HUMAN DEVELOPMENT IN SOUTH ASIA 2001

Globalisation and Human Development

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ABBREVIATIONS

AIDS	acquired immune deficiency syndrome
ANZCERTA	Australia New Zealand Closer Economic Relations Trade Agreement
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of South-East Asian Nations
BIMSTEC	Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation
BWI	Bretton Woods Institutions
CDR	credit deposit ratio
CD-ROM	compact disk with read-only memory
ECO	Economic Cooperation Organisation
EEC	European Economic Community
EPZ	export processing zone
ESAF	Enhanced Structural Adjustment Facility
EU	European Union
FDI	foreign direct investment
FTA	free trade agreement
FTAA	Free Trade Association of the Americas
G-8	Group of Industrialised Countries
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GEP	Group of Eminent Persons
GNP	Gross National Product
ICT	information and communication technology
IDA	International Development Association
IDS	infrastructure development surcharge
IGG	Inter-Governmental Group
IMF	International Monetary Fund
IOR-ARC	Indian Ocean Rim Association for Regional Cooperation
IPA	intergrated programme of action
IPR	intellectual property rights
IT	information technology
MERCOUSOR	Southern Cone Common Market (Argentina, Brazil, Paraguay, Uruguay)
MFA	Multi-Fibre Arrangement
MFN	most favoured nation
MNCs	Multinational Corporations
NAFTA	North American Free Trade Area
NTBs	non-tariff barriers
NGO	non governmental organisation
ODA	official development assistance
OECD	Organisation for Economic Cooperation and Development
PPP	purchasing power parity
PRGF	Poverty Reduction and Growth Facility
PRSP	Poverty Reduction Strategy Paper
PPM	process and production methods
R&D	research and development
RTAs	regional trading arrangements
SAARC	South Asian Association for Regional Cooperation
SADF	South Asia Development Fund
SAP	structural adjustment program
SAPTA	SAARC Preferential Trading Arrangement
SARC	South Asian Regional Cooperation
SBW	special bonded warehouse
SDT	special and differential treatment
TRIMS	Trade Related Investment Measures
TRIPS	Trade Related Intellectual Property Rights
UN	United Nations
UNICEF	United Nations Children Fund
UNDP	United Nations Development Programme
US	United States of America
VAT	value added tax
WTO	World Trade Organization

Foreword

In May 1998 at a brain-storming session of the UNDP, Mahbub ul Haq presented some ‘random thoughts’ on globalisation. His arguments were that globalisation was an irreversible force, and that developing countries must learn to manage it in their best interests or they would get drowned by its cross currents. He argued that to gain from globalisation developing countries must accelerate their human development, improve governance, and invest in infrastructure. If globalisation was superimposed on a poorly-educated and poorly-trained labour force with poor systems of governance and infrastructure, it would not lead to growth nor reduce poverty. Globalisation also had to be better managed by the institutions of global governance if these institutions were to achieve their professed goals of sustainable development and poverty reduction in developing countries. These ideas of Mahbub ul Haq guided the analysis of this year’s report.

Our purpose in this report has been to assess the nature and process of globalisation on economic growth and human development in South Asia. Our efforts, however, have been somewhat limited by the lack of availability of up to date data. The most current data available is only up to 1999. The speed with which the globalisation process is moving, two to three years’ gap is a significant one.

The report analyses the experience of the South Asian region with globalisation. Although some countries had opened up their economies before the 1980s, by the early 1990s all the countries in South Asia entered the globalisation process by liberalising their economies, opening up their markets, and implementing reforms to improve economic management. The results of these efforts have been uneven from one country to another and within each country. Even where economic growth rate has gone up, human welfare in terms of education, health or employment may not have improved. The report assesses this process from the point of view of its impact on people.

The report presents the experience of five South Asian countries, India, Bangladesh, Pakistan, Nepal and Sri Lanka. The questions this report raises and tries to answer are: What has been the extent of South Asia’s trade and financial integration with the world? How have the economic reform programmes fared in raising growth and improving human development? What has been the social impact of the globalisation process? Do South Asian nations have full access to the opportunities of expanded trade? Are free markets open to South Asia’s poor and the unskilled?

The report contains seven chapters, in addition to the Overview. Chapter one introduces the theme of this year’s report by presenting a conceptual framework for analysing globalisation and human development. Chapter two looks at the experience of South Asia’s integration with the world’s trade and investment. Chapter three focuses on the social impact of globalisation. Chapter four presents five country case studies on the economic reform programmes and their impact on growth and human development. Chapter five argues a case for increased regional cooperation. Chapter six revives some of Mahbub ul Haq’s views about the need for reforms of the institutions of global governance. And finally, in chapter seven, the report proposes an agenda that identifies the most pressing policy and institutional changes required to achieve humane globalisation in South Asia.

The report has benefitted tremendously from the comments and suggestions of Gustav Ranis, Frances Stewart and Paul

Streeten. Devaki Jain was very helpful in developing the initial ideas for the conceptual chapter. Also Devaki Jain, with Seeta Prabhu and Sandhya Iyer, prepared a background paper on social impact of globalisation in South Asia. I thank them for their commitment to this Centre. I am grateful to Jayati Ghosh for writing an excellent case study of India's globalisation experience. The section on India in chapter 4 is an abridged version of the paper prepared by Ghosh. I am also grateful to Henning Karcher, UNDP Representative in Nepal, to share with us a paper by A. R. Khan on 'Globalisation and Human Development in Nepal.' Our report benefitted from the analysis presented in that paper.

Words fail me when I try to acknowledge the contribution of CIDA for its consistent support of the Centre. CIDA has been on the forefront in supporting and advocating for the cause of social justice in South Asia as well as in other developing regions. A special thanks to the Canadian High Commissioner to Pakistan, H. E. Ferry de Kerckhove for the many ways he tried to help the Centre and its mission. As always, the report has benefited from the help extended to us by the field offices of UNDP in South Asia, particularly Onder Yucer, Brenda McSweeney and Henning Karcher, UNDP Representatives in Pakistan, India and Nepal. I am eternally grateful to Nazir Ladhani, Chief Executive Officer of the Aga Khan Foundation Canada, for providing the best support the Centre needed—two dedicated professionals from Canada to work with us in the preparation of the report. This in-kind contribution is much appreciated.

The research team at the Centre worked hard and for long hours to complete this report. I must recognise, in particular, Sarfraz Qureshi for providing support at each stage of the preparation of the report. The research team, consisting of Shazra Azhar, Umer Khalid, Wasay Majid, Farooq Malik, Faisal Haq Shaheen, Lubna Shahnaz, Shabnam Shallwani, Michael Wang and Hyder Yusafzai collected and compiled data and prepared tables and charts, besides preparing background notes. All this work formed the real foundation of the report. Aasim Sajjad Akhtar was very helpful in providing editorial assistance at the final stage of the preparation of the report. I also thank Taha Mustafa for composing and designing the report, and Malia Asim for handling the administrative details.

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July 31, 2001

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The preparation of this report owes a great deal to many individuals and organisations. The financial support for the report was provided by the Canadian International Development Agency (CIDA), Norwegian Agency for International Development (NORAD), and Aga Khan Foundation-Canada. Without the steady support of CIDA and NORAD for the production of this annual report for the past five years, it would have been impossible to sustain this important work. We are also grateful to the field offices of UNDP in various South Asian countries for their invaluable help in organising the launch of the report. All these financial, technical and moral support are gratefully acknowledged.

Several national, regional and international institutions shared their research materials and data with the MHHDC team. The report benefited from the data provided by the UNESCO Pakistan country office, International Labour Office, United Nations Children's Fund, United Nations Development Programme, United Nations Information Centre and The World Bank. We are grateful to the following Pakistani institutions: Federal Bureau of Statistics and Pakistan Institute of Development Economics (PIDE). The kind assistance provided by the librarians of the World Bank (Pakistan), UNDP (Pakistan), ILO (Pakistan), Institute of Regional Studies and PIDE are also acknowledged.

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About the Mahbub ul Haq Human Development Centre

Mahbub ul Haq Human Development Centre was set up in November 1995 in Islamabad, Pakistan by the late Dr. Mahbub ul Haq, founder and chief architect of UNDP Human Development Reports. With a special focus on South Asia, the Centre is a policy research institute and think tank, committed to the promotion of the human development paradigm as a powerful tool for informing people-centered development policy nationally and regionally, in order to reduce human deprivation.

The Centre organises professional research, policy studies and seminars on issues of economic and social development as they affect people's well being. Believing in the shared histories of the people of this region and in their shared destinies, Dr. Haq was convinced of the need for cooperation among the seven countries of the region. His vision extended to a comparative analysis of the region with the outside world, providing a yardstick for the progress achieved by South Asia in terms of socio-economic development. The Centre's research work is presented annually through a report titled, *Human Development in South Asia.*

Continuing Mahbub ul Haq's legacy, the Centre provides a unique perspective in three ways: first, by analysing the process of human development, the analytical work of the Centre puts people at the centre of economic, political and social policies; second, the South Asia regional focus of the Centre enables a rich examination of issues of regional importance; and third, the Centre's comparative analysis provides a yardstick for the progress and setbacks of South Asia *vis-à-vis* the rest of the world.

The current activities of the Centre include: preparation of annual reports on *Human Development in South Asia*; preparation of policy papers and research reports on poverty reduction strategies; organisation of seminars and conferences on global and regional human development issues, South Asian cooperation, peace in the region and women's empowerment; and publication of a semi-annual journal, Mahbub ul Haq Human Development Review. The Centre also organises an annual Mahbub ul Haq Memorial Seminar and a Mahbub ul Haq Lecture.

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Overview

Globalisation is no longer an option, it is a fact. Developing countries have either to learn to manage it far more skillfully, or simply drown in the global cross currents.

– Mahbub ul Haq

Overview

During the globalisation phase about half a billion people in South Asia have experienced a decline in their incomes

Globalisation, through movement of goods, services, people and information across national boundaries, has resulted in the opening up of economies and societies. The nature and speed of this process have been facilitated and accelerated by new developments in the information and communication technology. International financial markets, through short and long term capital flows, and trans-border production networks have been driving the global integration of economies.

The central thesis of the 2001 Report on *Human Development in South Asia* is that globalisation, though an inevitable process and an imperative for nations to participate in this process in order to draw its potential benefits, is by no means without its risks. It requires many enlightened policies on the part of national governments, international organisations, private sector and civil society to translate the benefits of economic growth that result from globalisation into enriching lives of ordinary people.

The report comes up with several messages:

The first message is that during the globalisation phase about half a billion people in South Asia have experienced a decline in their incomes. The benefits of economic growth that did take place were limited to a small minority of educated urban population. In South Asia, income inequality has increased. It is argued that at the initial stage of opening up the economies to a competitive global market, income inequality will rise, but eventually everyone will gain. With continuing reforms, productivity and efficiency will rise and the country's shares in global trade, finance and services will increase. But who bears the burden of short-term costs? The record so far shows that it is the poor who bear the heaviest burden, and they are the ones who do not have any means to support themselves in bad times.

The second central message, which follows from the first, is that economic growth and human development must move together, otherwise neither growth nor human development can be sustained. This requires much more investment in human development, particularly universal quality basic education as well as higher levels of education and skill training to enable the countries to compete in the global marketplace. In order for economic growth to be job-led, focus should be on labour-intensive as well as knowledge-intensive patterns of production.

The third message is that South Asia must reinvigorate its regional economic cooperation mechanisms already in place (SAARC and SAFTA) to enhance the region's ability to gain from regional as well as global trade, and to improve the negotiating capability of South Asia in global forums.

Globalisation, in the ultimate analysis, is to be seen as only a means to enhance people's wellbeing. All policies and programmes must focus on people. So, first, we need to understand the process that is at work here in South Asia as well as around the world. Secondly, we need to assess globalisation from the point of view of human development and poverty reduction. The mission of this Centre is to approach every issue from the perspective of the people. How globalisation is impacting on the majority of people? How are they participating and benefiting from globalisation? And, how national and global institutions of governance are responding to the needs and concerns of people? These are the questions that we raise and try to answer in this report.

The globalisation process in South Asia has focussed on integrating markets without improving the condition of the vast majority of South Asians.

To understand the globalisation process and its outcome, one needs to deconstruct globalisation. Not all the components or flows of globalisation are moving in the same direction. While capital moves freely, and information and communication are getting freer, labour movement, mostly the unskilled, is restricted, and trade is not fully liberalised, especially of goods of particular interest to developing countries. The balance sheet of gainers and losers in the globalisation process shows the uneven burden borne by the poor within and among nations.

During the globalisation period, income inequalities have widened in South Asia. The number of people in poverty has increased. The levels of human development, though improved since 1960s, have started to stagnate or even decline. The poor are being marginalised.

The opening up of markets has suddenly thrown the domestic industries to face a highly competitive world, resulting in the closure of many industries. On the other hand, trade barriers erected by the developed countries have hampered the growth of exports of labour-intensive goods from South Asia. The skilled labour, especially workers in the information/ communication technology sector, has been the main beneficiaries of globalisation in this region. The provision of social safety nets has also been weakened in the region, as the governments' ability to help the victims of globalisation has been eroded.

South Asia's integration with the trade and capital markets have expanded considerably, yet South Asia remains among the least-integrated regions in the world.

By the end of the 1990s, average tariff rates fell rapidly in all countries, with the regional average falling to 20 per cent. In Bangladesh, the average tariff fell from 114 per cent to 22 per cent, and in India, from 82 per cent to 32 per cent. Yet South Asia's average tariff rates remained much higher than, for example, Korea or Malaysia where the average tariff rate was 9 per cent or less.

Depreciation of real exchange rates, among many other export promotion measures, led to export growth rate of about 10 per cent per annum during the 1990s. Exports structures have also changed from primary commodities towards more manufactured goods and services. Within manufactures, labour-intensive goods, such as garments and textiles, jewellery and leather goods dominated manufactured trade. Exports remain concentrated in a limited number of products such as clothing and textiles, and destinations such as United States and European Union. Nepal's export is concentrated in only one product, carpets. India is the one country in South Asia with the fastest growing share of high technology exports.

South Asia has also become more financially integrated over the past decade. Aggregate net resource flows to the region have expanded rapidly during the 1990s, however most of these flows are composed of foreign direct and portfolio investments. Despite this increase, South Asia's share of total private capital to developing countries has declined over the past decade, falling from 7 per cent during the 1980s to 3 per cent in the 1990s.

From the record to date, it is unclear whether greater integration with the

Provision of social safety nets has been weakened in the region

world economy has benefited economic growth in South Asia. Comparing the average regional GDP growth rates between pre- and post-globalisation periods, it seems that growth has in fact been lower during the 1990s, despite India's high growth rates. It appears that greater economic integration has yet to translate into sustained growth for the majority of South Asian countries.

Most South Asian countries failed to maintain a balance between economic and social development policies

Globalisation has not been accompanied by reduction of poverty or improvement in human development.

Prior to globalisation, South Asia had experienced high population growth rates, high levels of illiteracy, poor health attainments, pervasive poverty and inequitable distribution of income and assets. These initial conditions did not improve much during globalisation as the South Asian average growth rate, which was 5.8 per cent during 1980-89 fell to 5.4 per cent during 1990-98. Also, during the globalisation phase, there were no adequate policies and funding in the social and economic development fields to reduce poverty or to make any meaningful difference in the lives of the majority of the population.

• South Asia, home of the largest number of poor people in the world (515 million) did not make much progress towards poverty reduction. While the incidence of poverty declined both in terms of depth and severity, disparities between rural and urban areas persisted. The income distribution across the various economic groups worsened during globalisation.

• On the educational front, South Asia didn't fare very well either. Over 40 per cent of children did not reach grade 5 in the 1990s. Sharp gender disparities were observed in the mean years of schooling between male and female students. With globalisation, the demand for highly skilled and specialised labour force increased. However, none of the countries mobilised or provided additional resources to the tertiary education sector.

• Health expenditures were reduced to levels that were lower than those in the pre-globalisation period. Over one fifth of population in the region did not have access to health care services. The globalisation period was thus characterised by declining provisioning of public health facilities, and declining population to health personnel ratio. The region also experienced increasing cases of infectious diseases like TB, malaria and the emergence of HIV/AIDS, which put further strain on the health care systems in the region.

• All South Asian countries have been implementing several poverty alleviation programmes over the past decades, financed mainly by the state. With the onset of globalisation, the resource allocations to these programmes have been declining, reducing their effectiveness. The social security provisions, available to the working population, also decreased with changing employment structures, as more people were pushed into the informal sector.

Most South Asian countries failed to maintain a balance between economic and social development policies during globalisation. An equitable globalisation process requires the integration of the financial, trade and investment policies with those of social development. The stabilisation and structural adjustment programmes of the IMF and the World Bank, and the new trading regime of the WTO, have led to fiscal compression, tariff reductions and cutbacks of public provisioning of social services. The social services expenditures in the post-globalisation period remained stagnant at the prevailing pre-reform levels, reducing the coverage and effectiveness of service delivery.

Economic reform programmes have failed to increase growth substantially or achieve macroeconomic balance.

In Bangladesh and Nepal, the growth rates during globalisation have been modest and in Sri Lanka the growth rate has faltered during the second-half of the 1990s. In Pakistan, growth has declined. Only India has been able to achieve a growth rate of above 6 per cent.

The sequencing of reform measures, such as reducing tariffs before expanding tax base and improving collection, or curtailing government borrowings from the banking system before restructuring the public sector expenditure, was not well-tailored to achieve the desired results.

Agriculture has performed badly during globalisation. Not enough policy focus was given to this sector either to protect it from the vagaries of the market or to make it more competitive to face globalisation.

Trade and current account balances have remained negative in all countries during the 1990s. India's position has been relatively better, and Nepal's worse. Despite increased inflow of FDI to India and Sri Lanka, South Asia has not been a preferred region for attracting FDI.

Employment expansion in none of the countries has been significant. Weak employment creation, low growth and low allocation to social sectors explain South Asia's slow progress in poverty reduction and human development during the globalisation period.

There is a worldwide movement for forming regional trading blocs, yet intra-regional trade within South Asia is very low compared to such trade in other regional groupings.

There are many advantages for forming regional trading blocs: it promotes economic cooperation among the members; improves the competitive position of the group in a globalised world; facilitates political harmony within the group; and forges a collective bargaining position in global negotiations. Yet in 1999, trade among the South Asian countries was less than 5 per cent of the region's total exports, compared to 22 per cent in ASEAN and 55 per cent in NAFTA.

In South Asia there are enough economic reasons for promoting intra-regional trade and cooperation. Direct trade in goods that are being diverted through third countries will benefit all countries. Besides, many goods being imported at higher costs from outside the region can be made available from within the region.

If South Asian countries remain aloof in a world of trading blocs, they stand to lose. In a world that is headed towards free trade, regional agreements would facilitate the entry of smaller nations in the multilateral trading system on a preferential basis. It is important for South Asia to acknowledge the welfare gains from their own regional arrangements which would at the same time prepare the domestic producers for the rigours of multilateralism.

Liberalisation policies have yet to lead to efficient allocation of resources

A global economy has emerged, but the institutions of global governance are not performing either efficiently or equitably.

The Bretton Woods Institutions (IMF, World Bank, GATT/WTO) were created to serve as global institutions for maintaining financial stability and for promoting development and trade. But the impact of policy conditions of these institutions falls disproportionately on the poor.

While the early policies of these institutions were designed in the spirit of building the capacity of the state, over time there has been a trend towards reducing the role of the state and moving towards liberalisation and privatisation. The IMF loans are useful as a certificate of creditworthiness for accessing other multilateral and bilateral loans and grants, but the conditions attached to these loans make it impossible for countries to get out of debt trap.

It is true that the decisions regarding the budgetary allocations for social development are made by national governments. However, in view of diminished revenue and increased costs of debt servicing, the governments in South Asia are finding it increasingly difficult to allocate adequate resources for social sector programmes.

Reforms must continue but with a human face

Since the late 1980s, poor economic management of the public sector led both the IMF and World Bank to shift their focus from state-led development efforts towards market and private sector-led development. But the liberalisation policies have yet to lead to efficient allocation of resources, higher growth rates and reduced deficits. Most developing regions, including South Asia, have been running higher current account deficits without achieving higher growth rates. This is primarily due to widening trade deficits as exports are not expanding as much as imports.

It is generally feared that the structural adjustment programmes of subsidy elimination, removal of trade restrictions on agricultural commodities, and an overall unification of local with global prices will leave the poor farmers in South Asia most vulnerable.

As tariff barriers have fallen in developing countries, the world has been further divided along income lines, separating the global rich from the global poor. While developing countries have reduced their tariffs to levels lower than what was required by the WTO agreement, developed countries have not delivered the promised tariff reductions on goods of key interest to poor countries.

Agriculture in most developed countries is sheltered behind high tariff walls, farm subsidies, loan guarantees and non-tariff barriers. Developing countries that are heavily dependent on agricultural exports are at a great disadvantage in terms of competing against the heavily-subsidised agricultural products of the North.

From the human development perspective, institutional policies of multilateral organisations have resulted in increased deprivation of the poor , rising unemployment and unsustainable development practices.

Positive effects of globalisation on economic growth and human development depend on how the process is managed nationally and internationally.

At the national level, South Asian countries need to make sustained efforts in four policy areas: accelerate human development, especially education; reduce poverty; improve economic management; and enhance regional and global integration.

- South Asia must prepare its labour force to face global competition. Central to this is the strategy to provide quality primary education to all school-age children, provide them appropriate skill-training as well as higher levels of education in new technological fields. While governments should allocate sufficient resources for primary and secondary education, private sector should be mobilised to set up technical institutions for imparting training for higher levels.
- Poverty reduction strategies must be built into the micro and macro policies. Globalisation policies to focus on cash crops instead of food crops, and capital-intensive rather than labour-intensive industries need to be analysed to assess their impact on the poor.
- Economic management in all countries needs to be improved. Reforms must continue but with a human face. The focus should be on improving management of resources, reducing corruption, taxing the rich, cutting the non-merit subsidies, and establishing the institutions to implement and monitor reforms. All globalisation policies and strategies must be judged by one yardstick: how are they impacting on

people, on poverty reduction, on job creation, on children and on women.

• Integration with the global economic system should be enhanced. But South Asia needs to continue in more traditional labour-intensive low-technology exports, as well as diversify into more high technology goods and services. India's success in establishing a niche for itself in the fast-growing global software and information technology market demonstrates that such diversification can be achieved.

At the global level, a time may have come to revisit some of the excellent ideas for reforming the institutions of global governance. This report has listed only three: World Central Bank, Economic Security Council, and the Tobin Tax. The developing countries badly need today a lender of last resort at the global level to rescue them from short-term liquidity crisis, without turning it into a long-term development crisis. There is also a need to establish an Economic Security Council at the United Nations to address the economic and human security aspects that threaten the global community, just as the UN Security Council looks at the political and military aspects. Also, in view of the recent volatility of financial markets exacerbating poverty and human crisis, the Tobin Tax proposal to tax speculative movements of short-term capital needs to be considered seriously by the global community.

The roles of civil society in guarding the poor against the disproportionate burden placed on them, and the private sector in playing a supportive and compassionate role in humanising globalisation are essential. Governments alone cannot monitor everything and deliver all the services. But globalisation process requires an activist government to protect the vast majority of South Asians, with the help and active support of the civil society and private sector.

1

Globalisation and Human Development: A Conceptual Framework

We approach every issue from the vantage point of people. Do they participate in economic growth as well as benefit from it? Do they have full access to the opportunities of expanded trade? Are their choices enlarged or narrowed by new technologies? Is economic expansion leading to job-led growth or job-less growth? Are free markets open to all people?

– Mahbub ul Haq

Chapter 1

Globalisation and Human Development: A Conceptual Framework

"Markets cannot become neutral or competitive unless the playing field is even and playable"

"…markets are not very friendly to the poor, to the weak or to the vulnerable, either nationally or internationally. Nor are markets free. They are often the handmaidens of powerful interest groups, and they are greatly affected by the prevailing distribution of income….Is everybody in a position to compete in the market, or will some people fall outside the market-place because they do not have enough education, health and nutrition to compete on any footing, let alone an equal footing? That is why much better distribution of income and assets. of credit, of power structures and certainly of knowledge and skills are vital to making markets work more efficiently. Markets cannot become neutral or competitive unless the playing field is even and playable."

(Mahbub ul Haq, 1995)

This wisdom of the founder of the Human Development Centre has guided us in developing a conceptual framework for this report on globalisation and human development in South Asia. The new development paradigm that underpins the current globalisation process is based on an ideal view of the world where markets work efficiently, capital and technology flow freely and that people have all the knowledge, information and ability to take part in the market on an equal footing. But in the real world situation of most developing countries, including South Asia, this process becomes a nightmare for a great number of people. As such, in this report we first try to understand the globalisation process; secondly, we analyse the policies through which the countries of this region are attempting to get better integrated with the world market; thirdly, we assess the costs and benefits of the reform efforts; and finally, we try to develop an alternative framework that would combine economic growth with human development and better distribution of gains from globalisation.

What is globalisation?

The origin of globalisation can be traced all the way back to the period of colonisation in the 16th century. However, the process of global economic integration gained momentum only in the 1970s with the development of international capital markets. During the debt crisis of the 1980s, several developing countries implemented programmes, popularly known as stabilisation and structural adjustment programmes, to qualify for loans from the International Monetary Fund (IMF) and the World Bank. These programmes aimed at creating conditions for liberalisation of developing-country markets. The process of outward-orientation gained momentum in the 1990s when the World Trade Organization (WTO) was established following the conclusion of the Uruguay Round of trade negotiations. Early 1990s was also the time when most South Asian countries, heavily burdened by debt and deficit, entered into programmes with the IMF and the World Bank and opened up their economies to the world trading system.

Globalisation is defined as the free movement of goods, services, people and information across national boundaries. It creates and, in turn, is driven by an integrated global economy, which influences both economic as well as social relations within and across countries. The opening up of an economy increases competition internally as well as externally, leads to structural changes in the economy, alters consumer preferences, lifestyles and demands of citizens.

Globalisation means different things to different people. In business school literature, it refers mainly to company specific strategies designed to overcome the constraints of national boundaries through the mechanism of globalised production and marketing networks. In the economic field, it is considered synonymous to economic interdependence between countries covering increased trade, technology, labour and international capital flows. In the political debate, globalisation refers to the integrative forces drawing national societies into a global community covering the spread of ideas, norms and values. Last but not the least, the tidal wave of global culture is sweeping the indigenous cultures the world over (see box 1.1).

Views about globalisation differ widely, influenced by the particular vantage point of an individual or a country. In South Asia, for example, during the period of globalisation the absolute number of people in poverty has increased, despite the fact that the largest country in the region (India) has been experiencing a growth rate of over 6.5 per cent during this period of increased integration with the global economy. Although the other indices of human development in South Asia have improved during the last three decades, they are still among the worst in the world. Should it lead us to conclude that globalisation has been bad for human development in South Asia? If yes, then should we look for answers within our own societies and governments? Or, should we look at the workings of the institutions of global governance for such an inequitable outcome of globalisation for the poor nations?

This is what we would like to explore in this report on *Human Development in South Asia*. The challenge facing South Asia is to use the forces unleashed by globalisation for improving its human development while expanding opportunities for economic growth and overall socio-economic development.

Box 1.1 Views on globalisation

'…Globalization encapsulates both a description and a prescription. The description is the widening and deepening of international flows of trade, finance and information in a single, integrated global market. The prescription is to liberalize national and global markets in the belief that free flows of trade, finance and information will produce the best outcome for growth and human welfare.' (UNDP, HDR 1997)

'…Globalization is a double-edged sword: a powerful vehicle that raises economic growth and increases living standards in rich and poor countries alike, but also an immensely controversial process that assaults national sovereignty, erodes local culture and tradition and threatens economic and social stability.' (Robert J. Samuelson, International Herald Tribune January 2000)

'Globalization is praised for the new opportunities it brings, such as access to markets and technology transfer-opportunities that hold out the promise of increased productivity and higher living standards. But globalization is also feared… it brings instability and unwelcome change…exposes workers to competition from imports… undermines governments…'. (World Bank, WDR 1999)

'World 2000 is a misshapen creation demographically, economically and culturally. It is a world Charles Dickens would recognize as the best of times available for the lucky many and the worst of times…for even more numerous unlucky. Most of whom live in the Third World'. (Jim Hoagland, Washington Post, 1999)

'Globalization has encouraged an explosion of wealth and technology never approximated in any historical epoch. Such rapid change inevitably challenges prevailing social and cultural patterns…A sense of political unease is inevitable—especially in the developing world—a feeling of being at the mercy of forces neither the individual nor the government can influence any longer.' (Henry Kissinger 1999)

Nature and character of the globalisation process

The nature and character of globalisation has been fundamentally altered by new developments in the information and communication technology and the globalisation of financial markets. These developments have enabled the movement of jobs to places where skills are available for the information/communication technology sector. But the extent to which different countries have participated in globalisation is far from uniform. The least developed countries have been, by and large, excluded from the globalisation process (with the possible exceptional case of Bangladesh). While some developing countries, especially in East and South East Asia, have increased their share in

Global integration has turned out to be quite unbalanced with uneven participation of countries and people

trade and capital flows, the bulk of international flows are still situated within developed industrial countries. It is no surprise, therefore, that global integration, though rapid, has turned out to be quite unbalanced with uneven participation of countries and people in the expanding opportunities from globalisation.

Flows relating to trade, investment and other capital flows, and technology and labour are the cutting edge of the globalisation process. These flows are both the cause and effect of the emergence of a new global economic system in the post-war period. The main elements shaping this new system are the emergence of a new global trading order, the unprecedented speed and scale of global financial system, and the global reach of multinational corporations. The facilitating roles of the information/ communication technology revolution and the ideology of free market capitalism have been critical in shaping the new economic system in its current form. The role played by civil society groups in both developing and developed countries in challenging this new development paradigm and the evolution of universal norms as a guide for economic policy making have also been important factors in shaping globalisation (Burki & Savitsky 2000).

New global trade patterns

The rapid expansion of world trade during the last fifty years is a direct outcome of trade liberalisation efforts as well as the evolution of a legal framework governing trade between countries. The establishment of GATT in 1947 had started this process of trade liberalisation. There were a series of rounds of trade negotiations. The latest of these rounds— the Uruguay Round— produced the most fundamental reform of the world trading system. In 1995, following the conclusion of the Uruguay Round of trade negotiations, World Trade Organization (WTO) was established to settle trade disputes among nations. All previous rounds had facilitated the expansion of trade flows for the manufactured goods only, as tariff and non tariff barriers were gradually reduced for the imports of such goods. The last round had extended the scope of trade to include agriculture and services. Of special interest in this context is the treatment given to new aspects of trade such as Trade Related Investment Measures (TRIMS) as well as Trade Related Intellectual Property Rights (TRIPS). The rule based trading system with a broader coverage of commodities and services has come to be known as the new international trading order.

This rapid increase in trade has become the driving force in the globalisation process. The phenomenal increase in world trade flows has been beneficial to many countries participating in trade. World exports had increased from US$ 61 billion in 1950 to $315 billion in 1980 to $3447 billion in 1990 and $6844 billion in 1998. The share of world exports in world GDP has also increased over time rising from 6 per cent in 1950 to 16 per cent in 1992 and to 24 per cent in 1998. The developing countries including South Asia have also played a key role in the global expansion of trade. The share of exports from developing countries in total world exports increased from 23 per cent in 1991 to 31 per cent in 1998. It should, however be noted, that South Asia had barely managed to increase the share of its exports in GDP, i.e., by only 1.5 per cent from 8.2 per cent in 1991 to 9.7 per cent in 1998. The key players in the developing world in this context have been East and South East Asia which had increased the percentage of their merchandise trade in GDP from 40 per cent to 60 per cent between mid 1980s and 1994 (Nayyar 1998, World Bank 2000b & 2001).

The composition of world trade has also changed in at least three fundamental ways. The share of primary commodities in exports has fallen while that of manufactured goods especially of higher value products has risen. Intra-firm and intra-industry trade has emerged as a key factor in the global trade expansion. Trade in services has outpaced the trade in goods. The sustained growth in trade and the nature of its composition have opened new opportunities for countries to capture the benefits from globalisation. In South Asia, only India seems to have been able to take advantage of this opportunity.

Global financial flows

The external savings are considered crucial for increasing investment rates in developing countries. For the poor countries, with low domestic savings rates, the reliance on external savings was an obvious choice to raise their investment rates. The most significant source of external savings provided to developing countries initially was in the form of official development assistance (ODA). But ODA as a percentage of developed-country gross national income (GNP) never reached 0.7 per cent as was expected by the developing countries, and in fact went down considerably to a level of about 0.3 per cent of the combined GNP of developed countries.

However, private capital flows have filled the gap, especially after the mid 1980s. But the private capital is more mobile as well as more volatile than ODA. It is driven mainly by the profit motive. The two main components of private flows— portfolio investment and foreign direct investment (FDI)— have exhibited rapid expansion in the 1990s. Portfolio investment has, however, been more volatile than FDI.

Foreign direct investment has obvious benefits in terms of not only augmenting the domestic savings but providing increased access to technology, management skills and export markets. Like the world trade expansion, international investment flows have also shown rapid expansion. The stock of FDI worldwide has increased from US$ 68 billion in 1960 to $502 billion in 1980 to US$ 1948 billion in 1992 and US$ 3456 billion in 1997. The FDI flows increased from US$ 52 billion in 1980 to US$ 171 billion in 1992 and to US$ 360 billion in 1997. The stock of FDI in world GDP and FDI inflows as a percentage of gross fixed capital formation have gone up considerably (Nayyar 1998, World Bank 2000b, 2001).

The geographical trend of FDI shows that it has gone mainly to the industrialised countries. This is true for all indicators of FDI. The share of developing countries in FDI stock has increased in relative terms from 22 per cent in 1992 to 30 per cent in 1997. However, FDI stock as well as flows are concentrated mainly in a few developing countries including, China, Mexico and Brazil. According to data available for 1998/1999, the share of South Asia in FDI inflows has so far been insignificant. South Asia's share in total FDI inflows to developing countries was only 1.8 per cent in 1999. The lop-sided geographical distribution of FDI is also reflected in the sectoral distribution of such flows. Services and manufacturing sectors account for the bulk of these flows. The share of primary sectors, which are the dominant producers and employers in most of the developing countries, has been low and falling.

Rising influence of international financial markets and the importance of short and long-term capital flows have been driving the global integration of economies

The rising influence of international financial markets and the importance of short and long-term capital flows have been driving the global integration of economies. The internationalisation of financial markets is reflected in an explosive growth of portfolio investment flows and bank loans in the 1980s and 1990s. Like FDI, such flows are also situated mostly in the developed countries. The bulk of such flows are short-term capital flows. Mutual funds have emerged as major players. The movements in interest rates and exchange rates determine the direction and the magnitude of these flows. Countries that manage their economies well are in a better position to attract private capital flows and benefit, relative to those countries which have poor macro economic policies.

