. Providing incentives for greater involvement of the private sector in program design, on-the-job training, and temporary initial placements is critical for achieving the required expansion rates in high-quality jobs. Self-employment and entrepreneurship programs would also be important.

Inclusion and human capital

Poverty diagnostics, an important tool for decision making on improving inclusion and human capital, needs to be strengthened. Outdated data and inaccuracies make it difficult to diagnose poverty, and it is critical that the capacity and autonomy of the Pakistan Bureau of Statistics (PBS) be assured, with its findings made public. In the meantime, the Human Opportunity Index provides a useful way to identify whether there has been progress in both the coverage and quality
of service provision. Inclusion policies should ensure equal opportunity for the vulnerable segments of population including women, underserved pockets in Punjab and Sindh, and conflict-affected regions of Khyber Pakhtunkhwa, Federally Administered Tribal Areas, and Balochistan where outreach and service delivery has become increasingly challenging. One promising option to expand coverage is to contract nongovernmental organizations or private providers on a low-cost basis to reach out to population in difficult areas.

**Accelerated progress in basic education and health services will enable Pakistan to make faster progress in growth and jobs.** Businesses need more productive, healthy, and educated workers to grow. But while human development indicators have improved in the last decade, they still lag countries at a similar income and many of Pakistan's neighbors. Pakistan ranks 145 of 187 countries in the United Nations Development Programme's Human Development Index. It has the world's second highest out-of-school population (7 million), of which two-thirds are girls. Enrollment and completion rates for primary education are among the world's lowest. Health coverage is also dismal, with under-five malnutrition rates as some of the world's worst. And the country is also one of the lowest spenders on education (1.9 percent of GDP) and health (0.9 percent of GDP); less than a third of the minimum average for countries at similar incomes per capita. As noted, it will be critical to make progress on reducing nontargeted power subsidies and increasing tax revenues in order to have the fiscal space to increase education and health spending. Reform initiatives in Punjab and Sindh have delivered on some counts, but the challenges continue to be huge as these provinces are overspending on staff salaries rather than on nonsalary priority social investment. With the management and financing of social services decentralized to the provinces, national and provincial standards need to be coordinated, and their achievements monitored to address inequities. Developing a system to set standards in hiring, track performance, and monitor learning outcomes should be the cornerstone of quality service delivery.

**Consolidating progress on social protection will make a huge difference not only for the targeted poor but also for the government to reduce nontargeted subsidies.** Whereas Pakistan spends about 3 percent of GDP in untargeted subsidies, the pro-poor–targeted Benazir Income Support Programme (BISP) spends barely a 10th of that figure, with more inclusive results. The BISP has an efficient and modern system for targeted cash transfers to the poor, and its database can be expanded to integrate other social programs under a targeted approach. However, efforts are also needed to consolidate these gains through a coherent social protection framework across provinces, while replacing expensive universal subsidies (power, wheat) with more targeted interventions. This will require an increase in social protection spending but be far less expensive than the current nontargeted programs.

**Better management of natural disasters is a prerequisite for sustained growth.** Pakistan is a disaster-prone country that is extraordinarily exposed to earthquakes, floods, droughts, and cyclones. The country has had 2 floods in the last 3 years, 14 cyclones in the last 40 years, 2 droughts in the last 12 years, and 2 earthquakes in the last 15 years. This hazard profile, when combined with rapid population growth and urbanization, greatly increases the vulnerability of human and physical capital. The major challenges in managing natural disasters are threefold: preparedness, well-executed emergency response, and strong dedicated institutions and data systems to oversee mid- to long-term rehabilitation. It will also be critical to mainstream disaster risk reduction in urban planning, factory design, and other infrastructure.

