

**BUILDING A HUMAN  
ECONOMY TO OVERCOME  
UNDERDEVELOPMENT:  
A STRATEGY OF SUSTAINED  
GROWTH AND ECONOMIC  
INDEPENDENCE**

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### **Abstract**

*Overcoming underdevelopment requires building a human economy that places people at the center of the development process as well as the measure of progress. Pakistan can be pulled out of underdevelopment through a change in the institutional structure from one that works for the rich to one that works for the poor. This would establish a human economy that provides equality of opportunity to all citizens to actualize the human potential of the society. It is within a human economy that the enterprise, talent and innovation of the people can become the real strength of a state and the basis of achieving sustained economic growth. The research paper presents the outline of a four pronged strategy of transformative development that generates growth through equality.*

**Keywords:** Human Economy, Human Capabilities, Institutional Structure, Innovation, Product Space, Transformative Development, Sustained Economic Growth.

### **Introduction**

**E**ven after over seven decades of independence Pakistan remains underdeveloped. The country is locked in structural constraints to the actualization of its great human potential. Consequently, the economy lacks a base of innovations, long term productivity increase and is thereby prevented from achieving sustained economic growth. Persistent mass poverty, inequality, deprivation of basic services for the majority of the people continues to sap the vitality of its people and the strength of the state.

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\*Dr. Akmal Hussain is an Economist who specializes in action research on Development. He is Distinguished Professor and Dean, School of Humanities and Social Sciences, Information Technology University (ITU), Lahore, Pakistan, Co-chair, Governing Board, South Asia Centre for Policy Studies (SACEPS); and Senior Fellow, Pakistan Institute of Development Economics. The author's email address is [akmal.hussain@itu.edu.pk](mailto:akmal.hussain@itu.edu.pk).

We begin by redefining underdevelopment as a condition of systemic constraints to the actualization of the human potential of society and bringing to bear human development to achieve economic and social dynamism.

We argue that overcoming underdevelopment requires building a human economy that places people at the center of the development process as well as the measure of progress.

In section 2, we propose a strategy of transformative development for a human economy. Here we identify the key structural constraint to growth sustainability: an export structure that is unable to generate high enough export earnings to finance the import requirements of rapid GDP growth.

In section 3, we present new research findings to identify the challenges of diversifying the export structure towards knowledge intensive high value added goods that could enable high export growth. These research findings establish the link between innovation-based development of products for export and economic growth.

In section 4, we discuss the emerging new approach of achieving sustained growth through equality rather than inequality. In section 5, we outline the main elements of a strategy of achieving sustained growth through equity.

## **Redefining Underdevelopment**

Underdevelopment has been historically understood as a state of society and economy where the material conditions cannot improve substantially. In the orthodox literature this could be due to shortage of natural resources or finance.<sup>1</sup> Yet many underdeveloped countries are poor despite being rich in natural resources. At the same time large volumes of finance may be extracted from such countries for transfer to the advanced countries, often through the market mechanism. In the political economy tradition it is argued that the economic structure of these countries within a colonial or neo-colonial framework is such that most of the investable surplus in the economy while being generated, is systematically extracted and transferred out instead of being reinvested for economic growth within the country<sup>2</sup>. This approach while being a major improvement on the “natural resource” theory is limited by the fact that it does not specify a mechanism through which the dynamics of rapid growth can be initiated while remaining within the globalized market system. The common problem with both these traditional but distinctly different approaches to understand

underdevelopment is that they implicitly consider economic growth to be an end in itself. Human beings in these approaches are considered as a 'resource' and an input into the growth process. In our view economic growth while being necessary is not an end but a means to achieving human well-being. If human beings become the center-piece of the economic process, then the institutional and organizational forms through which growth is conducted become as important as the pace of growth itself.

In this paper, we redefine underdevelopment as a condition where there are systemic constraints to the actualization of the human potential of a society. It is the lack of development of human capabilities<sup>3</sup> that restricts mobilization of resources, productivity increase and innovation, thereby preventing sustained improvement in the material conditions of the people.

### **The Link between Development of Human Capabilities and Economic Growth**

Professor Amartya Sen first formulated the concept of human capabilities. He applied this concept to show that the development of human capabilities provide individuals with entitlements over goods and services<sup>4</sup>. These entitlements widen the choices available to lead the kind of life the individual considers meaningful. We argue further that the development of human capabilities of individuals have important implications for macroeconomic growth in particular and the development of society in general. A new socio-economic dynamic is introduced whereby, if institutional conditions can be created to enable individuals to be occupied in the field in which they have developed their capabilities, and then innovation in every field would be accelerated. This would continuously increase productivity and hence achieve sustained long term economic growth. In this regard we may mention Professor Aghion who in his seminal work has empirically established that the deeper and more wide ranging the process of innovation in a country, the higher the long term economic growth<sup>5</sup>.

