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**A PERSPECTIVE ON PAKISTAN-INDIA RELATIONS:  
POWER DYNAMICS, DEMOCRACY AND DEVELOPMENT**

By

Akmal Hussain,  
*Distinguished Professor of Economics,*  
*Forman Christian College University*

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## **A PERSPECTIVE ON PAKISTAN-INDIA RELATIONS: POWER DYNAMICS, DEMOCRACY AND DEVELOPMENT**

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### **INTRODUCTION: A HISTORIC OPPORTUNITY**

A seismic change is taking place in the global economy as its centre of gravity shifts for the first time in three centuries from the West to Asia. At the heart of this process is the rise of China and India. If China is able to sustain an annual GDP growth rate of about 9 percent and India can overcome its present decline in GDP growth to maintain a trend rate of growth of even 7 percent over the next three decades, then China will become the world's largest economy and India the third largest after the US before the middle of the 21<sup>st</sup> century<sup>1</sup>. If India can integrate its economy with South Asia the resultant economic synergies could well enable South Asia to become the world's second largest economy in the next four decades. In the emerging strategic economic configuration, Pakistan can be a bridge between two of the greatest economic power houses in human history. Objectively, the choice before Pakistan is clear: If this opportunity can be grasped, Pakistan's economy can be catapulted on to a new trajectory of high economic growth. South Asian regional economic integration could also give a new impetus to India's economic growth through a much wider base of markets, investment, trained person power, talent and innovations.

The powerful catalytic effect of a region wide growth process could help to unleash the creative potential of the people of Pakistan as well as India and transform their material

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\* The author would like to thank the anonymous reviewer of this chapter for helpful comments on an earlier draft without implicating her/him.

<sup>1</sup> Akmal Hussain, A Vision for South Asia, chapter in, Imtiaz Alam (ed), Whither South Asia, Journal of the South Asian Policy Analysis Network (SAPAN), 2006, Lahore. Page 54.

conditions of life in this century. At the same time the economic linkup between Pakistan and India could strengthen the endeavour for peace and help nurture pluralistic societies, thereby deepening their respective democratic structures. If on the other hand this historic opportunity is lost and ideology overrides the rational pursuit of the interests of the people, then Pakistan is likely to remain mired in slow long term per capita income growth rates, economic deprivation of the people, social polarization and widespread violence by armed militant groups. This internal conflict could not only threaten the nascent democratic state but could overspill into neighboring countries to create regional instability. This could become a festering wound weakening the capacity of both Pakistan and India to actualize their economic potential.

In this paper we will in section I examine the dialectic of power within Pakistan's state structure that shapes Pakistan's constrained economic relations with India and the emerging social and economic factors that could help begin a new era of peace and economic cooperation with India. In section II, we will discuss the attempts by different governments over the last decade to craft a new approach to Pakistan India relations. We will indicate the dynamics of power that underlay both the attempts as well as the constraints to normalization of economic relations between the two countries. In section III, the logic of normalization of relations with India in terms of strengthening democracy, economy and the state will be articulated. A paradigm shift from "national security" to human security will be proposed. In section IV, we will briefly examine Pakistan's economic crisis to suggest that some of the main constraints to GDP growth can be released by opening up trade and investment flows with India. Finally in section V, we will present an outline of the adverse effects of climate change in South Asia with special reference to the problem of water scarcity in Pakistan. The climate change dimension brings a new urgency to the imperative of Pakistan-India cooperation.

## **I. DYNAMICS OF POWER, DEMOCRACY AND ECONOMIC RELATIONS WITH INDIA**

I.1 *Power Structure and Policy.* Governance in Pakistan has been shaped not only by the Constitution but the power structure that underlies it. Although the formal rules of the Constitution stipulate that the military is subordinate to elected civilian authority, yet within

the functioning power structure the military is a key player. The power structure consists of the President, the Prime Minister, influential members of Parliament, key members of the bureaucracy and the military. The elite coalition represented in the power structure consists of the landlords, dominant groups in the large scale manufacturing sector, big traders, networks within the bureaucracy and the security apparatus. The judiciary which had earlier lacked independence being subject to the interplay within the power structure, has now asserted its independence and in recent years has played a vital role in maintaining and strengthening constitutional rule.

For most of Pakistan's history since 1958, the military has been the dominant element within the power structure and has played either a direct role during authoritarian regimes or an important indirect role in governance during periods of elected civilian governments. It is not surprising therefore that the paradigm of national security has been formulated by the military which shapes policy not only in the sphere of security but also foreign affairs. Within this paradigm India has been seen as an adversary and relations with India a zero sum game. The armed conflicts with India in 1948, 1965, 1971 and 1999 have given sustenance to this conception. Thus for most of Pakistan's history the military has had a predominant influence not only on security policies but also economic and political relations with India.

I.2 *Power Dynamics and the Development of Democracy, 2008-13.* Over the last five years during the tenure of the democratic coalition government led by the Pakistan People's Party important changes have occurred in the institutional structure of Pakistan's democracy. These changes have occurred in the face of intense contention for power amongst the main organs of the state: the Executive, the Parliament, the Military and the Judiciary.

The government perceived a threat of destabilization of democracy when the so called Memo gate affair emerged. In November 2011, the press made public a secret memo which suggested that a conspiracy had been hatched to seek the support of the US through a go between to prevent what the authors of the memo considered an imminent coup. Allegations were made that the then Ambassador of Pakistan to the US, Mr. Hussain Haqqani was implicated in this conspiracy which allegedly involved treasonable changes

within the military establishment. The Supreme Court set up a commission of enquiry and Ambassador Haqqani was removed from his post. During this crisis there was a faceoff between then Prime Minister Gillani and the military: he defiantly declared in Parliament on 22 December 2011, that the military's continuing role in politics was unacceptable<sup>2</sup>. These events signified that the contradictions of Pakistan's power structure had reached a point of inflection. The political system weathered the storm and the democratic government survived.