**Governance and accountability**

**Strengthening governance and accountability is the glue that will accelerate growth and improve social service delivery.** The governance indicators of the Global Competitiveness Report 2012–2013 ranks Pakistan as follows: 109 in transparency of government, 116 in property rights, 119 in irregular payments and bribes, 127 in reliability of police, 129 in favoritism in decisions of public officials, 132 in business cost of crime,
and 143 in business costs of terrorism. But not all news is bad. Recent positive developments include the growing entrenchment of democratic processes, the transfer of greater responsibility for service delivery to the provinces, and the exponential growth in electronic media (enhancing transparency and accountability). The governance agenda is multidimensional and includes four priority areas:

- **Improved public administration and service delivery.** Improvements can be achieved by reforming the civil service, building subnational and local capacity to monitor and ensure effective implementation, allowing citizen’s voice and participation in local planning, monitoring, and accountability, and establishing a local government system that has the requisite administrative and financial autonomy.

- **Transparency.** Pakistan needs to consolidate its public financial management system and establish effective right to information regimes at the federal and provincial levels. The former revamps budget and cash management, strengthens the complaint mechanisms at public procurement regulatory authorities with data publicly available, and conducts performance audits of key public transactions. The latter requires passage of right to information legislation, followed by proper implementation and enforcement and awareness-raising campaigns for citizens.

- **Accountability.** Setting goals and contracts up front and holding officials accountable should enable the government to regularly report on progress and then reduce excessive control or political interference. For example, in revenue mobilization, this could make a difference in designing a tax system that is broad, simple, and equitable and that facilitates tax registration and compliance through transparent information technology systems.

- **Anticorruption.** Pakistan should undertake a thorough systemic diagnosis, focusing on key institutions (such as the police, tax administration, and the like), devising carefully deliberated strategies to address the issues, ensuring proper implementation of the strategies, and reaching out to the international community to make progress visible and widely supported and appreciated.

**Stronger public financial management can be a foundation for improving service delivery and making public expenditures more transparent.** The public financial management system is fairly well developed but is not consolidated. The most notable initiatives have been adopting a uniform International Monetary Fund–Government Finance Statistics compliant chart of accounts for budgeting and accounting, separating accounting and auditing functions, introducing a pilot medium-term budgetary framework at the federal level, implementing a governmentwide financial management information system, enabling automated budget compilation, and establishing procurement regulatory authorities for Punjab and Sindh. Beyond keeping pace with these achievements, the next priorities are to develop an effective decentralized budget management system, improve cash management, and strengthen the capacity of the regulatory authorities for procurement.

**Decentralization can promote efficient service delivery.** The 18th Amendment requires greater accountability by provincial governments, which is a strong incentive for them to improve the outreach and quality of services. Although a wide range of central ministries were abolished, a large number of ad hoc functions seem to have simply been assigned to new federal ministries. Further accountability at the provincial level could be devolved toward the local and community levels. And given the fiscal imbalances in the federal budget, the level of budgetary transfers may need to be rebalanced to ensure consistency with the devolution of responsibilities—or new revenues will have to be generated both at the provincial and federal levels. In this regard, the roles and functions of each level of government should be further clarified. Beyond service delivery and accountability, decentralization holds the promise of stronger revenue mobilization, but provincial rules on expenditures and debt management may need to be revisited.
Mobilizing more revenue fairly and effectively is critical not only for growth and macroeconomic stability but also for governance. If Pakistan wants to create the fiscal space required for its development needs—both for infrastructure and social service—it has no choice but to implement a comprehensive tax reform agenda that is perceived as equitable in its policy design and effective and free of corruption in its administration. At less than 10 percent of GDP and decreasing, the tax ratio is among the lowest worldwide. The focus needs to be on making taxation simple, on broadening the tax base, on ensuring compliance, and on modernizing the tax administration—with steady tenure and professional hiring policies in the Federal Board of Revenue (FBR), and enhanced transparency and accountability about its results. On tax policy, the elimination of SROs, exemptions, and zero rates that make compliance low should enable authorities to raise more revenue with equity. Lowering personal and corporate income taxes to international averages could also be considered once revenues start to pick up. Customs tariffs should be simplified to a maximum of three slabs. Here again, governance is critical. Creating a more autonomous, performance-based, and modernized FBR and a joint Finance-FBR Tax Policy Commission would be two important steps toward more effective revenue mobilization. As tax revenue relies too heavily on federal taxation (about 95 percent), while paying too little attention to provincial governments collection potential, provincial revenue administrations should also follow such a results-oriented model.