### **Growth and Institutions**

In order to elaborate the relationship between the development of human capabilities and economic dynamism it is necessary to explore the literature of the New Institutional Economics. We would suggest that to enable the placement of individuals who have developed their capabilities in fields relevant to their talent, it is necessary to have an efficient institutional structure. An institution has been defined by Douglass North as a set of formal rules and informal norms, which through the incentives and disincentives they embody, structure human

interaction<sup>6</sup>. So an efficient institutional structure is a particular configuration of economic, social and political institutions which on the basis of competition, incentivize hiring based on merit, hard work, innovation, productivity increase and thereby generate long term economic growth<sup>7</sup>. By contrast an inefficient institutional structure is one which by restricting competition systematically generates rents (unearned income)<sup>8</sup> for an elite coalition. Such a rent based institutional structure induces hiring based on nepotism, lacks incentives for hard work, productivity increase and innovation. Consequently, the economy based on an inefficient institutional structure is unable to achieve sustained long term per capita income growth.

In the New Institutional Economics (NIE) the distinguishing feature between developed and underdeveloped countries is that the developed countries are able to achieve sustained per capita income growth while the underdeveloped countries are unable to do so.<sup>9</sup> This is not to say that underdeveloped countries don't grow at all, they do. However, these countries can grow only in spurts followed by periods of stagnation or even negative per capita income growth. So the gains made during the periods of positive per capita income growth are largely lost during periods of stagnation or negative per capita income growth. Thus over the long run there is no substantial increase in per capita incomes, keeping the country in the low or middle income category with mass poverty persisting and governments cash strapped. Thus in the NIE, the challenge of development is to change the institutional structure from an inefficient to an efficient one, to enable sustained economic growth.

## **Transformative Development**

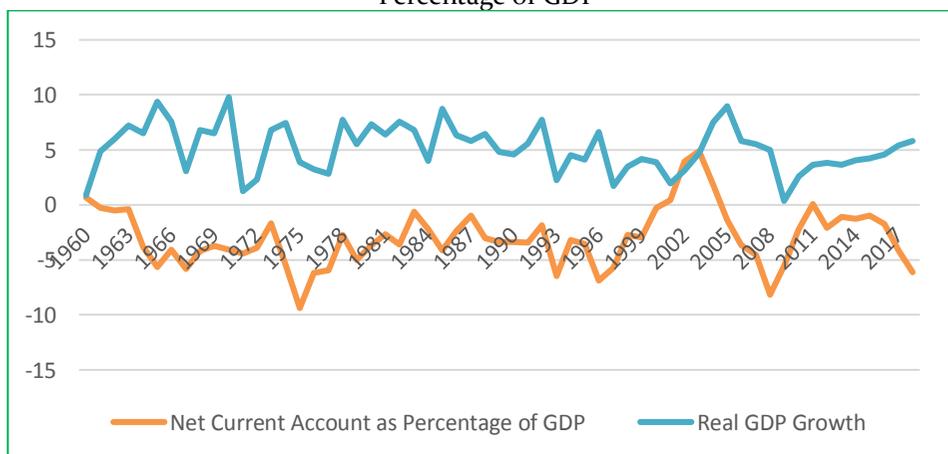
Pulling Pakistan out of underdevelopment through a transformative development process requires a change in the institutional structure from one that works for the powerful and rich to one that works for the powerless and the poor. This would enable establishing what can be called a *human economy*. Such an economy provides equality of opportunity to all citizens to actualize the human potential of society. When the institutional framework and organizations of state and society enable the development of human capabilities, then the process of transformation is triggered. It is within a human economy that the enterprise and talent of the people can become the real strength of a state and the basis for achieving a dynamic economy.

In the context of transformative development for a human economy two central organizing principles of society<sup>10</sup> may be considered: first, all human beings are of equal worth. This principle is rooted in all major religions particularly Islam where saving the life of a single human being is tantamount to saving all humanity.<sup>11</sup> The principle of human equality also forms the basis of post-Enlightenment Western thought.<sup>12</sup> The second principle postulates that social justice demands disproportionately favorable treatment of the deprived sections of society. This aspect of justice has been powerfully articulated by<sup>13</sup> Professor Amartya Sen. These two principles indicate that the aim of developing human capabilities on an equitable basis should be of central importance in the design of public policy and measurement of progress.

### A Strategy of Transformative Development for a Human Economy

Let us begin with an analysis of the structural basis of Pakistan's pattern of stop-go growth with the associated perennial problem of large balance of trade deficits. Pakistan's economy is a typical case of the inability to sustain GDP growth. Each time a relatively high GDP growth is achieved, the economy plunges into a balance of payments crisis. This feature is illustrated by Figure 1. It is interesting that the graph for the net current account deficit is a mirror image of the graph for real GDP growth rates, illustrating the fact that high GDP growth rates are associated with high balance of trade deficits that underlie growth instability.