Global reach of MNCs

An important development in the globalisation process has been the emergence of trans-border production networks between firms located in different countries. Such firms employ global strategies including worldwide sourcing of materials and locating activities in many different nations. The increased volumes of FDI has enabled multinational corporations to transfer process and product technologies across national borders and by doing so enhance their competitiveness. The emergence of trans-border production networks has globalised production of goods and services as different components are produced in different locations in many countries. The flexible production systems have reduced the importance of economies of scale since enterprises need not be large to participate in the global markets. The small countries can also develop a niche for themselves in the new system (see box 1.2).

Information/communication technology

The information and communication technology (ICT), in particular the internet, is the most visible component of an integrated world. This technology, with its tremendous potential for bridging the time and space and the income and knowledge gaps, has had a dramatic impact on the globalisation process. ICT has reduced the geographical barriers to trade, finance and production relationships between actors spread all over the world. ICT has changed the competitiveness of countries and helped increase capital market inter-nationalisation by reducing transaction costs. But in order to harness the potential of ICT, a country needs to have an educated and skilled labour force. How globalisation impacts on human development in South Asia would depend a lot on how these countries could take advantage of this technology.

Box 1.2 Teleworking: India's new growth sector

In recent years multinational corporations, mostly from the developed world, have begun to use strategies that would reduce costs without lowering quality and efficient use of time. A whole range of work—from customer service to ordinary accounting work and transcribing medical records—is being shifted out of headquarters in developed countries to developing countries. In India, which has a large pool of English-educated human resource for use in this new area of globalised employment, this has led to the growth of a new service industry that has the potential to earn more than the highly skill-intensive computer programming sector. It is predicted by NASSCOM, the main national association of information technology companies that by 2008 1.1 million Indians would be employed and approximately US$17 billion will be generated by such 'IT-enabled services'.

Companies like GE Capital Services have been outsourcing India for simple jobs such as collecting money from delinquent credit card users. British Airways along with other airlines like Swissair have large centres for programming and handling everything from computer messages to ticket booking information. It has been estimated that 40-50 per cent of cost is saved by such companies simply by shifting these type of work to India.

But cost-effectiveness is not the only attraction of India; the standards of service provided by the Indians are just as good. As a matter of fact, currently the standards are very impressive: Funds International, part of a company spin-off from Deluxe (America's main printer of cheques) has cut the number of errors in data processing for one client by 90 per cent. Furthermore, the days taken to close monthly accounts have been reduced to three from five. Indian workers outperform their U.S. counterparts due to greater job determination and higher qualifications.

Source: Outsourcing To India, The Economist, May 5th 2001.

Challenging globalisation

After the financial crises in Latin America and East Asia, both the process and the outcome of globalisation are being challenged. The critics of globalisation argue that in order to understand the globalisation process and its outcome, we need to deconstruct globalisation. This exercise is important to highlight the fact that not all the components, or flows, of globalisation are moving at the same pace and in the same direction. While capital has free movement and information and communication are getting freer, labour movement, especially the unskilled, is restricted, and trade is not fully liberalised, especially of goods of particular interest to developing countries.

- Financial flows have been globalised. The increased mobility of capital has positioned some countries to boost their investment rates beyond their domestic savings rates. Such flows in the form of foreign direct investment have also facilitated the transfer of technology. However, most capital flows take place within the developed countries and a few selected developing ones.

- Technology flows have also been large and growing. Although there is asymmetry in sharing some technologies between the developed and developing countries, in the case of information technologies the transfer to the developing countries has been relatively more liberal.
- In theory, free trade between developed and developing countries leads to a more efficient structure of production and expanded opportunities for consumption. Both are expected to lead to higher national and world income and welfare. But trade rules are highly asymmetrical between developed and developing countries. There are all kinds of restrictions on trade in goods and services in which developing countries enjoy comparative advantage. The trade in agriculture has been restricted by high subsidies and non-tariff barriers in developed countries. While developing countries have drastically reduced tariffs on goods from developed countries, products from developing countries, especially processed and semi-processed goods face non-tariff barriers and tariff escalation. Then there is the constant threat of invoking social (labour and human rights) and environmental clauses for continued protection against the goods of interest to the developing world.
- Labour mobility among countries has not always been restricted. Movements of labour from Europe to the areas of new settlement (the USA, Canada, Australia, South Africa and Latin America) was free before the First World War. Restrictions of such movements have increased after the Second World War. These have applied mostly to unskilled labour. Restrictions on the movement of skilled labour, especially scarce professional manpower, have been much less pronounced; indeed, to the pressures to emigrate has recently been added intense demand in the rich countries for these skilled people, depriving the developing countries of this scarce resource on whose education they may have spent large sums.

Overall, it seems that despite the rhetoric of free trade the terms and rules guiding globalisation are loaded against the developing countries. A balance sheet of gainers and losers in the globalisation process, shows the uneven burden borne by the poor within and among nations (see box 1.3). This is the reason why the opponents of globalisation raise their voices in global forums.

Box 1.3 Gainers and losers of globalisation

Gainers	Losers
Output	*Employment*
People with assets	*People without assets*
Profits	*Wages*
People with high skills	*People with low skills*
Educated	*Uneducated*
Professional, managerial and technical people	*Workers*
Capital	*Labour*
Creditors	*Debtors*
Those independent of public services	*Those dependant on public services*
Large firms	*Small firms*
The strong	*The weak*
Risk takers	*Human security*
Global markets	*Local communities*
Sellers of technically sophisticated products	*Sellers of primary and standard manufactured products*
Global culture	*Local cultures*
Global elite	*Global poor*
Firms with market access and branding	*Firms without market access and no branding*

Source: Streeten 1998.

Globalisation and South Asia

The ongoing globalisation process in South Asia has focussed on integrating markets without improving the condition of the vast majority of South Asians. As

The uneven and unbalanced nature of globalisation in South Asia has inflicted a social cost

a result, income inequalities have widened, the number of people in poverty has gone up during the period of globalisation, and human development levels, though improved since 1960, have started to stagnate or decline. The poor are being increasingly marginalised. Some ethnic groups are virtually faced with a complete exclusion from the benefits of globalisation.

The magnitude of unemployment and/ or underemployment has always been high in South Asia. The problem has been made worse by recent policy initiatives. Trade liberalisation has exposed domestic industries to fierce competition from imports. Over-staffed public enterprises have been either privatised or restructured resulting in loss of jobs. The effects of implementation of IMF stabilisation/ adjustment packages have been deflationary on the economy. The shortage of capital has reduced the ability of the private sector to absorb the laid-off workers. The increased exports of labour-intensive goods that was expected to happen never did. Trade barriers have dampened the demand for manufactured goods from South Asia. So the workers have seen globalisation as leading to job losses, increasing work insecurity and lower wages.

The empirical evidence also supports the view that globalisation increases inequality within and between countries, and also between different sectors. A few globalised enclaves, such as export processing zones, in a vast hinterland are the most commonly observed features of globalisation in developing countries. The skilled labour and the innovators in the ICT in India and in other South Asian countries have concentrated themselves at the technology parks. This has increased job opportunities for the skilled but it has also led to increased income inequality. The worsening of income distribution is also due to proportionately more gains accruing to capital and rents than to wages.

One of the negative side-effects of globalisation has been the breakdown of traditional support systems in the community. The bond between employers and employees and between different social groups has become weak. Victims of globalisation do not have the support to ride over the bad times. Simultaneously, the ability of governments to put in place social safety nets has become weak. To attract private capital, tax rates have been reduced. Tariff reductions have reduced the sources of revenue for governments. The revenue losses have come at a time when more revenue is required in order to finance the much needed infrastructure, social services and other anti-poor programmes. The erosion of the governments' ability to help the victims of globalisation process needs to be arrested if the outcome of globalisation is to benefit all people in South Asia.

The uneven and unbalanced nature of globalisation in South Asia has inflicted a social cost. Fortunately, to-date the globalisation era in this region is in its early stages. A rethinking of the whole process is called for in order to minimise the risks and maximise the benefits of globalisation.

Rethinking globalisation

The restriction of labour flows between the South and North, the volatility of short term capital flows, the mismatch between the efficacy of institutions of governance and the potential of regional associations are some of the issues that need to be examined in the context of South Asia.

Neglected labour flows

Most discussions on globalisation tend to be limited to trade and financial flows. Indeed, these are the most obvious manifestations of a world with increasingly porous borders, where massive amounts of capital can be transferred from one end of the world to the other in a matter of seconds. Nevertheless, the theory of trade is not simply limited to capital flows, but also extends to other factor endowments. Specifically, labour as a factor of production features heavily in any trade theory. Unfortunately, the importance of labour flows in this era of globalisation has been somewhat overshadowed by the constant discussion of capital movement. Even when labour movements are discussed, they are discussed most often in the form of remittances and transfer payments within and across countries.

This is not to say that the social impacts of globalisation are not discussed. Indeed, the single most important concern in this day and age is how consumers and workers across the world are affected by liberalising trade and financial markets. However, the question that begs to be answered is how labour as a factor of production affects globalisation. This will not only shed light on the true nature of globalisation and how best to benefit from it, but will also provide further insight into how people across the world are faring.

Conventional trade theory is governed by the law of comparative advantage according to which it can be predicted that developing countries export labour-intensive goods to the developed countries. According to factor price equalisation theorem, there would occur a convergence of incomes. However if only capital is allowed to move freely across borders, then not only is it unlikely that there will be convergence of incomes, but the benefits from trade will be extremely skewed.

Naturally there is never likely to be a world without any national restrictions at all on capital or labour flows. Nevertheless, by omitting consideration of labour flows, the broad framework of globalisation suffers from incompleteness and, much like the experience to date, is likely to adversely affect some players in the world economy. Therefore, it is extremely important to rethink globalisation with this in mind and to assert that globalisation is concerned with the fate of people. A discussion of labour flows fundamentally alters the concept of globalisation and allows for not only a more complete analysis but the prospect that better policies be put into place that take account of the various facets of globalisation and thereby derive greater benefit from it. It is important to note also that technology as a factor of production has become increasingly important in the past few years and should also not be neglected.

The stipulated benefits of globalisation are basically expanded opportunities—better opportunities for work, more choice in terms of consumption, higher quality of goods and services available, all at a lower cost. While this has occurred for a minority of South Asians, the realities faced by most South Asians as a result of globalisation to date have been harsh. Indeed, for most South Asians the outcomes of globalisation have been higher prices, fewer employment opportunities, increased disparities in income and higher incidence of poverty. Poor terms of trade have made matters worse.

For most South Asians the outcomes of globalisation have been higher prices, fewer employment opportunities, increased disparities in income and higher incidence of poverty

It becomes obvious that all of these issues relate more to capital flows than to labour flows, at least on the surface. The only regularly mentioned issue relating to labour movements in such discussions is that of remittances. Interestingly however, remittance payments to South Asia from its own workers abroad were greater in the 1970s, prior to the present era of globalisation. This highlights the fact that the labour flows abroad have actually decreased in the past ten to fifteen years, which is when the movements of capital and technology have increased immensely. Therefore a central piece of the globalisation puzzle seems to be missing.

The current vogue of open markets is clearly limited to capital and to an extent technology markets. Indeed the developed economies of the West have an aversion to unskilled or low-skilled labour from South Asia, despite having a huge bias in favour of skilled labour from the region, particularly from the

Information Technology (IT) field. Policies that limit immigration in the developed world seriously affect South Asian labour and industry.

In a world where trading partners are often at extremely disparate levels of development, and where factor endowments are very different, a globalising economy is affected heavily by labour movements or their absence.

Managing volatility

The occasional financial crisis causing widespread misery provides a strong case for evolving a policy package to limit extreme volatility. Some of the crucial elements are strengthening of financial sectors and particularly stock and bond markets, controlling excessive inflow of short-term capital, having an adequate level of foreign reserves and evolving credible policy-making institutions in monetary and fiscal areas. South Asia has weaknesses in most of these areas except that the governments still retain considerable control on the inflow of short-term portfolio flows. Action in all other areas is needed before the region faces a serious crisis.

Relative roles of local, national and global institutions of governance

The issue of reviewing the relative roles of local and national governments, international institutions and international civil society in a rapidly globalising world has become urgent to ensure that the integrated world works for people and not the other way around.

The revolution in technology has moved much faster than the institutions. The nation-state is in need of a massive rethink. It is too big for small things and too small for big things. There is a need for some of its function to be delegated downwards and some upwards (Streeten 1998).

The shifting downwards of some functions is a response to the demand for localisation and decentralisation, i.e., greater political, fiscal and administrative autonomy. The cry for local participation in governance structure is a worldwide phenomenon; South Asia is no exception to this new trend. Some governments in this region have gone a long way towards a real devolution of power to the level of the local communities.

The case for upward delegation of some functions is straightforward. If markets are global, their regulation must then rest with a global authority. The examples of possible institutional innovations include a global central bank, a global energy facility, and a global technology policy. The danger to avoid is that the global institutions need not subject countries to blue print formulas and should instead concentrate on improving processes and rules. However, the exact details of the possible functions of institutions of global governance need to be carefully thought through.

The nation state, despite a double squeeze on its roles, remains an important entity

The nation state, despite a double squeeze on its roles, remains an important entity. In two areas particularly the role of the nation state has become more important than before: (a) in accelerating human development, and (b) in providing social protection to the vulnerable.

(a) Success in the global economy, for individuals as well as for national economies, depends on their levels of education and training, that is, on their human development achievements. Human development then is more than crucial for further advance in economic growth, and for subsequently greater achievements in human development. Spreading education to everyone is an important means of spreading opportunities and incomes and countering the tendency for rising inequality and social exclusion.

(b) Globalisation has been accompanied by rising vulnerability of individuals, families, communities and regions. National economic fluctuations rise and individual job insecurity rises. Moreover traditional mechanisms for protecting people in these situations weakens. It is essential for economies to put in place new mechanisms of social protection. However, the tendency is in the opposite direction because of downward pressure on tax revenue and social expenditure.

Regionalism in a globalised world

Globalisation manifests itself as a significant expansion of world trade, investment, technology and labour flows. The globalised economy has simultaneously witnessed a process of regionalisation. More than 23 Regional Trading Arrangements (RTAs) have been notified to GATT and its successor organisation, WTO. These RTAs, and related arrangements in the areas of regional cooperation, liberalise regional flows of investment, labour and commodities trade, transforming national economies into regional economies.

The question that is often raised is whether the policies of globalisation and regional integration can be reconciled. In other words, whether existing or proposed regional blocs are building blocks or stumbling blocks to globalisation?

The answer to the puzzle lies in the form most blocs would take. If trade creation prevails over trade diversion, such blocs would lead to effective globalisation. If trade diversion dominates, there is a real danger of globalisation being effectively blocked. In the case of South Asia, open regionalism is the ideal form to support. The region should itself form an effective bloc of its own to gain an increased voice in international negotiations and also to benefit from increased intra-regional trade.

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This Centre's annual reports analyse every issue from the vantage point of people. "Do people participate in economic growth as well as benefit from it? Do they have full access to the opportunities of expanded trade? Are their choices enlarged or narrowed by new technologies? Is economic expansion leading to job-led growth or job-less growth? Are 'free' markets open to all people?" (Mahbub ul Haq, 1995). These are some of the issues we intend to address in this report.

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Trade and Financial Globalisation of South Asia

It is simply unacceptable that while aid transfers so few resources to the developing world, several times more is taken away through trade protection, immigration barriers and an increasing debt burden. In such a situation, it is critical for poor nations to bargain for more equitable access to global market opportunities.

– Mahbub ul Haq

Chapter 2

Trade and Financial Globalisation of South Asia

Confronted by lagging growth rates and external payments crises, the majority of South Asian countries adopted a more outward-oriented development strategy

As defined in chapter 1, globalisation is a multi-dimensional process, encompassing economic, political, cultural and social dimensions. While each of these forces undeniably shapes the impact of globalisation for human development, the focus in this report is on its economic dimensions. In this context, globalisation refers to the increasing movements of goods, services, finance, and factors of production across national borders. Over the past decade, the level of global trade and investment have reached unprecedented heights, and more countries than ever are integrating into global economic networks. The purpose of this chapter is to examine how far South Asia has participated in this process, using the extent of trade and capital market integration as the criteria, as well as the fundamental changes that have occurred in those sectors, as they have been driving the globalisation process world-wide.

Until the last decade, South Asia was one of the least integrated regions in the world economy. Following independence, most countries in the region favoured development strategies which limited the region's participation in the global economic system. Historical circumstances clearly played a role, as South Asia's colonial heritage fostered the sentiment that a more open economy, as under British rule, would lead to exploitation. India led the way in pursuing inward-oriented policies that accorded the state a dominant role in directing economic development and limited the development of the private sector. A vast network of government controls and subsidies emerged to manage economic decision-making as well as economic assets, comprising the well-known panoply of overvalued exchange rates, quantitative restrictions and tariffs, and industrial regulations associated with import-substitution industrialisation (Bhagwati 1993). Although Pakistan initially pursued more outward-oriented policies based on private sector development, it eventually followed suit, as did other countries in the region. By the 1970s, all South Asian countries were pursuing inwardly-focussed development strategies.

By the late 1980s, however, the situation was fundamentally altered. Confronted by lagging growth rates and external payments crises, the majority of South Asian countries adopted a more outward-oriented development strategy, emphasising greater integration with the world economy. The system of import-substitution based on controls and incentives was gradually replaced by: (i) near current account convertibility; (ii) reductions in the level of quantitative restrictions and tariffs, as well as more uniform rates of protection; (iii) improved incentives for exports; and (iv) a more hospitable environment for foreign investors. Although it is difficult to date the beginning of reforms exactly, Bangladesh and Sri Lanka began reforming first during the late 1970s, while Pakistan and India began last, starting in 1991. By the early 1990s, all countries had begun reforms to make their economies more open.

What has been the effect of these changes? Have they helped in bringing about a greater integration of South Asian economies into the world economy?

Trade integration

Level of trade integration

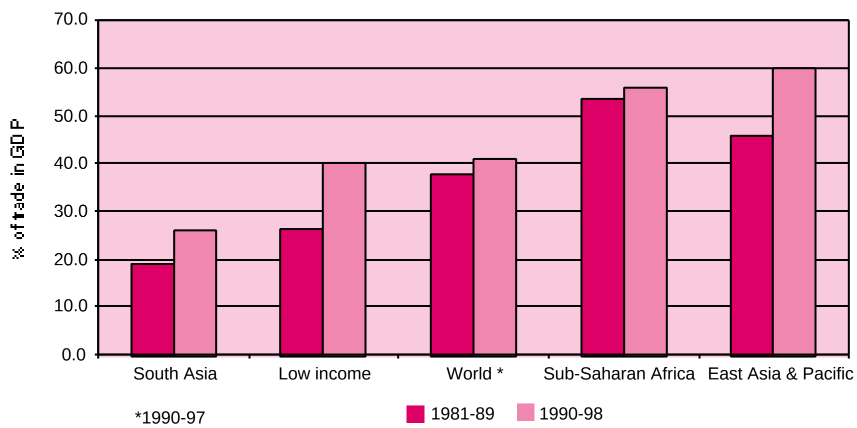
Integrating the region's trade flows more closely into international markets has been a fundamental focus of the liberalisation efforts in South Asia. One way to measure the level of this integration is to examine import tariff rates, which serve as a proxy for the difference between domestic and international prices. According to this indicator, South Asia has become more integrated into the world trading system over the last decade. Average tariff rates, which were among the highest in the world at the start of the 1990s, fell rapidly in all countries by the end of the decade. The decline has been particularly dramatic in Bangladesh, where average tariff rates fell from 114 per cent to 22 per cent, and in India, from 82 per cent to 32 per cent (table 2.1). The 1990s also saw all South Asian countries reduce the level of non-tariff barriers (Panagariya 1998; Kemal 2001). Nevertheless, South Asia remained less integrated in terms of this indicator than other developing regions. At the close of the 1990s, average tariff levels still hovered around 20 per cent, compared to 9 per cent or less in Korea and Malaysia, and 14 per cent or less in Brazil and Mexico (table 2.1).

Table 2.1 Mean unweighted tariff rates (%)

		All products	Primary products	Manufactured products
Bangladesh	1989	106.6	79.9	110.5
	1999	22.0	22.4	22.0
India	1990	79.1	69.6	80.3
	1999	32.2	30.5	32.4
Nepal	1993	24.0	15.7	26.0
	1999	17.7	12.9	18.9
Pakistan	1995	50.7	44.5	51.4
	1998	46.5	42.7	46.9
Sri Lanka	1990	28.3	31.8	27.9
	1997	20.1	23.9	19.7
Memo Items				
Korea	1990	13.3	15.7	12.7
	1999	8.7	12.8	7.8
Malaysia	1991	16.9	15.3	17.8
	1997	7.1	6.0	7.5
Brazil	1991	25.1	19.8	26.3
	1999	13.6	10.8	13.9
Mexico	1991	13.2	12.2	13.3
	1999	10.1	11.5	10.0

Source: World Bank 1998, 1999a, 2000c, 2001.

Figure 2.1 Improving trade to GDP ratios



Source: World Bank, World Development Indicators CD-ROM, 2000.

Another indicator of the degree of trade integration is the share of trade in national income. Countries that are highly integrated in the world economy tend to exhibit a high trade to GDP ratio. The trend along this indicator also shows an increasing level of trade integration in South Asia (figure 2.1). Trade to GDP ratios for the region as a whole rose from 19 per cent during the 1980s to 26 per cent during the 1990s.[1] The rate of integration has been rapid, with trade to GDP ratios increasing from an average of 0.1 per cent per year during the 1980s to 3.6 per cent per year during the 1990s, only slightly slower than East Asia (5 per cent), but faster than Latin America (2.2 per cent) (see annex table 1). Again, when viewed in a comparative context, however, South Asia remained among the least integrated regions; its overall trade to GDP ratio four times less than that in

[1] It must be kept in mind that trade to GDP ratios are an imperfect measure, subject to systematic influences, such as a country's size (varying inversely), and to movements in real exchange rates. Examining the PPP-adjusted trade to GDP ratios tells a slightly different story (see annex table 2). They report very little change in the share of trade to GDP in South Asia between the 1980s and 1990s, as well as lower ratios for other regions as well. But the PPP corrected ratios are a conservative measure because the GDP of many developing countries is larger in PPP terms than at official exchange rates. The actual change in South Asia's trade to GDP ratios is therefore likely to fall somewhere in between the nominal and PPP-adjusted ratios, the former serving as an upper bound and the latter a lower. That is, South Asia's trade to GDP ratios have most likely increased, but less than reported by nominal figures.

East Asia and sub-Saharan Africa (figure 2.1).

Export performance

To reap benefits of globalisation as well as to ensure a balanced integration with the external economies, it is absolutely essential to improve the performance of the export sector. Empirical studies have shown that export growth promotes efficient allocation of resources, as well as generating dynamic sources of growth, for example, by raising productivity (Srinivasan 1998). How have South Asian exports performed since the period of trade liberalisation?

South Asia's export performance has improved rapidly. The share of exports in regional GDP expanded from 7.6 per cent during the 1980-84 period to 12.4 per cent during the 1995-98 period

Compared to the era before reforms, South Asia's subsequent export performance has improved rapidly. The share of exports in regional GDP expanded from 7.6 per cent during the 1980-84 period to 12.4 per cent during the 1995-98 period (annex table 2). As this occurred during a time of positive GDP growth, the increase indicates real export expansion. Exports grew extremely fast at 10 per cent per annum during the 1990s, almost double the rate a decade earlier and among the highest in the developing world (annex table 3). The increasing importance of exports was especially evident in Bhutan, Nepal and Sri Lanka, unsurprising given their small size, but was also the case throughout the region. In India, for example, exports as a per cent of GDP nearly doubled from about 6 per cent at the start of the 1980s to 11 per cent at the end of the 1990s.

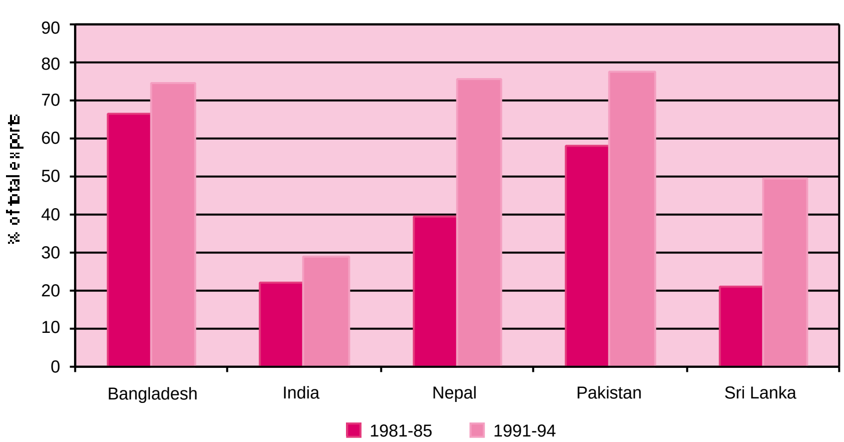
Part of the reason for this extremely fast export growth during the 1990s lies with the changes in real exchange rates. Between 1990 and 1996, the real effective exchange rate depreciated by nearly 30 per cent in India, 15 per cent in Nepal, and Bangladesh, and 10 per cent in Pakistan, making exports more competitive (annex table 4). Sri Lanka was the exception, with the exchange rate appreciating around 10 per cent over the first half of the 1990s. Despite becoming more competitive, South Asia's share of total world exports remained minimal both before and after reforms, comprising only about one per cent, up from half a per cent a decade earlier (annex table 5). In comparison, the relevant shares for East Asia and Latin America in 1997 were 8.7 per cent and 4.4 per cent, respectively.

Export structure

Export expansion, however, is only half of the story. Equally important is how the export structures have changed in response to new opportunities in the global trading system. Historically, fast-integrating countries, such as those in East Asia, have progressively increased the share of manufactured goods in merchandise exports. Over the past two decades, South Asian merchandise exports have also followed this trend, gradually shifting away from primary commodities, such as, unprocessed cotton, jute and tea, towards more manufactured goods. The share of manufactured goods in the region's total merchandise exports grew from 53.8 per cent in 1980 to nearly 77.6 per cent in 1997, comparable to the world (79.6 per cent) and East Asian ratios (82.4 per cent) (annex table 6). The ratio in 1998 ranged from 91 per cent in Bangladesh to 73 per cent in Sri Lanka.

Within manufactures, labour-intensive goods, such as garments and textiles,

Figure 2.2 Share of clothing and textiles in total exports



Source: World Bank 1997a.

gems and jewellery and leather products, dominated manufactured trade (see, e.g., World Bank 1997a). Fibres, textiles and clothing, in particular, have become extremely important to South Asia's exports. Their share increased in all countries for which data is available, comprising nearly three-quarters of all exports by the mid-1990s in Bangladesh, Nepal and Pakistan, and nearly half in Sri Lanka (figure 2.2).

Given the importance of textiles and clothing in exports, the gradual phasing out of the Multi-Fibre Arrangement (MFA) by 2005 holds important consequences for South Asia's world shares in these sectors. The potential effect of removing the imposed quotas on exports of garments to developed countries depends on a number of factors, but the gains to South Asian countries from phasing out of the MFA are expected to be large because they are severely constrained by quotas and are among the lowest cost producers (see, e.g., ESCAP 1998b). The largest gains will most likely be in India, which has the most constrained apparel sector in South Asia. Other South Asian countries will also benefit from abolition of quotas, but less so, as they are typically less-restricted suppliers.

While these labour-intensive industries are a source of growth in employment and exports, and historically have been important for the industrialisation process in other countries (e.g., the UK and Japan), what is particularly important in the age of rapid globalisation is the extent to which countries are moving from traditional exports to producing goods of higher value-added, particularly technologically advanced products. There has been growing concern that labour intensive, low-technology manufactures are beginning to acquire the features of primary commodities in world markets, facing a secular downward trend (UNCTAD 1999a). In South Asia, the share of high technology exports has been marginal, rising slightly from 2.1 per cent of total manufactured exports in 1991 to 3.85 per cent in 1997 (table 2.2). In contrast, high-tech exports rose rapidly in East Asia and Latin America during the 1990s, accounting for nearly one-quarter and one-tenth of total exports, respectively. India is the country with the fastest growing share of high-technology exports.

Table 2.2 Share of high technology exports in manufactured exports

	1991	1992	1993	1994	1995	1996	1997
Bangladesh	0.05	0.06	0.02	0.07	0.03	0.06	0.01
India	3.07	2.32	2.63	3.20	4.52	5.38	5.09
Pakistan	0.03	0.04	0.07	0.04	0.05	0.05	0.10
Sri Lanka	0.67	1.05	1.12	1.27	n/a	n/a	n/a
South Asia	2.08	1.56	1.82	2.30	3.36	3.99	3.85
Memo Items							
East Asia & Pacific	20.64	16.93	19.12	20.52	23.40	25.02	26.60
Latin America & Caribbean	5.63	6.79	6.64	7.45	8.87	9.04	9.55

Source: World Bank, World Development Indicators CD-ROM, 2000.

An area of increasing importance for exports in all countries has been in the services sector. Although the trade in goods has traditionally dominated, trade in services has increased in importance as a result of reductions in domestic and international barriers brought about by the General Agreement on Trade in Services (GATS), and technological changes that have made services more tradeable. Exports of services in the region doubled from US$5 billion per year during the 1980s to more than US$10 billion per year during the 1990s, although they still account for only one per cent of the world's total (annex table 7). An important service export from the region has been the supply of labour to other countries, particularly to those in the Middle East and East Asia. Their remittances have formed a very important source of foreign exchange for most South Asian countries, and are among the highest in the world, growing from roughly half a billion dollars per year during the 1980s to more than one billion during the 1990s (annex table 8). Given the importance of these remittances, the restrictions to the free flow of labour in other countries remain a concern for South Asia.

Table 2.3 Percentage of total exports accounted for by top three products

	1983-84	1994-95
Bangladesh	56.4	46.3
India	30.7	24.5
Maldives	n.a.	64.0
Nepal	36.7	80.9
Pakistan	35.0	41.4
Sri Lanka	69.0	38.1
Korea	36.1	25.0
Malaysia	48.7	28.8
Singapore	41.1	37.8

Source: UNCTAD 1999b.

Export diversification

Increasing trade integration requires a well-diversified export base, geographically as well as by product. Dependence on a few exports and export markets increases significantly the risks associated with market fluctuations. South Asian economies have increasingly become less dependent on primary commodity exports, increasing the share of exported manufactured goods as described above. Only Bhutan and the Maldives still had primary commodities comprising more than 50 per cent of total exports during the 1990s (ESCAP 1997b). Most South Asian economies have, therefore, decreased their vulnerability to events in commodity markets.

Export vulnerability, however, can also result from dependence on a limited number of export products. A high dependence on a few exports can render countries vulnerable to variations in export earnings and economic performance, independent of whether exports are primary commodities or manufactured goods. Although most South Asian countries have shifted away from primary commodities, their export structures remain relatively concentrated into a limited number of exports (table 2.3). The percentage of total exports accounted for by the three most important products in 1994-95 was above 60 per cent in the Maldives and Nepal, and 40 per cent or more in Bangladesh and Pakistan. Only India had a ratio of less than 30 per cent, comparable to that found in high-exporting countries of East Asia. Nepal, Maldives and Pakistan's concentration indices all rose during the 1990s, suggesting increasing exposure to export risk. The major source of the region's export concentration has been, as already mentioned, the textile and clothing industries, which in some countries accounted for more than 75 per cent of export revenue. The concentration of exports on cotton fibre, fabric and garments leaves countries not only vulnerable to swings in cotton prices, but also to production failures, for instance, from drought, disease, and pests. In Nepal, the situation has been precarious with just one product, carpets, accounting for more than half of all merchandise earnings (UNCTAD 1999b).

Export diversification can also be judged in terms of the destination of exports. The 1990s saw a redirection of the region's exports away from Eastern Europe and developing countries, and an increasing concentration towards developed countries, which absorbed nearly 50 per cent or more of total exports (annex table 9). The United States and European Union have become especially important markets for Bangladesh, Pakistan and Sri Lanka, and East Asian countries markets for India. The growing concentration of exports to industrial countries has been particularly acute in Bangladesh and Sri Lanka, where they make up more than three-quarter of total exports.

Intra-regional trade

The low level of exports directed at developing countries is especially evident in the level of intra-regional trade in South Asia. As discussed in chapter 5, intra-regional trade can convey many benefits. For example, it can reduce transactions costs associated with linguistic and cultural differences, as well as unfamiliarity with administrative and legal systems (ESCAP 1997b). It can also stimulate trade-creating opportunities through regional spill-overs and other complementarities. More importantly, perhaps, it can also create opportunities for cooperation in other areas, such as in the political arena. Despite these potential gains, the level of trade between South Asian countries has been low. At the end of the 1990s, trade between South Asian countries barely accounted for 5 per cent of the region's total trade in 1998, up from only 2 per cent at the start of the decade (annex table 10). This is in stark contrast to the 40 per cent or more of total trade accounted for by trade between neighbouring countries in the East Asian and NAFTA regions. The level of South Asia's intra-regional trade, however, is likely to be much higher than reported by official statistics, as illegal trade between neighbours is thought to be substantial, particularly between Bangladesh and India, and between India and Nepal (ESCAP 1997a). Moreover, within the past decade, several countries have become more reliant on South Asian markets for exports and imports. India, for example, has become an increasingly important export destination for Nepal, absorbing 33 per cent of total Nepalese exports in 1998, up from just 7 per cent in 1990 (annex table 11). Similarly, Bangladesh, Nepal and Sri Lanka have more than doubled their imports from India (annex table 12). India's imports from South Asia as a whole, however, have failed to keep pace, and accounted for only one per cent of its total import bill in 1998.

External payments situation

Balance-of-payment concerns have traditionally played a decisive role in the design of trade policies in South Asia. During the period of import substitution, policy makers utilised high rates of protection, export subsidies, and foreign exchange controls as a means to manage trade balances and current account deficits. A fundamental consequence of adopting more liberal trade policies, however, has been the relaxation of such controls. What has been the effect on the external payments situation in South Asia?