A Menu of the Most Urgent Actions

A solid start by the government to move forward comprehensively across many areas in the first 100 days will be essential. What has derailed past reforms is hesitant and fragmented reform efforts. A carefully chosen set of front-loaded measures would, by contrast, earn the government the political capital to make further (and earlier) medium-term advances on the reform agenda. Within the power sector, action is needed on several fronts simultaneously. First, a single-point power authority should be established—and managerial autonomy, performance standards, and accountability should be introduced for power utility firms, while considering some for privatization. This approach should provide clear incentives to reduce theft and losses and to increase collections. Second, a clear schedule of power tariff increases must be established to bring average notified tariffs closer to determined tariffs alongside visible enhancements on power reliability. The goal would be to enable distribution companies to achieve full cost-recovery and perform basic operations and maintenance (life-line below-cost tariffs on the basic block could be maintained for the poorest). This can be combined with a schedule to improve power reliability for paying customers and reduce subsidies. Third, while the circular debt is a symptom and can be unwound over time once the system is put on better footing, consideration can be given for taking it off the books of the energy companies and parking it for now. Fourth, a medium-term plan for sequenced priority investment in both domestic gas and hydropower should be initiated, including opening domestic gas to private sector investment. The Water and Power Development Authority’s financial and planning capacity should be strengthened to enable it to raise investment funds more easily from the private sector.

The second most important reform to initiate early on is revenue mobilization. This, combined with a reduction of power subsidies, is a precondition to creating the fiscal space for increased investments in infrastructure and human development. First, ad hoc tax and tariff reductions and SROs (except priority medicines and food items for the poor) should be eliminated. Second, the tax base should be broadened by using existing information technology systems to identify and register taxpayers and businesses that have not yet been included. This can be combined with enhanced electronic filing of taxes to facilitate compliance. Third, customs tariffs should be simplified to a maximum of three slabs; corporate and personal income tax can also be streamlined. Fourth, the FBR
should be made more autonomous with greater enforcement capacity. Finally, incentives may be considered to allow provinces to raise own-generated resources, perhaps starting by broadening the coverage of services taxed by the general sales tax, upgrading the urban property tax (combined with an agricultural income tax), and replacing the one-time registration tax on motor vehicles with an annual license tax and fixed fuel levy. Excise taxes on discretionary and luxury items could also be considered.

The third most important action is to reinvigorate SOE reform and the business environment. Deploying the private sector as the engine of development is long overdue, and many actions could be done quickly. To create a level playing field and improve services, the government should prepare a roadmap to privatize or restructure loss-making SOEs in a short time-frame. To reduce red tape, it should also prepare fairly quickly the ground for a one-stop shop for new investors. On the financial sector, the State Bank of Pakistan (SBP) could monitor and make private SME expansion a priority for banks. Streamlining construction permits would also be important. Improving the registration base for land and housing, and allowing movable collateral, would increase the number of firms and individuals using more collateral to borrow funds. Special programs should be considered for youths and women to ensure they can participate in this growth, through targeted on-the-job training programs and greater microfinance for potential entrepreneurs.

The fourth priority should be the regional agenda, focused not only on India but on all regional countries. Completing the trade normalization process with India and granting it MFN status would help Pakistan benefit quickly from the fast growth and large markets. Conservative estimates suggest that bilateral trade flows could multiply at least three times, and most observers agree that the growth-enhancing dynamics that this process would unleash would be even more significant for foreign direct investment (especially information technology and manufacturing), services (including financial and tourism), integrated value chains in manufacturing, and power projects. A power transmission link with India, under a power tariff arrangement benefiting both countries, could be implemented in the next 6–12 months with a potential capacity of 1,000 megawatts. And over the medium term, bringing electricity and natural gas from Central Asia could have similar potential. Trade reform should be done in combination with improving trade logistics, including upgrading border management, with a focus on the Wagha border. Special economic zones in border areas could also be considered.