**Figure-1:** Pakistan's Real GDP Growth Rates and Net Current Account as Percentage of GDP



**Source:** Calculations based on State Bank of Pakistan Data

The balance of trade deficits repeatedly oblige the government to seek balance of payments support from the IMF which attempts to address the problem primarily by constricting import expenditures through reduction in the aggregate demand. They do this by undertaking policies (devaluation, interest rate increase and a sharp reduction in public expenditure) which effectively slow down the GDP growth rate.

At a proximate level the recurrent balance of payments crises occur because the growth of Pakistan's exports cannot keep pace with the increased import expenditures associated with high GDP growth. Consequently, the balance of trade deficit becomes so large that it is difficult for the government to finance it.

At a deeper level the question that arises is, why over seven decades, Pakistan has been unable to accelerate its export growth sufficiently to have the import capacity for sustaining GDP growth. The answer lies in the failure so far to diversify exports towards high value added knowledge intensive goods and services that constitute an increasing share of global export demand.

For seven decades Pakistan's export structure has been predominately oriented towards low value added exports with low knowledge intensity such as cotton, cotton yarn, rice, leather and textiles. These low value added goods even now contribute 82% of total exports earnings, while high tech exports constitute less than 2% of total manufactured exports. Even in textiles, lack of innovation, efficiency, consistent quality and marketing effort have led to a reduced share of Pakistan in global textile exports while Bangladesh and India have increased their share.

The inability to diversify exports for high export growth is rooted in the failure of our policy makers so far to understand the nature of export diversification in the contemporary global economy, the complexity of technology intensive production, the process of innovation and its relationship with what can be called the knowledge infrastructure of a country. Understanding of these dimensions of the modern economy would result in focusing policy towards nurturing citizens with a capacity for critical thinking and original contribution to knowledge. The development of such human capabilities would enable Pakistan to devise knowledge intensive goods and services and thereby enter new product spaces for diversification of exports.

## **Export Structure, Product Space and Growth Sustainability**

Recent research has shown that a higher weight of knowledge intensive goods in the export structure is an important determinant of long term economic growth of a country. For example, an UNCTAD study by Dasu and Das provides evidence for this proposition.<sup>14</sup> Their panel data analysis of 88 developing countries from 1995-2007 shows that countries with a higher percentage of their export sales coming from knowledge intensive products, have higher long term rates of per capita income growth.

## **Knowledge Intensity and Product Space**

A new way of looking at the issue of knowledge intensive exports and its relationship with the development of new productive capabilities was provided by Hidalgo and Hausmann<sup>15</sup> with their concept of *Product Space*.<sup>16</sup> It is based on the application of Network Theory to economics and uses graphical representation of internationally traded products to depict how different products are connected to each other within a network called Product Space. Apart from showing the composition of internationally traded products in terms of product category, the graph can also map countries within the product space according to the types of products they produce.

The product space map can show within different categories of products, the differing degrees of connectedness. More sophisticated products are found in the densely connected *core* of the product space while low knowledge intensive products being the least connected, are found in the periphery of the Product Space.

## **Economic Complexity Index (ECI)**

Economic Complexity Index (ECI) is a numeric measure which shows the relative position of countries within the Product Space by capturing the degree of complexity of their productive structures. Economic Complexity of countries is determined by the sophistication and knowledge intensity of the products they export. The type of products manufactured in an economy reflect the knowledge and capabilities possessed by that economy. Therefore, complexity of an economy is “expressed in the composition of a country’s productive output”.<sup>17</sup> The evidence shows that the Economic Complexity Index is a powerful predictor of per capita income growth.

## **Product Connectedness, Collaboration and Product Space**

An interesting aspect of highly connected products is that they are likely to be produced through collaboration between different countries. Therefore, such products for their production and export involve networks of firms not only within a country but also between countries. The ability to produce knowledge intensive products involves a high degree of connectedness between the products and collaboration between the production units manufacturing them. So production of sophisticated goods and services requires diversified production capabilities. The evidence shows that countries producing knowledge intensive products, occupy the core of the Product Space and are in fact high income countries while countries with less diversified production capabilities exporting low knowledge intensive goods, turn out to be low income countries, lying at the periphery of the Product Space. Thus, the location of a country within the Product Space is a determinant of its per capita income<sup>18</sup>. Hidalgo and Hausmann<sup>19</sup> have shown that countries follow trajectories of growth whereby over time, they tend to approach the level of income indicated by the complexity of their productive structures.

## **Economic Growth, Product Space and Diversification**

The question that arises is whether countries that seek high growth trajectories should develop a complex and diversified production capability. According to the traditional view, efficiency and economic growth require specialization on the basis of comparative advantage. This view has been rejected by new research and actual evidence on the nature of economic growth. For example, Imbs and Wacziarg<sup>20</sup> present strong evidence to show that countries with high per capita incomes become more diversified and less concentrated. Furthermore, cross-sectional as well as time series econometric analysis shows that higher economic growth is strongly associated with increased *diversification* and not specialization within a narrow product set.