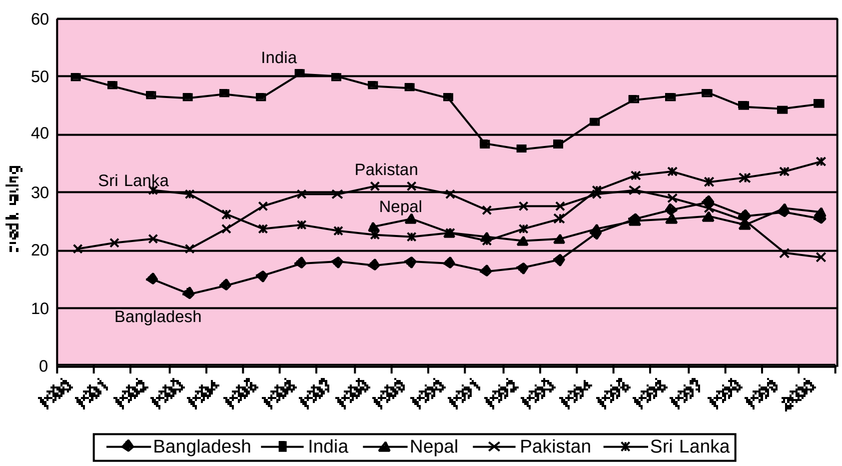
Although a deterioration in the trade balance generally accompanies trade liberalisation due to a surge in imports, South Asia's trade deficit actually improved from an average of -4.6 per cent of GDP during the 1980s to -3.5 per cent during the 1990s, the result of strong and sustained export growth that outpaced import growth by one per cent per year on average (annex tables 13 and 14). The current account moved broadly in line with the trend in the trade balance, remaining in deficit over the past two decades (annex table 15), but also improving during the 1990s in all countries except Nepal and Pakistan, the latter as a result of international sanctions imposed following nuclear tests. There was large variation in current account deficits, though, ranging from quite low in India (1.2 per cent of GDP) during the 1990s, to quite high in Bhutan (13.3 per cent). The external payments situation in most countries remains vulnerable to cyclical downturns, as most have poorly diversified export bases. In addition, in Bangladesh, Sri Lanka and Nepal, net food importers, remain vulnerable to changes in prices of food imports, while India and Pakistan remain susceptible to oil price and supply shocks due to their relatively high reliance on imported energy (see, e.g., ESCAP 2000).

Financial integration

South Asia's attempts to integrate more closely into the world economy have encompassed not only trade reforms, but liberalisation of the financial sector as well

South Asia's attempts to integrate more closely into the world economy have encompassed not only trade reforms, but liberalisation of the financial sector as well. The rationale for opening up domestic financial sectors to external flows lies with the ability of foreign capital to ease a country's foreign exchange constraint and increase its capacity to import, although considerable risks are attached, such as exposure to external volatility and restrictions on monetary policy. To varying degrees and

Figure 2.3 Institutional Investors credit ratings, 1980-2000



Source: Institutional Investor, various issues.

at different times, policy initiatives in South Asian countries have, nevertheless, begun to deregulate financial markets, introducing convertibility on the current and capital accounts, making exchange rates flexible, and liberalising investment regimes. How financially integrated has South Asia become as a result? And what have been the trends in external financing to the region in the era of rapid globalisation?

Level of financial integration

The degree of South Asia's integration into international financial and capital markets can be measured in several ways. One is to measure countries' ability to attract private external financing, as reflected in the ratio of FDI and portfolio flows to GDP. Another is to examine countries' access to international financial markets as reflected in their credit ratings. More highly integrated countries generally have better ratings, allowing them to borrow at lower rates, for longer maturities, and to access more diversified sources of funds. According to this measure, the South Asian region has become more financially integrated over the past decade. Credit ratings, as compiled by the Institutional Investor, have improved steadily since the early 1990s, indicating improved access to external sources of finance, although Pakistan has been the exception, with declining ratings starting in the middle of the decade (figure 2.3).

In order to judge the level of financial integration, credit ratings below 20 can be taken to indicate low access (and therefore, integration), above 50 high access and, in between, medium access (World Bank 1997a). According to this criterion, Bangladesh, India, Nepal and Sri Lanka have reached a 'medium' level of integration, with India nearing the 'high' category, while Pakistan has become less integrated in recent years, falling from the 'medium' to 'low' categories (figure 2.3).

Financial integration can also be judged by the development of new types of financial markets in the economy. In countries with a low degree of financial integration, the development of stock markets and other markets is weak, while in more integrated economies, equity markets are well developed and play an important role in financing. In South Asia, stock markets have grown rapidly since financial sector liberalisation (annex table 16). Capitalisation of stocks in the region has nearly tripled in value over the last decade, and doubled as a per cent of regional GDP. Moreover, the number of domestic companies listed on stock exchanges has doubled since the early 1990s to more than 7000, greater than in any other developing region. Comparatively, however, financial integration through stock market development in South Asia is still relatively underdeveloped, with the capitalisation of stock markets among the lowest in the developing world, only one-fifth and one-quarter the value of those found in East Asia and Latin America, respectively (annex table 16).

Trends in overall resource flows to South Asia

Aggregate net resource flows to South Asia have expanded rapidly since financial reforms, rising from an average of US$8.6 billion per year during the 1980s to US$11.9 billion per year during the 1990s (annex table 17). What is significant about this increase has been its changing composition. In contrast to the 1970s and 1980s, when public funds in the form of official loans were the main source of external finance, private capital flows have come to dominate these flows over the past decade. Their share of total net resources rose from less than a third during the 1980s to more than half during the 1990s. At their height in 1997, private capital flows were three times the value of official flows. Despite this increase, South Asia's share of total private capital to developing countries has declined over the past decade, falling from 7 per cent during the 1980s to 3 per cent in the 1990s (figure 2.4).

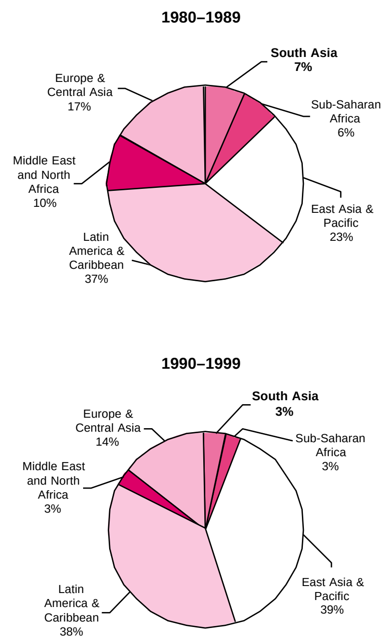
Foreign Direct Investment

Over the last decade, the composition of private capital to South Asia has also changed markedly. In contrast to the start of the 1990s, when private debt flows comprised the majority of total private capital to the region, non-debt flows came to form over 70 per cent by the decade's end (annex table 17). A primary component of these non-debt flows has been foreign direct investment (FDI). Empirical evidence has shown that FDI has a positive impact on the economic growth of host countries, more so than other types of external flows and domestic investment, as a result of various inter-related factors including improvements in productivity, technology transfer, research and development expansion, and promotion of exports (Blomström *et al.* 1992). Compared to other types of investments, FDI flows also tend to be relatively more stable, typically based on a long-term view of the market and growth potential of recipient countries, and relatively difficult to disinvest, reducing the risks of sharp reversals during adverse situations. Most countries in the region have reformed their investment regimes to encourage these inflows by reducing foreign ownership restrictions, domestic-equity and licensing requirements, and introducing fiscal and financial incentives.

In response to these measures and owing to improving macroeconomic fundamentals more generally, the flow of foreign direct investment to South Asian countries has increased over the past decade. Most of these flows have originated from either the developed countries or the newly industrialised countries of East and Southeast Asia. The United States and Europe have been the main providers of FDI to India and Pakistan during the 1990s, while Japan, Hong Kong, Korea and Malaysia have been important for Bangladesh and Sri Lanka (World Bank 1997a and ESCAP 1998a). Their average value increased ten-fold from US$256 million per year during the 1980s to US$ 2.1 billion per year during the 1990s (annex table 18). Annual average growth rates were also among the fastest in the developing world, increasing from 25 per cent per year to 31 per cent over the last two decades, attesting to increasing and rapid financial integration. In relative terms, however, the increase in FDI to South Asia has been more modest, accounting for less than half a per cent of regional GDP during the 1990s, compared to 2.7 per cent for East Asia, 1.9 per cent for Latin America, and 1.4 per cent for sub-Saharan Africa (annex table 18). South Asia has also had the lowest ratio of FDI to gross domestic investment, roughly four times less than those found in East Asia, Latin America and sub-Saharan Africa.

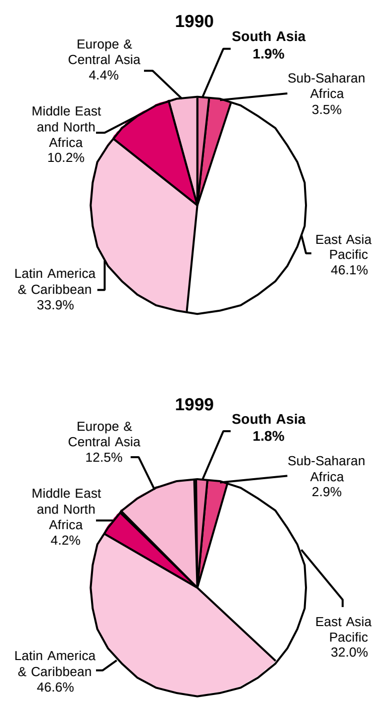
Cross-regional comparisons, moreover, point to South Asia's stagnating share of total FDI to developing countries. During the 1990s, South Asia's share of these flows remained less than 2 per cent of the developing countries' total, the lowest among developing regions (figure 2.5). In contrast, Central and Eastern Europe, Latin America, the Middle East and North Africa, and sub-Saharan Africa all managed to increase their shares over the same period. The distribution of FDI within South Asia has also become more

Figure 2.4 Private capital to developing countries



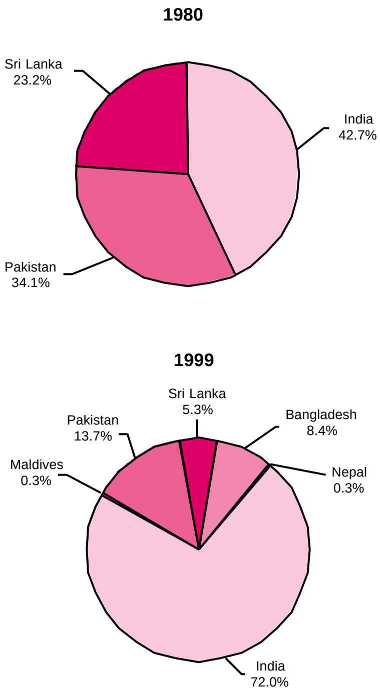
Source: World Bank 2000a.

Figure 2.5 South Asia's share of FDI to developing countries



Source: World Bank 2000a.

Figure 2.6 Distribution of FDI in South Asia



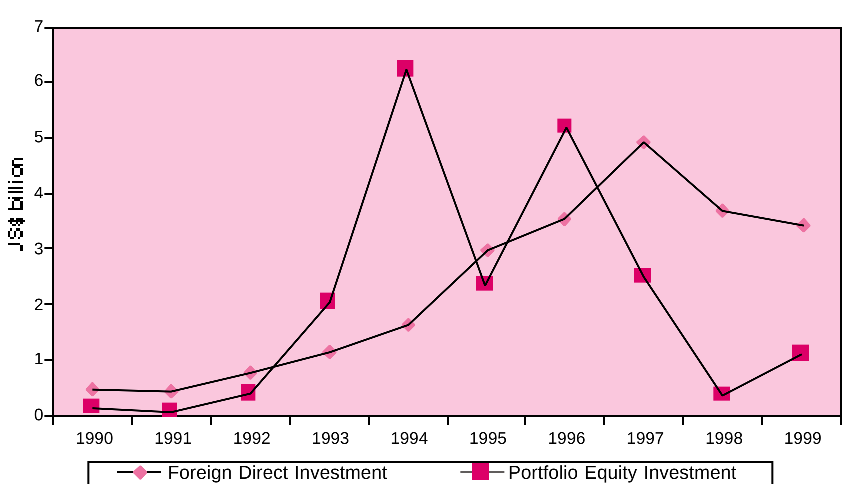
Source: World Bank 2000a.

concentrated over time. While India received roughly 40 per cent of total FDI to the region in 1980, its share expanded to more than three-quarters of the total, with the share of other countries dropping accordingly (figure 2.6). Pakistan's reduction has been particularly acute, dropping from 34 per cent in 1980 to 14 per cent in 1999.

The sustainability and usefulness of FDI for a country relates not only to its aggregate levels, but also to its uses. Given its labour surplus and comparative wage advantage, the kind of FDI most likely to bring the strongest benefits to long-term growth in South Asia is that associated with manufacturing (World Bank 1999a). While the majority of foreign investment funds have in fact been directed to manufacturing sectors in most South Asian countries, their shares have been declining. In 1990, 85 per cent of flows in India went to manufacturing, however, in 1995 this figure dropped to 59 per cent (World Bank 1997a). Similarly, in Sri Lanka, the share of FDI directed to manufacturing fell from 60 per cent of cumulative FDI from 1978 to 1993, to 55 per cent afterwards (World Bank 1997a). FDI to Pakistan, meanwhile, has increasingly gone to natural resource exploration, most notably in the oil and energy sectors, which carries fewer benefits in terms of new technologies and human capital improvement (World Bank 1997a).

What is also important in assessing the potential benefits of FDI for host countries is the degree to which investment is being allocated to export sectors. The available information indicates that a relatively small portion of FDI has gone to export-oriented sectors in South Asian countries; most FDI is targeted at industries producing for domestic markets. In India, for example, textiles, an important source of exports as well as employment, has attracted less than 4 per cent of total FDI in the mid-1990s (annex table 19), while in Sri Lanka, the share of textiles has lost ground to agricultural products and beverages (World Bank 1997a). In Pakistan, by the mid-1990s, less than US$100 million had been invested in the Karachi Export Processing Zone since its inception in the early 1980s (World Bank 1997a). These trends strongly contrast the pattern of FDI use in other regions (e.g., East Asia), and suggest that South Asia may be benefiting proportionately less from the trend toward the globalisation of production. The only exception is Bangladesh, which has been fairly successful in attracting FDI to its export processing zones, particularly in the ready-made garment sector (ESCAP 1998a).

Figure 2.7 FDI and portfolio equity investment to South Asia, 1990-99



Source: World Bank 2000a.

Portfolio equity flows

The other major component of private non-debt flows to South Asia has been portfolio equity investments. Even though it is widely accepted that developing nations have benefited from inflows of FDI, the verdict is less clear regarding portfolio flows (Claessens *et al*. 1995). There are clear benefits to portfolio flows and from opening stock markets to foreign investors, including wider access to international capital at lower cost, risk sharing and pricing, and greater efficiency in the allocation of capital. But there are also substantial risks. Portfolio investments are more volatile than FDI, representing short-term assets that can be withdrawn quickly from the economy. As the liquidity crises in Mexico (1995) and East Asia (1997) have shown, countries with high levels of portfolio investment are vulnerable to massive outflows of capital when investor sentiments quickly change, leading to possible currency and financial crises. Moreover, the volatility associated with portfolio equity flows also renders countries more exposed to shocks in the international economy, such as changes in the interest rates and stock market returns, particularly where capital markets are small and inflexible, and institutional frameworks incomplete or inadequate.

Given these risks, the rising share of portfolio investments in South Asia is a source of concern. Although their amount has dropped since the East Asian financial crisis in 1997, the level of portfolio equity investment to South Asia over the last decade had risen from negligible amounts to US$6.2 billion at their peak in 1994, accounting for nearly 70 per cent of all private capital flows that year (annex table 20). Even though their share in net private flows has generally averaged less, roughly 30 per cent per year during the 1990s, their volatility still renders countries in the region vulnerable to shocks. Since the 1990s, there have been two sharp reversals of net portfolio investment, in 1995 and 1998, when the value of such flows dropped by more than 60 and 90 per cent of the previous year's value, respectively. In contrast, FDI to the region over the same period followed an increasing trend, with only slight variations since the East Asia crisis (figure 2.7). India has received the bulk of portfolio equity flows, accounting for US$4.4 billion alone in 1996, 85 per cent of the region's annual total, reflecting its maturing stock market and the presence of well established corporate names on its exchange. Pakistan, until the mid-1990s received the second largest amount, but has received declining shares since due to its worsening macroeconomic conditions and political instability. Bangladesh and Sri Lanka have received small shares due to the relatively early stage of their stock market development.

Prevention of financial crises: Lessons from East Asia

The record of developing countries integration into financial markets over the past decade suggests that the risk of financial crisis rises sharply with financial liberalisation and integration. The costs of these crises can be severe, both in terms of lost output and social costs. Although considerable debate surrounds the exact causes precipitating systemic crisis, there is a general consensus that the following factors exercised a role in varying degrees in the 1997 East Asian crisis: (i) macroeconomic policies that exacerbated financial risks; (ii) financial sector weakness, particularly weak domestic bank regulation and supervision; and (iii) short-term capital flows (see, e.g., ESCAP 1999; World Bank 1999a; UNCTAD 1998). Although financial sector integration in South Asia has yet to reach the level experienced in most East Asian economies, rendering the risks of financial crisis and contagion less, it is none the less instructive to analyse the South Asian economies along these categories.

The risk of financial crisis rises sharply with financial liberalisation and integration

(i) Poor macroeconomic policies appear to have played a considerable role in leading to financial turmoil in East Asia. Prior to the crisis, most countries in the region ran large external and internal imbalances, aggravated by fixed or pegged exchange rates that created adverse incentives to over-borrow and limited the effectiveness of monetary policy to adjust large inflows (ESCAP 1999). In this respect, most South Asian countries appear to be less susceptible, most having had improving external balances since financial sector reforms buoyed by strong export growth as discussed earlier. Moreover, the two largest economies in the region, India and Pakistan, have moved to more flexible exchange rates

Greater economic integration has yet to translate into sustained growth for a majority of countries

(independent floating and managed floating, respectively), with other countries in the region (viz., Bangladesh, Bhutan, Maldives, Sri Lanka) pegged to the Indian rupee, which may limit some of the boom-bust effects of capital flows (Corbo and Hernandez 1996).

(ii) Weakness in financial and corporate sectors has also been blamed for the onset of crisis. Inadequate supervision or regulation of domestic banking systems in East Asia created conditions for excessive risk taking by lenders and borrowers. In particular, loans were not made on the basis of strict business standards, but on so-called 'crony capitalism', with political influences interfering with loan allocations. In this regard, most South Asian countries are still relatively vulnerable, as bank supervision, accounting standards, and legal infrastructures remain weak (Nayak 1995, and ul Haque and Kardar 1995). In Pakistan, for example, financial regulatory bodies have limited autonomy in enforcing regulations, and tend to focus on monitoring compliance with ratios rather than prudential regulations, such as conflicts of interests and moral hazard (ul Haque and Kardar 1995). Nevertheless, the banking sector in most countries has not been allowed to fuel large domestic credit booms, and most have instituted regulatory reforms. In Nepal, for example, the government is in the process of opening local markets to international accounting and auditing firms (ESCAP 2000).

(iii) Lastly, short-term capital inflows have also been linked to the financial crisis in East Asia. Preceding the crisis in most East Asian countries, there was a surge in volatile short-term capital inflows in the form of short-term debt and portfolio equity flows, which subsequently reversed when investors panicked. In this regard, South Asian countries have experienced a worsening trend, as portfolio flows during the 1990s have risen sharply to account for a large portion of private capital to the region, as described earlier. Nevertheless, the risks from short-term capital flows in most countries are still comparatively low. The continued existence of capital controls in most countries has limited exposure to short-term foreign debt, and the offshore forward markets for currencies in all countries remain thin and hard to use for speculative purposes (World Bank 1999b).

Economic performance during globalisation

Given that South Asia has experienced greater integration with the world economy, what has been the impact on economic performance so far? Closer integration in the global economy is expected to lead to faster economic growth. Increasing trade and financial openness theoretically improves a country's allocation of resources along its comparative advantage, exposing previously restricted sectors to increased competition, investment and technology, thereby raising long-term growth prospects.

From the record to date, it is unclear whether greater integration has benefited growth in South Asia. When comparing GDP growth in the region between the two periods, growth has, in fact, been slightly lower during the 1990s than the 1980s (table 2.4). The record of growth in individual countries also points to a mixed picture. Three countries—Bangladesh, Nepal and Sri Lanka—experienced higher average growth during the 1990s than in the earlier period, but another three—Bhutan, India and the Maldives—had slightly lower rates. India's growth rate has, however, picked up during 1999-2000, reaching almost 7 per cent. Pakistan had the worst record of all, with growth rates dropping from among the highest during the 1980s to among the lowest in the next decade. It therefore, appears that greater economic integration has yet to translate into sustained growth for a majority of countries. It must be kept in mind, however, that many of the benefits of increased integration may be long-term, and can be expected to surface only with a lag.

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Globalisation has become an increasingly dominant feature over the past decade, as more nations are becoming integrated into the global economy through trade and capital flows. South Asian economies have also begun to participate in the process, pursuing market-oriented policies and reducing barriers to trade and investment. Despite rising shares of trade and capital flows in national income, South Asia remains among the least integrated regions in the world. South Asia's exports are still more than seven times lower on a per capita basis than in East Asia, and barely account for one per cent of the world's total. Private capital flows to South Asia are also ten times less than in East Asia and Latin America, and South Asia's share of the developing countries' total has actually decreased over the past two decades. Moreover, wide disparities characterise the globalisation process within the region, as foreign direct investment and portfolio flows have become increasingly concentrated in India, with other countries in the region lagging behind.

Table 2.4 GDP Growth (%)

	1980-1984	1985-1989	1990-1994	1995-1998	1980-1989	1990-1998
South Asia	5.7	6.0	4.9	6.0	5.8	5.4
Bangladesh	4.9	3.6	4.7	5.2	4.3	4.9
Bhutan	7.7	7.4	6.0	6.8	7.5	6.3
India	5.6	6.3	4.9	6.6	5.8	6.0
Maldives	n.a.	8.9	8.6	6.7	8.9	7.7
Nepal	3.3	4.9	5.4	4.0	4.1	4.8
Pakistan	7.3	6.4	4.7	3.7	6.9	4.2
Sri Lanka	5.1	3.2	5.5	5.1	4.1	5.3

Source: World Bank, World Development Indicators CD-ROM, 2000.

Although the potential benefits to greater integration in terms of economic growth have yet to surface, the potential costs of becoming marginalised from the global economy may be great in terms of lost efficiency, technology and growth that globalisation could ultimately bring. If South Asia is to avoid such costs, and take advantage of the global trend towards integrated economic activity, reforms must keep apace to sustain trade and financial integration in the region, while at the same time minimising the risks of greater integration. In the context of minimising risks, we need to see the impact of economic reforms during the period of globalisation on the people in South Asia. The next chapter addresses this concern.

Annex Tables: On trade and financial statistics

Annex Table 1: Trade to GDP ratios (%)

	Nominal level		Annual average change		PPP-adjusted level		Annual average change	
	1981-89	1990-98	1981-89	1990-98	1981-89	1990-98	1981-89	1990-98
East Asia & Pacific	45.8	60.1	1.0	5.0	14.6	15.9	-2.5	1.4
Latin America & Caribbean	26.0	29.0	0.3	2.2	10.9	14.9	-3.7	7.4
Middle East & North Africa	60.3	63.1	-2.6	-0.5	30.9	20.7	-10.3	-0.6
South Asia	19.4	26.3	0.1	3.6	4.9	4.7	-4.5	1.3
Bangladesh	20.8	25.4	-0.4	6.3	4.9	5.6	-4.1	4.8
Bhutan[a]	66.0	75.3	7.9	0.5	28.2	21.5	0.4	-0.6
India	14.5	21.9	1.0	4.7	3.8	3.6	-3.9	1.4
Maldives[b]	100.4	n.a.	8.3	n.a.	29.6	34.9	2.3	0.8
Nepal	31.7	49.8	0.9	7.0	5.8	6.6	-2.2	3.9
Pakistan	34.3	38.7	-0.2	0.3	11.7	9.1	-5.8	-1.3
Sri Lanka	65.9	76.0	-3.2	2.3	13.7	15.7	-6.0	5.5
Sub-Saharan Africa	53.7	56.3	-1.6	1.2	19.7	16.8	-9.0	1.3
Low income	26.5	40.3	1.9	5.3	8.9	7.9	-7.1	2.1
World[c]	38.0	41.2	-0.4	2.1	22.4	26.3	-3.4	3.4

a: relevant intervals for PPP-adjusted figures are 1990-97
b: relevant intervals for PPP-adjusted rates are 1985-89 and 1986-89 for rate of change based on PPP adjusted figures
c: 1990-97

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 2: Exports of goods and services (% of GDP)

	1980-84	1985-89	1990-94	1995-98
East Asia & Pacific	21.5	24.0	27.6	34.1
Latin America & Caribbean	13.5	14.7	13.4	15.1
Middle East & North Africa	36.0	23.4	31.8	30.1
South Asia	7.4	7.6	10.6	12.4
Bangladesh	4.9	5.5	7.9	12.1
Bhutan	13.9	23.8	31.0	34.3
India	5.9	6.0	8.9	10.8
Maldives	20.8	31.8	n.a.	n.a.
Nepal	11.4	11.5	16.0	24.0
Pakistan	11.5	12.6	16.2	15.8
Sri Lanka	29.0	25.7	31.7	35.8
Sub-Saharan Africa	26.9	27.5	26.5	29.3
Low income	11.7	13.0	18.7	21.8
World	19.5	18.7	20.0	22.1

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 3: Exports of goods and services (annual % growth)

	1980-89	1990-98
East Asia & Pacific	10.1	12.5
Latin America & Caribbean	5.3	8.1
South Asia	6.3	10.0
Bangladesh	7.0	15.7
Bhutan	n.a.	n.a.
India	5.3	11.1
Maldives	n.a.	n.a.
Nepal	3.9	15.1
Pakistan	10.7	5.4
Sri Lanka	6.3	8.4
Sub-Saharan Africa	1.5	4.0
Low income[a]	6.0	10.6
World[b]	4.9	6.8

a:1982-89 b: 1990-97

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 4: Real effective exchange rates (1990=100)

	1990	1991	1992	1993	1994	1995	1996
Bangladesh	100	98.2	92.3	91.6	88.3	86.0	85.7
India	100	85.2	71.9	71.4	73.9	71.3	70.0
Nepal	100	90.5	88.6	84.3	84.6	79.7	80.6
Pakistan	100	98.1	96.8	96.5	94.3	93.6	91.8
Sri Lanka	100	104.8	104.5	106.2	106.5	101.4	110.2

Source: World Bank 1997a.

Annex Table 5: Share of world's exports (% of total)

	1980-84	1985-89	1990-94	1995-97
East Asia & Pacific	3.8	4.9	6.6	8.6
Latin America & Caribbean	3.8	3.9	3.9	4.2
South Asia	0.6	0.6	0.8	0.9
Sub-Saharan Africa	2.1	1.8	1.6	1.5
Other	89.7	88.7	87.2	84.8

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 6: Structure of merchandise exports

	Food		Agricultural Raw Materials		Fuels		Ores and Metals		Manufactures	
	(% total)		(% total)		(% total)		(% total)		(% total)	
	1980	1998	1980	1998	1980	1998	1980	1998	1980	1998
East Asia & Pacific	18.2	6.4	12.3	1.8	16.4	5.4	6.8	2.1	44.8	82.4
Latin America & Caribbean	32.3	25.4	4.3	2.9	31.1	12.8	12.3	9.1	19.7	49.2
Middle East & North Africa	3.2	4.1[e]	1.2	0.6[e]	87.4	76.0[e]	3.0	2.3[e]	6.1	16.9[e]
South Asia	28.0	15.5[f]	10.0	2.2[f]	2.8	1.0[f]	5.1	2.1[f]	53.8	77.6[f]
Bangladesh	12.0	7.0	19.0	2.0	0.0	0.0	0.0	0	68.0	91.0
Bhutan	92.0	23[d]	1.0	8.0[d]	n.a.	26.0[d]	0[a]	3[d]	4.0	40.0[d]
India	28.0	18[f]	5.0	2[f]	0.0	1.0[f]	7.0	3[f]	59.0	74.0[f]
Maldives	84.0	n.a.	5.0	n.a.	1.0	n.a	2.0	n.a.	9.0	n.a.
Nepal	21.0	10[f]	48.0	1.0[f]	n.a.	n.a	0.0	0[f]	30.0	77.0[f]
Pakistan	24.0	14.0	20.0	2.0	7.0	0.0	0.0	0	48.0	84.0
Sri Lanka	47.0	21[d]	18.0	4.0[d]	15.0	0[d]	1.0	1[d]	19.0	73[d]
Sub-Saharan Africa	22.3	n.a.	6.2	n.a.	26.5	n.a	8.6	n.a.	12.3	20.1[c]
Low income	16.3[b]	9.2	n.a.	1.9	32.5[b]	6.2	2.8[b]	2.5	39.0[b]	76.7
World	12.5	8.1	4.4	1.9	10.9	4.4	4.8	3.0	65.9	79.6

a: 1981; b: 1984; c: 1991; d: 1994; e: 1996; f: 1997

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 7: Service exports (current US$ billion)

	Average	Average	Average	Average	Average	Average
	1980-84	1985-89	1990-94	1995-98	1980-89	1990-98
East Asia & Pacific	11.9	21.2	46.9	96.7	16.6	69.1
Latin America & Caribbean	16.4	20.1	32.7	44.4	18.3	37.9
Middle East & North Africa	15.0	15.0	22.4	28.4	15.0	25.1
South Asia	4.5	5.4	8.2	13.7	5.0	10.6
Bangladesh	0.2	0.2	0.5	0.7	0.2	0.6
Bhutan	0.0	0.0	0.0	0.0	0.0	0.0
India	3.1	3.7	5.1	9.4	3.4	7.0
Maldives	0.1	0.1	0.1	0.3	0.1	0.2
Nepal	0.2	0.2	0.3	0.7	0.2	0.5
Pakistan	0.7	0.9	1.5	1.8	0.8	1.6
Sri Lanka	0.3	0.3	0.6	0.8	0.3	0.7
Sub-Saharan Africa	8.0	7.9	11.5	14.4	8.0	12.8
Low income	12.1	15.8	28.8	52.3	14.4	39.3
World	394.5	560.7	963.1	1,326.5	477.6	1,124.6

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 8: Average workers' remittances per year (US$ million)

	1980-84	1985-89	1990-94	1995-98	1980-89	1990-98
East Asia & Pacific	56	90	129	319	73	214
Latin America & Caribbean	145	282	691	1,170	213	904
Middle East & North Africa	557	668	1,119	1,159	612	1,137
South Asia	558	558	725	1,389	558	1,020
Bangladesh	41	60	88	135	50	109
Bhutan	0	0	0	0	0	0
India	254	234	410	1,000	244	672
Maldives	0	0	0	0	0	0
Nepal	4	6	6	10	5	8
Pakistan	234	225	165	156	229	161
Sri Lanka	25	34	55	89	29	70
Sub-Saharan Africa	74	84	105	202	79	149
Low income	641	643	935	1,878	642	1,354

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 9: Direction of exports (% of total), 1980, 1986 and 1998

		Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan	Sri Lanka
USA	1986	32.2	n.a.	27.7	n.a.	23.2	12.4	30.4
	1998	35.8	n.a.	20.9	33.7	25.9	21.6	38.3
European	1986	29.8	n.a.	27.8	n.a.	28.5	37.2	30.1
	1998	45.7	n.a.	26.5	23.5	33.1	30.7	29.4
Japan	1986	10.1	n.a.	14.6	n.a.	1.0	12.3	7.2
	1998	1.7	n.a.	5.1	9.2	0.7	3.4	4.7
East Asia and Pacific	1986	6.6	n.a.	8.7	n.a.	3.8	12.8	6.2
	1998	4.4	n.a.	15.4	13.3	0.2	14.7	5.3
East Europe	1980	8.0	n.a.	20.3	n.a.	20.5	3.8	4.2
	1998	1.3	n.a.	3.9	1.0	0.2	2.1	3.2
Developing Countries	1980	56.2	n.a.	30.1	n.a.	32.6	59.1	42.6
	1998	13.1	n.a.	41.6	3.16	36.9	39.9	21.3
Industrial Countries	1980	35.8	n.a.	49.2	n.a.	46.9	37.1	41.7
	1998	86.4	n.a.	56.5	68.4	61.3	60.1	76.0

Source: World Bank 1997a; UNCTAD 1999b; IMF 1999.

Annex Table 10: Intra-regional trade

	Share of intra-regional trade in total exports (%)			Share of intra-regional imports in total imports (%)			Share of intra-regional trade in total trade (%)		
	1990	1995	1998	1990	1995	1998	1990	1995	1998
Bangladesh	3.6	2.7	2.7	6.8	17.7	17.5	5.8	12.8	12.4
India	2.7	5.1	5.6	0.4	0.6	1.1	1.4	2.7	3.2
Maldives	25[a]	22.0	17.3	14.1 [a]	13.2	9.2	16.0 [a]	14.3	10.7
Nepal	6.9	9.3	36.5	11.5	17.5	31.7	10.0	15.0	32.8
Pakistan	4.0	3.3	4.9	1.6	1.5	2.4	2.6	2.2	3.6
Sri Lanka	3.3	2.7	2.5	6.8	11.4	12.0	5.3	7.5	8.1
South Asia	3.1	4.4	5.3	1.8	3.8	4.8	2.4	4.1	5.0
Memo Items									
East Asia	33.3	41.6	41.4[b]	32.6	37.9	39.3[b]	32.9	39.7	40.4[b]
Sub-Saharan Africa	8.0	11.5	11.3[b]	9.3	11.7	13.0[b]	8.6	11.6	12.2[b]
NAFTA	41.4	46.2	47.3[b]	33.9	38.4	39.7[b]	37.2	41.9	43.2[b]

a: 1992; b: 1996.

Source: IMF 1999; World Bank 1997a.

Annex Table 11: Bilateral export flows among South Asian countries (% of total exports)

From	To	Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan	Sri Lanka
Bangladesh	1990	..	..	1.32	..	0.42	1.38	0.48
	1998	..	..	1.44	..	0.47	0.76	0.03
India	1990	1.67	0.01 [a]	..	0.04 [a]	0.22	0.24	0.57
	1998	2.83	0.03	..	0.02	0.88	0.37	1.45
Maldives	1992	0	..	..	..	..	0	25
	1998	1.02	..	..	..	..	1.08	16.33
Nepal	1990	0.46	..	6.48	..	..	1.56 [b]	0
	1998	6.17	..	32.88	..	..	0.23	1.13
Pakistan	1990	1.84	0.01 [a]	0.88	0.12 [a]	0.02	..	1.24
	1998	1.27	0.01	2.4	0.02	0.09	..	1.13
Sri Lanka	1990	0.53	..	1.06	0.36 [a]	0.04 [a]	1.69	..
	1998	0.14	..	1.04	0.64	0.05	0.70	..

a: 1992; b: 1991

Source: IMF 1999.

