Board Meeting of January 21, 1999
Statement by Matthias Meyer

Pakistan: Country Assistance - Progress Report
Pakistan: Structural Adjustment Loan

We welcome the timely CAS progress report. Our overall assessment of the country's performance and its prospects are not as optimistic as those presented in the progress report. Nevertheless, we concur with Management that the risks of not supporting Pakistan at this stage are greater than the risks associated with the proposed program. The social and economic vulnerability of the country is such, that in the absence of the Bank’s support and in the context of the international creditors' and investors’ lack of confidence, it might embark on a rapid downward spiral with potentially serious consequences. Hence, we support the coordinated response as outlined in the report. We have the following comments and questions.

1. The lack of data and analysis in the report tracing the impact of the economic decline on the poor is rather surprising. Even if hard data were not available, a qualitative assessment would have been warranted. After all, poverty reduction is the overarching objective of the Pakistan CAS, given the country’s high poverty levels and the notorious inequalities in the access to economic opportunities and basic services. The statement that the poor have so far been relatively insulated, contrasts with social discontent, described in the report, arising from the difficult economic situation. We urge Management, to give high priority to the ongoing poverty assessment. We hope it will address causes of poverty, be action-oriented and guide the CAS planned for FY00.

2. With regard to the fiscal area, we would like to know how poverty has been considered in prioritizing public expenditures, above and beyond protecting the budgets for the Social Action Program. Are the expenditure reductions in the public sector development program (PSDP) equitable with respect to how they affect rural vs. urban areas, poor localities vs. others? Likewise, we are concerned about the lack of agreement between the Bank and the Government on limiting spending for large infrastructure programs outside the PSDP framework.

3. The Social Action Program (SAP) is a cornerstone for poverty alleviation by enhancing access to education and primary health care. However, feedback from our field mission, contrasts with the rather positive assessment in the CAS progress report, in two areas:
- Education outcomes: Apparently, third party validation revealed deficiencies, including that of "ghost schools" and absent teachers which puts into perspective the increase in primary school enrollment. Hence, we support the intended focus on qualitative improvements under SAP-II.

- Community and NGO participation: The acceptance and inclusion of NGOs and communities as partners of government institutions in design and implementation of social services programs is still a major challenge. This seems to be evidenced by local press reports on government action vis-à-vis NGOs (e.g. in Punjab) and questioning of NGO motivations.

4. **Agricultural taxation** is crucial both for fiscal and equity reasons. An agricultural income tax has been introduced but much remains to be done, both in terms of extending coverage to all provinces and improving the design of the tax which does not comprise an adequate land valuation component. We stress this, because a fair and well designed agricultural tax helps reducing the bias against small farmers, and it contributes to the better functioning of land markets. We expect that good progress on this front will constitute a key prior action for the agricultural adjustment operation.

5. We fully support the Bank’s strengthened focus on governance and value highly the Government’s acknowledgement that poor governance is the country’s core problem. The stronger focus on improved financial governance in the power, banking, gas and fiscal areas is thus most appropriate. However, we would like to highlight the importance of empowering communities, and enhancing participation of civil society in the development process. As a trusted intermediary, the Bank can and should play a proactive role in promoting more participation as an important ingredient of good governance. We trust that the FY00 CAS process will be participatory.

6. Our chair welcomes the rationale of the SAL to reward prior actions with respect to financial governance in key sectors. This is fundamental and a prerequisite for successful implementation of the strong but ambitious reform program, as set out in the PFF. We appreciate that there is evidence for achievements for example in the banking sector. The prior actions taken are significant given the difficult political and economic context. However, they constitute only first steps and require decisive follow-up. We question the heavy front loading of disbursement and we are not fully convinced that Pakistan’s track record justifies the move to the high base case scenario at this point. We do have a clear preference for re-phasing part of the loan while ensuring that the program remains fully funded. Moreover, the SAL covers initial reform steps in many areas, most of which are also covered by IMF. This raises the question of division of labor between the IMF and the Bank, with respect to policy dialogue and monitoring of reform implementation. We will reserve our final position on the SAL and await with interest Management response.

In conclusion, we stand ready to support the Bank’s necessary but risky approach to assist Pakistan. We expect that implementing the program and determining levels of lending will depend on strong policy performance, improved governance, programs reaching the poor and sustained improvements in portfolio performance. We expect that staff will focus monitoring and policy dialogue on these crucial elements for implementing performance-based lending.