The "Memo Gate" affair was followed by tensions between the Judiciary and the Executive when the Supreme Court (SC) asserted its constitutional authority to convict the sitting Prime Minister, Mr. Gillani for contempt of court when he failed to implement the SC order to write a letter to the Swiss Court. The letter required rescinding the earlier Pakistan government decision to withdraw a graft case against Mr. Asif Zardari prior to his becoming President. Prime Minister Gillani was removed from office on the orders of the Supreme Court subsequent to his conviction in the contempt of court case.

During the same period another case was taken up by the Supreme Court in response to a petition made by Mr. Asghar Khan in which key politicians in the opposition two decades ago were found to have been bribed by military and intelligence officers to destabilize the government of the Pakistan Peoples Party (PPP). During the hearings of the case, it transpired that in the period 1990-1994 the then Chief of Army Staff Mirza Aslam Beg (allegedly at the behest of then President Ghulam Ishaq Khan), had initiated payments amounting to Rs.140 million through the ISI chief Asad Durrani and Javed Nasir to various politicians for creating the anti PPP alliance called Islami Jamhoori-Ittehad and bank rolling campaigns of opposition politicians<sup>3</sup>. This case (popularly called Mehran Gate) manifested the contention within the power structure and the attempt by democratic forces to bring the practice of governance in congruence with the Constitution.

The dialectic of power illustrated by the above mentioned cases signifies the attempt by democratic forces to achieve a new balance within the state structure whereby the judiciary

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<sup>2</sup> Akmal Hussain, Democracy at Bay, The Express Tribune, 23 January 2012.

<sup>3</sup> The Express Tribune, 9 November 2012.

maintains its independence, Executive excess is constrained by the limits of law and the military could be subordinated to elected civilian authority as stipulated in the Constitution.

During the period 2008 to 2013 apart from the struggle for democracy within the elite coalition, the elected government was able to achieve a broad consensus in the Legislature to pass key constitutional amendments and improve the institutional framework of centre-province financial relations. Through these institutional changes the formal democratic structure was strengthened and the possibility of a future coup d'état was significantly reduced. This was done by: (a) restoring the main features of the 1973 Constitution and thereby rectifying the distortions introduced in the democratic Constitution by successive military governments to facilitate the overthrow of elected civilian governments. Prime Ministerial authority was re-established and the power of the President to arbitrarily dismiss an elected government withdrawn. (b) Devolving greater power to the provincial governments. (c) The federal structure was further strengthened by the consensus achieved amongst the provinces in passing the National Finance Commission Award under which the share of the provinces as a whole in federal government revenues (the Divisible Pool) was increased, particularly the share of the relatively undeveloped province of Balochistan.

Like all formal rules, the Constitution is embedded in the normative structure and the core values of a society. Repeated military interventions in Pakistan can only be prevented if the principles of the Constitution become part of the norms and political culture of society so that the people are willing to defend the democratic constitution. An important step in Pakistan's journey to democracy was the Citizens' Movement led by the lawyers during 2007-08. This popular mass movement which was unprecedented in its intensity, sacrifices and geographic coverage, served to restore the judiciary. In so doing the citizens' movement helped establish a new norm in the political culture of Pakistan: the people of Pakistan are willing to preserve, protect and defend the Constitution. The independent judiciary after restoration drew its strength from the courage and consciousness signified by the Citizens' Movement. It was this strength that enabled the Supreme Court in the period 2008-13 to hold to account not only the incumbent government for corruption and malfeasance, but through suo moto action strove to protect the rights of citizens who had been abducted by various security agencies in Balochistan; publicly scrutinized interference

in political affairs by the behavior of the military in the Asghar Khan case; and sternly castigated elements in the military establishment who had stepped outside the law in Baluchistan<sup>4</sup>. Such dispensation of justice without fear or favour has played a significant role in the development of democracy in Pakistan.

A vital element in the struggle for democracy was the heroic initiative by former Prime Minister Benazir Bhutto of risking her life to launch a campaign against the dictatorship of General Musharraf. In sacrificing her life for democracy she joined the pantheon of martyrs whose memory inspires the resolve of the people to defend their freedom. Her sacrifice was the main driving force behind the staunch defence of democracy by the PPP led government in the power struggles during 2008-13.

As the people of Pakistan build democracy they face two major threats: (i) An economy that within its existing rent based structure extracts the fruits of labour of the people for the profligacy of the elites. The sense of economic deprivation of the people has been accentuated as GDP growth rates have declined sharply in the last five years compared to the preceding five years. Mass poverty has persisted, food insecurity has increased and inter personal as well as inter regional inequalities have accentuated. While a large proportion of the population is deprived of the minimum conditions of dignified life, fiscal pressures constrain the government from seriously addressing the problems of food insecurity, severe shortages of electricity and gas and lack of access of the majority of the people to quality education and health. (ii) The religious extremists pose a serious threat not only to democracy in Pakistan but to the security of the state itself. Armed militant groups have emerged as rival powers to that of the state within its territorial domain. They have captured significant swathes of Pakistan's territory in FATA (Federally Administered Tribal Areas), have in recent years launched deadly attacks on key military installations, civilian population centres and have assassinated important political leaders. Over the last five years the religious extremists have killed 30,000 civilians and 3,000 military personnel<sup>5</sup>. The

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<sup>4</sup> The Express Tribune, 19 October 2012.

<sup>5</sup> The Friday Times, Vol. XXV, No.2, February 22-28, 2013.

cost of terrorism to the economy has been estimated at USD 43 billion<sup>6</sup>. It is not surprising therefore that both the civilian and military leadership now consider terrorism to be the principal security threat for Pakistan<sup>7</sup>. Yet the response to them appears to be ambivalent: they are reported to have penetrated the security apparatus, captured sections of the ideological space through influence over parts of the media and have won allies amongst some of the right wing political parties. The way democratic forces address these challenges will shape the future of democracy in Pakistan as much as relations with India.