Annex Table 12: Bilateral import flows among South Asian countries (% of total imports)

	To	Bangladesh	Bhutan	India	Maldives	Nepal	Pakistan	Sri Lanka
From								
Bangladesh	1990	..	0.11 [a]	4.65	..	0.05	1.91	0.22
	1998	..	0.07	16.12	..	0.19	1	0.08
India	1990	0.06	0.01 [b]	..	..	0.06	0.19	0.09
	1998	0.15	0.03	..	..	0.34	0.5	0.1
Maldives	1992	..	..	7.33	..	..	0.52	6.28
	1998	..	..	1.62	..	..	0.46	7.16
Nepal	1990	1.76	..	9.47	..	..	0.22	0.21 [a]
	1998	0.42	..	30.68	..	..	0.42	0.14
Pakistan	1990	0.51	0.02 [a]	0.62	..	0.04 [a]	..	0.5
	1998	0.39	0.02 [c]	1.65	..	0.01	..	0.37
Sri Lanka	1990	0.34	..	4.48	0.26 [a]	0.69 [a]	1.93	..
	1998	0.02	..	9.94	0.27	0.08	1.66	..

a: 1992; b: 1994; c: 1995

Source: IMF 1999.

Annex Table 13: Trade balance (% of GDP)

	1980-84	1985-89	1990-94	1995-98	1980-89	1990-98
East Asia & Pacific	-1.1	0.7	-0.1	2.0	-0.2	0.8
Latin America & Caribbean	1.0	3.1	0.0	-1.6	2.1	-0.7
Middle East & North Africa	1.2	-5.7	-2.5	1.1	-2.2	-0.9
South Asia	-4.9	-4.3	-3.0	-4.1	-4.6	-3.5
Bangladesh	-11.6	-9.0	-5.5	-6.3	-10.3	-5.9
Bhutan	-29.2	-24.1	-11.8	-8.3	-26.7	-10.3
India	-2.6	-2.6	-1.7	-3.2	-2.6	-2.4
Maldives	-49.8	-41.0	n.a.	n.a.	-45.4	n.a.
Nepal	-8.2	-9.2	-9.9	-11.6	-8.7	-10.7
Pakistan	-11.4	-9.4	-7.0	-6.2	-10.4	-6.7
Sri Lanka	-15.7	-10.9	-9.7	-8.2	-13.3	-9.1
Sub-Saharan Africa	-2.1	1.6	-0.4	-1.3	-0.2	-0.8
Low income	-1.1	-2.3	-0.3	0.0	-1.7	-0.2
World	-0.2	0.2	0.2	0.4	0.0	0.3

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 14: Average export and import growth (%)

	1980-89		1990-98	
	Exports	Imports	Exports	Imports
East Asia & Pacific	10.1	9.2	12.5	10.1
Latin America & Caribbean	5.3	1.4	8.1	12.1
Middle East & North Africa	n.a.	n.a.	n.a.	n.a.
South Asia	6.3	5.1	10.0	9.0
Bangladesh	7.0	6.7	15.7	12.5
Bhutan	n.a.	n.a.	n.a.	n.a.
India	5.3	6.9	11.1	10.5
Maldives	n.a.	n.a.	n.a.	n.a.
Nepal	3.9	7.3	15.1	10.8
Pakistan	10.7	1.4	5.4	2.9
Sri Lanka	6.3	3.0	8.4	8.6
Sub-Saharan Africa	1.5	-0.1	4.0	4.1
Low income	6.0	5.0	10.6	8.9
World	4.9	4.7	6.8	6.2

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 15: Current account balance (% of GDP)

	1980-84	1985-89	1990-94	1995-98	1980-89	1990-98
Bangladesh	-3.6	-4.3	-2.7	-2.3	-3.9	-2.5
Bhutan	-42.3	-31.8	-14.3	-12.0	-36.5	-13.3
India	-1.1	-1.9	-1.1	-1.4	-1.5	-1.2
Maldives	-40.2	3.7	-7.7	-6.5	-18.2	-7.2
Nepal	-4.6	-6.5	-7.2	-9.4	-5.5	-8.2
Pakistan	-2.6	-2.8	-3.6	-4.7	-2.7	-4.0
Sri Lanka	-9.4	-6.0	-5.0	-3.8	-7.7	-4.5

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 16: Stock market indicators

	Market capitalisation (billion US$)		Market capitalisation (% of GDP)		Value of trade (% of GDP)		Number of listed domestic companies	
	1990	1999	1990	1998	1990	1998	1990	1998
East Asia & Pacific	197.1	536.9	21.3	33.0	13.3	30.3	1,443	3,702
Latin America & Caribbean	78.5	402.9	7.6	20.8	2.1	10.7	1,748	2,166
Middle East & North Africa	5.3	113.9	29.0	26.6	1.5	5.8	817	1,619
South Asia	42.7	113.6	10.6	20.4	5.5	13.4	3,231	7,178
Bangladesh	0.3	1.0	1.1	2.4	0.0	1.9	134	208
India	38.6	105.2	11.9	24.5	6.8	15.0	2,435	5,860
Nepal	0.3	0.3	6.5	5.6	0.3	0.1	72	104
Pakistan	2.8	5.4	7.1	8.5	0.6	14.4	487	773
Sri Lanka	0.9	1.7	11.4	10.9	0.5	1.8	175	233
Sub-Saharan Africa	142.6	183.1	52.0	80.3	3.8	26.3	1,011	1,117
Low income	54.6	375.6	7.5	22.2	3.1	22.1	3,446	9,089
World	9,398.4	27,459.0	51.2	97.4	28.4	81.3	25,424	47,465

Source: World Bank, World Development Indicators CD-ROM, 2000.

Annex Table 17: Aggregate net long-term resource flows, South Asia (US$ billion)

	Annual average	Annual average
	1980-89	1990-99
Aggregate net resource flows	8.6	11.9
Total public flows	5.9	5.8
Official grants	2.4	2.5
Official loans	3.4	3.3
Bilateral	1.1	1.3
Multilateral	2.3	2.1
Total private flows	2.7	6.1
Private debt flows	2.4	1.8
Bonds	1.7	0.5
Commerical banks	0.2	0.4
Others	0.4	0.0
Non-guaranteed loans	n.a.	0.8
Private non-debt flows	0	4.3
Foreign direct investment	0	2.3
Portfolio equity investment	0	2.0

Source: World Bank 1997a, 2000a.

Annex Table 18: Foreign direct investment

	US$ million		% of GDP		% of Gross Domestic Investment		Average annual growth in value (%)	
	Average	Average	Average	Average	Average	Average	Average	Average
	1980-89	1990-98	1980-89	1990-98	1980-89	1990-98	1980-89	1990-98
East Asia & Pacific	3966.8	41326.5	0.67	2.67	2.15	7.52	26.9	26.2
Latin America & Caribbean	5714.0	31714.0	0.71	1.86	3.31	8.76	9.3	31.0
Middle East & North Africa	806.2	3365.3	0.38	0.74	1.53	3.85	150.1	-210.1
South Asia	256.2	2151.4	0.08	0.44	0.38	1.92	25.0	31.3
Bangladesh	0.7	55.3	0.00	0.13	0.02	0.62	-44.9	378.4
India	104.7	1424.3	0.04	0.37	0.19	1.58	85.0	57.1
Maldives	1.6	7.8	1.57	3.28	n.a.	n.a.	18.5	12.4
Nepal	0.5	9.7	0.02	0.22	0.08	0.97	-20.0	80.7
Pakistan	107.9	501.7	0.33	0.88	1.76	4.72	27.0	13.9
Sri Lanka	40.7	152.7	0.75	1.22	2.81	4.93	-0.5	64.6
Sub-Saharan Africa	1101.5	3279.3	0.74	1.44	5.24	8.32	373.9	20.4
Low income	2942.9	36048.0	0.34	2.36	1.33	7.85	56.6	31.2
World	84620.9	295419.0	0.67	1.16	2.93	4.59	19.4	15.8

Source: World Bank 1997a, 2000a.

Annex Table 19: Top ten industries in India receiving FDI approval between August 1991 and June 1995

Industry	Amount	% Share
Fuels	99,601.85	28.39
Chemicals	29,314.09	8.36
Service sector	868.74	7.66
Metallurgical	25,802.64	7.36
Electric equipment	22,799.82	6.50
Telecommunications	22,418.23	6.39
Food processing	20,912.99	5.96
Transportation	18,407,078	5.25
Hotel & Tourism	17,710.87	4.90
Textiles	13,710.87	3.91

Source: World Bank 1997a.

Annex Table 20: Portfolio equity flows (US$ billion)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
All developing countries	2.76	7.55	14.06	51.02	35.16	36.06	49.17	30.19	15.57	27.59
South Asia	0.11	0.02	0.38	2.03	6.22	2.34	5.20	2.48	0.35	1.09
Bangladesh	0.00	0.00	0.00	0.00	0.05	0.03	0.03	0.01	0.00	n.a.
Bhutan	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n.a.
India	0.11	0.00	0.24	1.84	4.73	1.52	4.40	2.12	0.34	n.a.
Maldives	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n.a.
Nepal	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	n.a.
Pakistan	0.00	0.02	0.14	0.19	1.34	0.73	0.70	0.25	0.00	n.a.
Sri Lanka	0.00	0.00	0.00	0.00	0.11	0.06	0.07	0.10	0.01	n.a.
Sub-Saharan Africa	0.00	0.00	0.14	0.17	0.86	4.87	2.01	1.51	0.68	0.49
East Asia & Pacific	1.57	1.05	5.10	20.65	12.61	18.27	18.09	9.19	9.01	18.97
Latin America & Caribbean	0.90	6.23	8.23	27.19	13.16	7.64	13.89	9.95	1.75	3.59
Middle East and North Africa	0.00	0.00	0.00	0.00	0.11	0.20	1.63	2.26	0.88	0.61
Europe and Central Asia	0.19	0.23	-0.18	0.98	2.20	2.73	8.35	4.81	2.90	2.84

Source: World Bank 2000a.

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Social Impact of Globalisation in South Asia

Economic growth is (like) a wild horse; it needs to be trained to serve the real interests of society. If the horse misbehaves in some societies, leading to deprivation of many human lives, then the fault is not that of the horse but the skill of the rider. Economic growth is essential in poor societies—but even more important is its structure and distribution.

– Mahbub ul Haq

Chapter 3

Social Impact of Globalisation in South Asia

An equitable globalisation process requires the integration of the financial, trade and investment policies with those of social development

Globalisation affects developed and developing countries differently. While the developed-country worries focus on the protection of their domestic industries and agriculture, particularly if it involves the cost-reducing measures by shifting production processes abroad, the developing countries contend with increased poverty, vulnerability, inequalities and inequities generated by the globalisation process on the poorer sections of their population. An equitable globalisation process requires the integration of the financial, trade and investment policies with those of social development in order to improve the quality of life of the whole population, instead of only a minority.

In theory, higher growth rates would generate sufficient revenue for the state to reduce poverty and income inequality. But there is no automatic link between the increase in growth rates and reduction of income inequality. This link between growth and distribution has to be created consciously by progressive fiscal policy to redistribute income and social policy to improve education, health, employment and other social needs.

It is in this context that there is a need to assess the impact of globalisation on human development, particularly in South Asia, the region with the highest absolute number of poor people in the world. As the founder of the human development model, Mahbub ul Haq, asserted, 'Human development is the process of enlarging people's choices'. While globalisation increases the choices of goods and services and alters consumer preferences, human development enlarges people's choices by expanding human capabilities and opportunities so that the majority of people in poor countries can have access to resources needed for a decent standard of living.

Globalisation creates opportunities but it also increases risks. The financial turmoil in East Asia in 1997-99 demonstrated the inherent risks of global financial markets. The negative social impacts in East Asia, including rising unemployment, rising prices, declining real wages and rising social unrest, were severe and continued long after the economic recovery.

There is very little hard data available to establish a causal connection between globalisation and increased social deprivation. But it cannot be denied that the relentless pressures of globalisation, including the stabilisation and structural adjustment programmes of the IMF and the World Bank, and the new trading regime of the WTO, lead to fiscal compression, tariff reductions and cutbacks of public provisioning of social services. In the 1990s, the tax/GDP ratio had declined in most developing countries. But in South Asia, the already low tax/GDP ratio had declined further from 12.9 per cent in 1988 to 9 per cent in 1999. These have led to stagnant or decelerating allocation to social services.

Globalisation in South Asia

The globalisation process in South Asia was initiated to accelerate economic growth through enhanced internal and external competition, privatisation and trade liberalisation. It included measures to reduce domestic credit expansion in general and fiscal deficit in government expenditure in particular. It was assumed that the surplus generated from expenditure compression would reduce the balance of payments deficits. Further, reduction of public expenditure was considered to be a means to divert resources towards a relatively more productive private sector. The World Bank/IMF package of stabilisation-cum-structural adjustment programmes aimed at correcting the imbalances at the macro and micro levels and put the economy on to a higher economic growth path.

After over a decade of implementing economic reforms, an assessment of the globalisation process in South Asia is a very relevant and useful exercise not only for the region but also for other developing countries which have and/or are going to initiate the process of reforms. But we must insert a cautionary note here. In order to make an assessment of the impact of globalisation on human development in South Asia, we must consider the initial conditions, prior to globalisation, in these countries. If the initial conditions were of high human deprivations, as they were in South Asia mainly because of the governments' lack of commitment to human development, inefficiency of administration of public sectors and poor governance, then the globalisation process may have only exacerbated the already poor human development records of these countries.

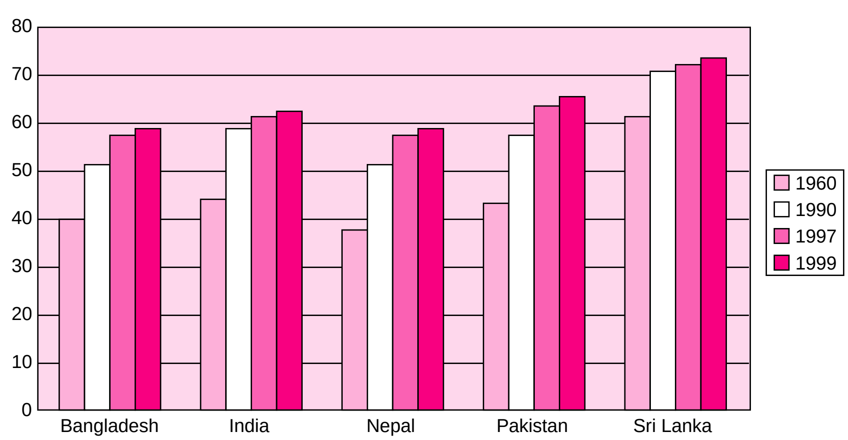
In the pre-globalisation period, the region was characterised by high population growth rates, high levels of illiteracy, poor health attainments, pervasive poverty and inequitable distribution of income and assets. However, there were considerable differences within and between South Asian countries in their performance in social and economic development prior to and during the globalisation phase. The final assessment of globalisation on the people in South Asia has to be made on the basis of these initial conditions.

The average growth rate of South Asia during 1980-89 was 5.8 per cent (see table 2.4). However, during 1990-98, the South Asian average growth rate had gone down to 5.4 per cent, although India's growth rate reached almost 7 per cent during the period, and Pakistan recorded the lowest growth rate of 4.2 per cent. Further, the composition of total income generated in the region was mainly from non-agricultural activities. Although the relative proportion of income and output generated from industrial and service sector activities increased, the agricultural sector continued to be a predominant source of employment. The growth of income and employment in the industrial sector was sluggish and at lower levels during the globalisation period. Thus most South Asian countries were experiencing a process of incomplete structural transformation.

In 1990, while Sri Lanka was among the medium human development countries, Bangladesh, India, Pakistan and Nepal were among the low human development countries in the world. By 1999, Sri Lanka and India were among the medium human development countries, while Pakistan, Bangladesh and Nepal continued to remain as low human development countries. Compared to the initial conditions in these countries, there was considerable improvement in increasing life expectancy and improving literacy rates. However, the nature of social and economic development in all the countries of the region had not been sufficient to reduce poverty or to make any meaningful difference in the lives of the majority of the population.

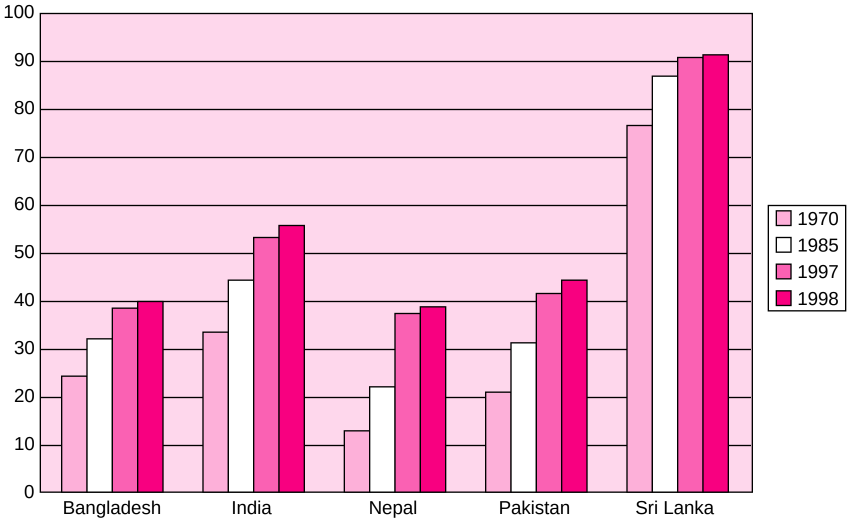
To make an assessment of the impact of globalisation on human development in South Asia, we must consider the initial conditions, prior to globalisation

Figure 3.1 Life expectancy (years) in South Asia: 1960-1999



Source: UNDP 1991, 1999, 2000; MHHDC 1999.

Figure 3.2 Adult literacy (%) in South Asia: 1970-1998



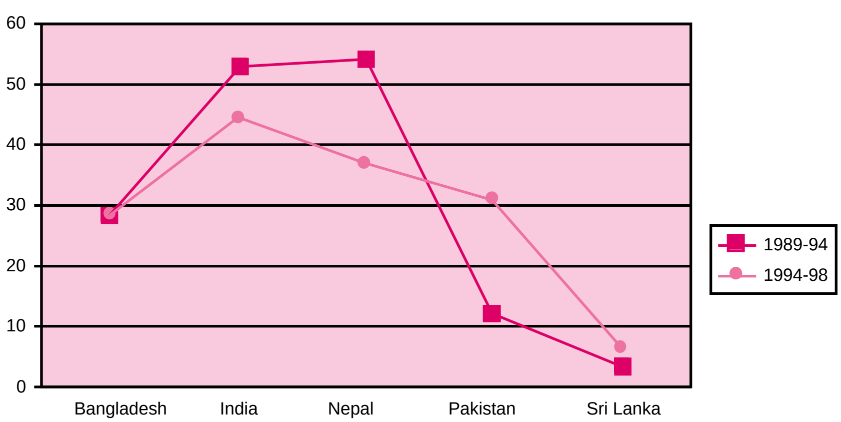
Source: UNDP 1991, 1999, 2000; MHHDC 1999, 2001.

Figures 3.1 and 3.2 show the progress achieved since 1960 in improving the life expectancy and literacy in five South Asian countries. But this progress had slowed in 1997 and 1998/99. Most of the South Asian countries failed to maintain a balance between economic and social development indicators during the period of globalisation.

Poverty and inequality

In 1995, out of 1.3 billion poor people in the world, 515 million lived in South Asia. The head count ratio (HCR), measured as a percentage of population whose income or consumption level falls below the poverty line, continued to remain at high levels, though at varying rates. Between 1989-94, while income poverty was as low as 4 per cent in Sri Lanka and 11 per cent in Pakistan, it ranged between 29-53 per cent in Bangladesh, India and Nepal. An analysis of the incidence of poverty across two time points viz., 1989-94 and 1994-98, indicated that it had increased in *three out of five* South Asian countries in the second half of the 1990s (UNDP 2000) (see figure 3.3).

Figure 3.3 Population below income of $1 per day (%) in South Asia: 1989-98



Source: UNDP 1991, 2000.

The available information on the depth of poverty measured by the poverty gap index (PGI), and severity in terms of Foster-Greer-Thorbecke (FGT) index across South Asia points towards an overall decline in poverty during the period 1985-86 to 1990-91. However, the disparities in the rates of reduction of poverty between rural and urban areas persisted. For instance,

- In Sri Lanka while the depth and severity of poverty declined at the national level, they increased in urban areas and declined in rural areas (South Asia Poverty Monitor 1997b).
- In India, as per national poverty line, the HCR, PGI and FGT declined in both rural and urban areas, but at differential rates. The declines of head count ratio, the depth and severity were faster in the urban areas as compared to the rural areas. The coefficient of variation in the incidence of income poverty in 16 major states in India had increased from 0.40 in 1973-74 to 0.67 in 1993-94, pointing towards rising inter-state disparities. Additionally, poverty levels varied across social groups as well and remained at high rates (Mahendra Dev 2000).
- In Bangladesh, the head count ratio, the depth and severity of poverty had increased not only at national level but at the regional level as well. The magnitude of increase was considerably higher in the rural areas as compared to the urban areas.
- In Pakistan between 1986-87 and 1993-94, the head count ratio, the depth and severity of poverty had increased (see table 3.1).

Table 3.1 Nature of poverty in selected South Asian countries

(per cent)

Year	Region	Sri Lanka			Year	India		
		HCR	PGI	FGT		HCR	PGI	FGT
1985/86	Rural	31.62	7.67	2.75	1983	49.02	0.14	0.05
	Urban	16.43	3.48	1.11		38.33	0.10	0.04
	Total	27.33	6.54	2.31		n.a	n.a	n.a
1990/91	Rural	24.41	5.27	1.78	1993/94	39.65	0.09	0.03
	Urban	18.32	4.14	1.57		30.65	0.08	0.03
	Total	22.36	4.82	1.62		n.a	n.a	n.a
		Bangladesh				Pakistan		
1985/86	Rural	45.90	10.90	5.90	1986-87	28.1	20.2	1.7
	Urban	30.80	7.30	2.50		28.8	21.2	1.9
	Total	43.90	10.40	3.50		28.6	20.6	1.8
1991/92	Rural	52.90	14.60	5.60	1993-94	37.7	27.5	4.2
	Urban	33.60	8.40	2.80		29.9	24.1	2.8
	Total	49.70	13.60	5.10		35.7	27.9	4.1

Note: HCR indicates head count ratio; PGI indicates poverty gap index; FGT indicates Foster-Greer-Thorbecke index.
Source: South Asian Poverty Monitor 1997a, 1997b; Ravallion and Sen 1996, *A Profile of Poverty in Pakistan* HDC 1999.

The income distribution across various economic groups had worsened. Between 1987-98 the richest 20 per cent of population had between 41 to 46 per cent of income while the poorest 20 per cent had less than one-tenth of the total income (see table 3.2).

Human poverty in South Asia

The human poverty index (HPI), conceptualised by Mahbub ul Haq and subsequently developed and constructed by UNDP in the Human Development Reports (UNDP 1996, 1997), attempted to broaden the concept of poverty in order to capture the deprivations in survival, education and income. In South Asia, the imbalance between social and economic development in the 1990s had led to insignificant improvements in the human poverty levels of the region. In 1999, the percentage of population not expected to survive to age 40 years was 37 in India, 35 in Pakistan, 41 in Bangladesh, 42 in Nepal, 26 in Sri Lanka, 38 in Bhutan and 35 per cent in Maldives (see table at the end of this report). In 1999 about half the total adult population in the region was illiterate. There were large differences between countries and within each country. While the rate of illiteracy in Sri Lanka was the lowest at 9 per cent, Nepal continues to have the highest number of illiterate population at 60 per cent. Public provisioning of basic services such as health, sanitation and child nutrition influences the quality of public health. There are major inadequacies of such provisions in the form of poor coverage and utilisation in the region. For example,

- There had been improvements in the provisioning of safe drinking water in most South Asian countries from 77 per cent coverage in 1995 to 89 per cent in 2000. All the countries had made significant improvements in the provisioning of safe drinking water.
- In 1995, over one-fifth of the population in the region did not have access to any health services. Except Sri Lanka and India, provisioning of health services had remained inadequate in other South Asian countries ranging between 25 per cent in Maldives to 55 per cent in Bangladesh.

Table 3.2 Percentage share of real per capita GDP (1987-98) in South Asia

	Bangladesh	India	Nepal	Pakistan	Sri Lanka
Poorest 20%	8.7	8.1	7.6	9.5	8.0
Richest 20%	42.8	46.1	44.8	41.1	42.8
Richest 20% to poorest 20%	4.9	5.7	5.9	6.9	5.4

Source: UNDP 1991, 1999, 2000.

Box 3.1 Globalisation and the children[1]

A number of studies suggest that during the most recent decades, when policies of globalisation have been implemented by a growing number of countries *in various degrees*, income distribution, globally and in most countries, has worsened, and as a result is having a dampening impact on long-term economic growth trends—and on the prospects for poverty reduction necessary to meet the UN Millennium Declaration Goal of halving the number of people living in extreme income poverty.

Extreme income poverty affected some 1.2 billion people at the end of the twentieth century, similar to the number a decade earlier. UNICEF estimates that children make up about half of the income poor. An assessment of progress towards the achievement of the social goals for children, agreed at the World Summit for Children in September 1990, suggests that overall progress has been less than anticipated. Recent research[2] suggests that despite decline in the global and most national average trends for under-5 mortality rates, the improvement in some countries is due to declines among the richest quintile, while progress among the poorest 40 per cent is falling behind. This phenomenon is particularly apparent among countries with lower levels of child mortality rates. There is evidence to suggest that public policies are crucial to narrowing the gap by ensuring that access to quality basic social services is universal.

The global annual resource requirement to fund these services of $80 billion has not been met. Country studies suggest that developing countries on average allocate some 12-14 per cent of their budgets to these sub-sectors, while the donor community allocates some 11 per cent of ODA to these.

The trade aspects of globalisation also alter the context of many issues and areas affecting children, in some cases intensifying problems and in other cases affecting the policy actions required to address the problems. For example, by increasing employment opportunities for unskilled and semi-skilled workers globalisation changes the demand for child labour, although the net effect in this area is not yet clear. Increasing employment of women, and enhancement of their opportunities in society, accentuates the importance of child-care policies within an overall framework for child development.

Foreign direct investment and trans-national corporations have brought with them employment opportunities, capital and trade, and broadened the domestic supply of (international) goods and services. While some have seriously undercut domestic production of goods and services, others have brought risks to the health status particularly of women and children. This applies particularly to the cases of marketing breast-milk substitutes and tobacco. The International Code has contributed to reversing the trend away from breastfeeding but is still often violated. Similarly, advances in bio-technology have greatly expanded the opportunities to prevent and treat child illness through vaccines and medicines but requires public-private partnerships to ensure that these benefits reach the poorest children.

A comparative study[3] of responses to the South East Asian financial crisis in 1997 shows that as governments in Malaysia, Korea and Thailand continued to prioritise social development some adverse effects on children were contained. The crisis was primarily transmitted to children through household employment and real income changes. In the worst affected countries, Indonesia and Thailand, the situation of children appears to have deteriorated. Child abuse appeared to have worsened. Several millions of children, who were severely malnourished even before the crisis, were neglected. As families faced difficulties and stress arising from economic hardships, drug abuse and related problems increased. The crisis confirmed that without pre-existing mechanisms of reaching the population with social protection measures, emergency assistance often failed, or was slow, to reach those for whom it was intended.

The globalisation package embeds a perception that the public sector should be contained to reduce the fiscal strain on the economy. But the same package potentially lessens revenue generated from trade by the reduction of trade tariffs and taxes and other measures to attract foreign investment.

– contributed by UNICEF

[1] The panel draws on Cornia 'Globalisation, inequality, growth and child poverty' mimeo and other background papers for the UNICEF booklet on 'Harnessing Globalisation for Children', which will be published in time for the Special Session on Children, September 2001.
[2] Minujin and Delamonica 'Social disparities, child mortality and globalisation' mimeo.
[3] Abeysegera and Kittiprapas 'Financial Instability and Child Wellbeing: A Comparative Study of Social Policy Responses in Asian Crisis-Affected Countries' mimeo.

Sources: Khan and Mahmood 2000.

• Public provisioning of sanitation facilities had been poor in South Asia. In 2000, 63 per cent of the total population in the region did not have access to sanitation facilities. This deprivation was as high as 73 per cent in Nepal and 69 per cent in India.

• In 1990-98, 51 per cent of the children under five years were malnourished. This number remained stagnant in Bangladesh, India and Pakistan, and fluctuated in Sri Lanka and Nepal around 38-56 per cent. The survival and development of children continues to be a daunting problem in the era of globalisation (see box 3.1).

Education

In the 1990s, over 40 per cent of children did not reach grade 5 (see table 3.3). Between 1995-99, this proportion ranged between 30 per cent in Bangladesh to 56 per cent in Nepal. It was the lowest in Sri Lanka at 3 per cent.

In 1970, secondary enrolment rates were the highest in Sri Lanka at 47 per cent, while Nepal had the lowest enrolment rate at 10 per cent. By 1996-97, while there had been improvements in the overall enrolment rates in the region, Bangladesh recorded the lowest gross as well as net enrolment at the secondary level. In 1992, tertiary enrolment rates in the natural and applied sciences accounted for 26 per cent of the total tertiary enrolment. These rates were highest in Sri Lanka at 34 per cent, followed by India, Bangladesh and Nepal. Between 1995-97 these rates declined in most South Asian countries and ranged between 14-29 per cent.

An inter-temporal examination of the mean years of schooling displays minor improvements in educational outcomes between 1980 and 1992. In 1998, the region continued to have mean years of schooling as low as 2.4 years indicating less than primary level education with the only exception of Sri Lanka where it was much higher at 7.2 years. While globalisation process demands better educated and skilled labour, the overall levels of education and skill-training continued to remain low.

Further, there was also a sharp gender disparity in the mean years of schooling attained by male and female students. In 1998, mean years of schooling for boys in Bangladesh, India, Pakistan and Nepal ranged between 2.9-3.5 years, while those for girls were lower ranging between 0.9-1.2 years. Thus, while boys came closer to completing primary education, girls failed to complete even two years of schooling. In contrast, boys in Sri Lanka had an average of 8 years of schooling while girls completed 6 years of schooling. Moreover, the teacher-pupil ratio in 1986-88 ranged between 32-60 students per teacher. In 1995, the ratio deteriorated in *three out of five* countries viz., Bangladesh, India and Pakistan (UNDP 1991, MHHDC 1999).

Table 3.3 Profile of education in South Asia

(per cent)

Year	Bangladesh	India	Nepal	Pakistan	Sri Lanka	South Asia
1. Children not reaching grade 5 (%)						
1990-95	53	38	48	52	2	41
1992-95	–	41	–	–	17	38
1995-99	30	48	56	50	3	46
2. Secondary enrolment						
1970[a]	–	26	10	13	47	25
1986-88[b]	17	41	30	19	71	–
1996[a]	19	49	38	26	75	44
1997[c]	22	60	55	–	76	–
3. Combined enrolment at all levels (%)						
1980	30	40	28	19	58	37
1995	37	55	56	41	67	52
1998	36	54	61	43	66	51
4. Tertiary natural & applied science enrolment (% of total tertiary enrolment)						
1992	25	26	17[d]	–	34	26
1995-97	–	25	14	–	29	22

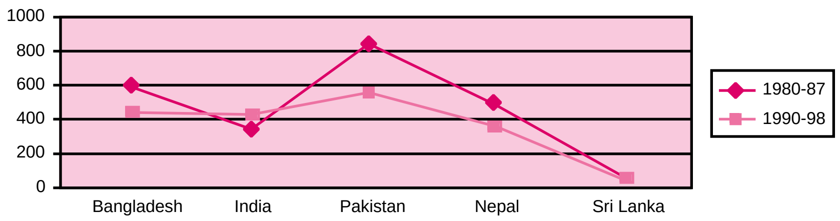
Note: [a]indicates gross enrolment rates, [b]indicates net enrolment rates, [c]is per cent of relevant age group, [d]data provided pertains to 1993.
Source: UNDP 1991, 2000; MHHDC 1999.

Health

Since the 1970s, in most South Asian countries notable improvements had taken place on some of the health indicators, mainly as a result of large-scale government programmes. But the health status of the vast majority of population continued to remain very poor. Between 1990-97, the proportion of low birth weight babies was 32 per cent in the region, with Bangladesh having the highest rate at 50 per cent. The maternal mortality rate per 100,000 live births, between 1990-98, was estimated to be around 480, with the highest rate in Nepal at 540 per 100,000 live births (see figure 3.4).

Despite efforts by the governments and the private sector to improve the overall health status of the population, incidence of old diseases like tuberculosis (TB) and malaria continued to remain very high. In 1996, the region had the second highest, after sub-Saharan Africa,

Figure 3.4 Maternal mortality rate (per 100,000 live births)



Source: UNDP 1991, 1999, 2000; MHHDC 1999.

A critical facet of the new labour market is the extent of informalisation and casualisation of employment

TB cases of 107 per 100,000 population. The estimates for 1997 revealed that this rate had declined to 94 per 100,000 population. In Pakistan, pulmonary tuberculosis in adults continued to be a major public health problem, acute respiratory tract infections were common, and malaria continued to be a big threat. Since 1995, the number of malaria cases reported in Sri Lanka increased from 786 per 100,000 population to 1196 in 1997.

Social sector services are the responsibility of the states/provinces in India and Pakistan, yet in 1998 a substantial proportion of the population in these two countries was not able to access health services. Although most South Asian countries have adopted a mixed approach of public and private-sector participation in providing education and health, the ratio of social sector personnel to population continues to remain inadequate minimising the effectiveness of the provisioning.

The increase of HIV/AIDS cases poses a challenge for the health planners as well as service providers. In 1997, total AIDS cases, aged 0-49 years, were 4.1 million in South Asia of which 97 per cent cases were reported in India. Even within India, great disparities existed across different regions. Three-quarters of AIDS cases in India were in three states—the states of Maharashtra, Tamil Nadu and Manipur (Maniar 2000). The World Health Organization has estimated that in South Asia children account for 4 per cent of all HIV cases.

Rapid proliferation of HIV/AIDS has been attributed to the globalisation process, which has increased the rate of global labour migration at inter-regional, intra-regional and international levels. Other reasons cited for the rise of the epidemic are low levels of literacy that lead to low awareness amongst the potential risk groups, increase of drug addicts, unsafe blood transfusion and reproductive tract infection amongst men and women. In Bangladesh, Sri Lanka and Pakistan, separate National AIDS Committees with multidisciplinary and multi-sectoral representatives have been created. The respective national governments and the committees jointly undertake measures such as surveillance of health services, blood safety measures and education awareness programmes. They are implemented in coordination with the help of non-governmental organisations and international donor agencies. But in India, analysts argue, that despite alarming statistics of AIDS/HIV cases, the government response has so far not been adequate to the challenges faced by the country (Jain *et al*. 2000).

Employment

In this era of globalisation and market liberalisation, there has been a trend to move away from large enterprises, stable workforces and wage systems towards flexible production processes, and flexible employment and payments. Flexibility of employment has spread across the developing, transitional and industrialised countries. While national governments have created the space for various forms of flexibility by controlling labour unions, and introducing labour legislation and regulations to promote flexibility, firms have increased their control by relying largely on contracted employment. Global labour flexibility has become pervasive as it is advocated as a means to lower unemployment, raise economic growth, improve incomes and reduce inequality (Standing 1999).