The fifth priority should be to improve human development. With the management and financing of education and health decentralized to the provinces, there is a need to strengthen national and provincial standards and provide transparent mechanisms for increased budget transfers linked to performance. In education, building on the programs already under way in Punjab and Sindh, there is room to increase support for low-cost private provision of education, particularly in areas underserved by the state, as well as to strengthen accountability and learning assessments to provide incentives to improve education and reduce absenteeism. In health, the most pressing need is to increase spending on nonsalary activities. To fight staff absenteeism and strengthen outreach, the government could consider contracting out management or greater use of nongovernmental and community organizations. Expanding the Lady Health Workers Program is necessary since the regions not covered are the most disadvantaged. For social protection, the BISP database provides a golden opportunity to contain untargeted subsidies and redirect more resources to the poor to help them manage the aftereffects of reductions in nontargeted subsidies. Pilot BISP programs for primary education and health insurance should be assessed and scaled up, with a contingency fund for natural disasters considered.

The sixth priority for making all these efforts more effective is to strengthen governance and accountability. A key first step in reforming the energy sector is to commercialize or privatize energy
companies to strengthen their accountability to consumers and their ability to make cost-recovery decisions. For decentralized service delivery, a critical element will be to set goals, collect data on them, and hold service providers responsible for meeting them. Greater use of contracting out service delivery in some areas of education and health can help deliver. It is also recommended that three critical institutions—the FBR, SBP, and PBS—be made more autonomous, with greater capacity and enforcement authority. Beyond these steps, greater use of e-services throughout the government can facilitate service delivery with feedback mechanisms. Financial management can be enhanced by improving the capacity of the regulatory authorities for procurement to monitor the performance of public entities and switch to e-procurement. The right to information laws and regulations should be approved. On devolution, there is a need to clarify roles and responsibilities (including budgeting, financial reporting, and taxation powers) between national and provincial authorities to strengthen accountability. Finally, civil service reform should be initiated to reduce turnover, to attract solid and specialized professionals, and to rationalize pay scales and make them transparent.

**Implementing to Succeed**

*Far-reaching reforms will take both leadership and building consensus.* The suggested actions included here should be considered as a menu of options, to be selected and guided by the new administration’s goals and ambitions—and by political realities. But the challenge for the government is that incremental (piecemeal) actions will not be enough to change the dynamic. For comprehensive reform, implementation will require strong political will, expert design, and persuasive negotiation. Powerful individuals and well-organized groups with vested interests will continue to avoid changes, as in taxation, agriculture, and trade reform. Thus, a broad consensus with a solid communication effort is needed as part of the change management process to overcome these interests. The near-crisis situation in Pakistan can also become a positive motivator for change. And early gains (low-hanging fruit) can provide momentum for further progress.

Achieving success will also take competent and skilled managers and expert designs. Political leadership at the top is essential for commitment and credibility. But vision and political decision need to be complemented by skilled managers and persuasive negotiating capacity to champion and design reforms through the complex political and social milieu. All successful past reforms in Pakistan featured strong support from top leaders, essential for reaching political support, and from highly respected professionals, both for their academic credentials and deal-making skills. Solid technical design also makes the acceptance of reform more likely, especially if it rightly identifies winners and losers and provides for proper contingency actions to minimize opposition. Financial support from donors is secondary, and not determinative; if it forces reform with no ownership, it can even be counterproductive. But it can prove useful when complemented by solid institutional ownership and timely advice and technical assistance.