## II THE POLITICS AND ECONOMICS OF NORMALIZING INDIA PAKISTAN RELATIONS.

During the last decade the attempt by military as well as civilian administrations to engage in a peace process with India and seek economic cooperation has been driven by three considerations:

- (i) Normalizing economic relations with India is necessary for Pakistan's economic growth which would provide the material basis of maintaining the integrity of the nation and strengthening the state.
- (ii) Reducing tensions with India on the Eastern front is necessary to avoid a three front situation as Pakistan battles the enemy within, and secures the Western front with Afghanistan to prevent intrusions by hostile extremist elements into Pakistan.
- (iii) Unlike earlier decades, peace with India has become a popular aspiration and so pursuing the peace process has become politically advantageous.

II.1 *Normalizing Economic Relations with India: Musharraf's Initiative.* These strategic imperatives induced General Musharraf in July 2001 to reach out to India with a new

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<sup>6</sup> Pakistan Economic Survey 2009-2010, Government of Pakistan, Finance Division, Economic Adviser's Wing, pg 7. Islamabad, 2010.

<sup>7</sup> (i) General Kayani in his Independence Day Address (14<sup>th</sup> August 2012) at the Pakistan Military Academy, Kakul, declared that the war against "extremism and terrorism.....is our war and a just war". He went on to say that "the war against extremism and terrorism is not only the Army's war but that of the whole nation. We as a nation must stand united against this threat."

(ii) In a joint statement Prime Minister Gillani and Prime Minister Manmohan Singh agreed that terrorism is the main threat and both resolved to fight terrorism. Reported in Hindustan Times on 16<sup>th</sup> July 2009.

approach based on a number of key innovations. First the earlier demand of a plebiscite as a precondition for normalizing economic relations with India was replaced by the idea of a composite dialogue. In this context economic relations were to be discussed alongside the resolution of outstanding political and territorial disputes including that of Kashmir. Second, given the different temporal scales of the two tracks, it was realized that trade relations would yield results sooner than talks on the Kashmir dispute due to its intractable nature. Indeed it was thought that improved economic relations and the resultant peace dividend would not only create stakeholders in both countries for sustaining the peace process, but would also build confidence and trust that would facilitate the political dispute resolution process. Third, there was a tendency to set aside rigid positions on the Kashmir issue conceived earlier as essentially a bilateral dispute. Instead a flexible approach was adopted and there was an attempt to seek a resolution of the dispute that was acceptable to India, Pakistan as well as the people of Kashmir<sup>8</sup>.

General Musharraf's policy initially produced encouraging results with a significant increase in trade volumes and increased visa permits that enabled a larger number of travelers from Pakistan and India respectively to visit each other's countries. However the institutional features of India Pakistan economic relations constrained a sustained rapid increase in trade volumes. These institutional factors included tariff as well as non tariff barriers and the restriction of trade to a limited number of items in the so called positive list. These constraints on trade persisted even after the historic Islamabad Declaration at the SAARC Summit in 2004 when the idea of establishing a South Asia Free Trade Area (SAFTA) was agreed to in principle. In spite of the optimism it generated, SAFTA was effectively stalled near the end of President Musharraf's government. Fears began to circulate that the Pakistani economy would be swamped by cheap Indian goods, that it would constitute a betrayal of the sacrifices of the Kashmiri people and would undermine the very identity of the national security state. In the face of this political campaign, Prime Minister Shaukat Aziz reversed the new approach and returned to the original position when he publicly declared that improvement in economic relations was contingent upon progress in the resolution of

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<sup>8</sup> Akmal Hussain, *The Challenges and Drivers of Regionalism in South Asia: The India-Pakistan Peace Process*, chapter in, Rafiq Dossani, Daniel Sneider, Vikram Sood (ed), *Does South Asia Exist?: Prospects of Regional Integration*, Stanford University, Shorenstein APARC, August 2010.

the Kashmir dispute<sup>9</sup>. The view that trade restrictions and an adversarial relationship with India was necessary to maintain a large share of the budget for the military, apparently prevailed. The alternative view that improved economic relations with India would be a major stimulus to economic growth and would thereby make a large budget for the military politically and economically feasible, was for the moment set aside.

II.2 *Normalizing Economic Relations with India: Initiatives by the Democratic government.* After the elections of February 2008 the coalition government led by the PPP engaged with India once again on the basis of the composite dialogue approach that had been given up near the end of the previous government's tenure as President Musharraf's political position within the Establishment had weakened. As the democratic government sought to win space from the military within the power structure, Foreign Minister Shah Mahmood Qureshi, called for a "comprehensive settlement" with India. At the same time President Zardari declared his government's intention to accelerate the peace process and focus on economic cooperation<sup>10</sup>. It was clear that the elected civilian government saw normalization of relations with India as integral to the process of sustaining democracy as well as development. Just when Pakistan's foreign minister was in India to take the peace process forward it received a major setback with the monstrous Mumbai massacre by Pakistan based militants. It was after several months that the dialogue between the two sides could be restarted in February 2010, when the foreign secretaries of the two countries met in New Delhi.

Pakistan's government even as it faced multiple pressures sought to normalize economic relations with India. An important manifestation of this attempt was the cabinet decision to, in principle, grant MFN status to India by the end of 2012. This was to enable a free flow of goods and capital between the two countries just as in the case of other members of the WTO. Both countries made major concessions with Pakistan undertaking (after the formal granting of the MFN status) to replace the existing "positive list" with a relatively short "negative list" as in the case of normal trade relations between countries. At the same time,

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<sup>9</sup> Ibid.

<sup>10</sup> Ibid.

India undertook to reduce its list of impermissible imports from Pakistan by 30 percent and lower the duty rate of imports from Pakistan to 5 percent by April 2013<sup>11</sup>.