A critical facet of the new labour market is the extent of informalisation and casualisation of employment. In South Asia, more women are also joining the labour force, especially in the

Box 3.2 Globalisation and the women

Globalisation affects women from different walks of life differently. Urban, educated and relatively affluent women benefit from the increased opportunities for work that come with the influx of foreign companies and investments. These employment avenues are complemented by greater opportunities to receive education and skills training of a higher quality. The new technologies that define this era, in particular the computer and internet, are accessible primarily to this group of women. In general, the liberalisation of trade and financial markets also promise benefits for this group, including a greater variety of goods at cheaper prices due to increased competition, and much more attractive interest rates for women entrepreneurs to undertake business ventures.

Conversely, poor, uneducated, credit-constrained, informal and agriculture sector women—by far the majority of women in South Asia—are supposed to benefit in a much less direct manner. These women are supposed to benefit from long-term economic growth brought about by correcting price distortions in factor and product markets. By making markets competitive, higher agricultural growth is expected and this in turn is expected to increase rural income. It is also expected that the expansion of the industrial sector would increase employment in the urban as well as rural areas. The proponents of globalisation argue that the process may entail some short-term difficulties in terms of reduced income and consumption; unemployment might also increase. But eventually the reform process would lead to greater gains all around.

But the efforts to become competitive often hurt the social sectors first. It is most often these sectors that face budgetary reductions when liberalisation policies are implemented. Conservative monetary and fiscal policies are often undertaken and these too, independent of reductions in the size and scope of social sectors, can indirectly reduce allocations to social services and basic provisions. Such cuts in social spending are likely to hit the poor rural women the hardest, who already have such limited access to education and health facilities.

It is true that significant opportunities have become available for women in low-technology manufacturing industries such as textiles and garments. In Bangladesh, the overall participation of women in the economy has increased considerably, and in the low-skilled manufacturing sector women's wages are almost equal to those for men. But even in these new avenues of employment, women generally get stuck at the lower rung, with long hours, poor working conditions and little job security. The most exploited are the home-based women workers.

The gains of globalisation have so far accrued to those who already have education and skill advantage, easier market access and possession of assets for use as collateral to access credit. For the poor women of South Asia, globalisation has been associated with rising prices, loss of job security, lack of healthcare and rising social tension.

Sources: Khan and Mahmood 2000.

informal sector (see box 3.3). In India, the proportion of workforce formally covered by legal protection (minimum labour standards) is not more than 10 per cent, while informal sector activities accounted for 90 per cent of employment. Even within non-agricultural employment, the proportionate share of informal sector economic activities has increased.

With globalisation and increasing competition, demand for skilled and semi-skilled workers has increased. The educational attainments of the labour force govern the extent of adaptability of the labour force to changed market demand. But in South Asia, due to the prevalence of high illiteracy rates and low levels of educational attainments the quality of labour force continued to remain relatively poor in two out of three countries (see table 3.4).

In the 1990s, the structure of employment in the region had shifted towards self-employment and own-account enterprises. Only 30 per cent of the total workers were in the category of wage and salaried workers, and employers. These shares had fluctuated in Bangladesh, India and Pakistan around 12 per cent, 30 per cent and 32 per cent,

Table 3.4 Educational attainments of the employed

(per cent)

Country/Gender		Illiterate	Literate upto primary	Middle school	Secondary & above but below graduate	Graduate & above
1. India-	Total	49.2	24.0	11.5	7.3	8.0
	Male	37.2	28.2	14.6	9.6	10.3
	Female	74.3	15.0	4.9	2.7	3.7
2. Pakistan-	Total	56.8	17.8	8.5	13.2	3.7
	Male	53.5	19.3	9.5	14.1	3.7
	Female	80.8	7.1	1.5	7.0	3.6
3. Sri Lanka-	Total	6.9	21.3	45.4	17.5	8.8
	Male	4.3	21.2	49.6	17.7	7.2
	Female	13.0	21.5	35.8	17.2	12.6

Source: Anant *et al*. 1999.

Although the incidence of income poverty had declined in the region, inequalities had increased within each country

respectively. The proportionate shares of self-employment and own-account enterprises in Bangladesh and Pakistan were 60 per cent and 66 per cent. Casual employment in India had increased from 68 per cent in 1983 to 70 per cent in 1993-94. Own-account enterprises had emerged as an important source of employment during the period, thus pointing towards growing informalisation of economic activities and growing casualisation of labour force (ILO 1999). Globalisation has pushed the real wage rates downwards both in the formal and informal sector, though at different rates. Two distinct features emerge in terms of the impact of globalisation on real wages in South Asia:

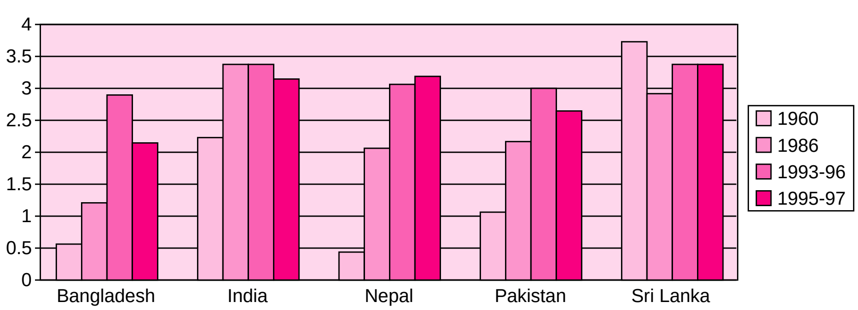
- First, in Sri Lanka between 1980-90 and 1990-93, the formal sector with 60 per cent of employment had experienced negative growth rates of real wages while the growth rates of wages in the unorganised sector increased at an annual rate from 0.53 per cent to 2.83 per cent (Anant *et al*. 1999).
- Second, Bangladesh, India and Pakistan, with predominantly informal sector workers, experienced rising real wages ranging between 2 to 11 per cent in the pre-globalisation period. However, the growth rates in the formal sector were lower at 2 per cent to 7 per cent. In the globalisation phase, increasing labour flexibility and dismantling of labour market institutions caused deceleration of real wages in both formal and informal sector. In Bangladesh, real wages declined in the formal sector at an annual rate of 3.9 per cent, and in the informal sector by 0.28 per cent in 1986-90 and further to 0.83 per cent in the 1990s (Rahman and Sen 1997). Trends in India were quite different. While formal sector real wages increased at an annual rate of 0.86 per cent in the globalisation phase, wages in the informal sector declined at an annual rate of 2.53 per cent. In Pakistan, real wages in the formal sector increased at a diminishing rate of 1.14 per cent and the informal sector wages fell by one per cent per annum (Anant *et al*. 1999).

Thus, lower labour flexibility in Sri Lanka pulled wage rates down in the organised sector, mainly due to fiscal compression. However, the wage differentials between the organised and unorganised sector minimised. In other South Asian countries, dismantling of labour institutions increased employment insecurities, reduced real wage rates and widened wage gaps between the formal and informal sector.

Rising labour costs also lead to lay-off of redundant labour, which is governed by the structure of employment. Sri Lanka with a predominant formal sector employment had been facing the problem of growing youth unemployment at the rate of 14 per cent in 1990-92 which declined to 13 per cent in 1994 (UNDP 1999; MHHDC 1999). In 1993, India, Bangladesh, Pakistan and Nepal were facing the problem of unemployment and underemployment of 22, 13 and 43 per cent, respectively (ILO 1993).

Clearly, in critical areas such as improving the capability of the poor through better access to education and health and expanding their opportunities through improved access to jobs and real wages, the situation has worsened during the globalisation phase in South Asia. Although the incidence of income poverty had declined in the region, inequalities had increased within each country. While the extent of illiteracy has declined, there is still a huge backlog of out-of-school children. Also, malnutrition among the children continued to remain a daunting problem for most countries in

Figure 3.5 Public education expenditure (as a % of GNP)



Source: UNDP 1991, 1999, 2000; MHHDC 1999.

the region. Additionally, deprivation in terms of accessibility of public provisioning of basic health services continued to be neglected in the region.

Social development policies in South Asia

In the 1990s, all South Asian countries made commitments at the UN conferences in Jomtien (education), Cairo (population), Copenhagen (social development), and Beijing (women) to develop and implement policies and programmes for social development. Thus the social sector policies at the central and state/provincial levels were developed in accordance with the global goals and national aspirations. Increased allocations were one of the imperatives to implement these goals. Yet, if we look at only two sectors—education and health—we see that public expenditure as a percentage of GNP has in fact gone down in almost all countries during 1995-97. However in the context of India and Pakistan, social sector expenditures are funded mostly out of state/provincial budgets, and thus are not fully reflected in central budgets (see figure 3.5).

In 1960, public education expenditure was 2 per cent of South Asia's Gross National Product (GNP), in the 1990s it continued to remain low, at less than 3.5 per cent. In terms of the share of education in total public expenditure during 1995-97, it was less than 12 per cent. This proportion varied across the region with the highest in Nepal at 14 per cent and the lowest at 7 per cent in Pakistan.

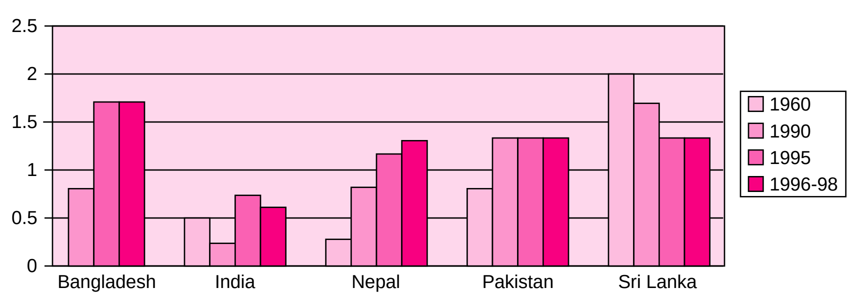
Globalisation is driven by knowledge and new technology. Thus there is a need not only to provide good quality primary, secondary and technical education but also to spend more on higher level of professional education. But in South Asia a trend of declining or stagnant tertiary enrolment rates is emerging. The relative allocations to higher education need to be selectively enhanced to upgrade the level and quality of education. A facilitative role of the state is very important here to make the private sector play an important part in providing high-quality professional/technical education.

Thus it seems that in the globalisation phase most South Asian countries continued to either reduce or maintain the already low levels of education expenditure, despite poor educational outcomes and growing demand for quality labour force. This had led to the deterioration of public provisioning causing poor enrolment rates as well as low attainment rates. Similarly, none of the South Asian countries had adapted the education to meet the growing demands of globalisation through increased allocations for higher education.

In the health sector, the already negligible proportionate share of health expenditure in GDP had increased at a decelerating rate in South Asia over the past three decades. In 1960, health expenditure in the region was as low as 0.5 per cent of GDP, which increased insignificantly to 0.9 per cent in 1996-98. In Bangladesh, the proportionate share of health expenditure had been rising from 0.8 per cent in 1990 to 1.6 per cent between 1996-98. In India, the proportion of health expenditure in GDP had been fluctuating at extremely low levels of less than one per cent over the past three decades. The expenditures on health sector had increased in Nepal from 0.2 per cent in 1960 to 1.3 between 1996-98. Sri Lanka, with health achievements equivalent to the East Asian countries, had been reducing health expenditures

South Asian countries continued to either reduce or maintain the already low levels of education expenditure

Figure 3.6 Proportion of health expenditure in GDP in South Asia: 1960-1998



Source: UNDP 1991, 1999, 2000; MHHDC 1999.

from 2 per cent of GDP in 1960 to 1.4 per cent in the late 1990s. Although public health expenditures in Pakistan had been less than one per cent of GDP, per capita health expenditures had been rising over the past 15 years, with expenditures from the private sector accounting for 2 to 3 per cent of GDP (Ghaffar *et al.* 2000a).

Poverty alleviation programmes

With the onset of globalisation the resource allocations to the poverty alleviation programmes in real terms have been declining

South Asian countries, characterised by pervasive poverty, have been implementing several poverty alleviation programmes over the past decades. These programmes have been in the form of self-employment creation (SEC) or asset building programmes, and wage employment creation (WEC) programmes. These programmes were mainly targeted towards the poor or very poor families on the basis of income threshold. However, a feature of most programmes is that they are financed by the state and, as such, periodic funding inadequacies often lead to either abandonment or reduced effectiveness of the schemes. However, with the onset of globalisation the resource allocations to these programmes in real terms have been declining.

The impact of the programmes varied across South Asia reflecting the different approaches of the governments. In Sri Lanka, direct poverty alleviation programmes included land redistribution in pre-globalisation period. In the post 1977 period direct wage-employment and asset-generation programmes were implemented. A specific direct poverty alleviation programme, the Janasaviya Programme was launched in 1989. The main objective was to enhance human development through upgrading skills and investment, and economic rehabilitation of the 'very' poor families. The Samurdhi Programme replaced the Janasaviya Programme in 1994 as income-support and economic rehabilitation programme. The programme is implemented by thousands of youth at village level who are required to work alongside divisional and village level administration staff already in place (Sri Lanka Poverty Report 1997).

In Bangladesh in 1996, an estimated 20 different poverty alleviation programmes were implemented. Food-based wage employment programmes and microcredit-based self-employment programmes broadly constitute the poverty alleviation measures in the country. The targeted groups for the former programmes are mainly landless rural poor who seek seasonal wage employment and receive training for skill developments (ILO-SAAT, 1997). These programmes include the Test Relief (TR), Food for Work (FFW), Vulnerable Group Development Programme (VGDP) and Rural Maintenance Programme (RMP). TR and FFW beneficiaries receive food aids instead of cash payment in lieu of maintenance and/or construction of rural infrastructure. Most FFW programmes create seasonal employment. FFW programme has been transformed into a multi-sectoral development project called Rural Development Project (RDP), currently being implemented by five ministries and more than 60 NGOs.

Since the 1970s, the Grameen Bank has been leading the micro-credit programmes, with a goal to empower the rural poor and alleviate poverty. These programmes are targeted towards the landless poor, particularly women. During 1990-94, the total number of beneficiaries across various credit programmes, implemented both by the government and NGOs, increased at the rate of 25 per cent per annum, while credit disbursements increased by 151 per cent per annum (Rahman and Sen 1997). The NGOs, each having their own target groups, dominated the credit programmes in Bangladesh.

In India, poverty alleviation programmes included self-employment programmes for poor households/ persons such as the Integrated Rural Development Programme (IRDP) and Training for Youth for Self-employment

(TRYSEM) and Development of Women and Children in Rural Areas (DWCRA). The wage employment programmes were Jawahar Rozgar Yojana (JRY), Employment Assurance Scheme (EAS) in rural areas, while Prime Minister's Rozgar Yojana (PMRY), Nehru Rozgar Yojana (NRY) and Prime Minister's Integrated Urban Eradication Programme (PMIUEP) were implemented in the urban areas.

The IRDP was initiated in 1978-79 to enable poor families in rural areas to cross the poverty line by providing productive assets and inputs, financial assistance in the form of subsidies from the government and term-credit from financial institution. In April 1995, IRDP, TRYSEM, DWCRA and supply of improved toolkits for rural artisans and Ganga Kalyan Yojana were merged to constitute the Swarna Jayanti Gram Swarojgar Yojana (SGSY), which was intended to function as a single self-employment programme. It had major features of all the schemes and the objective was focused on poverty alleviation, capitalising on the advantages of group lending, and overcoming problems of multiplicity of programmes.

The JRY programme, the principal national wage employment scheme, was the outcome of the merger of the National Rural Employment Programme (NREP) and the Rural Landless Employment Guarantee Programme (RLEGP), initiated in 1989. The main objective was to generate additional gainful employment through creation of rural physical infrastructure. Over the period 1980-95, a total amount of Rs. 317.2 billion was disbursed to the rural economy through IRDP and WECs, covering a cumulative total of 47 million poor families. However, there had been an overall decline in the coverage of poverty alleviation programmes in the globalisation era.

In Pakistan, reducing poverty has always been a declared policy in all development plans. As most of the poor lived in rural areas, rural development was considered as essential for any poverty alleviation programme. The first attempt at this was the setting up of Village Agricultural and Industrial Development (Village AID) programme in 1953, which was replaced by Rural Works Programme (RWP) in 1962 with a view to stabilise food prices and create employment at the same time. Later, the Integrated Rural Development Programme (IRDP) was launched to improve the socio-economic conditions of rural masses.

During the period of structural adjustment, direct poverty alleviation programmes were essential to hold the poverty line, as well as to provide social safety nets for the vulnerable. However, these programmes could find only a limited space in the steeply declining government expenditures. During this period, the most important poverty alleviation programmes was the Social Action Programme started in 1992-93. In addition, there were also programmes, primarily based on political considerations, such as Junejo's Five Point Programme, Benazir's People's Programme, and Nawaz Sharif's Tameer-i-Watan—all implemented by the politicians without a clear sense of priority or effectiveness. Other measures included self-employment schemes like Youth Investment Promotion Society (YIPS) and Prime Minister's Self employment Scheme to provide small loans. Social safety nets included Zakat, Ushr and Baitul-Mal, and a limited food stamp programme. The total expenditures of these programmes were no more than half a per cent of GDP.

The inadequate and ineffective public programmes for the poor in Pakistan had left a large space for the NGOs to initiate some successful programmes for social development and poverty alleviation. The Aga Khan Rural Support Programme and Orangi Pilot Project are two examples of how communities in Pakistan are getting together to solve their problems. Recently, a renewed focus of the government to reduce poverty has seen the revival of the old food stamp programme, and the setting up of a micro-credit bank (Khushali Bank) and a Poverty Alleviation Fund.

Social protection programmes

The social protection that a country provides for its citizens through a series of measures against the economic and social distress resulting from sickness and death of an income-earner, unemployment and old age, etc., is the backbone of the modern welfare state. In this era of globalisation, job and income insecurity are increasing, especially for women and other vulnerable groups who are dependent on informal and casual work without any provisions for social protection. In South Asia, where about 80-90 per cent of the labour force is in the informal sector, they are mostly outside the existing social protection schemes that cover only the formal sector.

Inefficient provisioning coupled with leakages in expenditures led to deteriorating quality of services

Sri Lanka is the only South Asian country with a formal sector labour force of over 60 per cent, so the social security programmes in Sri Lanka such as pension, provident funds, and life insurance schemes cover the majority of the workforce. But in Bangladesh, India, Pakistan and Nepal where the majority of the workforce depends on the informal sector, social security system covers only about 10 per cent of the population. The poverty alleviation programmes are designed to provide social assistance to the poor, but due to the rising budgetary cuts, inefficiency and high costs of service delivery even these programmes are not being effective in protecting the needy.

To summarise, the social services expenditure in the post-globalisation period stagnated at the prevailing pre-reform levels. The ratios of expenditures were higher in Sri Lanka as compared to other countries. The South Asian countries are implementing the fiscal compression policy without restructuring the patterns of expenditure. Thus, even in the 1990s, while on the one hand expenditures on social services were being reduced, overall public expenditure continued to be high due to non-development expenditure. The cut-backs of expenditures also reduced the effectiveness of service delivery.

Conclusions

During the globalisation period in 1990s, demographic transition was faster with improved life expectancies and declining death rates of population. The structure of the population had a growing share of the aged population. The composition of the population indicated persistent gender disparities with females constituting less than 50 per cent of the total population. Such disparities were particularly sharp in low human development countries and persisted in terms of education, health, nutrition, and employment opportunities.

The already poor social attainments remained at lower levels during the globalisation period. While in Sri Lanka, mean years of schooling improved from seven years of schooling in early 1970 to eight years in the 1990s, the average in other South Asian countries were as low as less than primary level education in both periods. With globalisation the demand for highly skilled and specialised labour force increased, however none of the countries mobilised or provided additional resources to the tertiary education sector.

The region has been facing dual challenges posed by infectious diseases as well as increasing burden of non-communicable diseases or lifestyle diseases. The countries are also subjected to increased cases of TB, malaria and HIV/AIDS. Over one-fifth of the population in the region did not have access to health care services. Overall health expenditures were reduced to levels that were lower than those in the pre-reform periods in most countries.

Inefficient provisioning coupled with leakages in expenditures led to deteriorating quality of services. Thus, there has been a trend of rising proportion of drop-out rates at the primary education level, declining provision of public health facilities, disproportionate population and health personnel ratio, and poor off-take of food grain provisions from the public distribution system. Improvements in human development indicators during this period were very slow, largely due to the social policies implemented in the pre-globalisation period.

Bulk of the labour force in Bangladesh, India, Pakistan, and Nepal was characterised by high illiteracy and lower educational attainments. Such attainments restricted the entry of such labour into formal sector employment, and led to rise in the movement towards informal sector activities that included casual employment, self-employment, own account enterprises and unpaid family work. The informal sector wage rates in these countries were lower than the formal sector wages. Hence, we observe the trend of rising underemployment rates in these countries rather than unemployment.

In Sri Lanka, on the other hand, better literacy levels maintained the formal sector employment opportunities. The proportionate share of public sector employment in total formal sector employment was far higher than private sector employment. The fiscal compression during the globalisation period reduced employment opportunities in the sector. In the process, unemployment rates reached staggering heights of 14 per cent.

While incidence of poverty declined both in terms of depth and severity, inter and intra regional disparities persisted. Income distribution was skewed towards higher income groups. While, on the one hand growing marginalisation of land holdings led to rising agricultural labour, on the other hand, poor agricultural wage rates led to migration of labourers to urban areas in search of non-agricultural employment. But the freezing of formal sector employment opportunities led to a rise in unemployment rates, as in Sri Lanka, and resort to informal sector activities, as in other South Asian countries.

Rising investments from transnational corporations, as well as rising domestic competition, increased reliance on flexible production processes that changed employment patterns drastically. Rising sub-contracting and growing casualisation of labour reduced the share of formal sector employment.

The resource crunch during this period led to cut-backs of expenditures of asset creation and wage employment programmes that were initiated as a direct poverty alleviation measure. However, better targeting in Sri Lanka and involvement of NGOs in Bangladesh provided safety-nets to the poor.

The resource crunch led to cut-backs of expenditures of asset creation and wage employment programmes that were initiated as a direct poverty alleviation measure

The social security provisions available to the working population also decreased with changing employment structure. Since bulk of the workforce in Bangladesh, India, Pakistan and Nepal are employed in the informal sector, formal sector social security measures did not reach this population. The coverage of these schemes was better in Sri Lanka because of sizeable proportion of formal sector workforce. The income security in the country was also maintained due to the presence of traditional labour market institutions that regulate levels of wage rates. Thus, the majority of work force in Sri Lanka was covered by income, employment as well as social security. But Bangladesh, India, Nepal and Pakistan had fewer social protection provisions.

Social policy in the region prior to the globalisation process was pro-poor that aimed at raising growth levels through equitable distribution of assets and income. During the reform period the social policy largely driven by a growth-mediated process had led to inequitable distribution of assets and income. The role of government was transformed from a provider to a facilitator. The Sri Lankan experience in this context is particularly relevant. In the pre-1977 period the government policy was in-built with egalitarian ethos that aimed at raising human capabilities through investment in basic education and public health. This enabled the country to achieve high human development levels. In the post-liberalisation period, human development outcomes in the country remained around the pre-reforms levels, pointing towards a lack of continued commitment for raising social development in the country. Bangladesh and India on the other hand, had been implementing a plethora of programmes that were administered by several ministries, departments and agencies, thus, raising administrative costs of the programmes. In the reform period, fiscal cuts were directed towards reducing development expenditures rather than the administrative expenditure, by integrating the programmes to a unified scheme. Globalisation was thus characterised by social policies that were not sensitive to people's needs and concerns.

The assessment of the economic reform policies initiated in the region to facilitate the globalisation process and their impact on growth and human development are discussed in the next chapter.

4

Economic Reforms and Globalisation: Country Case Studies

While policy-makers must accept the logic of the marketplace, they must also turn around and make markets work more efficiently in the interest of all people. It is people-friendly markets that are needed.

– Mahbub ul Haq

Chapter 4

Economic Reforms and Globalisation: Country Case Studies

Reform measures implemented focused on reducing trade barriers, achieving macroeconomic stability, increasing the role of the market and enhancing private sector participation

Introduction

The disappointing outcomes of the economic and social development policies in South Asian countries since their independence are evident from the low levels of per capita income, low human development indicators, high levels of fiscal and current account deficits, and pervasive poverty. All major countries in the region had adopted an inward-looking import substitution policy for industrial development. The state became the dominant player in all economic activities.

The trade and foreign exchange management policies were designed to provide incentives for rapid industrial growth. The scarcity of foreign exchange and food shortages had in due course forced a review of the earlier policies. An attempt was made to improve incentives for both the agricultural sector and export. For agricultural development, policies were focused on providing rural infrastructure, high yielding seeds, chemical fertilisers and irrigation facilities. As a result, major breakthroughs in agriculture were achieved in India, Pakistan and Bangladesh. Selective incentives were also provided for the promotion of exports of manufactured goods. However, the industrial sector, which had initially registered a high growth rate, did not sustain its growth momentum. The import substitution strategy had, however, helped in laying the foundation for industrialisation in terms of both skill development and production of goods for the domestic market. But the strategy did not succeed in accessing the world market. South Asia had missed out on the export expansion of manufactured goods during the past few decades when the world export markets for such goods were growing. East Asia and China were the main beneficiaries by opening up their economies—domestically as well as internationally. Their successes were seen as opportunities that could be exploited if the economies were to open up to world markets and global competition.

South Asian countries started the process of rapid integration into the world economy in the 1990s, except Sri Lanka which had started in the 1970s. The forces determining the architecture of the reform programmes are many and have played themselves out in a complex manner in different countries of South Asia. The need for integration arose out of the realisation of the opportunities for exporting labour-intensive manufactured goods. Access to scarce foreign exchange and advanced technology further underscored the rationale for opening up to world capital and technology markets.

The reform measures implemented focused on reducing trade barriers, achieving macroeconomic stability, increasing the role of the market and enhancing private sector participation in a wide variety of activities, including social sector. In view of the differences in the initial conditions in different economies, it was expected that there would need to be some differences in the design, content and management of the reform programmes. Most reform programmes were initiated and supported by the IMF, World Bank and the Asian Development Bank.

There are many commonalties as well as differences in the implementation of reform programmes. The early attempts in each of the countries were piecemeal and had limited impact. The decade of the 1990s represented a turning point for reforms in the case of all countries. There was a consensus reached by the early

1990s that reforms were needed for accelerating growth. All countries had turned to donors for financial and technical assistance in support of reforms. There was also political support from within the countries for reforms. India had managed to evolve a stable political consensus on the need and type of reforms. Sri Lanka had solved the sustainability issue for reforms due to its longer experience beginning in 1977. Pakistan, Nepal and Bangladesh had an indifferent record in terms of implementation of reforms despite widespread agreement on the need for reform. Changes in governments had invariably affected the extent of implementation of reforms in these countries.

Stabilisation and structural adjustment programmes, often supported by the World Bank and IMF, had aimed at reducing high fiscal and current account deficits, making the economy work more efficiently through macro economic reforms and to integrate the economy to the world economic forces. The governance issues were of critical importance to the outcome of reforms. Political instability often impeded the implementation of reforms and determined the outcome of reforms. Substantial insecurity in the region, mainly due to political differences between India and Pakistan, had resulted in a large burden of defence expenditure in both Pakistan and India. Civil strife in Sri Lanka, Nepal and Bangladesh had also been detrimental to the development prospects of the countries. High security-related expenditures often squeezed the development expenditures, including expenditures on social sectors.

The impact of reforms on growth has generally been positive for all countries in South Asia except Pakistan, where growth has decelerated to about two-thirds of what it was in the pre-reform era. External trade orientation has increased only mildly in all countries. Fiscal deficits have remained high, especially in Pakistan, Sri Lanka and Nepal. India has reduced its current account imbalance considerably, but deterioration has been seen in most other countries. Despite an acceleration in growth, excepting Pakistan, poverty has not been reduced significantly due to worsening distribution of income. In the case of Pakistan, the number of people in poverty has doubled during the 1990s.

This chapter examines the reform programmes undertaken in India, Pakistan, Nepal, Bangladesh and Sri Lanka. It outlines how these programmes relate to the ongoing world-wide globalisation as well as domestic liberalisation processes. In each country, we briefly examine the main features of the reform process and assess their impact on growth, employment and poverty.

The impact of reforms on growth has generally been positive for all countries in South Asia except Pakistan

India[1]

Until at least the 1970s, the Indian economy was seen as a classic case of postwar state-led economic development, within a mixed-economy framework. This approach incorporated the major tendencies of Indian economic planning, including the emphasis on heavy industrial investment until the mid 1960s and the focus on state ownership/control of the 'commanding heights' of the economy (the basic and core infrastructure industries as well as other strategic and economically significant industries), as well as state regulation of many other aspects of economic activity even in the non-core areas. It also meant recognition of the role played in the subsequent decades of Indian development, by the state in subsidising private investment activity in both industry and agriculture.

Over four decades, this broad mixed economy approach brought about some significant if qualified economic successes, as well as glaring failures. The more striking successes were in terms of the substantial increase in aggregate

[1] This is an abridged version of the paper prepared by Jayati Ghosh.

growth rates over the pre-Independence period, as well as the steady diversification of the economy and the building up of a substantial productive base in a range of modern industry. The most striking failures were in the persistence of absolute material poverty among a very large section of the population (such that even at present more than 30 per cent of the population is officially described as below the poverty line) and in the inability to achieve basic human development goals such as education and adequate health provision for the entire population.

Public expenditure reduction has involved a substantial reduction in the expenditure on capital formation, besides cuts in subsidies

The basic elements of the changed economic regime since 1991 have included a system of more liberal imports and reduction/elimination of external trade controls generally; a progressive removal of administrative controls over capacity creation, production and prices, including a move to free markets in foodgrains and a cutting down of food subsidies; a strictly limited (and declining) role for public investment even in important infrastructure sectors, the privatisation of publicly-owned assets over a wide field; a focus on reducing implicit subsidies by raising user charges over a wide range of public utilities and services; an invitation to MNCs to undertake investments (under substantially liberalised conditions relating to ownership, operation and profit repatriation); and financial liberalisation measures that have substantially reduced priority sector lending and subsidised credit and allowed greater capital market innovation.

Overview of economic reforms

A process of creeping liberalisation had been launched by consecutive Indian governments since the late 1970s, and especially after 1985. However, the current phase of economic reform dates back to July 1991, when following a balance of payments crisis generated by the withdrawal of international credit and non-resident Indian (NRI) deposits, India's foreign exchange reserves collapsed. The government opted for conditional credit from the International Monetary Fund to deal with the situation, necessitating policies of stabilisation, and an acceleration of 'structural reform' as well as its extension into the external and financial sectors.

Stabilisation

In theory, stabilisation required a sharp reduction in the fiscal deficit from its record high of 8.3 per cent of GDP in 1990-91 to a targeted 3-4 per cent of GDP over a short span of time. In practice, however, public expenditure reduction has involved a substantial reduction in the expenditure on capital formation, besides cuts in subsidies as well as certain other types of expenditures. The process of stabilisation also required a sharp reduction in the 'monetised deficit' of the government, or that part which was earlier financed through the issue of short-term, *ad hoc* Treasury Bills to the Reserve Bank of India, with the aim of giving the central bank a degree of autonomy and monetary policy a greater role in the economy.

However, progress on reducing the fiscal deficit as a whole has been far short of target. The fiscal deficit which declined from 8.3 per cent to 5.7 per cent by 1992-93, rose sharply to 7.4 per cent in 1993-94. It has since remained above 6 per cent of GDP in three out of five years, and has never fallen below 5 per cent.

The disconcerting feature of the fiscal deficit is not so much its level as the fact that a large proportion of it is due to a deficit on the revenue account of the government, rather than capital expenditure which would presumably lead to future growth. The revenue deficit, which stood at 3.5 per cent of GDP in 1990-91, peaked at 4.0 per cent in 1993-94 and has remained well above 3 per cent in most subsequent years. This implies that the government has had to borrow large sums to finance even its current expenditure. With access to credit in the form of low interest Treasury Bills having been closed as a result of the financial liberalisation agenda, the government has had to borrow at relatively high interest rates from the open market, substantially increasing the interest burden on the budget. In fact, the revenue deficit of central and state governments combined was at the historically high level of 7.2 per cent of GDP in 1999-2000.

This has occurred at a time when the ratio of central taxes to GDP has fallen because of (i) a loss of customs revenues as a result of tariff-reducing trade liberalisation; (ii) reductions in excise duties aimed at triggering a consumer boom; (iii) cuts in direct taxes, partly aimed at providing incentives to save and invest; and more recently (iv) an industrial recession that has affected tax collection adversely. As a result of these various processes, the tax-GDP ratio has fallen quite significantly over the years of economic reform, from close to 11 per cent of GDP to less than 9 per cent in 1999-2000.

This has meant that even to constrain the fiscal deficit at existing levels, expenditures have had to be restrained largely through cuts in subsidies and capital expenditures. Subsidies, which accounted for 2.3 per cent of GDP in 1990-91 fell to 1.3 per cent in 1996-97 and remained at that level in 1998-99. Food subsidies have been sought to be cut through increases in the prices of food issued through the public distribution system to the population above the poverty line, and capital expenditure, which fell from 5.9 per cent of GDP in 1990-91 to 3.7 per cent by 1997-98, have risen only marginally to 4 per cent in 1998-99.

Structural adjustment

The principal aims of the structural adjustment policies adopted as a part of the reform process were: (i) to do away with or substantially reduce controls on capacity creation, production and prices, and let market forces influence the investment and operational decisions of domestic and foreign economic agents within the domestic tariff area; (ii) to allow international competition and therefore international relative prices to influence the decisions of these agents; (iii) to reduce the presence of state agencies in production and trade, except in areas where market failure necessitates state entry; and (iv) to liberalise the financial sector by reducing controls on the banking system, allowing for the proliferation of financial institutions and instruments and permitting foreign entry into the financial sector. Policies specific to the various sectors are considered below.

Industrial policy

Post-reform industrial policy has moved in three principal directions. The first was the removal of capacity controls by 'dereserving' and 'delicensing' industries, or abolishing the requirement to obtain a licence to create new capacity or substantially expand existing capacity. As a result of the dereservation of areas earlier reserved for the public sector and the successive delicensing of industries, there were only nine industries for which entry by private investors was regulated at the end of 1997-98.

The second area of industrial reform related to the dilution of provisions of the Monopolies and Restrictive Trade Practices (MRTP) Act, so as to facilitate the expansion and diversification of large firms. The MRTP Amendment Bill removed the threshold limits with regard to assets for defining MRTP or dominant undertakings, thereby removing any special controls on large firms.