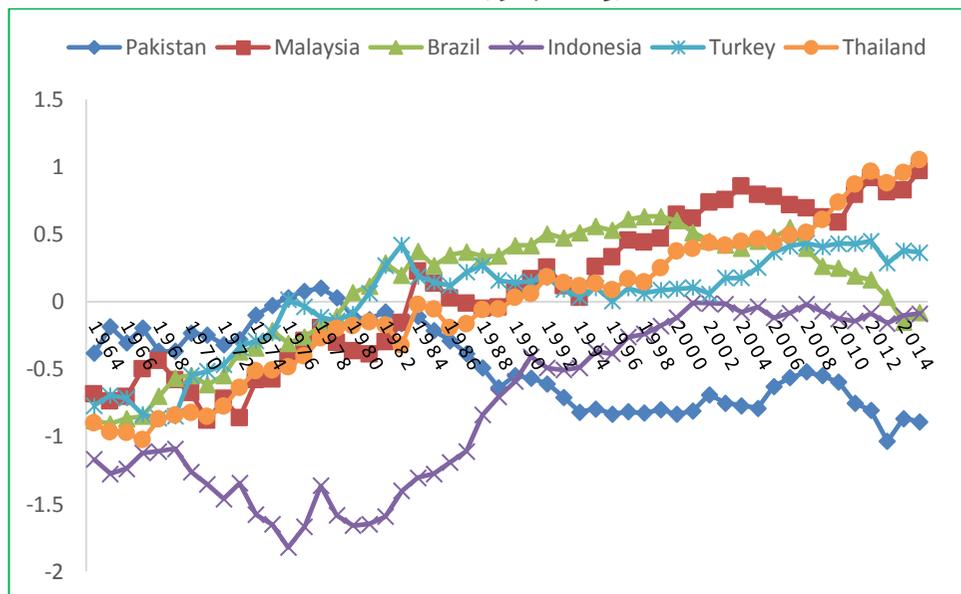
The corpus of recent research on Product Space makes clear that sustained economic growth requires countries at the periphery of the Product Space to undertake policies of industrial diversification for developing knowledge intensive products. This would make possible for underdeveloped countries to shift from the low income periphery of the Product Space to the high income core.

## **Pakistan's Export Structure in Comparative Perspective**

In terms of the Economic Complexity Index Pakistan is ranked at 87<sup>th</sup> out of 108 countries in the year 2015. One of the main reasons why Pakistan got left

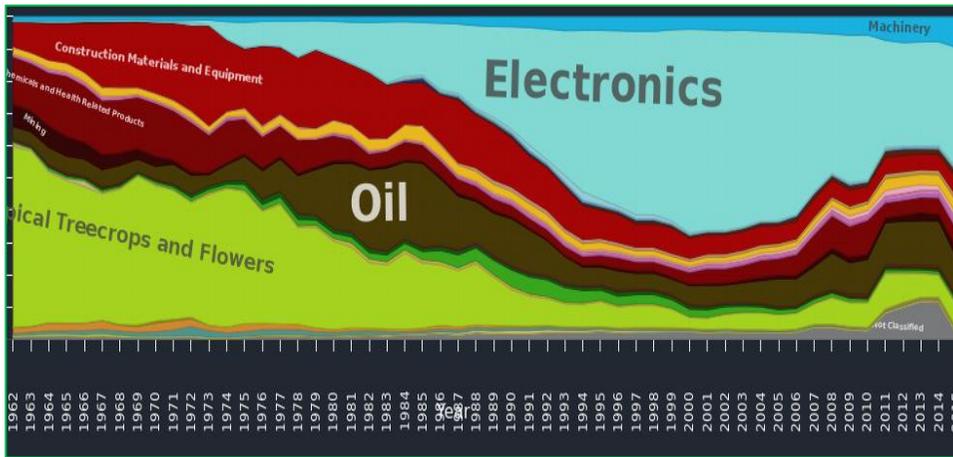
behind while Brazil, Malaysia, Indonesia, Turkey and Thailand forged ahead was that these countries changed their export structures towards more knowledge intensive products. Pakistan's productive structure remained stagnant.

**Figure-2:** Economic Complexity Index: Pakistan's Comparison with selected Countries (1964 – 2015)

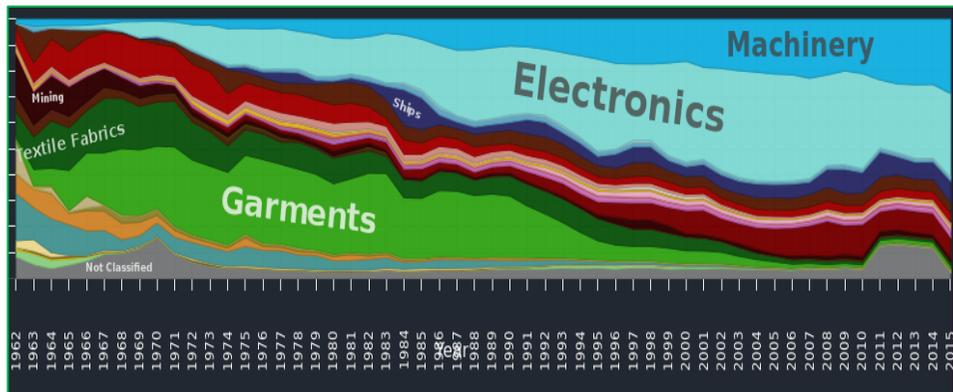


**Source:** Ishtiaq and Chaudhry (2017); Calculations by Nazeef Ishtiaq based on the data obtained from the MIT Observatory of Economic Complexity