However, a detailed comparison of the tariff structures of the two countries indicated that there were certain anomalies and asymmetries in the tariff structures between the two countries which placed Pakistan at a disadvantage, and which had to be addressed during detailed negotiations before the MFN status and associated liberalization of the trade regime could be implemented. Some of the asymmetries that were pointed out<sup>12</sup> include: (a) The number of items in India's sensitive list of imports from Pakistan was 1,753 which was significantly more than the number of items 1,577 in Pakistan's sensitive list of imports from India. Furthermore, the items in this list were weighted towards agriculture and textiles even though in some of the sub sectors of this commodity group Pakistan had a comparative advantage<sup>13</sup>. (b) Import duties on rice at 70 percent and 100 percent on wheat were considered prohibitive by Pakistani exporters. Such distortions of the relative prices of these items constituted indirect obstacles to free trade. They were reinforced by the huge subsidies on agriculture inputs provided by the Indian Central as well as state governments. These amounted to 5.2 percent of GDP, compared to 1 percent in the Pakistani case. (c) It is now well established that non tariff barriers even in the absence of formal tariffs can be a major constraint to trade liberalization. Non tariff barriers such as lack of harmonization of customs procedures, certification procedures for quality standards of traded goods, institutional constraints to opening letters of credit and transfer of funds across the border are legion in both countries. While a mechanism is in operation to address these barriers to trade, the process is not time bound. Yet at the level of the individual exporter non tariff barriers are seen to be as important as tariff structures. This was a significant factor in building up pressure to delay the implementation of the MFN decision.

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<sup>11</sup> The Beaconhouse National University's ongoing study was reported by one of the authors, Shahid Kardar, in his article in the Daily Dawn: Shahid Kardar, MFN Status for India Now, Dawn, 19 February 2013.

<sup>12</sup> Ibid.

<sup>13</sup> Ibid.

Bureaucratic mismanagement of the transition process to a free trade regime was manifested in the failure to address expeditiously the anomalies and asymmetries in the respective sensitive lists and tariff structures and non tariff barriers prevailing in the two countries. This led to delays in the implementation of the decision by the two governments at the highest levels to move towards free trade between the two countries. As the implementation of Pakistan's cabinet decision to grant MFN status was delayed beyond the December 2012 deadline, there was an unfortunate incident on the Line of Control in Kashmir in early January 2013, which enhanced tensions. Once again, political dynamics prevented an important initiative for normalization of economic relations from coming to fruition: With the elections round the corner the government of Pakistan on 25<sup>th</sup> February 2013, announced that the decision to grant MFN status to India would be left to the next government<sup>14</sup>.

II.3 *The Logic of Normalizing Trade Relations.* In spite of the vicissitudes of India Pakistan relations there is an undeniable logic to persist with efforts to normalize economic relations. Free trade with India would place Pakistan on a new high growth trajectory not only through gains from trade but also through increased investment by Indian entrepreneurs. Moreover, imports of relatively cheaper capital and intermediate goods from India could help reduce capital output ratios in Pakistan and thereby achieve a higher GDP growth for given levels of investment. At the same time the distribution of real income in Pakistan could be improved through the reduction in food inflation that would become possible through stabilization of food prices associated with import of food products during seasonal shortages when surpluses are available on the other side of the border. At the same time, increased tourism, trade in services and retail sectors would increase employment elasticities and improve income distribution. Thus normalizing economic relations with India could enable Pakistan to achieve a higher and more equitable GDP growth that could play a key role in the struggle against extremism.

If the institutional mechanisms could be created for rectifying the current anomalies and asymmetries in the tariff structures and substantially reduce non tariff barriers within a time bound framework, both countries can achieve immense economic gains. The stimulation of

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<sup>14</sup> Pakistan Today, 26 February 2013.

equitable GDP growth resulting from trade and investment could create large constituencies in both Pakistan and India to counter their respective extremist groups that seek confrontation rather than cooperation. In Pakistan a shift from an adversarial to a mutually beneficial cooperative relationship with India would enable a shift from a national security state paradigm to the paradigm of a state that is secured through the economic welfare of its citizens. This would help to strengthen and deepen democracy.

Building a sustainable democracy requires building a pluralistic society where diverse communities can co-exist and prosper together and where multiple identities can be maintained by each individual within a variety of relations with other individuals<sup>15</sup>. Essential to deepening democracies in Pakistan and India is the opening up of new cultural spaces within which people of the two countries can encounter the 'other' as a vital fertilizing presence in the growth of the self. Such an engagement could help in discovering within the cultural diversity of each country, the shared wellsprings of human civilization. Thus national integrity would be strengthened not by the denial of cultural diversity but by creating forms of social existence in which such diversity can flourish.

II.4 *Towards a new Paradigm of Security.* Within the modes of governance in India and Pakistan, national security has been conceived in terms of building a military apparatus designed for mass annihilation of each other's citizens. This has led to a policy paradigm within which priority in public resource allocation is given to building the capacity to destroy an imagined adversary across the border rather than creating the capacity for improved conditions of life within the country. India is the world's largest importer of arms and Pakistan, not far behind, is the 10<sup>th</sup> largest<sup>16</sup>. Thus Pakistan and India have the capability for mass destruction through a conventional or a nuclear war. Even in a limited nuclear exchange, over a hundred million people could be killed with many hundreds of millions more dying from radiation related illnesses<sup>17</sup>. Yet these two countries together contain 40

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<sup>15</sup> Amartya Sen, *Identity and Violence: The Illusion of Destiny*, Penguin Books, England, 2006. Pages 1 to 5.

<sup>16</sup> Akmal Hussain, *Challenges and Drivers of Regionalism in South Asia: The India-Pakistan Peace Process*, op.cit. Page 4.

<sup>17</sup> Newsweek June 8, 1998.

percent of the population of the world that is living in poverty<sup>18</sup>. At the same time, 37 percent of the population of Pakistan and India is living below the poverty line<sup>19</sup>, over 40 percent of the children are malnourished and only 21 to 31 percent of their respective populations have 7 to 12 years of schooling<sup>20</sup>.

While the governments of the two countries have been pursuing national security through war making capacity, the citizens of these adversarial states share the aspiration of human security: from extremist violence, hunger, loss of livelihoods, social injustice and the ravages of floods and droughts associated with climate change. This incongruence between the preoccupations of the state and those of civil society needs to be addressed if the social contract that underlies the functioning of the state is to be maintained<sup>21</sup>. The time has come for Pakistan and India to change state perceptions of each other as adversaries and recognize their economic, social and ecological interdependence. A shift is required in the policy paradigm whereby the policies and resource allocation priorities of democratic governments could aim to create the material conditions for actualizing the human potential of their people. Only then can these two states achieve development, sustainable democracy and meaningful national security.