The third type of liberalisation in industry involved foreign investment regulation. The first step in this direction was the grant of automatic approval, or exemption from case by case approval, for equity investment of up to 51 per cent and for foreign technology agreements in identified high-priority industries so long as royalty does not

Food subsidies have been sought to be cut through increases in the prices of food issued through the public distribution system

exceed 5 per cent of domestic sales (8 per cent of export sales). As a follow up, the Foreign Exchange Regulation Act was modified so that companies with foreign equity exceeding 40 per cent of the total were also to be treated on par with Indian companies. Further, Non-Resident Indians and overseas corporate bodies owned by them were permitted to invest up to 100 per cent equity in high priority industries, with repatriability of capital and income. Foreign investors were also allowed to use their trade marks in Indian markets.

The process of tariff reduction has not been uniform across industrial sectors

Trade liberalisation

A distinguishing feature of the economic reforms of the 1990s was the effort to eliminate import controls by rapidly reducing the number of tariff items subject to quantitative restrictions, licensing and other forms of discretionary controls on imports as well as by cutting the rates of tariff on a range of commodities. By the middle of 1998 there were 7117 items that could be imported freely under the Open General Licence (OGL) Scheme.

However, the process of tariff reduction has not been uniform across industrial sectors. Imports of capital goods have been substantially liberalised by placing them under the OGL category, by reducing tariffs and by offering concessional duties for 'project imports' and imports allowed at zero duty subject to promises of exports to be realised. The same is true of imports of intermediates, access to which have been simplified and subjected to lower duties.

In the case of consumer goods, until recently the government was more cautious, especially with regard to duty reduction. This was justified by revenue considerations and with arguments regarding 'non-essentiality'. However, recently, in the two annual export-import policies for 1998-99 and 1999-2000, there has been fairly wide-ranging liberalisation of the import of consumer goods which have been placed on the OGL list, so that currently very few items remain on the negative list for imports.

Reforms in agriculture

The economic reforms did not include any specific package for agriculture. The presumption was that freeing agricultural markets and liberalising external trade in agricultural commodities would provide price incentives leading to enhanced investment and output in that sector. However, the pattern of structural adjustment and the government's macro-economic strategy since 1991 have actually been associated with a reduced rate of overall agricultural growth, declines in per capital foodgrain output and inadequate employment generation.

The post reform strategy involved the following measures specifically related to the rural areas :

(1) Actual declines in Central government revenue expenditure on rural development (including agricultural programmes and rural employment and anti-poverty schemes), as well as on the fertiliser subsidy, in the budgets of 1991-92 and 1992-93 and 1998-99. Some of these cuts, such as that on the fertiliser subsidy, were partially reversed subsequently, but the overall decline in per capita government expenditure on rural areas has remained.

(2) Very substantial declines in public infrastructure and energy investments which affect the rural areas. These have not related only to matters like irrigation but also to transport which indirectly contributes significantly to agricultural growth and productivity through its linkage effects, besides being an important source of rural employment.

(3) Reduced transfers to state governments which have been facing a major financial crunch and have therefore been forced to cut back their own spending, particularly on social expenditure such as on education and on health and sanitation. Quite apart from their welfare implications, these provided

an important source of public employment over the 1980s.

(4) Reduced spread and rising prices of the public distribution system for food. This had a very important effect on rural household food consumption in some areas of the country.

(5) Financial liberalisation measures, including reducing priority sector lending by banks, which have effectively reduced the availability of rural credit, and thus reduced farm investment, especially by smaller farmers.

(6) Liberalisation of trade in agricultural commodities. Imports of a range of agricultural commodities have been shifted from quota controls to tariffs and these tariffs have been very substantially lowered over the 1990s. Exports of important food items, especially rice, have been freed from controls, leading to increased exports of these commodities. These have led to declines in the relative price of importables such as edible oils, and increases in the relative price of exportables such as rice and cotton.

Exchange rate policy

In a series of steps the government has moved to a situation where there is a unified, market determined exchange rate of the rupee, which is fully convertible for current account transactions. In addition, various financial liberalisation measures, discussed below, have had direct and indirect implications for exchange rate management, since they affect the inflow and outflow of short-term capital into the country.

Until the East Asian crisis, the government appeared keen on moving to full convertibility of the rupee. The official Tarapore Committee, set up to draw up a road map for the process, had recommended that the implementation be spread over 1997-98 to 1999-2000 and suggested preconditions to be met sequentially for this. Besides fiscal consolidation, a mandated inflation target and the restructuring of bank capital, the road-map prescribed a stepwise process of financial liberalisation. However, the East Asian crisis put plans for a rapid transition to capital account convertibility on hold for a time, and the capital account of the balance of payments still continues to be governed by a range of restrictions.

Financial liberalisation

An important area where major reforms have been continuously implemented is in the financial sector. The process started with the repeal of the Capital Issues (Control) Act, 1947 and the abolition of the Controller of Capital Issues. Companies could freely seek finance through the capital market, subject to the regulations of the newly created Securities and Exchange Board of India (SEBI). Indian companies were allowed to access international capital markets through Euro-equity shares. A range of non-bank financial companies, including private mutual funds were allowed to operate. Investment norms for NRIs were liberalised and Foreign Institutional Investors (FIIs) were allowed to register and invest in India's stock markets, subject to an overall ceiling (30 per cent) and a ceiling for each individual FII in a particular company's shareholding. In addition, the government did away with the higher rate of capital gains taxation which applied to foreign and NRI investment that chose to invest in the stock market. Besides these, a number of guidelines to ensure transparency in share issues were specified.

The other element in financial sector reform was the regulation of the banking sector in terms of controls on entry by private domestic and foreign players, cash reserve ratios and statutory liquidity ratios, entry of financial institutions into the banking sector, priority sector credit provision and investments and activities, have been substantially eased. A range of new instruments have also been permitted.

Overall, one of the consequences of financial sector reform was India's

Domestic policies with regard to expenditure, interest rates and exchange rates were now influenced by perceptions of how it would affect foreign investor sentiment

growing dependence on volatile short-term flows of capital in the form of FII and NRI investments and NRI deposits. Combined with the decision to allow the value of the rupee to be determined by market forces, which made central bank purchases and sales of foreign exchange the only means by which the government could influence the value of the rupee, resulting in considerable uncertainty regarding the value of the rupee. Further, domestic policies with regard to expenditure, interest rates and exchange rates were now influenced by perceptions of how it would affect foreign investor sentiment. This has substantially reduced the manoeuvrability of the government.

Assessment of reforms strategy

Agriculture

A slowdown is evident in the agricultural sector, where the growth rate in the production of foodgrain in particular has declined sharply. This is evident from table 4.1. For a long time the Indian economy has experienced a secular growth rate of foodgrain production of around 2.5 per cent per annum which was a little higher than the population growth rate.

However, over the period 1990-91 to 1997-98 (both good agricultural years), the growth rate of foodgrain production dropped to 1.2 per cent which was distinctly lower than the population growth rate. In this context, increased volumes of exports (both foodgrain and cash crop) along with higher rupee prices of such exports because of rupee devaluation, have also meant rapidly rising prices of food in the domestic market.

One important factor behind the drop in foodgrain output growth is the drastic decline in real public investment that has occurred in agriculture over a long period. Gross capital formation remained low throughout the 1990s. During the 1990s there has no doubt been a step up in real private gross capital formation in this sector. But much of the increase in private investment has been in the non-traditional sectors of agricultural exports rather than in foodgrain production.

The year 1999-2000 was notable for some significant trends in the agriculture sector. First of all, while aggregate output did not increase much over the previous year's level, output trends in various crops (especially wheat) turned out to be much better than anticipated. Secondly, although intersectoral terms of trade moved marginally against agriculture from the high reached in 1998-99, this continued to be more favourable for agriculture. However, the price situation was markedly different for non-foodgrains than foodgrains. Prices of most non-foodgrain crops continued to remain weak, and those of some, especially oilseeds, plummeted. This reflected not only domestic demand conditions but also the growing role played by international prices consequent upon greater integration with world markets in this sector. On the other hand, foodgrain prices increased at double digit level, despite record production. This is related to the third feature, that food stocks held by the public sector continued to grow, and consumer offtake declined as measures designed to reduce the budgeted food subsidy led to substantial increases in the prices of foodgrain in the Public Distribution System.

In terms of the aggregate price level, 1999-2000 was characterised by low inflation, with the rise in the Wholesale Price Index (WPI) for all commodities contained to about 3 per cent per annum. Inflation was even lower for agricultural commodities, with the WPI for this group increasing by only about one per cent over the year. There was, however, a difference in this regard between cereals and the other crop groups. The WPI for cereals averaged about 10 per cent higher during 1999-2000 than during 1998-99.

The combination of lower output and lower prices suggests that in 1999-2000, the distress was greatest among growers of oilseeds. Even for cotton, although production was lower than the previous year, there were large declines in raw cotton prices.

Table 4.1 Growth of agricultural output (%)

	1980-81 to 1989-90	1990-91 to 1997-98
Food grains	2.85	1.41
Non-food grains	3.77	3.28
All Crops	3.19	2.35
Rice	3.62	1.69
Wheat	3.57	3.28
Coarse cereals	0.39	0.19
Pulses	1.49	1.38
Total food grains	2.73	1.92
Oilseeds	5.46	3.74
Sugarcane	2.71	2.48
Cotton	2.79	3.52

Source: RBI Annual Report 1999-2000.

One important feature that has emerged is that for several of these crops, as indeed even for rice and wheat in certain periods, prices for producers have fallen below the government's Minimum Support Prices (MSP), which were raised significantly especially for rice and wheat. In a closed economy, lower output is normally accompanied by some price increase. But the emerging pattern of relatively lower prices accompanying relatively lower output seems to have become more frequent during the past five years. This reflects the effect of the growing integration of Indian agriculture with world markets, consequent upon trade liberalisation. As both exports and imports of agricultural products have been progressively freed, international price movements have been more closely reflected in domestic trends. And the stagnation/decline in the international prices of many agricultural commodities has meant that their prices in India have also plummeted, despite local declines in production.

Given the current pattern of implementation of the GATT Agreement on Agriculture, most developed countries continue to maintain high levels of explicit and implicit subsidies for their agricultural producers. Subsidy levels in the OECD member countries, after falling slightly in 1995-96, are now back to their pre-Uruguay Round levels. This means that Indian cultivators are not only operating in a highly uncertain and volatile international environment, but are effectively competing against highly subsidised large producers in the developed countries.

All this suggests that the government is no longer able to meet the basic objectives of agricultural price policy, to stabilise prices and ensure producer incentives while simultaneously protecting the poor against undue food price increases.

Industrial growth

Until recently it appeared that there were two distinct phases of growth in the post-reform period, a phase of deflation during which the economy was being sought to be stabilised, and a subsequent phase of recovery, starting from 1993-94. It is now clear, however, that this recovery was a result of transient phenomena. These included the stepping up of the fiscal deficit in 1993-94, and, even after the fiscal deficit had been lowered in the subsequent years, the satisfaction of pent-up demand for a variety of hitherto-not-available luxury consumer goods. Since the rate of growth of the demand for such goods, as opposed to the once-for-all splurge that the satisfaction of pent-up demand entails, is much lower, the stimulus which such demand imparts to industrial production evaporates quickly.

Industrial performance was dismal in 1997-98 and 1998-99. As a result, compared to an average annual growth rate of 8.4 per cent in the index of industrial production (which is distinct from real value added in industry) during the period 1985-86 to 1990-91, the rate for the eight years 1991-92 to 1998-99 comes to 5.7 per cent (see table 4.2).

During 1999-2000, Indian industry appeared to have once again turned a corner. According to figures released by the Central Statistical Organisation, after three years of poor or indifferent performance starting from 1996-97, the industrial sector has experienced a robust recovery during 1999-2000. The growth in the general index of industrial production, which stood at 8.4 per cent in 1994-95 and 12.8 per cent in 1995-96, had fallen to 5.6, 6.6 and 3.9 per cent respectively, in the subsequent three years. The index of industrial production for 1999-2000, however, points to a return to a higher rate of growth of

Table 4.2 Industrial growth rates per annum

(%)

	1981-82 to 1990-91	1991-92 to 1998-99
General Index	7.8	5.8
Manufacturing	7.6	5.9
Electricity	9.0	6.8
Mining and quarrying	8.3	3.0

Source: RBI Annual Report 1999-2000.

Table 4.3 Annual rates of growth of the Index of Industrial Production

(%)

	General	Manufacturing	Mining	Electricity
1990-91	8.2	9.0	4.5	7.8
1991-92	0.6	-0.8	0.6	8.5
1992-93	2.3	2.2	0.5	5.0
1993-94	6.0	6.1	3.5	7.4
1994-95	8.4	8.5	7.6	8.5
1995-96	12.8	13.8	9.6	8.1
1996-97	5.6	6.7	-2.0	4.0
1997-98	6.6	6.7	5.9	6.6
1998-99	4.0	4.3	-1.7	6.5
1999-00	8.3	8.7	9.3	6.6

Source: GOI 1999e.

8.0 per cent. Furthermore, this recovery has occurred predominantly in the manufacturing sector, where the rate of growth rose from 4.3 to 9.0 per cent between 1998-99 and 1999-2000 (see table 4.3).

There are, however, three factors calling for caution when interpreting the implications of the industrial growth figures for fiscal year 1999-2000. First, the pattern of industrial growth underlying the overall improvement in growth is disconcerting. While there are signs of a sharp recovery in both intermediate goods and consumer durables production, with rates of growth rising from 5.9 to 15 per cent and 4.7 to 12.2 per cent respectively, the performance of the capital goods sector has been disappointing with growth actually declining from 11.8 to 4.8 per cent. This is all the more significant since machinery imports registered a negative rate of growth of 11.22 per cent during the year.

Secondly, despite the revival of industrial demand in a more open trading environment, non-oil imports have registered an extremely low rate of growth of just 1.36 per cent during 1999-2000. This points to a stagnation in imports required to service domestic industrial production.

Finally, even before the extent and nature of the recovery in the industrial sector could be fully assessed, there are signs of a slackening of demand in certain industries. The automobile industry, where sales figures are quick to come in, is a case in point.

Furthermore, data just released by the CSO (mid-January 2001, reported in The Hindu, January 16, 2001) indicates that the actual growth rate of manufacturing production in 1999-2000 was only 7.1 per cent, certainly lower than was suggested earlier, and this may be related to some of the weaknesses in the industrial growth that were mentioned above.

The external sector

One of the failures of structural adjustment in India has been its inability to stimulate India's exports to a degree that would counteract any tendency towards stagnation in the domestic market. In the recent period, as well as in the 1990s overall, Indian exports have performed much worse than world exports, and India's share of total world trade has fallen.

Over the fiscal year 1999-2000, the main features of the external trade and balance of payments of India included the following: a recovery in exports after three years of stagnation/decline; an even sharper increase in imports which consequently meant a substantial enlargement of the trade deficit; the continued positive role played by inward remittances in keeping the current account deficit in check; and an increase in portfolio inflows which became the most important form of capital inflow over the year. These processes occurred in a period which was marked by significant policy changes on the external front as well. There was a substantial liberalisation of imports, with the removal of hundreds of items from the list covered by quantitative restrictions, and progressive reduction in import tariffs. The inability to provide export subsidies meant that commodity exporters in particular faced problems in a depressed world market. Meanwhile, there have been substantial changes in the capital account as well. Some of these features can be easily observed from table 4.4.

Exports increased by 13.2 per cent in US dollar terms, in positive contrast to the decline of more than 5 per cent of the previous year. As a result, the value of exports amounted to $37.6 billion. The turnaround was evident mainly for all categories of manufactured goods except leather and leather manufactures. The exports of primary goods, especially of agricultural products, fell by nearly 9 per cent, with very sharp falls evident for rice, tea and coffee. Software exports, which are classified under service exports rather than commodity exports, are estimated to have increased by 53 per cent to reach the level of more than $4 billion.

Imports also accelerated over the year, with total dollar imports increasing by 11.4 per cent to reach $47.2 billion, after only 2.2 per cent increase in the previous year. Much of this was due to the increase in international oil prices. However, non-oil imports also increased.

The invisibles account remained the source of strength for the balance of payments. The net surplus on invisibles amounted to nearly $13 billion, up from just above $9 billion in the previous year. This was essentially due to the continued strength of remittance income, which amounted to $12.26 billion and was able to counteract the increase in outflows of investment income (profits and interest) which was as high as $3.6 billion. One healthy sign is that the geographical base of such remittance income has expanded beyond the Middle East.

It is significant that in 1999-2000, as indeed in almost every other year since 1991, total net invisibles (led essentially by remittance income) have been greater than all forms of capital inflow taken together (see table 4.5).

Portfolio investment recovered from the net outflow recorded in 1998-99, and in fact grew so rapidly as to outstrip FDI as it had earlier in 1995-97. The difficulty with excessive reliance on such inflows is well known after the experience of several emerging markets over the 1990s. Thus, the rediscovery of India as a desirable destination by international portfolio investors is at best a mixed blessing.

Table 4.4 Key Indicators of the balance of payments (as per cent of GDP)

	1990-91	1996-97	1997-98	1998-99	1999-2000
Exports	6.2	8.9	8.8	8.2	8.5
Imports	9.4	12.8	12.6	11.3	12.3
Net invisibles	-0.1	2.7	2.4	2.2	2.9
Current account deficit	-3.2	-1.2	-1.4	-1	-0.9
Foreign investment	0.03	1.6	1.3	0.6	1.1

Source: RBI Annual Report 1999-2000.

Over the year, the capital account has been progressively liberalised. There have been measures to further liberalise ease of entry and exit of foreign capital, as well as access of domestic firms to foreign borrowing. Thus, Indian companies have been permitted to issue rights/bonus shares and non-convertible debentures to non-residents, as well as to issue units to FIIs with repatriation benefits. Policies for both external commercial borrowing and foreign direct investment have been very substantially liberalised. Similarly, rules for capital export have also been liberalised for Indian companies in sectors like IT, pharmaceuticals and biotechnology.

Fiscal patterns

The usual justification for 'rolling back' the state is that the fiscal deficit must be cut, since it is a source of instability of the economy. Not only is this argument questionable, but, what is more, this package tends to intensify the fiscal crisis.

Table 4.5 Capital inflows (in US dollar million)

Per cent of total	1990-91	1997-98	1998-99	1999-2000
Foreign direct investment	1.4	36.2	29	21.2
Portfolio investment	0.1	18.6	-0.8	29.5
External assistance	31.3	9.2	9.6	8.8
External commercial borrowing	31.9	40.6	50.9	3.1
Short-term credits	15.2	-1	-8.7	3.7
NRI deposits	21.8	-7.8	-9.4	-6.9
Rupee debt service	-16.9	-7.8	-9.4	-6.9
Other capital	15.2	-7.2	9.1	19.8
Total - US$ million	7,056	9,844	8,565	10,242

Source: RBI Annual Report 1999-2000.

The fiscal adjustment in India has left the size of the revenue deficit unchanged or even enlarged, and instead impinged heavily on public investment and welfare expenditure

There is an important distinction to be made here. In an economy that is liberalised with respect to the capital account of the balance of payments, and hence open to speculative capital flows, it may well be the case that speculators look at the size of the fiscal deficit which thus becomes a determinant of their state of confidence, but this is different from saying that the fiscal deficit *per se* is destabilising. The latter argument is untenable for several reasons.

First, the size of the fiscal deficit, which shows the net demand arising from the government, does not have anything to do directly with 'instability' in the sense of either generalised inflationary pressures or an unmanageable trade deficit, since the latter depend upon *ex ante* excess aggregate demand. Secondly, while borrowing to meet current expenditures does require scrutiny (though it is not always reprehensible, for example, in a recession) since it is indicative of 'living beyond one's means', there is nothing necessarily wrong with borrowing to meet investment requirements. If the focus was on a reduction of the revenue deficit, then it might make sense, but by emphasising the fiscal deficit as distinct from the revenue deficit, the IMF and the World Bank deliberately try to negate the role of the government as an investor. Thirdly, a reduction in the revenue deficit, or in the fiscal deficit, can be brought about in a number of different ways, the obvious one being by an increase in direct tax revenue. Indeed in any developing economy where glaring poverty coexists with offensive opulence, increased revenue from direct taxes is urgently called for anyway as a means of reducing inequalities. But policies of liberalisation underplay this avenue of deficit reduction and emphasise cuts in investment and welfare expenditures.

Not only is the theory underlying such cuts invalid, but the fiscal deficit which is invoked to legitimise such cuts gets aggravated because of structural adjustment. Since inviting direct foreign investment becomes an overriding objective of economic policy, the rates at which they are taxed get reduced in competition with other countries. This, for reasons of symmetry, means that direct tax rates on the rich as a whole are lowered. Since customs duties are cut as part of the import liberalisation package, and excise duties, again for reasons of symmetry, cannot be raised as a consequence, indirect tax revenues too suffer. This is aggravated by the sluggishness in output growth rate that cuts in government expenditure may engender.

While tax revenues cannot be raised for lowering budget deficits, the increased interest rates result in a larger interest burden on the government. Increased interest rates on public sector borrowing are typical results of the financial liberalisation process. Two features are particularly significant in this process : first, the removal of interest rate caps and other such restrictions in the credit market, which allow all interest rates to go up; and the raising of norms on the statutory liquidity ratios and other such compulsory holding of government securities, which force the government to take recourse to open market borrowing to finance deficits.

Thus this type of structural adjustment, which aims to restrict the fiscal profligacy of the state, contains within itself processes which work to aggravate further the fiscal situation, through lower taxes on the rich and higher interest rates.

The fiscal adjustment in India has left the size of the revenue deficit unchanged or even enlarged, and instead impinged heavily on public investment and welfare expenditure. The process of adjustment has further entailed a very specific fiscal regime, which has increased transfers from the state to rentiers in the form of interest payments, and to enforce larger fiscal burdens on the people and cuts in public investment (see table 4.6).

Poverty and employment

There is now substantial evidence that India's success at reducing the incidence of poverty during the 1970s and 1980s was halted, if not reversed, during the 1990s. Estimates made at the World Bank (Datt 1999) show that the incidence of poverty, which between 1972-73 and 1989-90 fell from 55.4 per cent to 34.3 per cent in rural India and from 54.3 to 34.1 per cent nationally, has in subsequent National Sample Survey (NSS) rounds up to 1997 (when the incidence was 34.2 per cent national and 35.8 per cent rural) never gone below the 1989-90 level and has in fact risen to much higher levels in individual years. Other estimates (eg., Gupta 1999) suggest an even greater increase in rural poverty during the 1990s. The estimates for the head count ratio of per cent of rural population living in absolute poverty, are provided in table 4.7. All these estimates indicate, moreover, that the gap between rural and urban areas, which had decreased during the 1980s and the 1970s, increased considerably during the 1990s.

Food items have a large weight in the indices of consumer prices for industrial workers and agricultural labourers, especially the latter. The faster rise in these indices are therefore, likely to result in faster increase in the prices of various food items, particularly cereals, than of other items consumed by the rich. Thus what emerges is that one of the reasons for the stagnation in real per capita consumption and therefore of the incidence of rural poverty during the 1990s is the adverse consequence that rising food prices have had for the poorer sections of India's population. Clearly, the rise in the relative food prices during the 1990s has hit the poor hard, even at a time of relatively high income growth which itself was accompanied by some increase in the inequalities in nominal consumption expenditures.

But in addition to this decline in the purchasing power of the incomes of the rural poor, the rate of growth of per capita rural income in real terms has sharply decelerated. This fall in rural incomes is, however, not just because the share of agricultural income in national income has fallen. The share of non-agricultural incomes in total rural incomes which rose sharply between 1977-78 and 1990-91, has stagnated since then. One reason why rural poverty declined during the 1970s and the 1980s was that income

Table 4.6 Some fiscal magnitudes as ratios of GDP

(%)

	Revenue deficit	Fiscal deficit	Interest	Subsidies
1988-89	-2.7	-7.8	4	2.2
1989-90	-2.6	-7.8	4.3	2.6
1990-91	-3.5	-8.3	4	2.5
1991-92	-2.6	-5.9	4.3	2.2
1992-93	-2.6	-5.7	4.5	1.9
1993-94	-4	-7.4	4.5	1.6
1994-95	-3.2	-6.0	4.6	1.3
1995-96	-2.7	-5.4	4.5	1.2
1996-97	-2.6	-5.2	4.6	1.3
1997-98	-3.3	-6.3	4.7	1.4
1998-99	-3.8	-6.5	4.8	1.3
1999-00*	-2.3	-4.4	3.7	0.9

Notes: * refers to Budget estimates
- Revenue deficit refers to current expenditure minus current revenue
- Fiscal deficit refers to all expenditure minus current revenue, that is revenue deficit plus capital expenditure
- Interest refers to all interest payments of the government
- Subsidies refers to all direct budgetary allocation for subsidies, i.e. Food and Fertiliser subsidies

Source: Economic and Political Weekly, Budget Number, May 1997 & Budget at a Glance, Ministry of Finance, Govt. of India, 1999-2000.

Table 4.7 Estimates of rural head count poverty ratios

NSS Round	Year	Rural poverty ratio World Bank	Rural poverty ratio S.P. Gupta	Real per capita consumption (1973-74 prices)	Gini-Index
46	Jul 90 - Jun 91	36.43	35.00	66.73	27.72
48	Jan 92 - Dec 92	43.47	41.70	63.80	29.88
50	Jul 93 - Jun 94	36.66	37.30	67.45	28.58
51	Jul 94 - Jun 95	41.02	38.00	66.39	30.17
52	Jul 95 - Jun 96	37.15	38.30	67.37	28.43

Source: Datt 1999 and Sarvekshana, various issues.

Table 4.8 Work participation rates for rural men and women (%)		
	Male	Female
1972-73	54.5	31.8
1977-78	55.2	33.1
1987-88	53.9	32.3
1989-90	54.8	31.9
1990-91	55.3	29.2
1993-94	55.3	32.8
1994-95	56	3.17
1995-96	55.1	29.5
1997	55	29.1
1998	53.9	26.3

Source: Sarvekshana, various issues.

earning opportunities in the rural non-agricultural sector, expanded substantially, driven mainly by a large expansion of government expenditure in the rural areas. The reduction in such expenditure during the years of reform has affected that expansion adversely.

In terms of rural employment patterns, table 4.8 presents the work force participation rates (number of all workers as a ratio of total population) for men and women in rural India from the early 1970s to the late 1990s. It is evident that the male work force participation rates have remained broadly stable over this entire period. The overall picture of female work force participation in the rural areas is one of fluctuations around a *declining* trend. Female work force participation rates were, on average, significantly higher in the 1970s until the mid-1980s. The latest year in fact shows the lowest rate over the entire period.

There is now significant evidence that the main dynamic source of rural employment generation over the period from the mid 1970s to the late 1980s was the external agency of the state rather than forces internal to the rural economy or other extra-rural forces including modern industry and commerce. In fact, in most areas the pivotal role in the expansion of rural non-agricultural employment appears to have been played by the expansion of government expenditure.

The pattern of structural adjustment and government macroeconomic strategy since 1991 involved the following measures which specifically related to the rural areas : (i) Actual declines in Central government revenue expenditure on rural development (including agricultural programmes and rural employment and anti-poverty schemes), resulting in an overall decline in per capita rural government expenditure. (ii) Substantial declines in public infrastructure and energy investments which affect the rural areas. These have related not only to matters like irrigation but also to transport and communications which indirectly contribute significantly even to agricultural productivity, besides being an important source of rural non-agricultural employment. (iii) Reduced transfers to state governments which have been facing a major financial crunch and have, therefore, been forced to cut back their own spending, particularly on social sectors such as education and health and sanitation, which had provided an important source of public employment over the 1980s. (iv) Reduced spread and rising prices of the public distribution system for food. (v) Financial liberalisation measures which effectively reduced the availability of rural credit. Thus, in the 1990s, several of the public policies which contributed to more employment and less poverty in the rural areas in the earlier decade, have been reversed.

Pakistan

Like India, Pakistan had adopted a mixed economy approach to development, consisting of an import-substitution strategy and the public sector domination of major sectors of the economy. However, the role of the private sector till the 1970s was relatively more pervasive than in India. With nationalisation of the financial sector institutions and heavy industry during the early 1970s, the public sector became more prominent. As a result of growing inefficiency and losses by the public sector enterprises, Pakistan was soon faced with high macro imbalances. In 1988, the government was forced to enter into stabilisation and structural adjustment programmes with the IMF and World Bank. However, the economic performance during the 1990s had been unsatisfactory. The growth rate had declined considerably and poverty had increased.

Overview of economic reforms

The adjustment programmes agreed with the World Bank, IMF and the Asian

Development Bank comprised policies of stabilisation as well as structural adjustment. The IMF was mainly concerned with the stabilisation of the economy, while the other two donors were responsible for the structural reforms. The reform measures introduced since 1988 had historical precedents as Pakistan had negotiated a number of loans with the World Bank and IMF during the 1980s. However, these attempts were mostly piecemeal and ad hoc in nature. The reforms introduced since 1988 were comprehensive in scope, comprising of stabilisation, structural adjustments and institutional reforms.

Stabilisation policies

The high macro-economic imbalances minimise the efficacy of market signals provided by the incentive structure to the economic agents. It is for this reason that stabilisation measures precede the introduction of structural reforms. The various programmes negotiated with the IMF had, therefore, stipulated sharp reduction in the fiscal deficits from about -8 per cent of GDP to a sustainable level of about -4 per cent of GDP over the programme period. The measures recommended were reduction of subsidies, upwards adjustment of user charges, expenditure curtailment and tax reforms aimed at revenue mobilisation. The stabilisation measures had also stipulated sharp credit restraints and a reduction of the monetisation of fiscal deficit through monetary reforms.

Structural adjustment policies

Pakistan had been suffering from deep-rooted structural distortions hindering achievement of high economic growth. Slow growth rates had increased the incidence of poverty during the 1990s. The high protection to industries became a source of inefficiency. The pervasive presence of public enterprises has exacerbated the fiscal deficits. The resource mobilisation has been constrained by a narrow-based tax system, high interest payments, subsidies, and non-development expenditure on defence and establishment. Other economic problems were due to deteriorating irrigation and drainage system slowing down agricultural growth, anti-export bias of the trade and tariff regimes leading to weak export growth, and weak financial system constraining private sector growth. The government had adopted a comprehensive structural reform programme to address these problems.

Public finance reforms

With respect to public finance, the adjustment programme had aimed to reduce the fiscal deficit by improving resource mobilisation and curtailing public expenditure. On the revenue side, resource mobilisation was to be done by expanding the coverage of the tax net and improving its elasticity. A structural shift away from taxes on international trade and excise duties was to be effected. It was envisaged that a revamped direct tax system including taxation of agricultural incomes and the broad-based sales tax would generate enough resources to make up for the loss of revenue from reduced taxes on international trade and domestic production. The reduction in rates of direct tax on incomes was introduced to curb tax evasion.

The increases in the expenditure on social sectors and essential development projects were envisaged. The adverse impact on the size of fiscal deficit was to be avoided by counter-balancing the increased public expenditure by planned reductions in transfer payments (especially subsidies) and current expenditures in areas such as defence.

Financial sector reforms

The monetary and fiscal mismanagement in Pakistan has been the root cause of macro-instability. High fiscal deficits were accommodated either by increased money supply or by requiring commercial banks to hold extensive government debt at below market rates. Subsidised lending to agriculture, exports and locally manufactured machinery was also an implicit tax on the banking system.

Government of Pakistan initiated a process of financial sector reforms at the beginning of the 1990s. The aim of the reform process was to enhance the efficiency of the financial sector and to ensure its health and viability. The reforms cover enhancement of competition in financial sector through privatisation of the state-owned financial institutions and by allowing the establishment of new financial institutions in the private sector; rationalisation of interest rates structure by eliminating subsidised credit; replacement of direct controls by market-based monetary and credit management and strengthening of regulatory and supervisory framework by making the State Bank of Pakistan autonomous.

Monetary and credit management

A number of fundamental changes have also been made in the conduct of monetary and credit management which essentially marked a departure from administrative controls and quantitative restrictions to market-based monetary and credit management. The introduction of public debt auctions, abolition of credit ceiling and credit deposit ratio (CDR), active open market operations, the prudential regulations announced by the State Bank of Pakistan and strengthened system of loan recovery were meant to improve monetary and credit management.

Capital market reforms

Since the start of the privatisation and opening up of the capital account in 1991, equity market in Pakistan has grown rapidly. The equity market remains however, underdeveloped, shallow and subject to manipulation from insider trading. The government has implemented a number of reforms to rectify the malpractices and strengthen the capital market. Removal of tax anomalies and provision of incentives by way of relaxing limits in shares by provident funds and insurance companies have been the main reform areas. The conversion of the Corporate Law Authority into an autonomous Securities and Exchange Commission has also been helpful for rapid growth of the capital market.

Trade policy reforms

Historically, Pakistan's trade policy was biased towards import substitution with pervasive non-tariff barriers, high average tariffs, a wide dispersion of tariff rates with numerous exemptions and a duty draw-back system and cash subsidies for the selected manufactured exports. A substantial move towards trade liberalisation was negotiated by the government with the IMF and World Bank in the early 1980s. The reductions in quantitative barriers were to be followed by tariff reforms. The reduction in non-tariff barriers has been a continuous process during the 1980s and the 1990s. Each year, at the time of the finalisation of the budget and the trade policy, measures aimed at trade liberalisation were announced. But the tariff reforms were slow in actual implementation. The fear of loss of revenue from tariff reforms by the government was a dominant consideration in the slow implementation of tariff reforms. The pace of trade reforms was faster since 1988-89, however (see table 4.9).

Like most countries in the developing world, the tariff structure of Pakistan is cascading in nature. The maximum rate of tariff in 2000-2001 was 30 per cent, with the exception of automobiles and alcoholic beverages which attract higher rates of duties. The minimum rate of import duty of zero per cent is generally charged on basic raw material, food stuff and other essential imports.

In March 1993, import licences were abolished for all goods except those on

Table 4.9 Indicators of trade liberalisation

Fiscal Year	Items removed from negative list[a]	Items removed from restricted list[b]	Maximum tariff (%)[c]	Import surcharge (%)	Iqra surcharge (%)	License fee (%)
1987-88	136	10	225	5	5	4
1988-89	169	51	125	6	5	5
1989-90	70	20	125	7	5	5
1990-91	97	43	95	10	5	6
1991-92	23	17	90	10	5	6
1992-93	21	11	90	0	5	6
1993-94	1	1	90	0	5	6
1994-95	8	–	70	0	0	0
1995-96	11	–	65	0	0	0
1996-97	–	17	65	0	0	0

Notes:
a: Items removed are a mixture of numbers and categories and, therefore, are only a broad indication.
b: the concept of restricted list abolished in 1994-95. Restricted list contains importable products by specified importers and industrial consumers only.
c: Automobiles and alcohol continue to carry tariffs up to 425%.

Source: MHHDC staff calculations.

Most of the goods produced in the country have continued to remain on the negative list

the negative and the restricted list. The scope of lists specifying prohibited and/or restricted imports has also been sharply reduced. However, the trade regime even now contains some anti-export bias as the tariffs are still high and some items remain in the restricted list for imports.