A bold start, with a properly sequenced rollout, will enhance the likelihood of success. A carefully chosen set of front-loaded measures would earn the government the political capital to make further (and earlier) medium-term advances. A possible sequence would be for the government to begin with measures that consolidate fiscal sustainability, set new growth dynamics into motion, and address the most pressing social commitments. Phasing out expensive subsidies, initiating energy and tax reform, and taking key actions in social protection—like consolidating and expanding the BISP—should also not be delayed. These steps might be followed by a thorough exercise reviewing spending priorities, consolidating ongoing sectoral reforms (especially for education, energy, and agriculture), and introducing institutional reforms (especially those for public financial management, trade, and vocational training). These reforms would stimulate exports, strengthen governance, and give the new government an image of commitment, participation, and
transparency—which would help it win support for further reforms.

**Special attention should be given to the most vulnerable people or areas.** Many of the reforms noted here are most likely to benefit those already well integrated into Pakistan’s economy. Large groups of people—particularly the poor, youths, and women—will need special measures to ensure that they too can participate in and benefit from these reforms. So, too, will special measures be needed to ensure that the most conflict-affected areas are not left out. This will require a deeper understanding of the drivers of conflict, so that they can be addressed.

**Above all, sustained implementation matters.** There is no substitute for political will to make bold decisions. But the key to success will be implementation, implementation, and implementation. It does no good, and probably some harm, to take half-hearted steps that are then partly reversed when facing obstacles. Most reforms, because they are complex and intertwined, will need concerted actions by multiple official entities across several years. A cross-sectoral reading of the policy notes would facilitate collective thinking on the complexity of the issues—and highlight the need for strong and coherent collective and comprehensive government action. To facilitate reform implementation and coordination across multiple entities, the government could consider creating small monitoring cells or performance management units at the Prime Minister and Chief Minister offices to follow up and manage the overall progress on targets.

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**Box**

**A possible list of the 12 most urgent transformational reforms to initiate**

1. **Strengthen power sector governance.** Establish a single point power authority and appoint professional management in the boards of power distribution companies, bring average notified power tariffs close to determined tariffs along with visible reduction in power outages, and create incentives for private investment in gas fields.
2. **Attract private investment.** Restructure and privatize selected power distribution companies and other loss-making SOEs, and expand commercial credit to SMEs.
3. **Manage fiscal crisis.** Eliminate tax exemptions and zero rates (and related SROs); identify and register 1 million new taxpayers using information technology systems and databases, and increase fuel taxes and special excise duties.
4. **Reorient public spending.** Phase down untargeted subsidies to power and SOEs, and reassign funds to key infrastructure spending and maintenance (power, water irrigation, and roads) and targeted social spending.
5. **Reinvigorate trade liberalization and competitiveness.** Eliminate trade-related SROs and simplify customs tariffs to a maximum of three slabs.
6. **Strengthen economic governance.** Strengthen the autonomy and enforcement capacity of the FBR, SBP, and PBS, and ensure stability of tenure and accountability of key government positions.
7. **Enhance business environment.** Establish a one-stop shop for investors in obtaining licenses and registration, and streamline construction permits and property registration procedures.
8. **Tap regional potential.** Complete normalization process with India granting it MFN status, and sign a power transmission connection and trade agreement.
9. **Improve social service delivery.** Double funding for education, health, and nutrition nonsalary budgets, set a system for tracking teachers’ professional recruitment and performance, and use low-cost private outsourcing mechanisms.
10. **Protect the poor and vulnerable.** Consolidate gains under the BISP through a coherent social protection framework across provinces, increase the BISP budget and extend pilot programs on education, child labor prevention, and health insurance, use the BISP scorecard to redirect expensive power subsidies to poor households, create contingency fund and micro-insurance programs against the risk of natural disasters, and make poverty data available to the public.
11. **Address corruption.** Approve right to information law, set e-procurement to make public biddings transparent, perform audits of major procurements, and establish public procurement regulatory authority two-tier complaint redressal mechanisms.
12. **Complete devolution.** Establish financial and administrative autonomous local governments, and clarify roles and responsibilities among national, provincial, and local authorities (budgeting rules, financial reporting, and taxation incentives).