The rise of India on the economic and technological plane may be associated with a tendency to translate economic strength into military power as Western states have tended to do over the last two centuries. Yet the new world in the 21<sup>st</sup> century is different from the past in that there is far greater inter dependence in facing global challenges of economic instability, poverty, economic inequality and crucially, the threat to the life support systems

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<sup>18</sup> The Tendulkar Committee estimate of the percentage of the Indian population living below the poverty line was 37 percent, while for Pakistan the estimate by Haroon Jamal (SPDC, 2011) was 36.6 percent. On the basis of these figures applied to the figures on world population, and the populations of Pakistan and India respectively in 2012, I have estimated the total number of poor in India at 451 million and for Pakistan at 70 million. Thus the combined poor population of India and Pakistan comes to 521 million which is 40 percent of the world's population (1,290 million).

<sup>19</sup> The incidence of poverty in India is estimated by the Tendulkar Committee at 37 percent. The poverty figure for Pakistan in 2010 has been estimated by Haroon Jamal (SPDC, 2011) at 36.6 percent.

<sup>20</sup> The figure on education is taken from Human Development Report 2011, Statistical Tables, UNDP, Palgrave Macmillan, New York, NY, 2011.

<sup>21</sup> Akmal Hussain, Challenges and Drivers of Regionalism in South Asia: The India-Pakistan Peace Process, op.cit. Page 6.

of the planet. In this new world, the influence of an emerging power will be determined not by the magnitude of its capability of destruction but by its contribution to enhancing life of the human community facing critical challenges to its prosperity and very survival. Therefore it is not the military strength of a state that will be the emblem of status but its contribution to meeting the global challenges of peace, poverty and environmental degradation<sup>22</sup>. Countries of the South Asian region share deep rooted though dormant traditions of harmony with nature, values of sharing and caring and the sensibility of connecting with the 'other' as a mode of actualizing the self<sup>23</sup>. Thus India and Pakistan are culturally equipped to tap into these shared well springs of civilization to help build a better world together.

### III. THE NATURE OF THE CURRENT ECONOMIC CRISIS: 2008-11

III.1 *Investment and Growth: Persisting Recession.* Pakistan's GDP growth rate has declined sharply from 6.8 percent in 2006-07 to 1.2 percent in 2008-09 which indicates a negative per capita GDP growth in that year. Over the period 2007-08 to 2010-11 the average annual GDP growth has been about half the historical trend rate of 5.5 percent<sup>24</sup>.

Growth in agriculture during this period fell substantially on average and was subject to sharp fluctuations on a year to year basis, reflecting the increased variability in the quantum and location of rain fall associated with global warming. It fell from 4.1 percent in 2006-07 to 1 percent in 2007-08, rose again to 4 percent in the next year but declined sharply in the next two years<sup>25</sup>.

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<sup>22</sup> Akmal Hussain, A Vision for South Asia, in Imtiaz Alam (ed), Whither South Asia? South Asian Policy Analysis Network (SAPANA), Free Media Association, Lahore 2006. Page 56.

<sup>23</sup> For a more detailed discussion of this issue, see: Chapter 1 in, Akmal Hussain and Muchkund Dubey (ed), Democracy, Sustainable Development and Peace: New Perspectives on South Asia, Oxford University Press, New Delhi (Forthcoming).

<sup>24</sup> Akmal Hussain, Pakistan's Economic Crisis: Structure and Growth in Historical Perspective, paper presented at the ISAS Workshop on: Political and Economic Challenges in Pakistan, National University of Singapore, 28 April 2011. Table 1.

<sup>25</sup> Ibid. Page 8.

Growth of the large scale manufacturing sector has also declined sharply from 8.3 percent in 2006-07 to a negative growth of -3.7 percent in 2008-09. In the following two years although growth became positive, this sector was still in the grip of stagnation<sup>26</sup>. Fluctuations in the growth rate of the manufacturing sector suggest that changes in the volume of output, was the result of variations in the utilization of productive capacity rather than fixed investment. Indeed medium term growth of the manufacturing sector is constrained by structural factors such as the collapse of profitability of the highly leveraged and dynamic industrial units which face the double squeeze of sharply increased interest rates on the one hand and on the other, a sharp depreciation in the exchange rate leading to high rupee prices of imported inputs. Consequently, manufacturing investment fell sharply thereby constraining medium term growth. Fixed investment in the manufacturing sector as a percentage of total fixed investment declined sharply from 22 percent to 16.2 percent over the period 2005 to 2010. The contribution of this sector to employment generation in the country has also declined from 13.6 percent in 2005 to 13 percent in 2010. This indicates intensified unemployment stress on a society where 62 percent of the population is below the age of 25<sup>27</sup>.

A number of structural factors constrain investment and GDP growth. These include: (a) an institutional framework that restricts competition, lack of access over factor and product markets to a large proportion of the population and which lacks incentives for efficiency, innovation and hard work. (b) Lower water availability per acre due to falling irrigation efficiencies. This has occurred at a time when the water requirement per acre has gone up due to soil depletion and the need to leech saline soils before planting. (c) Inadequate infrastructure particularly electricity and gas generation, transport and communications and lack of trained personnel due to poor quality and coverage of education and vocational training facilities. (d) A severe shortage of electricity and an underutilization of even the low energy production capacity, due to the problem of circular debt arising out of nonpayment of government dues to independent power producers. (e) The ongoing war against militant extremism which is a major constraint to private investment, both domestic and foreign.

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<sup>26</sup> Ibid.

<sup>27</sup> Ibid.