Until 1983-84, the import licences could be issued for only those products which were specified either on the free list or the tied list. Import licences issued under the tied list could be used for imports from only those countries which were explicitly mentioned in the tied list. A major liberalisation of the import policy took place in 1983-84. The list covered all such products which could not be imported. Products on the tied lists can be imported from specified sources or for specified users. All other products can be imported from any country without any restrictions after obtaining an import licence. With the passage of time, the number of products on the negative list has been reduced, i.e., imports of more products has been allowed.

The introduction of the negative list has been a major step forward, as it allows free imports of capital goods and industrial raw materials. However, most of the goods produced in the country have continued to remain on the negative list. This has provided excessive protection even when the tariff rates are low.

Exchange rate policy

Pakistan followed a fixed exchange rate policy from 1947 to 1982. The appreciation of dollar in the early 1980s against other major currencies adversely affected the competitiveness of Pakistani products in international markets because at that time the rupee was linked to U.S. dollar. Given Pakistan's widely diversified trade and financial relations, the rupee peg to a single currency proved costly if the currency to which it was pegged appreciated considerably. To maintain competitiveness of exports, a managed floating exchange rate system was adopted with effect from 1982. Under this system, the value of the Pakistani rupee was reviewed daily with reference to a trade-weighted basket of currencies of the country's major trading partners/competitors. Small adjustments are made in the value of the rupee as and when circumstances indicate a need for such adjustments, keeping in view the relative changes in exchange rates and prices of the country's major trading partners/competitors, as well as major macro-economic indicators of Pakistan.

Deregulation of economic activity

The government had been regulating the resource allocation process through numerous direct controls in the form of investment sanctions, price controls and the practice of cost-plus pricing. The structural reforms introduced since 1980 had reduced, and in some cases even abolished, the direct controls on economic activity. Cost-plus pricing in key industries of cement, fertiliser and vegetable ghee had been stopped. The deregulation measures implemented during the 1980s made substantial progress towards market-orientation of the economy. The remaining regulations and administrative bottlenecks for both domestic and foreign investors were removed during the 1990s.

Investment controls were eased in the early 1980s. 170 industries were put on a positive list in 1984. Investors in these industries did not require an investment sanction if the value of the investment was below a certain specified limit. Industries with a value of investment above the specified limit required the sanction. Investment projects having a large import component for inputs and machinery, had to be approved by the government.

The nature of price reforms introduced in agriculture, energy and public utilities was to provide price incentives that lead to efficient consumption and production decisions. In the case of the agricultural sector, support prices of major crops were targeted to move closer to the import or export parity prices. This was to be done each year at the time of fixation of support prices for different crops. The input subsidies were to be curtailed and/or removed. The economic pricing of gas, oil and electricity was also introduced gradually during the 1980s and 1990s. Considerable progress has already been made in moving the prices of these goods to the level of import parity prices.

Under the Price Control and Prevention of Profiteering and Hoarding Act 1977, the government fixed prices of 66 essential products. With the de-control measures, the government no longer fixes the prices of these essential products. Despite this, the price controls continue to exist in many forms. The Ministry of Health continues to fix the prices of drugs and medicines. The prices of goods produced by the public utility companies are subject to control by the government. From time to time, provincial and local authorities also fix the prices of commodities they perceive to be in short supply.

In order to encourage investment in industries for which the prices were controlled, the government had operated a system of subsidies and surcharges to ensure a specified return on equity to producers. Profits higher than the specified rates were captured by government through surcharges. Any shortfall in the profit rate was matched by government subsidies. This system operated in cement, edible oils, fertilisers, and petroleum-refining industries.

The system of cost-plus pricing was not helpful in achieving efficiency. The improvement in productivity was siphoned off through surcharges while fall in productivity was protected by subsidies. With a view to improving productivity, cost-plus pricing system was ended for the cement, vegetable oil, and fertiliser industries. The prices and profits of these products are now determined by the market forces.

Industrial policy reforms

The industrial policy was revised with a focus on giving more space and freedom to the private sector, which is expected to assume a major role in future industrialisation process. In the past, effective implementation of industrial policy was hindered by the hesitant participation of the private sector in an atmosphere of uncertainty regarding government's economic policies, procedural delays in the approval of projects and inadequacy of infrastructural facilities.

Main feature of the industrial policy with respect to government controls has been that government sanctions are no longer required for the establishment of new industrial units, irrespective of size, sponsorship or location; the only exception to this policy framework are industries which are controlled for security or religious reasons. For newly-established industries, liberal tax and tariff concessions have been allowed; the requirement for obtaining sanctions for industrial investment has been removed; foreign exchange transactions have been liberalised; foreign investment is permitted up to 100 per cent of equity without prior approval; profits and capital can be remitted without difficulty; the fixation of interest rates, technical fees, and royalties has been left to the market forces.

In the past, tax holidays were granted to different industries and/or some industries in different locations. Such incentives implied huge losses in revenue for the government. These incentives were also non-transparent. The government's declared policy is to move away from the granting of tax incentives.

Restructuring of public sector enterprises

The significant burden on the treasury imposed by the losses of the public sector enterprises (PSEs) and their low efficiency levels were two main areas of policy concern for the public enterprises.

The government initially tried to improve the performance of public enterprises by the introduction of a 'public enterprises signaling system' which attempted to force such enterprises to behave like private firms. In addition, management autonomy was given to the state enterprises. The continuing burden on the treasury from the assured access to formal credit for such enterprises and other subsidies has forced the government to reduce the number of public enterprises in the economy. The privatisation programme is based partly on the perception that public sector enterprises are inefficient and have placed undue burden on the budget.

Privatisation

The privatisation of industrial and financial institutions was extremely slow during the 1980s. By the end of the 1980s the government-owned industrial enterprises constituted 10 per cent of value added in manufacturing industries. Government-controlled companies were dominant actors in a wide range of sub-sectors including fertilisers, cement, automobiles, iron and steel, agro-processing, engineering, chemicals and textiles. The government also had a monopoly control in telecommunications, the power sector, rail and air transport. Petroleum and gas extraction were controlled by the state-owned companies and/or joint ventures between the government and international oil and gas companies. The government had launched a huge effort in 1990 to privatise the PSEs. However, Pakistan has been successful in privatising only small and medium-sized industrial units and relatively smaller commercial banks. The pace of privatisation has been slow in the face of complexities of dismantling large units. Absence of regulating frameworks and retrenching surplus labour have emerged as major constraints.

Pace of privatisation has been slow in the face of complexities of dismantling large units

Assessment of reform strategy

At the time of introduction of comprehensive adjustment programme in 1988, the stability of Pakistan's economy, by reducing its fiscal and balance of payments deficits, was the key priority. The economy had grown strongly during 1980-87 at 6 per cent per annum. The incidence of poverty had declined sharply during this period. There was some concern about the sustainability of high growth as the growth was financed by large domestic and foreign borrowings.

The reform programme had two explicit objectives of stabilisation and assuring the sustainability of past high growth through removal of structural distortions. It was presumed that poverty would be automatically reduced with high and stable growth. However, the impact of reforms on growth, stability and human development has been contrary to the policy-makers' expectations. All previous

Table 4.10 Average annual growth rates

Sector	1980-81 to 1989-90	1990-91 to 1999-2000	Extent of Reduction (%)
GDP	6.5	4.6	-29.3
Agriculture	5.4	4.4	-18.5
Industry	8.2	4.8	-41.5
Services	6.7	4.6	-31.3

Source: Government of Pakistan, Economic Survey, various issues.

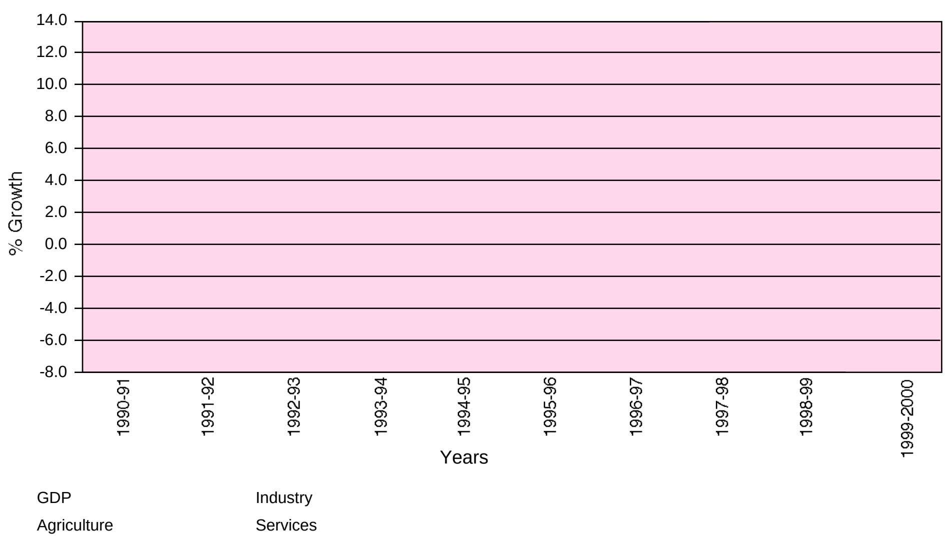
gains in terms of growth and poverty reduction were reversed in the 1990s.

Impact on growth

There is strong evidence showing that reforms had resulted in a significant slow-down in all sectors of the economy. Table 4.10 shows the average performance by decades, while figure 4.1 shows the GDP and sectoral growth rates on an annual basis during the 1990s.

The overall growth rate of GDP fell from 6.5 per cent in 1980s to 4.6 per cent during the 1990s. The growth in industry had declined by 42 per cent in the 1990s relative to the earlier decade. Agriculture and services also showed significant declines in growth rates. The yearly variation in the growth rates were large for agriculture and large-scale manufacturing sector.

Figure 4.1 Annual growth of GDP and sectors



Source: Government of Pakistan, Ecnomic Survey, various issues.

Agriculture

Despite the slow-down in agriculture during the 1990s, the value-added in the sector has grown at 4.6 per cent per year. The magnitude of agricultural growth had been larger than any country in South Asia. There had been two major problems with the nature of agricultural growth, however. First, there had been a lot of fluctuations in agricultural growth in the 1990s. In some years, there had been a decline in absolute terms. Secondly, the decline and instability in the agricultural sector had been concentrated mostly in the crops sub-sector. Livestock, fisheries and forestry had not exhibited much fluctuations. The decline in agricultural production had been attributed to bad weather, pest attacks, declining public investment in the sector and the deteriorating irrigation and drainage system. The impact of improved price incentives for agricultural sector from reforms was more than counter-balanced by the adverse non-price factors facing the agricultural producers. Table 4.11 shows the pattern of growth of agriculture.

Industry

The industrial sector had declined the most during the post reform decade. Value-added in large-scale manufacturing, especially cotton ginning and sugar industries, was hurt by the decline in output of cotton and sugar cane. The removal of export duty on cotton had increased the cost of raw material for cotton textiles. Cement output had fallen due to contraction in demand from slow-increasing private investment and sharp cut-backs in public investment. However, that variation in industrial growth was dominated by changes in the output of the manufacturing and construction sub-sectors. Electricity and mining had a limited impact on variability of growth rates in industrial sector due to their small weight in the industrial output (see table 4.12).

Table 4.11 Agricultural growth by crops

(% growth)

	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00
All crops	-10.9	1.1	6.6	7.7	-3.8	8.0	0.3	11.5
Food crops	1.3	4.5	7.4	3.4	0.6	8.8	1.5	13.4
Fibre crops	-29.2	-1.3	8.3	21.9	-11.4	-2.3	-4.3	27.8
Other crops	-1.4	6.9	11.0	-2.9	-4.2	22.6	3.6	-13.9

Source: GOP, Economic Survey, various issues & GOP, State Bank of Pakistan Annual Report 1998-99.

What are the factors responsible for the slow-down in industrial growth? Decline in public investment, high interest rates, shrinkage of demand from import liberalisation, low demand from a slowly growing agricultural sector, poor export performance and lower supply of credit are some of the factors that explain the slow-down in industry.

Table 4.12 Industrial sector growth

(% growth)

Years	Mining & quarrying	Manufacturing	Construction	Electricity and gas
1990-91	10.36	6.25	5.70	11.00
1991-92	2.44	8.05	5.98	9.07
1992-93	3.00	5.35	5.80	6.38
1993-94	4.66	5.39	1.64	3.17
1994-95	-4.30	3.69	1.01	16.83
1995-96	7.07	4.80	3.25	10.14
1996-97	1.87	1.29	1.09	-2.91
1997-98	-9.70	7.88	1.26	8.96
1998-99	3.17	3.73	-4.92	17.14
1999-2000	6.15	1.42	5.15	-9.83

Source: GOP, Economic Survey, various issues.

Impact on stability

Macroeconomic stability is an essential requirement for equitable, high and sustainable growth. High fiscal deficits eventually end up in high inflation with adverse consequences for export expansion, capital flight and social well-being of the majority of population. High fiscal and current account imbalances also make the country dependent on international financial institutions.

Despite the stipulation of structural adjustment packages negotiated with donors that the fiscal deficit will be reduced to the sustainable level of 4 per cent of GDP, Pakistan has never succeeded in decreasing the fiscal deficit.

There was, however, a reduction of about 2 per cent of GDP in the overall fiscal deficit. This has been brought about mainly by the reduction in development expenditure. There was no increase in tax to GDP ratio. There was, however, a slight decline in expenditure on subsidies in line with the conditions agreed between the donors and the Government of Pakistan. The expenditure on debt servicing has increased significantly as it has gone up from 7.2 per cent of GDP in 1990-91 to 11.8 per cent in 1999-2000. The size of public debt as a percentage of GDP is highest in Pakistan relative to all other countries in South Asia. Rising expenditure on interest payments is a source of increasing inequity. The reduction in fiscal deficit through cuts in public investment

Table 4.13 Fiscal imbalances

(% of GDP)

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-2000
Gross fiscal deficits	-8.8	-7.5	-8.1	-5.9	-5.6	-6.5	-6.4	-7.7	-6.1	-6.5
Revenue deficits	-3.5	-2.6	-2.6	-4.0	-3.2	-2.7	-2.6	-3.3	-3.8	-2.3
Interest (domestic)	4.9	5.2	5.9	5.8	5.2	6.3	6.6	7.6	7.5	8.3
Subsidies		0.9	0.7	0.6	0.5	0.5	0.6	0.8	0.7	0.9
Total debt servicing	7.2	8.0	8.3	9.3	8.8	9.3	10.8	10.7	11.7	11.8
Tax as % of GDP	12.7	13.7	13.4	13.4	13.8	14.4	13.4	13.2	13.3	12.8
Development exp.	6.4	7.5	5.7	4.5	4.4	4.4	3.5	3.3	3.6	3.2

Source: GOP, Economic Survey, various issues.

Table 4.14 Key balance of payments indicators

(% of GDP)

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-2000
Exports	13.0	13.9	13.2	12.9	12.8	13.2	13.0	13.6	12.8	13.3
Imports	18.5	18.6	19.6	16.8	17.0	19.0	18.0	16.6	16.4	15.6
Trade deficit	-5.5	-4.6	-6.4	-3.9	-4.2	-5.9	-5.0	-3.0	-3.5	-2.3
Current account deficit	-4.8	-2.8	-7.2	-3.8	-4.1	-7.2	-6.2	-3.1	-4.1	-1.9

Source: GOP, Economic Survey, various issues.

During the 1990s poverty has increased, and currently 35 per cent of households in the country are below the poverty line

has adversely impacted on the growth programmes. The wasteful expenditure on unproductive projects was symptomatic of deterioration in the quality of governance. The failure to achieve the targeted reduction in the fiscal deficit, especially by increased tax efforts, was due to the dominant influence of the vested interests.

The key indicators of balance of payments, shown in table 4.14, indicate weak export performance during the 1990s.

Imports were compressed to keep the trade imbalance from rising too rapidly. Nevertheless, large current account imbalances had emerged as a major source of instability and vulnerability. FDI and other forms of capital inflows were not attracted towards Pakistan on any significant scale. Due to high foreign indebtedness and occasional disputes with foreign investors, the investment climate in Pakistan was not attractive for large capital inflows. Foreign reserves had remained low.

Impact on human development

The economic reforms during the 1990s were not specifically aimed at employment generation. Rapid growth was expected to generate high employment expansion. In the past, increased job opportunities had resulted in rapid poverty reduction. Low inflation was also expected to result in reducing the incidence of poverty.

Changes in poverty levels

There is now considerable agreement that Pakistan's earlier success in reducing the incidence of poverty has been reversed during the 1990s. The trends in poverty for the period of 1984-85 to 1998-99 are reported in table 4.15. Data show that between 1984-85 and 1987-88, overall, as well as for rural areas, poverty levels decreased. Continued overseas remittances and introduction of the safety nets in the form of *Zakat* and *Usher* in the 1980s explain the progress made in the reduction of poverty by 1987-88.

During the 1990s poverty has increased, and currently 35 per cent of households in the country are below the poverty line. Poverty increased from 21 per cent in 1990-91 to 35 per cent in 1998-99. This increase in poverty is largely attributed to macro-level factors such as decrease in overseas remittances, high unemployment rate and low growth.

Worsening employment situation during the 1990s explains the rapid rise in poverty during this period. The real wages of the employees in public sector have declined due to high inflation and inadequate adjustment to the cost of living in the nominal wages. The work force in the informal sector has experienced a decline in their real wages.

Table 4.15 Trends in poverty by rural and urban areas, 1984-85 to 1998-99

(% of households)

Year	Pakistan	Rural areas	Urban areas
1984-85	22.8	24.1	19.4
1985-86	19.6	20.7	18.2
1986-87	17.0	18.1	15.6
1987-88	16.7	18.2	14.9
1990-91	21.4	23.5	18.7
1992-93	24.5	27.4	19.8
1993-94	23.9	27.9	17.6
1998-99	32.6	34.8	25.9

Source: 1983-84–1993-94, Ali and Tahir 1999; 1998-99, Qureshi and Arif 1999.

Table 4.16 presents indices of real wages of informal sector work force and the information on unemployment rates. Wages in the informal sector, both farm and non-farm, are flexible and adjust to the labour use in the economy. Earnings of the workers have remained low in the 1990s. The reduced access of the poor to labour market shown by declining real wages and high unemployment and/or underemployment rate has resulted from declining rates of economic growth and low employment elasticity in different sectors. High inflation also explains the reduction in the purchasing power of the poor during the 1990s.

Changes in income distribution

Adverse changes in income distribution also explain the rising poverty during the 1990s. Table 4.17 presents the Gini-coefficient, income share of the top 20 and the bottom 20 per cent population in total income and their ratio in 1993-94 and in 1998-99. The estimates reveal that not only has income distribution worsened during the 1990s but also that the income share of the rich increased while that of the poor declined in all of Pakistan in both the urban as well as rural areas. The worsening disparities in income combined with low growth have resulted in worsening of the conditions of the poor during the 1990s.

In conclusion, it needs to be pointed out that Pakistan's major failure in the 1990s has been the continuing macro-instability, massive slow-down of growth and rising poverty. These reversals happened despite various attempts at introducing stabilisation and structural adjustment programmes. Political instability and lack of political will to bear the short-term costs of reforms explain the failure of the reform programmes. Lack of attention to governance issues and institutional reforms have also played a major role in the backsliding of the reform process. Pakistan needs to continue with the ongoing reform programmes, but it must make sure that the poor are protected from short-term costs and the social sector expenditure, particularly on education and skill-training, is increased to improve the quality of its labour.

Table 4.16 Indices of daily real wages in informal sectors

Years	Carpenter	Mason	Labour	Farm workers	Unemployment (%)	Underemployment (%)
1990-91	100	100	100	100	–	–
1991-92	93	102	104	106	5.9	13.2
1992-93	100	100	100	100	–	–
1993-94	94	93	92	111	–	–
1994-95	98	96	100	106	–	–
1995-96	93	94	100	106	–	–
1996-97	94	94	100	106	6.1	10.8
1997-98	94	94	100	–	–	–

– denotes data not available

Source: Federal Bureau of Statistics, Government of Pakistan.

Bangladesh

At the time of independence in 1971, Bangladesh had adopted socialism as its ideology of development. Most industries and financial institutions were nationalised or taken over for management by the government. With the change in government in 1975, policies shifted in

Table 4.17 Household income distribution by region

Year	Area	Household Gini coefficient	Household income shares		Ratio of highest 20% to lowest 20%
			Lowest 20%	Highest 20%	
1993-94	Pakistan	0.40	9.2	40.2	4.4
	Urban	0.40	9.4	40.9	4.4
	Rural	0.35	10.6	34.6	3.3
1998-99	Pakistan	0.41	8.1	42.3	5.2
	Urban	0.41	8.2	42.5	5.2
	Rural	0.37	7.2	36.2	5.0

Source: GOP 1994; GOP 1999c.

favour of the private sector, but pervasive government interventions through controls or selective incentives remained. A modest effort towards economic liberalisation was made during the late 1970s. However, serious efforts, especially in the agricultural sector, were made in the early 1980s. A three year Structural Adjustment Facility (1986-87 to 1988-89) and Enhanced Structural Adjustment Facility (ESAF) for the period 1990-91 to 1992-99 from the IMF and adjustment programmes with the World Bank and the Asian Development Bank during the 1990s had launched Bangladesh on the road to stabilisation and structural reforms.

Overview of economic reforms

The adjustment programme initiated by the government in the 1980s was aimed at reducing macro instability by curtailing the trade and budget deficits, limiting inflation and achieving a satisfactory rate of economic growth. The programme included cautious monetary and fiscal policies, privatisation, liberal trade and industrial policies and a reform of the financial system. At the same time, the programme was also supplemented by anti-poverty measures to support the poorest and the most vulnerable groups. As a result of these early reforms, the economy was stabilised. Growth rate had also picked up by the mid-1980s.

Stabilisation policies

Due to natural disasters in 1987 and 1988 leading to decline in output and increase in government expenditure for relief and rehabilitation, progress achieved in the mid-1980s was to a large extent undermined. Recognising the deteriorating macroeconomic situation, the government had adopted in March 1990, a macroeconomic stabilisation programme to prevent the fiscal and balance of payments deficits from worsening further and causing rapid inflation.

The government attempted to improve the fiscal balance by reducing current expenditure and increasing tax revenue through expansion of the tax base and improving collection and administration. Despite stiff opposition, value-added tax (VAT) was introduced in 1992.

On the expenditure side, while development spending on human resource development and on physical infrastructure was emphasised, an attempt was made to curtail non-development expenditure. This was done to ensure a better environment for attracting more foreign capital from private sources, especially FDI.

The monetary policy, which was generally restrictive throughout the decade, was eased to stimulate economic activities. The bank rate was reduced from 8 to 7 per cent in August 1999 and cash reserve requirements were lowered from 5 to 4 per cent in October 1999. As a consequence, money supply went up by nearly 19 per cent in 1999-2000, compared with less than 13 per cent for the previous year.

Structural adjustment policies

During the 1980s the government had emphasised policies aimed at raising economic growth by reducing the role of the government, encouraging the private sector and attracting foreign investment. As part of a comprehensive set of structural reforms, Bangladesh tried to intensify the earlier reforms during 1991-96. The government did this by further liberalising the foreign trade and exchange regimes, restructuring the industrial sector, strengthening fiscal and monetary policies and privatising state owned enterprises. The major features of the reform programme are given below:

Industrial policy reforms

Liberalisation of the industrial sector was started with the announcement of the Industrial Policy in 1982. This was followed by successive industrial policies in 1991, 1992 and 1999 to make the economy more competitive in a globalising world. The main objectives of these policies were: (a) export-led industrial development by making the role of the government promotional rather than regulatory; (b) encouragement of domestic and foreign investment in overall industrial and infrastructure development; (c) encouragement of only efficient import-substituting industries; (d) expediting development of labour intensive industries through acquisition and improvement of appropriate technology; and (e) promotion of private sector through cost-effective incentives and privatisation of state-owned enterprises.

In line with the stated objectives, attempts were made to reduce government involvement in industry and to increase the role of the private sector. More than 600 state-owned enterprises (SOEs)—ranging from small to large, commercial to industrial—had either been denationalised or divested by 1986. In March 2000, the Privatisation Board was converted into a Privatisation Commission with greater power and flexibility. Around 90 SOEs were targeted for privatisation through direct sale or stock market flotation. However, the public sector still controls over 40 per cent of the country's manufacturing and utility assets. Moreover, as a result of bureaucratic and labour union resistance, the pace of privatisation has remained slow despite explicit government policy.

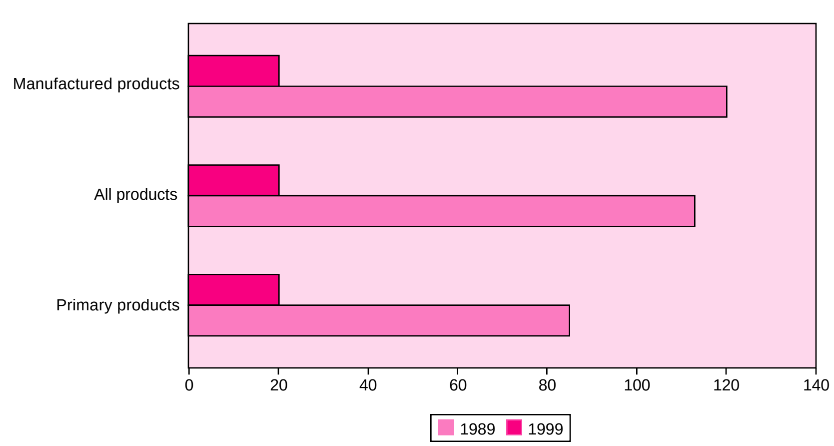
The liberalisation of industrial and investment policies during the 1990s has sharply reduced bureaucratic control over private investment and has opened up many areas previously reserved for the public sector. Exchange controls were liberalised for current-account transactions; the Board of Investment was given the task of facilitating rather than regulating investments; and import controls were reduced and import permits abolished. VAT replaced import sales taxes, and most domestic excise duties and tariff rates have been simplified and reduced. In 2000, the highest rate of import duty was 35 per cent, although an infrastructure development surcharge (IDS) of 2.5 per cent, introduced in 1997, has been retained. Import of cotton synthetic staple fibre yarn and fabrics are exempt from both the 2.5 per cent IDS levy and the 15 per cent VAT. During the 1990s, exports were encouraged through duty-drawback schemes and special bonded warehouse (SBW) facilities. The SBW schemes have been crucial for the success of the ready-made garment industry. Firms located in export processing zones (EPZs) can import capital and raw materials free of duty, retain foreign currency earnings, employ expatriates and non-unionised labour, and enjoy a ten-year tax holiday as well as preferential treatment in obtaining utility connections.

Trade policy reforms

After a slow start in the mid-1980s, Bangladesh's trade liberalisation effort picked up pace in the early 1990s as an important component of the country's structural reform programme. Compared to the highly restrictive and inward looking trade regime of the mid-1980s, Bangladesh's trade policy is now less restrictive and more outward oriented (see figure 4.2).

Bangladesh's trade policy is now less restrictive and more outward oriented

Figure 4.2 Mean unweighted tariff rates (%)



Source: World Bank, World Development Indicators CD-ROM, 2000.

Initial steps were ad hoc and had focussed on removing the quantitative restrictions. However, in the early 1990s a more comprehensive trade policy reform programme was initiated that covered both tariff and non-tariff barriers. Since then Bangladesh has continued to liberalise its trade regime by reducing tariffs and eliminating the quantitative restrictions on imports.

Major policy initiatives were undertaken in the inputs and outputs markets for the agricultural sector

Bangladesh has made considerable efforts to simplify and rationalise the tariff structure by reducing the number of tariff bands from 15 in 1992-93 to 5 in 1999-2000. The maximum tariff rate has also been lowered from 300 per cent to 37.5 per cent during the same period. The number of trade-related quantitative restrictions have also been reduced. However, tariff protection is still high and applied rates vary widely. The dispersion in tariffs remains high relative to the average rate and ranges from 0 to 37.5 per cent (World Bank 1999).

The government has also set up export processing zones in different areas to encourage exporters and thereby improve trade balance. The country's first export processing zone (EPZ) was built in Chittagong in the early 1980s and is dominated by garments manufacturing firms. The Dhaka EPZ, which specialises in high-tech firms, was opened in 1993. Up to January 2000, a total of US$413 million had been invested in the country's EPZs, which fetched export income of US$711 million, which was 13.4 per cent of the country's total export earnings in 1999-2000. A total of 149 firms are located in these EPZs, of which 23 per cent make ready-made garments and 11 per cent textiles, employing 85,238 persons.

Besides providing basic infrastructure facilities (warehouses, communication, water supply, electricity, gas, etc.), the factories situated within EPZs were provided additional incentives such as income tax exemption for ten years, duty free import of raw materials and machinery, etc., income tax exemptions on salaries of foreign entrepreneurs, etc.

Exchange rate policy

After unifying existing multiple exchange rates in 1992, the Central Bank pursued a 'managed but flexible' exchange rate policy to maintain the competitiveness of exports while controlling domestic inflation. In 1993, Bangladesh Bank (the central bank) liberalised foreign exchange regulations. The new measures introduced allowed dealers to fix exchange rates. The Bank permitted dealers to retain higher amounts of foreign currency. The Bangladesh currency, taka, was made convertible for all current account transactions in 1991. Foreigners were given permission to invest in the capital market and freely repatriate their profits and principal. In 1995 the government began a policy of allowing the value of the taka to depreciate against the US dollar. The taka has been devalued in stages ever since. The sharpest adjustment in the value of the taka came in early August 2000 in response to an earlier depreciation of the Indian rupee, when the taka was devalued by 6 per cent. Although export performance had been strong during the 1990s, a more competitive exchange rate policy would have had better impact on exports.

Financial liberalisation policy

Despite the Financial Sector Reform Programme during the 1990s, the banking sector remains plagued with poor credit discipline, inefficient loan recovery system, corruption, inefficiency and overstaffing.

The growth of private banks since the 1980s had injected some competition into the banking sector. There are now 43 private banks in the country—29 domestic and 14 foreign. Foreign banks are gradually emerging as competitors in the local deposit and credit markets. There are two bourses in Bangladesh: Dhaka Stock Exchange and Chittagong Stock Exchange. The stock market is poorly developed, with only about 200 shares traded.

Agricultural liberalisation

Being a major contributor to GDP, agricultural sector reforms have been given top priority in the structural adjustment programmes. The macroeconomic reforms in the area of removal of quantitative restrictions on trade flows, tariff reduction and market-based exchange rate have improved the incentives for the agricultural sector. In addition to these reforms, major policy initiatives were undertaken in the inputs and outputs markets for the agricultural sector.

The imports of seeds, pesticides and fertilisers were considerably liberalised. The private sector was encouraged to participate in the input markets. The rates of import duties on irrigation equipments were reduced. In the case of some inputs such as fertilisers, import duties have been abolished altogether. There has also been considerable deregulation of the markets for inputs as well as agricultural outputs. The subsidy on food crops has also been reduced. This process of lifting of quantitative restrictions on imports of agricultural inputs and the reduction of duties on imports of such inputs was undertaken mostly during the 1990s as a part of trade liberalisation reforms. There have also been serious efforts at the reform of agricultural research and extension systems and privatisation of some of the public sector institutions in the agricultural sector.

In addition to the crop sub-sector reforms, livestock and forestry sub-sectors have also been supported by policy reform. Bangladesh has a total forest area of approximately 2.5 million hectares, covering just over 17 per cent of the total land area. In 1999-2000 forestry contributed 1.9 per cent to GDP and 9.8 per cent to agricultural GDP and grew at a rate of 4 per cent. A twenty-year plan is being implemented since 1993 to expand forestry and preserve the ecological balance.

Assessment of reform strategy

The reform programme in Bangladesh had three main objectives: acceleration of economic growth, poverty alleviation and human development, and stabilisation of the economy. While the success on the growth and poverty eradication front has been limited, major success was achieved in the curtailment of fiscal and current account deficits. Stabilisation of the economy is an essential requirement for sustained growth rates, but a rapid reduction of fiscal deficits often has adverse impact on growth as well as human development, at least initially. A low rate of growth, unless accompanied by specific anti poverty measures, implies slower reduction in poverty.

Impact on growth

Based on the national account series (in 1985-86 prices), the economy grew at an annual rate of 4.26 per cent during the 1980s. This rate went slightly up to 4.91 per cent during the 1990s. The credit for this modest acceleration is said to be due to the rapid liberalisation process (see table 4.18 and figure 4.3).

During the 1990s, all sectors experienced some increase in growth rates, but with a large volatility in the manufacturing as well as agricultural sectors. The sluggish growth has been attributed by most analysts to low rates of savings and investment. Domestic savings rates increased to 17.8 per cent in 1999-2000 from 14.6 per cent in 1991

Table 4.18 Sectoral growth rates of GDP (% per year)

	1980-89	1990-98
GDP	4.26	4.91
Agriculture	2.29	3.29
Industry	3.64	3.89
Services	6.06	6.44

Source: World Bank, World Development Indicators, CD-ROM, 2000

Figure 4.3 Sectoral growth rates

Source: World Bank, World Development Indicators CD-ROM, 2000.

and investment rate to 22.6 per cent from 19.7 per cent during the same period. The public investment rate had marginally declined.

Agriculture

Agriculture is the largest sector of the economy, accounting for 22 per cent of GDP and 50 per cent of employment. The main impetus for growth in 1990 came from agriculture which grew by 7.7 per cent in 1990, partly because of improved agricultural policies that led to increased availability of irrigation and adequate supplies of seeds and fertilisers. However in 1995, the GDP growth rate went down to 4.1 per cent as a result of decline in agricultural output. Food grain production fell by 1.8 per cent in 1994 and by 5.7 per cent in 1995, partly because of unfavourable weather conditions and also as a result of infrastructure bottlenecks and inappropriate public interventions in the fertiliser market. In 2000, GDP growth rate went up to 5.5 per cent compared to 4.9 per cent the previous year—an increase that was mainly the result of good harvest.

There was increased production of different varieties of paddy. However, wheat production fell by 3.6 per cent. Total food grain production was 14 per cent higher than the previous year. Greater food production at home had a positive impact on the trade balance as food grain imports fell by over 60 per cent. Between 1989-91 and 1998-2000, crop production in the country increased by 110.4 per cent, food production by 114.5 per cent and livestock production by 136.2 per cent. Given the current trend, the agricultural sector which is the mainstay of the economy, is expected to grow further.

Industrial growth

The industrial sector of Bangladesh contributes more than 11 per cent to GDP and employs nearly 12 per cent of the labour force (GOB 1996). Its contribution has increased in recent years from about 9.9 per cent in 1984-85 to 11.5 per cent in 1995-96. The manufacturing sector has broadened from its traditional activities of processing traditional raw materials such as jute and tea to include ready-made garments. The garment industry employs nearly 1.4 million workers, of which 95 per cent are women. Clothing has emerged as the most important export item—comprising around 70 per cent of export earnings. However, most of the inputs of this sector have to be imported.