The figures 3 and 4 on next page show clearly that unlike Pakistan, these countries significantly changed their export structures towards more sophisticated and knowledge intensive products. While Pakistan remained at the periphery of the Product Space, Malaysia and South Korea were able to penetrate the core of the Product Space. In the case of Malaysia, the export structure which was initially dominated by primary commodities and some basic manufactures, changed the composition of its exports towards high value added goods such as electronics. Similarly, South Korea which had higher share of textiles and garments in its exports, started building capabilities in electronics, machinery and ship building. As South Korea increases the share of machinery in total exports, it will further strengthen its growth prospects as machinery is the most complex sector within the Product Space.

**Figure-3:** Evolution of Malaysia's Export Structure (1962-2015)

**Source:** Visualization generated from the web application of the MIT Observatory of Economic Complexity

**Figure-4:** Evolution of South Korea's Export Structure (1962-2015)

**Source:** Visualization generated from the web application of the MIT Observatory of Economic Complexity

## The Emerging New Approach of Growth with Equality Pakistan's Past Development Approach Growth with Inequality

Since the mid-1950s the prevalent view underlying policy design was to achieve high rates of economic growth on the basis of inequality. The idea here was that high GDP growth requires high rates of investment and having assumed that only the rich can save, a policy of transferring incomes from the poor to the rich was thought necessary to ensure growth. Hence the doctrine of "functional inequality" formed the basis of the growth strategy of the 1960s. This idea emerged

from the 1955 paper by Nobel Laureate Simon Kuznets who argued that during the growth process, inequality would first rise and at a later stage fall, through market forces.<sup>21</sup>

Pakistan's policy makers in the quest for growth with inequality proceeded to nurture industrial elite through a range of measures such as tariff protection, subsidies and financial incentives such as the export bonus scheme and cheap credit.

Since inequality was built into the growth strategy it is not surprising that during the 1960s while GDP growth was high at 6.9% annually, inequality increased sharply at both inter-personal and inter-regional levels. For example, by the end of the decade of 1960s, 66% of industrial assets were being controlled by richest 22 families. While the rich were amassing wealth the poorest 60% of the rural population suffered an absolute decline in the per capita food grain consumption from an index of 100 to 91 over the period 1964-70. At the same time there was a sharp increase in the interregional disparity between East and West Pakistan, so that by the end of the 1960s the per capita income of West Pakistan was 42% higher than that of East Pakistan.<sup>22</sup>

These interpersonal and interregional inequalities had devastating political consequences for the state. Interpersonal inequalities led to a mass movement that led to the over throw of the very political system within which growth had taken place. Interregional inequalities fueled a popular movement that led to a fratricidal civil war, rupturing of the state and the emergence of the independent Bangladesh.

### **Inequality is Not Good for Growth**

Recent research by Thomas Piketty<sup>23</sup> has over turned the old Kuznets proposition that initially inequality is good for growth and that overtime market forces would reduce inequality. On the basis of data over the last two centuries, Piketty has shown that inequality instead of falling has in fact increased<sup>24</sup>. This increase in inequality over the long run has occurred through the very market forces that Kuznets thought would reduce it<sup>25</sup>.

In the last three decades new research has challenged the view of economists held since the 1950s that income inequality enables higher economic growth. For example, Galor and Ziera<sup>26</sup> on the basis of cross-country data showed that high inequality of income and wealth, by narrowing the base of investment in

human and physical capital has a negative effect on long term growth. Similarly, Berg and Portillo<sup>27</sup> showed that inequality in low income countries is a key constraint to sustained economic growth. Another dimension of the negative effect of inequality on long term growth is through socio-political instability. For example econometric studies in the 1990s such as Alesina and Rodrik,<sup>28</sup> show that the negative effect of inequality on economic growth is accentuated as inequality increases socio-political instability.

Joseph Stiglitz in his recent book has challenged the orthodox view that market forces unfettered by government intervention, produce efficient outcomes and generate long term economic growth<sup>29</sup>. He argues on the contrary that “widely unequal societies do not function efficiently, and their economies are neither stable nor sustainable in the long term”<sup>30</sup>.