Of these constraints to investment and growth, the most immediate are the power shortage and terrorism. The annual increase in electricity and gas consumption in the industrial sector has declined from about 17 percent in 2004-2005 to minus 7 percent in 2008-2009. The deficit between electricity supply and demand reached 5000 megawatts by 2009-2010. It is estimated that the effect of low energy supply amounts to the equivalent of 2 to 2.5 percent of GDP.<sup>28</sup>

Pakistan has been mauled by militant extremism which has intensified during the last decade. The militants have captured significant swathes of Pakistan's territory which in earlier years had extended beyond the FATA region into some of the settled areas. Pakistan's armed forces mounted successful military operations against the insurgents and pushed them back to regain control over the settled areas. However, substantial areas in Waziristan are still under the control of the Al-Qaeda Taliban combine. In the last few years they have mounted a series of gun and suicide bombing attacks against major political leaders and also against a series of key military and civilian institutions. This intensified warfare within the country has resulted in large human and material losses, and created a sense of insecurity amongst the people. This has been a major factor in the decline in domestic and foreign investment and also in the process of production and sale. The National Crisis Management Cell estimates that between 2002 and April 2010 there were 8,141 incidents of terrorism in Pakistan resulting in 8,875 deaths of both civilians and law enforcement personnel and injuries to another 20,675 people. The estimated total cost of terrorism to the economy from 2005 to 2010 is US\$ 43 billion<sup>29</sup>.

III.2 *Inflation, Poverty and Inequality.* The inflation rate continues to remain high (14 percent). This is in spite of the government's contractionary policy of high interest rates (over 14 percent) and a sharp reduction in development expenditure (from 7 percent of GDP in the 1980's to about 1 percent of GDP last year). The food inflation rate at 18 percent is higher than the average inflation rate and this has further intensified the pressure on the poor. With GDP growth at a historic low and food inflation rate at a historic high, it is not

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<sup>28</sup> Pakistan Economic Survey 2009-2010, Government of Pakistan, Finance Division, Economic Adviser's Wing, Islamabad, 2010.

<sup>29</sup> Pakistan Economic Survey 2009-2010, Government of Pakistan, Finance Division, Economic Adviser's Wing, pg 7. Islamabad, 2010.

surprising that the percentage of population living below the poverty line has increased from 29.9 percent in 2004-05 to 36.6 percent in 2010-11<sup>30</sup>. This means that the number of people living below the poverty line has increased from 46 million to 60 million over the period. The percentage of food insecure population is even higher at 48.6 percent or about 80 million people. High levels of poverty and food insecurity together with twelve hours of power outages daily, add to the misery of the people.

The stress on society and the polity is intensified by the increasing inter-personal and inter-regional income inequality. The growth in income during the period 2001-08 was highly unequal with respect to the rich and poor. The average income growth for the top income quintile of the population is 2.36 times greater than for the lowest quintile. This inequality of interpersonal income distribution while being rooted in a highly skewed income distribution of productive assets is accentuated by the differential impact of high food inflation with respect to the rich and poor (this is because food expenditure constitutes a larger proportion of the income of the poor compared to the rich). The distribution of disposable income is made even more unequal by the fact that over 70 percent of government revenue comes from indirect taxes, which place a relatively greater burden on the low income groups compared to the high income groups.

The adverse social impact of inter-personal income inequality is reinforced by the political impact of increasing inter-regional economic inequality in Pakistan. Over the period 2001-02 to 2009-10, in the relatively better off provinces like Punjab and Sindh the employment growth over the period (2.7 percent and 2.2 percent respectively) is over twice as high as in the more backward provinces of Balochistan and Khyber-Pakhtunkhwa, (1.1 percent and 1.2 percent respectively)<sup>31</sup>.

The inter-regional economic inequality reflected in the provincial employment generation figures is also indicated by the provincial data on food insecurity. In the more backward regions of Balochistan and Khyber Pakhtunkhwa the food insecure population (61.2 percent

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<sup>30</sup> Haroon Jamal, Pakistan Poverty Statistics: Estimates for 2011, Social Policy and Development Centre, Karachi, Research Report No. 84, October 2012.

<sup>31</sup> Akmal Hussain, Pakistan's Economic Crisis: Structure and Growth in Historical Perspective, op.cit. Page 23, Table 8.

and 56.2 percent respectively) is much higher than in the more developed provinces of Punjab (38.5 percent and Sindh 44.3 percent respectively)<sup>32</sup>. In the Federally Administered Tribal Regions (FATA) which is the epicentre of militant extremism in Pakistan, food insecure population is highest at 67.7 percent.

III.3 *Debt Burden and Financial Fragility.* Pakistan's debt stock has risen sharply over the last five years from 2005 to 2009 and has now reached a level that suggests fragility in the fiscal structure. The external debt has increased from USD 35.7 billion in 2005 to USD 50.8 billion in 2009. Domestic debt has also increased from Rs. 2178 billion to Rs. 3275 billion over the same period. As a consequence total debt servicing (domestic plus foreign debt) has increased from 32.5 percent of federal government revenue to 38.6 percent during the period 2005 to 2009<sup>33</sup>. Since subsidies and defence expenditure could not be decreased, the fiscal situation has now reached a point where the entire government revenue goes into three items alone: debt servicing, defence, and subsidies. Consequently the entire operating expenses of the government as well as development expenditure have to be based on borrowing. This of course means a further increase in the stock of debt and the burden of debt servicing in the years ahead. This is an unsustainable fiscal situation, unless the stock of debt is substantially retired and the budget deficit reduced.

The improvement in the current account of the balance of payments in the last two years is due to a substantial increase in workers' remittances and a sharp reduction in imports. The most important factor in the decrease of import expenditures is a 30 percent decline in the import of machinery and to a lesser extent a slowdown in mobile phone and telecommunications imports, which are consistent with the decline in investment indicated in the previous sections<sup>34</sup>. Thus, the improvement in the current account of the balance of payments has occurred at the expense of future GDP growth. Export trends are such that the export earnings are unlikely to finance the increased import expenditures, when GDP growth picks up in the future. The WTO figures on manufactured exports show that Pakistan suffered a significant loss in market share in world exports. During the period 2005 to 2008

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<sup>32</sup> Ibid. Page 21, Table 6 (b).

<sup>33</sup> Ibid. Pages 11-12.

<sup>34</sup> Ibid. Page 12.

there was 40 percent expansion in world manufactured exports. During this period, while China's manufactured exports grew by 75 percent and those of India and Bangladesh grew by over 50 percent, Pakistan's exports in this sector grew by only 14 percent<sup>35</sup>. Consequently, Pakistan's market share, already at a low level, fell further. A major factor in this reduction of market share was the fact that Pakistan's textile industry is still heavily dependent on the export of low value added goods whose demand in the international market is growing much more slowly than demand for high value added textiles such as garments and clothing. Another factor is the lack of international competitiveness which has led to loss of market share in textiles and clothing to China, India, Turkey and Vietnam. The domestic security situation and power shortages have further exacerbated the problem.<sup>36</sup>

The Strategic Trade Policy Framework proposes a number of initiatives aimed at improving the international competitiveness of Pakistan's textile industry which if implemented could significantly accelerate export growth of this sector. The proposed initiatives include: (i) Reduction of anti export bias by withdrawing protection of inefficient industries, (ii) Minimization of taxation at the investment stage, and (iii) Zero rating of customs duties on key inputs to textiles and clothing exports. Apart from this the Textile Policy 2009-14 proposes specific initiatives for the development of infrastructure facilities, skills development and modernization of machinery and technology. The Textile Policy proposes that these initiatives should be financed through the establishment of a Textile Investment Support Fund (TISF). Support would also be given to undertake joint ventures for the expansion and modernization of this sector. Perhaps the most important policy initiative that could accelerate the growth of the textile industry would be to achieve free trade agreements with India and China which could aim at removing both tariff as well as non-tariff barriers between Pakistan and these new potential trading partners.

Since the financing of the balance of payments deficit in the last few years has been done through external flows, this has added considerably to short term debt obligations and worsened the foreign asset and liabilities position. Pakistan's external debt and liabilities

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<sup>35</sup> Third Annual Report 2010, State of the Economy: Pulling Back from the Abyss, Institute of Public Policy, Beaconhouse National University, Lahore. Page 32.

<sup>36</sup> Akmal Hussain, Pakistan's Economic Crisis: Structure and Growth in Historical Perspective, op.cit. Page 12.

have increased from USD 35.7 billion in 2005 -2006 to USD 50.8 billion in 2008-2009 and are estimated to be about USD 57 billion in 2009-2010<sup>37</sup>. This huge debt and liabilities burden increased sharply in the next year (2011- 2012) as large net payments obligations to the IMF had to be met.

The analysis in this section shows that even at very low GDP growth rates, fiscal and balance of payments pressures have mounted rapidly. Higher GDP growth in the years ahead, if achieved, will be difficult to sustain unless the structural constraints to increasing government revenues and foreign exchange earnings are overcome. As discussed in the preceding section-I, normalizing of economic relations with India within a level playing field for exporters and investors on both sides would enable Pakistan to accelerate its export growth as well as improve its capital account through investment from India. This would significantly improve the balance of payments. The gains from trade alone could increase the GDP growth and when combined with investment from India would have a substantial positive impact on the overall GDP growth. Ongoing research at the Beaconhouse National University suggests that trade liberalization with India, the implementation of the SAFTA agreement with respect to tariff reductions and structural reforms in Pakistan could together increase the GDP growth rate in the medium term from 1.5 percentage points to as much as 4 percentage points<sup>38</sup>.

#### **IV. CLIMATE CHANGE AND THE IMPERATIVE OF PAKISTAN-INDIA COOPERATION**

Given the highly integrated ecology of South Asia, regional cooperation is necessary to formulate and implement policy measures for addressing the socio economic impact of climate change. Let us briefly examine the nature of the impact of climate change on the economy and society of this region and its implications for India-Pakistan cooperation.

**IV.1 Vulnerability to Climate Change Impact.** The available evidence shows that climate change is already having a significant impact on the economies and societies of this region. South Asia with its delicately balanced ecology, its heavy reliance on monsoons, its critical

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<sup>37</sup> Ibid. Page 11.

<sup>38</sup> Shahid Kardar, op.cit.

dependence on agriculture and persistent mass poverty, make it one of the most vulnerable regions in the world to climate change. Increased variability in the magnitude and timing of rain fall during the monsoons could increase the instability of agriculture production and add to the burden of the poor<sup>39</sup>. The long and densely populated coastline with low lying islands, such as the Maldives, make the region vulnerable to sea level rise associated with global warming. The Himalayas containing the region's glaciers, source of its rivers, and the key to the region's climate and economy, are sensitive to temperature increases. Srivastava provides evidence to show that some Himalayan glaciers are melting faster than the global average<sup>40</sup>. This could have a critical impact on the stability of water supplies and thereby on the economy and society of the region.

IV.2 *Water Scarcity and the Need for Cooperation.* Pakistan has shifted from a water surplus to a water scarce country, as annual flow of rivers in the Indus Basin has declined from 119 million acre feet in 1960 to 102 million acre feet by 2011. In terms of per capita annual water availability in the Indus Basin there is a decline from 5,121 cubic meters in 1962 to 1,396 cubic meters in 2011. This indicates that Pakistan already faces water scarcity, since the minimum per capita annual requirement has been estimated at 1,700 cubic meters per capita. This will have major implications for Pakistan's economy, society and state. Effective management of the crisis requires urgent mitigation and adaptation measures in close cooperation between Pakistan's provinces of Pakhtunkhwa, Punjab and Sindh on the one hand and between Pakistan and India on the other<sup>41</sup>.

The declining river flows and increased seasonal fluctuations in these flows create the imperative for Pakistan to improve its water management and increase water use efficiency. At the same time collaborative efforts by India and Pakistan for forestation and management of the water sheds could slow down the increased sedimentation of rivers which reduces the life of dams downriver. Reforestation in the water shed could also

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<sup>39</sup> Akmal Hussain, Climate Change and Cooperation, The Express Tribune, 22 August 2011.

<sup>40</sup> Leena Srivastava, The Environmental Challenges in South Asia: Regional Cooperation for Adaptation Strategies, chapter in, Akmal Hussain and Muchkund Dubey (ed), Democracy, Sustainable Development and Peace: New Perspectives on South Asia, Oxford University Press, New Delhi (Forthcoming).