Despite new research that overturned the orthodox thinking on economic growth and the bitter lessons of unequal growth in our own history, no serious attempt has so far been made in Pakistan to chart a new course<sup>31</sup>. The institutional structure that induces inequality and growth unsustainability, remains unchanged. Consequently, inter-personal and inter-regional inequalities continue to increase. According to our 2016 estimate the richest 0.1% of the population, has a per capita monthly income (adjusted for tax evasion) of Rs 1 million. By contrast the poorest 60% of the population has a per capita income of Rs 6000 per month.<sup>32</sup> High income inequality is accompanied by persistent mass poverty. The UNDP 2015 estimate of the incidence of multidimensional poverty in Pakistan shows that 38.8% of the population lives below the poverty line.

Amidst persistent mass poverty equality of opportunity continues to be denied within the existing institutional structure: human capabilities lie largely dormant and the country remains underdeveloped.

### **Turning Orthodoxy on its Head**

It is time to turn the orthodox approach to growth on its head. We have argued in our recent work that a new trajectory of sustained high growth can be achieved *through* equality of opportunity to all citizens rather than only the elite.<sup>33</sup> Universal provision of quality healthcare and education, equitable access over markets, access over productive resources and credit for the middle classes and poor can generate a broad-based economic growth. As the middle classes and the poor are enabled to engage in investment, innovation and productivity increase,

the creative potential and previously untapped material resources of the people can be brought to bear to achieve a new trajectory of sustained economic growth through equality.

## Development as Transformation

It can be argued that sustained high growth based on equality would be the outcome of a broader approach that has been termed *development as transformation*.<sup>34</sup> This involves putting people at the center of the development process. It aims to develop their human capabilities and bring them to bear as the basis of the dynamism of the economy and society. The actualization of the human potential unleashes creativity, innovation and enterprise that not only powers economic growth but also enriches human civilization.

The universal provision of health, education and social security are essential to the application of the principle of equality in Transformative Development. There are some who believe that Pakistan cannot afford to undertake such a policy. However, there is definitive evidence to show that a wide range of countries (Germany and Sweden in Europe, China, Japan and South Korea in Asia), at the time that they took their first steps towards the universal provision of health, education and social protection had a per capita income lower than that of Pakistan today (see table-2). The provision of these basic services is not only a normative aspect of development but, as recent research shows, is the basis of sustained high growth<sup>35</sup>.

**Table-2:** Per Capita Income of Selected Countries when they Initiated Provision of Basic Services

Country	Year	Per Capita Income (2011 US \$) (PPP)
Germany	1883	3050
Denmark	1814	1706
Sweden	1842	1243
Norway	1848	1475
Finland	1866	1041
Japan	1911	1810
China	1951	899
South Korea	1962	1573

**Note:** Pakistan, which is yet to give a commitment for the universal provision of basic services, had a per capita income (2011 US\$, PPP) in 2016 of 5250.

## **An Outline of a Strategy of Growth through Equity<sup>36</sup>**

In this section we will outline a growth strategy which can place Pakistan on a new trajectory of inclusive and hence more equitable growth. The basic idea is to enable the middle classes, the poor and those living in backward areas to become participants in the process of savings, investment and innovation. They can thus become subjects of the growth process rather than merely the recipients of an uncertain trickle-down effect of elite based growth. Such a growth process could unleash the creativity, the enterprise and productive potential of the excluded majority of the population. In so doing the people as a whole rather than just the elite would be the drivers of sustained high growth.

A strategy of growth that reduces inter-personal and inter-regional disparities could not only sustain economic growth but could also contribute to social cohesion and political stability that in turn would reinforce growth sustainability.<sup>37</sup> Furthermore, such a growth process would be consistent with the vision of Quaid-e-Azam Muhammad Ali Jinnah and indeed the Constitution. Jinnah considered equality to be a foundational principle of Pakistan. He declared in ringing tones that echo in the silences of Pakistan's economic architecture that to marred by persistent inequality.

“The great ideals of human progress, of social justice, of equality and of fraternity constitute the basic causes of the birth of Pakistan...”

Jinnah's vision of equality is also expressed in Articles (38)a and (38)e of the Constitution of Pakistan. Article (38) a clearly stipulates that concentration of wealth and productive assets should be prevented.

“The state shall secure the wellbeing of the people irrespective of sex, caste, creed or race by raising their standard of living, by preventing the concentration of wealth and means of production and distribution in the hands of a few to the detriment of the general interest. . .”

Again Article (38)e of the Constitution requires the state to reduce income disparities.

“The state shall reduce disparity in the income and earnings of individuals, including persons in the various classes of the service of Pakistan.”

In the next section we will outline the main elements of a new strategy for equitable growth, that attempts to progress towards Jinnah's economic vision.

### **Elements of a Growth Strategy Based on Equality**

Such a growth strategy would have four main elements: (i) A shift from an elite farmer strategy of the last five decades to a small and medium farmer agriculture growth strategy, (ii) Rapid growth of small and medium enterprises in the manufacturing sector, (iii) A policy framework for reducing regional economic disparities, (iv) Universal provision for health, education and social security.

### **Small and Medium Farmer Agriculture Growth Strategy**

A key factor in growing rural inequality is the elite farmer strategy followed since the 1960s. In this sector a declining trend in crop sector growth has been observed as large farmers experience a decline in input productivity with existing farming practices. The preference of large farms in government policy and inadequate attention to the small farm sector, has also been a significant factor in growing rural inequality. A shift in policy emphasis towards a small and medium farm sector is now required to simultaneously accelerate agriculture growth and reduce rural income inequality. The data shows that at present 94% of the total number of farms and 60% of total farm area in Pakistan is operated by farms below 25 acres in size.<sup>38</sup> Accordingly, a policy of actualizing the considerable potential for crop yield increase and diversification within the agriculture economy could make the small and medium farm sector the leading edge of a new agriculture growth process based on equality. Four specific policy initiatives can be suggested in this regard:

- **Land for the Landless:** The first intervention would be to distribute 2.6 million acres owned by the state at present, to landless tenants in 5-acre packages. After the necessary institutional arrangements in the land market the remaining 42% of landless tenants may be provided credit to purchase 5-acres for themselves. This requires creating a credit fund for landless tenant farmers of Rs 350 billion.<sup>39</sup> Once landless tenants have become owner cultivators, they will have both the incentive and the ability (which they lack at the moment as tenants), to invest in increasing the productivity of the land they cultivate.
- 5-acre packages of agricultural land could be considered sufficient for landless tenants where they would not only have food security, but will also be able generate significant income for themselves. The average per

acre yield of wheat in Pakistan is 1204 kg whereas for rice it is 1018 kg. Considering the minimum support price for wheat and average price of rice paddy in 2016-17, farmers could generate an income of at least Rs. 78,000 per acre in a year, in areas where these crops can be grown.<sup>40</sup> Furthermore, there is significant potential for productivity increase in these two crops. For example, in Indian Punjab, the average per acre yield for wheat is 1861 kg (55 percent more than Pakistan), whereas for rice it is 1609 kg (58 percent more than Pakistan).<sup>41</sup> Yields per acre can be increased by providing to small farmers technologies such as laser levelling and drip irrigation for more efficient water use; soil testing for determining the precise nutrient requirements of farm specific soils and composite fertilizers whose chemical composition is congruent to these nutrient requirements. Small farmers can also be incentivized and facilitated to grow high value added crops, including fruits and vegetables, which would increase their prospects to earn a higher income and also increase the production of these crops in the country.

- Key support services need to be provided through which small farmers could be enabled to substantially raise their crop yields, change cropping patterns towards higher value added crops and diversify into export oriented dairy and livestock farming. The institutional basis of providing these support services are discussed in the following sub section.
- **Small Farmer Development Corporations (SFDCs):** The establishment of SFDCs could enable farmers in the small and medium farm sector to both increase crop yields and diversify. The functions of these corporations would be to provide to the small and medium farmers credit, equitable access over input and output markets and the provision of a whole range of support services. These include land development; new technologies such as drip irrigation; laser levelling; soil testing to ascertain the nutrient requirements of the soil so that composite fertilizers whose composition is congruent to the nutrient requirement of the soil could be prepared; tunnel farming for off season crops; and supply chain management for export. It is proposed that the SFDCs could be designed as Social Enterprises, owned by the small and medium farmers and managed by high quality professionals. Those who have acquired government land through the “Land for the Landless scheme” could be provided credit for acquiring equity in the SFDCs. The loan recipients could return the loans through their dividends.
- **Diversifying the Agriculture Economy:** In order to accelerate the growth of incomes of the peasantry and increase labor absorption in the rural

sector, a diversification beyond the crop sector into high value-added agriculture products is necessary. Diversification of the rural economy of the small and medium farm sector would involve creating an institutional framework for the production and marketing for the domestic and export markets of the following high value-added products: milk and milk products; meat production and packaging; inland fisheries; flowers; fruits and vegetables.

- **Supply Chain Management and IT based Solutions for Export:** The institutional basis for developing the capacity to export such products requires establishing an online portal that would provide information to potential importers, the details of the sellers, products they are willing to supply and the prices at a particular time and certification to the effect that the products meet international standards of quality. At the same time to ensure that the entire supply chain of a particular product meets international standards, individual farmers can be given online farm specific advice on each stage of the production process: land preparation, watering, seed application, fertilizer and pesticide application, grading, cleaning, packaging and storage.

### **Accelerating the Growth of Small and Medium Enterprises (SMEs) in the Manufacturing Sector**

Small and medium industries in the manufacturing sector requiring lower levels of investment are usually more employment intensive, have shorter gestation periods and in many cases have export potential. So, by accelerating the growth of these industries and increasing their weight in total industrial output, higher and more equitable industrial growth as well as higher employment and exports could be achieved for given levels of investment. It is proposed that special emphasis be given to the development of high value-added export-oriented SMEs. These include metallurgical goods such as moulds and dyes, electronics and software.