<sup>41</sup> Akmal Hussain, Rivers, People, States, The Express Tribune, 24 December 2012.

prevent devastating flash floods downstream during heavy downpours in the catchment areas.

Another significant impact of climate change is that the monsoons have shifted from the eastern part to the western part of what is Pakistan today while the timing is delayed compared to the past. At the same time there is reduced glacial melt in August a month in which glacial melt historically was high. The increased variability in the timing and location of monsoons as well as the change in the temporal pattern of glacial melt will further accentuate the observed shortages of water in the Indus Basin during planting seasons. It is therefore crucial for the people and government of Pakistan to realize the gravity of the water scarcity problem. This has urgent implications for policy and public action to improve the irrigation efficiency as well as the water use efficiency<sup>42</sup>.

IV.3 *Climate Change, Extreme Climatic Events and Crop Yield Decline.* The Inter-Governmental Panel of Climate Change (IPCC)<sup>43</sup> had predicted that global warming would increase the frequency and intensity of extreme climatic events. The study by Cruz et. al.<sup>44</sup> provides data to show that this is indeed happening in South Asia. For example, the frequency of intense rainfall events has increased, causing floods and landslides in Pakistan, Bangladesh, Nepal, Northeast India and Sri Lanka, during the last decade. Consecutive droughts in 1999 and 2000, in Pakistan and Northwest India adversely affected agriculture growth and the drought of 2002 in Orissa (India), caused crop failures which affected 11 million people<sup>45</sup>.

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<sup>42</sup> Ibid.

<sup>43</sup> Climate Change 2007, Impacts, Adaptation and Vulnerability, Working Group II Contribution to the Fourth Assessment Report of the Intergovernmental Panel on Climate Change, Cambridge University Press, Cambridge, 2007. Page 16.

<sup>44</sup> Cruz RV, Harasawa H, Lal M, Wu S, Anokhin Y, Punsalmaa B, Honda Y, Jafari M, Li C, Huu N (2007) **Asia. Climate change, 2007, impacts, adaptation and vulnerability.** In: Parry ML, Canziani OF, Palutikof JP et al (eds) Contribution of Working Group II to the Fourth Assessment Report of the Intergovernmental Panel on Climate Change, Cambridge University Press, Cambridge, pp 469–506. Cited in Srivastava, op.cit.

<sup>45</sup> Akmal Hussain, Climate Change and Cooperation, op.cit.

According to the IPCC the increase in temperatures in South Asia in the decades ahead are likely to be above the global average. The IPCC estimates that given the sensitivity of food grain seeds to heat, even a 2.5°C increase in average summer temperatures could cause a reduction of 30% in the yield per acre of food grain. The study by Giorgi and Bi<sup>46</sup> suggests that higher temperatures will lead to increased year to year variability of monsoon rains. This phenomenon which is already occurring when combined with the adverse effects of temperature on heat sensitive food grains could have a critical impact on agriculture production and accentuate the problem of food security in South Asia.

IV.4 *Climate Change and Population Dislocation.* As local communities across South Asia face a threat to their life and livelihoods due to climate change, large scale dislocation and migration of populations can be expected. Increased flooding and prolonged droughts could displace communities inhabiting the riverine plains; sea level rise would change the salinity profile of coastal areas, degrade large areas of fertile land and consequently displace the local communities which are dependent for their livelihoods on coastal plains<sup>47</sup>. Climate change could force 125 million people to leave their habitat and migrate to other places in South Asia<sup>48</sup>.

IV.5 *The Imperative of Cooperation between Countries facing a Common Challenge.* Managing population dislocation, natural disasters, instability of water supply and food shortages resulting from climate change, will require a high degree of inter-state cooperation in South Asia. The integrated ecology of the region, the mountains, rivers, forests and top soils constitute the basis of sustaining its economy and social life. The people of this region share this life support system. They also share the risks posed to it by climate change. Therefore, we the peoples of South Asia and our respective states must cooperate and bring to bear our shared humanity and innovativeness to face the challenge

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<sup>46</sup> F. Giorgi, Bi X (2005) *Regional changes in surface climate interannual variability for the 21st century from ensembles of global model simulations*. *Geophys Res Lett* 32:L13701. doi:10.1029/2005GL023002, cited in, Leena Srivastava, *The Environmental Challenges in South Asia: Regional Cooperation for Adaptation Strategies*, chapter in, Akmal Hussain and Muchkund Dubey (ed), *Democracy, Sustainable Development and Peace: New Perspectives on South Asia*, Oxford University Press, New Delhi (Forthcoming).

<sup>47</sup> Falkenmark and Widstrand (1992) cited in, Leena Srivastava, *The Environmental Challenges in South Asia: Regional Cooperation for Adaptation Strategies*, op.cit.

<sup>48</sup> Ibid.

of climate change. Cooperation not conflict is the key to building a better future for the people of South Asia.

## **CONCLUSION**

In this paper we have examined the dynamics of power that underlie the ongoing struggle to sustain democracy in Pakistan as well as the attempts to chart a new course of Pakistan India relations. Normalizing economic relations between the two countries could play an important role in stimulating economic growth. At the same time cooperative rather than adversarial relations between Pakistan and India would strengthen democracy in each country by providing economic security to citizens, building pluralistic societies and nurturing a sensibility which is enriched through the diversity of culture. There is therefore a need for shifting the policy paradigm in Pakistan and India, from an adversarial to a cooperative one. Within this new paradigm national security could be pursued not by enlarging the military apparatus of destruction but the construction of an economy and society for human security.

The structural constraints to GDP growth in Pakistan were analyzed, to conclude that free trade and investment between Pakistan and India would help to release some of these structural constraints.

Finally, the challenges posed by climate change which could have major adverse effects on the economies and societies of the two countries were discussed. In this context, regional cooperation for managing climate change and the associated water crisis is an imperative of preserving the very fabric of society, economy and state of both Pakistan and India.

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