To provide the institutional framework for accelerating the growth of SMEs in the high value-added metallurgical and electronics sector, it is proposed that Common Facilities Centers (CFCs) be established, based on public-private partnership. The CFCs should be located in those regions where there are large clusters of SMEs.<sup>42</sup> These CFCs would constitute a decentralized support mechanism for providing a package of support services designed to overcome the constraints to rapid growth of high value-added SMEs.<sup>43</sup> Some of the services that these CFCs could provide to SMEs include, facilitating outsourcing contracts between SMEs and large scale manufacturing industries; provision of credit for

upgrading equipment and management systems; raw material banks located in the CFCs for purchase of high quality steel in small quantities by SMEs; provision by CFCs of expensive equipment on a rental basis to SMEs which require forging and heat treatment for dimensional control of their products in their production process; setting up of quality control procedures; research and development of upgraded products and components for the SMEs.

The CFCs could catalyze SMEs growth in the existing clusters. They could also contribute to reducing regional economic disparities if they are located in those backward areas which are proximate to the CPEC and the associated new economic zones.

### **An Approach to Reducing Regional Disparities**

In a free enterprise economy where individual investment decisions are based on private profitability, there is a tendency for investment to get concentrated in the already developed regions. Initial investments in a particular area based on location advantages create external economies for future private investment as infrastructure, labor force skills and network externalities build up in that region, thereby making it more attractive for future investments. This phenomenon of “cumulative circular causation” in the market mechanism tends to accentuate regional inequalities overtime<sup>44</sup>.

Policy planning in Pakistan has so far involved achieving consistency between the aggregate GDP growth target with indicative projections of private sector investment, government expenditure targets at a sectoral level and the overall GDP growth target. Space has historically been assumed out of the planning exercise. Achieving regionally equitable growth would involve bringing the spatial dimension into the center of the planning exercise. The CPEC road network and investment projects could be used to identify and develop potential growth centers in the backward areas. Networks between the growth nodes in the backward areas and industry specific links between them and the developed regions should be established. Incentives for private sector investment and infrastructure together with ancillary roads that could link these new growth centers with the main CPEC high ways should be a part of the growth strategy.

The first step towards specifying growth nodes in some of the backward areas was our study on Industrial Potential of Selected Districts.<sup>45</sup> This study proposes growth nodes for example in Sanghar, Khairpur and Nawabshah in Sindh;

Bhakkar, D.G. Khan and Muzaffargarh in the Punjab. Special Economic Zones under CPEC have already been declared for towns such as Gawadar, Lasbella in Balochistan; Haripur in Khyber Pakhtunkhwa; and Larkana, Khairpur in Sindh. These Special Economic Zones as part of the CPEC project could be integrated with the regionally equitable strategy of economic growth and play a strategic role in reducing regional disparities.

We have already proposed that Common Facilities Centers (CFCs) could play a key role in stimulating small scale industries in the new growth centers in the backward regions. We have also proposed that growth in the existing clusters of SMEs could be accelerated by establishing CFCs in the following areas: Gujranwala-Sialkot Axis, Rawalpindi-Mianwali Axis and Bahawalpur-Bahawalnagar Axis in the Punjab. Similarly, in Sindh CFCs could be established for SMEs growth in the Larkana-Sukkhur Axis, Nawabshah-Sanghar Axis and Hyderabad-Nawabshah Axis. In Khyber Pakhtunkhwa province the CFCs could be located for the development of SMEs in the Haripur-Abbottabad Axis, Haripur-Hawalein Axis and Peshawar-Kohat Axis. In Balochistan Gawadar-Makran Axis and Lasbela-Quetta Axis could be promising candidates for location of CFCs to stimulate the developments of SMEs related with CPEC investments.

It is clear that a new spatial perspective in policy design is required for a regionally balanced economic growth. The CPEC road network and Special Economic Zones provide a historic opportunity for the rapid development of backward regions in every province.

The strategy of growth through equity outlined in previous paragraphs aims to unleash the potential and enterprise of human beings on an equitable basis.

## **Conclusion**

In this paper, we have articulated a new approach in which development is redefined as the actualization of the human potential of society. This requires placing human beings into the heart of the economic growth process by providing equality of opportunity for human development. The starting point would be a commitment by the state for the universal provision of health, education and social security.

We have argued that such a human economy by unleashing and harnessing the capacity for innovation would overcome the existing structural constraints to

growth sustainability and independence from foreign aid. These structural constraints to entering the ranks of developed countries are rooted in an inefficient rent based institutional structure which systematically excludes the deprived sections of society from the growth process. Consequently, a broad based process of investment, innovation and hence long term growth is precluded. The associated lack of a knowledge infrastructure prevents diversification of the export structure towards knowledge intensive high value added exports that could enable sustained high growth to be achieved.

In the end, we have outlined a strategy for the equitable development of human capabilities and the achievement of sustained growth through equity.

## END NOTES

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