Both foreign and local investment has been increasing in this sector. Foreign investment has largely taken place through the establishment of foreign-owned enterprises. The largest inflow of foreign direct investment has taken place in the textile sector. However, with the dismantling of the Multi-Fibre Arrangement, Bangladesh will have to face up to competition from other Asian countries.

Bangladesh's jute manufacturing industry is threatened by the limited market at home and by the growing use of synthetic substitutes globally. Added to

Table 4.19 Fiscal and monetary variables

Year	Fiscal deficit (% of GDP)	Money supply (% per year)	Inflation rate (% per year)
1973-80 (Average)	-9.3	39.6	13.4
1981-90 (Average)	-7.5	20.3	10.1
1990-91	-7.9	16.9	9.3
1991-92	-7.2	12.1	8.9
1992-93	-5.9	14.1	5.1
1993-94	-5.9	10.6	1.3
1994-95	-6.0	15.4	1.8
1995-96	-6.8	16.0	3.2
1996-97	-4.5	9.9	2.5
1997-98	-4.2	11.4	7.0
1998-99	-5.3	12.8	8.9
1999-2000	-5.8	18.6	3.8

Source: ESCAP, various issues; GOB 1996.

these is the inefficient production of jute goods. This is because the government remains the largest shareholder of many of the privatised mills.

Stability

The reforms introduced in Bangladesh for reducing fiscal deficit have been mostly successful (see table 4.19). Due to the introduction and implementation of the value-added tax, tax revenue has increased leading to reduction in fiscal deficit, slower increases in money supply and sharp reduction in inflation. Current account deficit has also been brought down due mainly to an increase in the manufactured exports- especially of ready made garments.

Manufactured exports have grown rapidly over the past decade showing an average annual growth rate of about 17 per cent compared with only 5 per cent of GDP at the beginning of the decade. The growth has been led by rapid expansion in the ready made garment industry. The non-traditional garments industry overtook jute goods as the major export earner in 1987-88 and by 1998 ready made garments became one of the major exports of Bangladesh. However, even today ready made garments are highly import dependent. The jute industry's share of total export earnings has fallen from 49 per cent in 1985-86 to less than 10 per cent in the late 1990s.

Impact on human development

The incidence of poverty declined from 59 per cent in 1983-84 to 45 per cent in 1999. The extent of rural poverty has always been higher than in urban areas. There has been a declining trend in poverty in both rural and urban areas. Between 1983-84 and 1995-96, urban poverty has declined at a faster rate than rural poverty. During 1997-1999, rural poverty fell but urban poverty had stagnated at 43.4 per cent (see table 4.20).

Table 4.21 presents data on income distribution in rural and urban areas. The data shows that income inequality, as measured by the Gini index, has increased in both rural and urban areas. Increasing income inequality explains the slow-down in poverty reduction during the 1990s, as the share of income going to the poor fell. The slowing down of poverty reduction is also attributed to lower growth of production and lower employment expansion during the 1990s. Bangladesh's direct attack on poverty, especially through the non-governmental organisations, has been able to provide some cushion here.

In conclusion, Bangladesh has made good progress in achieving macro stability. With a deepening of economic reforms, the country should be able to accelerate economic growth, reduce poverty and improve human development.

Table 4.20 Incidence of poverty in Bangladesh (head count ratio %)

Year	Rural	Urban	National
1983-84	59.6	50.2	58.5
1988-89	59.2	43.9	57.1
1991-92	61.2	44.9	58.8
1995-97	56.7	35.0	53.1
1997	46.8	4.34	46.0
1999	44.9	43.3	44.7

Source: World Bank, 1998; GOB 1998 & 2000.

Nepal

Overview of economic reforms

Nepal had started liberalising its trade and investment policies during the mid-1980s. During the early 1990s, widespread economic reforms were started when the Indian economy was substantially liberalised. Three years of high fiscal deficits, causing inflation, made it imperative for the government to initiate the stabilisation programme. In 1985, Nepal had approached the IMF for assistance. This was followed by structural

Table 4.21 Gini Index

Year	Rural	Urban
1983-84	35.0	37.0
1988-89	36.8	38.1
1991-92	36.4	39.8
1995-96	38.4	44.4
1997	39.0	43.0
1999	36.0	42.0

Source: GOB 1998 & 2000.

adjustment loans from the World Bank in 1987 and 1989, leading to a systematic and institutionalised economic reform programme of the IMF in the form of an Enhanced Structural Adjustment Facility (ESAF) in 1992.

Stabilisation policies

The major fiscal objectives included an increase in public savings, a reduction in domestic borrowing for financing of the budget and an improvement in the efficiency of public expenditure. Fiscal deficits in Nepal have remained at unsustainable levels with low revenue and high non-development spending, resulting in high domestic borrowing. The domestic savings rate in Nepal is one of the lowest, leading to heavy dependence on external sources for financing investment. As of 2000, the domestic savings rate was 13.2 per cent of GDP. Domestic investment was in excess of 20 per cent of GDP (ESCAP 1999 & 2001). External funding to finance this gap increased from 8 per cent of GDP to 10 per cent in 1994 (ADB 1997). In 1999, foreign grants and loans have financed approximately 65 per cent of development expenditures, as compared with 50 per cent in the early 1990s (ADB 1998).

A number of revenue enhancing and expenditure control measures have been introduced to reduce fiscal deficit. On the revenue side, sales tax and excise duties were introduced in 1992. Over the years, these taxes have been increased and rationalised further. The introduction of the value-added tax and increase in the rate of land taxes are expected to further enhance domestic revenues by expanding the tax base. Several other tax reforms measures have been introduced. Privatisation of state-owned enterprises has been one of the key policy interventions, primarily to reduce deficits.

On the expenditure side, a number of policy interventions have taken place. Subsidies have been gradually withdrawn as part of the structural adjustment policies on fertiliser and bank interest for the poor.

Auctioning of treasury bills and securities from the Central Bank and open market operations are being increasingly used to control domestic liquidity. Despite attempts to control the growth rate of money supply, money supply has increased at a high rate, rising from an annual growth rate of 18.5 per cent in 1990 to 21.6 per cent in 1999 (World Bank 2001). One of the major factors behind this increase has been the high level of public borrowing from the banking system.

Structural adjustment policies

The main aims of structural adjustment policies have been to: (a) abolish or reduce controls on capacity creation, production and prices; (b) promote competition in the domestic and international sector; (c) reduce the role of public sector organisations and agencies in production and trade, except in strategic sectors or in the case of market failures; and (d) liberalise the financial sector by permitting foreign entry and reducing controls in the banking system. Specific details of policy reforms introduced for Nepal's integration in the global economic arena are given below:

Industrial reforms

The Industrial Enterprises Act 1992 guarantees an explicit no nationalisation policy of industries in the private sector, provision of one-window system, abolishment of industrial licensing (barring a few industries) and swift decisions within thirty days for granting special privileges for export related industries.

The Industrial Policy of 1992 identifies foreign investment promotion as a cornerstone of the strategy to achieve the objectives of industrial production. Foreign Investment and One Window Policy was introduced in 1992 (Acharya *et al*. 1998). In the same year, the Foreign

Investment and Technology Investment Act was enacted, laying down the rules and regulations governing foreign investment. The aim of the Act is to attract foreign investment in the form of equity participation, loan extension, technology transfer and direct investment in domestic production. The broad areas open for foreign investment include manufacturing, agro-based energy and service industries (except public health and environment). Nepal encourages foreign investment as joint venture operations with local investors. As regards equity participation, foreign investors are permitted to own up to 25 per cent of the stock of listed companies and 100 per cent ownership for small and medium industries (Khan 2000). Returns on investment and amount received as payment of principal and interest on foreign loans in convertible currencies is guaranteed for repatriation. The dispute settlement mechanism of the Act allows for international arbitration in accordance with the prevailing arbitration rules of the United Nations Commission on International Trade Law (Mahendra 2000).

The privatisation process began in 1992, with the passage of the Privatisation Act (Acharya *et al*. 1998). A number of government owned industries in areas such as sugar, jute, cement and paper have been privatised. Privatisation of public monopolies in telecommunications and air travel is under consideration, allowing multinational companies a share in the development of cellular telephones and long distance communications.

Trade policy reforms

Trade policy reforms, initiated in 1992, introduced currency convertibility on the current account, duty drawback facilities for export industries and the introduction of foreign exchange accounts. The aim of the export duty drawback scheme is to provide a refund on taxes paid on its imported raw materials. The bonded warehouse scheme has facilitated tax refunds paid on imported raw materials for the exports of ready-made garment industry. Export service fees on exports have been reduced from 2 per cent in 1993-94 to 0.5 per cent to date. All taxes paid on the exports are refunded (Acharya *et al*. 1998).

Customs tariffs have also undergone rationalisation and simplification. The peak tariff rate has been reduced from a high of 300 per cent in the early 1980s to 80 per cent in 1997-98. In addition, the tariff structure has also been simplified, with tariff slabs brought down from 10 to 5 in 1995-96. In addition, additional duties charged on third country imports have been abolished.

The Foreign Exchange Regulation Act 1962 prohibited local banks from extending loans in foreign currencies. However, as of 1993, a provision has been introduced allowing commercial banks to extend loans in convertible currencies to export oriented industries, firms and producers for the import of raw materials.

Under the Structural Adjustment Programme, the Open General Licences (OGL) have been expanded in scope and import licenses have been categorised into three divisions namely industrial OGL, commercial OGL and import license auction. In order to enhance industrial production, entrepreneurs receive foreign exchange entitlement based on past production levels and current estimated production. Commercial OGL has aided in improving the supply of raw materials, impacting positively on production and export of woolen carpets. Moreover, the policy has resulted in the removal of import and export licenses, removal of import restrictions, replacements of tariffs with quotas, and the ability of banks to determine import cash margins. Furthermore, the Central Bank now requires only a 2 per cent deposit of the total value of letter of credit. As a consequence, the trade regime is now more open and liberal as quantitative restrictions on imports have been abolished.

Agricultural reforms

The government has liberalised both input and output markets in the agricultural sector. With effect from 1997, subsidies on all kinds of fertiliser, except urea, have been removed, imports liberalised and private companies and the Agricultural Inputs Corporation (AIC) have been allowed to avail of the urea subsidy (Abdelati *et al*. 2000). Furthermore, as part of the reform process AIC's monopoly on the import and distribution of fertiliser has been ended in order to encourage a greater role for the private sector. The transport subsidy extended to the AIC for distribution to remote regions has also been discontinued. Prices of chemical fertilisers have been deregulated at the wholesale and retail levels. In the distribution of food grains, the role of the state-owned Nepal Food Corporation is being modified to foster private sector activity.

The government has introduced reforms to strengthen agricultural research, extension and training systems. As part of this reform process, the government also aims to strengthen public institutions, use a decentralised user-oriented approach to research, focussing on the needs of farmers in each specific district, strengthen coordination mechanisms and maintain linkages with relevant international research institutes, and targeting high potential areas for extension. However, according to a 1998 report, the extension reforms have been limited, with only 12 out of the country's 75 districts targeted (Abdelati *et al*. 2000).

Exchange rate policy

Nepal's currency is pegged to the Indian rupee. The exchange rate policy has been considerably liberalised to attract FDI. The Foreign Exchange Regulation Act [FERA] 1962, was amended allowing foreign institutions, agencies, individuals (except those from Bhutan, India and Nepal) to operate US dollar and pound sterling accounts. Five additional currencies were added by 1993. This provision permits industrial producers, and companies engaged in the export sector to obtain loans in convertible foreign currencies. The Nepalese currency, the rupee, was made partially convertible in the current account in 1992, with 35 per cent to be surrendered at the official rate and 65 per cent to be sold at the market rate. By 1993 full convertibility for the current account was introduced. However, some minor controls were re-imposed in 1998-1999 and 1999-2000. (Abdelati *et al*. 2000). The commercial banks are permitted to undertake foreign exchange transactions without the permission of the Central Bank.

Financial liberalisation policy

The financial sector has been liberalised in phases. In May 1986, commercial banks were permitted to set deposit rates above a specified minimum. Excepting priority sectors, banks could also set the lending rates. In 1989 the banks were granted full authority to set the deposit and lending rates according to the market trends. In 1993, the Statutory Liquidity Requirement (SLR) was reduced, leading to a reduction in lending rates.

Commercial banks are now not forced to invest in government bonds and treasury bills with low yields. This has further eased liquidity constraints for commercial banks. In 1988, a mechanism of auctioning treasury bills was introduced. An inter-bank market was also set up to utilise the short-term excess liquidity of banks.

The Commercial Bank Act of 1974, amended in 1984, has removed the entry and exit barriers for banks so that joint venture banks with foreign collaboration could operate in the private sector (Acharya *et al*. 1998). The aim was to attract foreign capital and technical know-how into the economy, infuse modern banking skills to the domestic banks and widen the national financial structure.

Prudential norms for the long-term sustainability of the financial system were introduced which include capital adequacy ratio, loan classification, loan loss provisioning, income recognition and single borrower limit. The capital adequacy ratio requires banks to maintain 4 per cent core capital and 4 per cent supplementary capital (Abdelati *et al*. 2000).

A Credit Information Bureau was established in 1989. The Bureau is responsible for preparing credit information. Capital market reforms were also introduced. Promotional and operational functions were bifurcated in 1992 with the establishment of a Security Exchange Board to oversee regulatory functions, and the setting up of the Nepal Stock Exchange Centre with the responsibility for operational and trading functions.

Assessment of reform strategy

The data base for Nepal's economy is not strong enough to make an objective assessment of the reform strategy. However, we provide below some general information based on available information.

Impact on growth

Table 4.22 presents the average performance of different sectors during two time periods, 1980-89 and 1990-98. Figure 4.4 shows annual growth rates of different sectors.

A signifiant increase in the rate of growth in GDP is found as it rose from 3.7 per cent during the 1980s to 4.8 per cent during the 1990s. However, a breakdown of growth by sectors shows the weak impact of reforms in productive sectors. Agricultural sector and industry both show a slow-down. Only services show a sharp acceleration. The yearly variations on the growth rates shown in Figure 4.4 are large. The slowdown in agriculture is based on a decline in the use of fertiliser and pesticides. This has been attributed to the sharp increase in the prices of inputs due to the removal of subsidies. Between 1991-92 and 1999-2000 the use of fertiliser has experienced a decline of 35 per cent. At the same time, improved seed provision for major food crops has declined by 367 metric tons, from 2153 metric tons in 1991-92 to 1786 metric tons in 1999-2000 (HMG Nepal 2000). The removal of subsidies on inputs was not accompanied by public investment in rural infrastructure. This explains the sharp decline in agricultural performance.

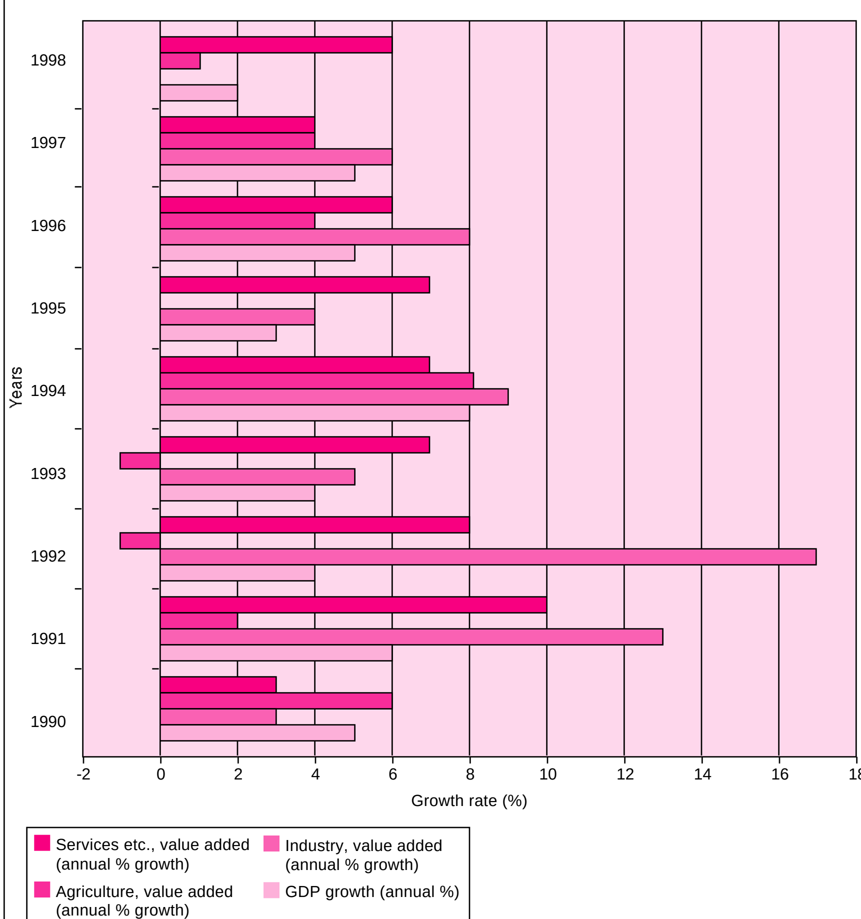
The weak performance in the industrial sector is due to numerous enterprises being forced to close down as liberalisation policies were introduced. Industrial and trade policy reforms have had an adverse impact on industrial production. Effective protection rates

Table 4.22 Average annual growth rates (%)

	1980-89	1990-98
Agriculture	3.59	2.57
Industry	7.8	7.2
Services	3.6	6.2
GDP	3.7	4.8

Source: World Bank, World Development Indicators CD ROM, 2000.

Figure 4.4 Sectoral growth rate and GDP



Source: World Bank, World Development Indicators CD-ROM, 2000.

Table 4.23 Trends of macro-economic indicators (as % of GDP)

	Current account deficit	Trade deficit	Fiscal deficit
1990	-6.9	-8.8	-10.0
1991	-7.8	-11.1	-10.7
1992	-7.9	-10.5	-8.6
1993	-7.9	-10.3	-9.2
1994	-5.6	-7.1	-7.0
1995	-7.8	-9.1	-6.6
1996	-11.7	-15.2	-7.5
1997	-9.4	-10.2	-7.3
1998	-8.8	-10	-7.7

Source: World Bank, World Development Indicators CD-ROM, 2000.

have declined from 98 per cent in 1989 to 9 per cent in 1996 (Khan 2000). Moreover, the manufacturing sector was constrained by a limited domestic market, lack of infrastructure, skills, capital and stiff Indian competition. The beneficial impact of opening up to the world other than India was not achieved due to high transport costs.

Impact on stability

Macro-economic stabilisation has been a major issue in Nepal. Fiscal deficit, trade and current account imbalances have been large and negative. Despite fiscal reforms, not much improvement has occurred in the fiscal balance. Trade deficit has been large. Receipts from tourism have had a positive impact on the current account, however, current account deficits continue to remain high. Foreign direct investment has not been a major source of support to the balance of payments.

Impact on human development

Since the onset of liberalisation policies in Nepal, negative trends have been observed on income distribution, unemployment and underemployment. While there has been a shift in employment away from agriculture towards the industrial and service sectors, the creation of employment opportunities has not kept pace with the increasing numbers of young people entering the job market. Distribution of income in Nepal has become increasingly unequal between 1984-85 and 1995-96. As shown in chapter 3 (table 3.2), the richest 20 per cent of the population in Nepal has 44.8 per cent of GDP, while the poorest 20 per cent has only 5.9 per cent. This income inequality has been associated with increased inequality in rural areas.

The labour force engaged in agriculture has declined, but it still remains the sector with the highest rate of employment. However, most of the underemployed labour force remains in the agricultural sector. At the same time, the labour force engaged in the non-agricultural sector has experienced an upward trend with the major growth sectors being construction, transport and communications. Most of this expansion has been associated with the service sector. On the other hand, as the employment in the service sector has grown accounting for greater non-agricultural employment, the level of employment in the manufacturing sector has been lower in the liberalisation period at 17.2 per cent (Rijal 2000).

Prices of food grains and agricultural inputs have increased, mainly due to fiscal measures, such as the removal of subsidies. These fiscal measures have affected the rural population by reducing agricultural output and incomes and raising the prices of food as this constitutes an important part of the consumption basket for these people. Increase in poverty is attributable to stagnation in growth and rise in food prices. Poverty has been accentuated as the integration with the global economy has imposed limitations on the extent of public expenditures for the welfare measures.

In sum, Nepal's growth record during the 1990s has been high relative to the 1980s. In fact, it has increased from 3.7 per cent during the 1980s to 4.8 per cent during the 1990s (World Bank 2000). But agricultural growth significantly decelerated during the 1990s, compared to the previous decade. The growth in agriculture has also fluctuated widely. The rate of industrial growth has also declined, though only slightly. But the service sector has grown significantly. The fiscal deficit, which was 11 per cent of GDP in 1991, has been brought down. But it is still quite high and unsustainable. Current account and trade imbalances have been negative and high. These imbalances have worsened during the 1990s. The decade of reforms has seen an increase in the levels of income inequality both in rural and urban areas. Poverty situation has also worsened due both to rising inequalities and declining growth in agriculture and industry.

Liberalisation policies to-date have had a limited impact on the growth performance. Merchandise exports have a concentration in two major goods, namely, ready made garments and woolen carpets. The ready made garments sector faces an uncertain future in view of the abolition of the Multi-Fibre Arrangement by 2005. Nepal has great potential to boost export earnings, by utilising its hydroelectric potential, establishing linkages with the software industry in India and further encouraging tourism.

Sri Lanka

Overview of economic reforms

Since 1977 globalisation, liberalisation and privatisation constitute the three core elements of the economic reforms carried out by different governments. While the economy has been liberalised gradually over the last twenty-five years, there have been certain watershed years for different reform initiatives. The initial reforms of 1977 had transformed the economic system and the incentives structure in an attempt to create an enabling environment for the private sector. Tariffs, trade restrictions and taxes were reduced. Prices were deregulated. Business was freed of unnecessary controls and regulations. Foreign capital was encouraged with generous incentives. But increased macro-economic instability and violence during the early 1980s had prevented the reaping of full benefits from the 1977 reforms. A second round of reforms was initiated in 1989 to strengthen the reform process.

Stabilisation programme

The 1977 liberalisation reforms were accompanied by large infrastructure projects during the early 1980s. The largest donor-funded project undertaken was the Accelerated Mahaweli Development Programme. The large size of Public Investment Programme had implicit in it enlarged budget and current account deficits. As a result of macro imbalances, inflation had accelerated. Export incentives had deteriorated. Private investment activity did not pick up. The ethnic violence and political instability had further made matters worse. The government expenditure on security had increased sharply. Some development projects with high rates of return were deferred. Both stability and growth was kept on hold.

The government was forced in 1989 to embark on a new stabilisation programme with the help of donor agencies. The government expenditure was to be substantially reduced through large cuts in public-sector jobs. A tight monetary policy was sought to be pursued through high interest rates and reduction in credit to the private sector. Current account deficit was to be reduced from 10 per cent of GDP in 1989 to about 5 per cent of GDP in 1993. The stabilisation measures were complemented with a further dose of economic liberalisation policies.

Structural reforms

Structural reforms were initiated in a number of major policy areas which are briefly reviewed below.

Trade policy reforms

The trade reforms have attempted to liberalise the imports and foreign exchange transactions. There was a sharp

While the economy has been liberalised gradually over the last twenty-five years, there have been certain watershed years for different reform initiatives

Price controls have been eliminated for most goods and services

reduction of import items subject to licensing and quota restrictions. There has also been a reduction and rationalisation of import tariffs. Both the level and dispersion of import duties have been reduced over time. Current account convertibility was achieved in early 1990s for the foreign exchange transactions. The capital account transactions were and are still subject to controls.

The Presidential Trade and Tariff Commission, appointed by the government in 1997 recommended further changes to the tariff structure. Some of the changes approved were, (i) all industrial raw material and machinery not manufactured in Sri Lanka came under the 5 per cent band; (ii) duty on imports of motor cars and jeeps, which were under the duty range of 50-100 per cent, was reduced and unified at 30 per cent; (iii) import duty on agricultural products remained at 35 per cent to allow the domestic agricultural sector to adjust to a lower tariff regime over the medium term; and (iv) items considered to be essential for the maintenance of minimum living standards were kept at zero tariff rate.

Export promotion measures have also been introduced. Tax holiday, previously applicable only to firms in the export promotion zones, was extended to any exporter who fulfilled the criteria announced by the government. In practice, the whole export sector has become free of taxes.

Foreign exchange rate reforms

A unification of the exchange rate and managed float was introduced as a part of reforms. The policy of managed float in the exchange rate determination had led to a gradual and consistent practice of depreciation of the Sri Lankan rupee to maintain international competitiveness. The rupee has depreciated from Rs.15 in the late 1970s to Rs.76 in 2000. Recent exchange rate reforms were aimed at recapturing most of the competitiveness that Sri Lanka had lost due to the sharp devaluation of the currencies in East Asia in the Asian crisis in 1997. The currency crisis in East Asia had little direct impact on the Sri Lankan rupee mainly due to existing capital account controls and small exposure of the country to short-term debt. Yet there was a need to take measures to avoid the adverse consequences emanating out of the crisis. The Central Bank had stepped up its surveillance on bank operations and used moral persuasion to counteract excessive speculative forces.

According to the analysis done by the Central Bank, devaluation of the currency was important to protect the profit margin of exporters that had been gradually eroded. Sri Lankan rupee was considered overvalued by exporters. A devaluation of the currency was effected by the Central Bank as a part of its policy of managed float.

Market reforms

A series of reforms were introduced to encourage the role of private sector in the economy. Areas reserved previously for the public sector were opened up to the private sector. The sole presence of government in import and domestic trade was ended. Private bus transport has been allowed to ply in competition with the public transport system.

The role of market forces has been given greater salience in the workings of public corporations. Price controls have been eliminated for most goods and services. Labour market reforms have also been introduced to let the low-wage economy work according to market forces. The powers of trade unions have been reduced.

Fiscal reforms

A number of reform measures on both the tax and expenditure sides of the budget have been introduced. A degree of fiscal discipline has been introduced in the budgetary process. Untargeted subsidies on food and fertiliser have been eliminated. Expenditure on social sectors like education and health was drastically cut. Initially after the 1977 reforms, especially during the early 1980s, capital expenditure on major infrastructure projects was increased. Subsequently, the dictates of reducing fiscal deficit had forced the government to curtail its capital expenditure.

Agricultural policy reforms

While Sri Lanka has traditionally been an agricultural economy, the contribution of agricultural sector to total GDP has been declining. It has fallen from 50 per cent in 1950, to 38.5 per cent in 1960, to 23.2 per cent in 1990 and to around 20 per cent in 1999.

With the liberalisation of the economy in 1977, the traditional agricultural sector has been subjected to major reforms in the 1990s, with the emphasis on a greater role for market forces. Tenurial reform and land distribution was carried out to improve access to land, food and income for the indentured workers. About 20 per cent of the land was distributed to the land-less in small blocks of 1/4 to one acre in size. The reform package included (i) ownership of tea plantations reverting to private companies; (ii) freeing agricultural markets and liberalising external trade in agricultural commodities, thus providing price incentives leading to enhanced investment and output in the sector; (iii) rationalisation of the tariff regime and granting of import licenses for agricultural commodities were replaced by a tariff system in 1996; and (iv) the introduction of duty free import of seeds and planting material.

Efforts have also been made to increase productivity in plantation agriculture—tea, rubber and coconut. This sector is currently under private sector management and ownership. Major reforms of the plantation sector namely in tea, rubber and coconut began in 1992, when management (but not land or assets) was privatised. Tea Small Holder Development Authority continued to assist the tea industry by implementing subsidy schemes for replanting and new planting of tea, and providing extension services. In 1995, the government of Sri Lanka began privatising regional holding companies. The government sold 20 plantation management companies in 1995-98. In 1998, tea and rubber plantation workers were given a substantial wage increase. Two new wage agreements contained a formula for profit sharing which affords the plantation companies the flexibility to weather downturns while also protecting the interests of the labourers.

Traditional agriculture sector has been subjected to major reforms in the 1990s, with the emphasis on a greater role for market forces

Industrial reforms

The private sector-led, export-oriented industrialisation strategy continued to be the top most priority for industrial sector development in the country. This strategy aimed at expansion, diversification and upgrading of both the domestic and foreign firms in matters related to physical and manpower resources, employment and income generation and promotion of regional industrialisation for sustainable industrial development.

The government offered a range of incentives in 1998 for the location of industries in backward regions. As a result, private industrialists opened up fifty new garment factories in the southern provinces. Textile and clothing, food, beverage and tobacco processing, and chemical, rubber and petroleum products were the main beneficiaries of these new incentives.

Fiscal incentives and other reforms for industrial growth include: (i) selling off 36 state-owned industrial enterprises; (ii) tax holidays being replaced by a 15 per cent concessional rate of tax for all investments; (iii) fiscal incentives were offered under the Advanced Technology Programme; (iv) developments were carried out in telecommunications and infrastructure facilities under the regional industrial parks programme. The major flaw of these policies, however, was the heavy import-dependence of the manufacturing sector, whose domestic value-added content was just a little over one-third of total value.

The structural problems in the industrial sector, such as continuing labour market rigidities, inadequate development of infrastructure, speedy transportation and communication system, roads and security related problems still persist despite some reforms in these areas. The introduction of free market oriented labour reforms are necessary to further enhance productivity and to create employment opportunities for the educated youth to resolve the unemployment problem.

In Sri Lanka, the privatisation process was presented as a 'peoplisation' programme

Financial sector reforms

Sri Lankan government policy of privatisation and deregulation had a significant impact on the revival of capital markets. In continuation of other financial reforms during the 1991-99 period, the government has shown its commitment to liberalise the money market. The reform package includes: (i) lowering of interest rates by reducing the statutory reserve ratio from 15 per cent to 12 per cent in 1996; (ii) new measures to raise finance such as a Global Depository Issue, forms of leveraged buyouts and emergence of derivatives; (iii) foreign ownership of equity and relevant exchange controls on remittances; and (iv) the creation of an appropriate regulatory environment. It has been realised by the government that healthy macroeconomic environment and political stability are both necessary for strong and sustained growth in these markets.

The financial and banking reforms over the period of 1990-99, encompassed broad macro issues including: (i) improvement in competitive banking and encouraging private sector in the development of financial system; and (ii) the 1995 amendments in the Banking Act, strengthening the regulatory powers of the Central Bank of Sri Lanka (CBSL) and extending its mandate beyond commercial banks to specialised banks, foreign currency banking units, and rural development banks. CBSL sets appropriate limits for foreign exchange.

The banking system has been opened to foreign competition. There is no limit to the number of branches a foreign bank may open. However, foreign ownership of domestically incorporated banks is limited to 40 per cent.

Privatisation

In Sri Lanka, the privatisation process was presented as a 'peoplisation' programme. A two stage process was envisaged. The state enterprises were first restructured in the form of public companies. A part of the shares of these companies were then floated on the stock exchanges. This policy was followed by an ambitious programme of privatisation in which some of the public companies were sold to the private sector.

Anti-poverty programme

The early liberalisation process in the 1980s was perceived by rural and urban poor as benefiting mostly the upper and middle income classes. By the end of the 1980s, the government had launched a number of policy initiatives to address the concerns of the poor. The cash value of food stamps was doubled. Programmes for school uniforms and midday meals were launched. Garment factories were located in rural areas by various incentive measures to generate employment opportunities in the rural areas.

Assessment of reform strategy

The reform programme in Sri Lanka had three main objectives, i.e., accelerating growth, stabilisation of the economy and reduction of poverty and unemployment. The Fund-Bank style of reforms currently in vogue imply an initial period of slow growth due to recessionary elements with in the prescribed package. The Sri Lankan initial reform of 1977 were not strictly guided by the stereotyped package of reforms as the design of such packages was evolved in later years. However, the reforms introduced during the 1990s had contained the stabilisation objectives in the conditionalities agreed between the donors and the government.

Impact on growth

Unlike the other countries in South Asia, Sri Lanka has had longer experiences with economic reforms as it started the reform process in 1977. Its growth rate rose from 3 per cent per annum from 1960 to 1976 to an average of 4.1 per cent during 1980-89 and to a still higher value of 5.2 per cent during 1990-2000. Table 4.24 shows the average performance of different sectors in the two reform decades. Table 4.25 shows the yearly rates of growth by sectors for the decade of the 1990s.

The beneficial impact of reforms on growth is obvious. However, Sri Lanka has grown at a lower rate in the post-reforms period than other countries in East Asia and South Asia did during their transformation period. As against the growth rate of 5.2 per cent in Sri Lanka during the 1990s, countries in East Asia had experienced growth rate of 9 per cent per year during 1960-1990. The relatively lower growth in Sri Lanka when the world economy was growing fast and world trade was expanding rapidly is due to low level of investment and lower efficiency of the economy.

The performance of the economy has also varied over time as well as between different sectors. The positive impacts of 1977 reforms were neutralised by ethnic conflicts during the second half of 1980s. The second wave of reforms during 1989-1993 had, however, resulted in an acceleration of annual growth rates, although with fluctuations The fluctuations in agricultural production were more marked than in industry and services sectors. The average growth rate during the 1990s at 5.7 per cent was slightly higher than the average growth of 5.3 per cent during the 1980s. The industrial sector performed well during the 1990s. While import liberalisation had certainly undermined several domestic industries, the restructured industrial sector had resulted in a higher growth rate for the entire industrial sector during the 1990s compared to the 1980s.

Agriculture

The agricultural sector decelerated during the 1990s as the average growth rate fell from 2.4 per cent per year during the 1980s to 1.8 per cent during the 1990s. There were large fluctuations in the annual growth rate in the sector with two years recording negative growth. All sub-sectors within agriculture, i.e., small subsistence holders, plantations and commercial farming, had experienced slow growth. Between 1994 and 1998, domestic agriculture had witnessed a sharp decline in production mainly as a result of globalisation and free trade in agricultural commodities. The flood of imports of most commodities had eroded the incentives for agricultural producers.

Impact on stability

Relatively low growth during the 1990s, especially in the agricultural sector, was associated with high macro-imbalances. Table 4.26 shows the fiscal, trade and current account deficits. The high levels of deficits have imparted a source of

Table 4.24 Growth rate of GDP (% per year)

	1980-1989	1990-2000
GDP	4.1	5.2
Agriculture	2.4	18.4
Industry	4.2	7.2
Services	5.3	5.73

Source: World Bank, World Development Indicators CD-ROM 2000.

Table 4.25 Growth rates of GDP and sectors during 1990s

(% per year)

Years	GDP	Agriculture	Industry	Services
1990-91	4.6	1.9	4.1	6.2
1991-92	4.3	-1.6	7.1	5.3
1992-93	6.9	4.9	9.8	6.3
1993-94	5.6	3.3	8.1	5.2
1994-95	5.5	3.3	7.8	5.1
1995-96	3.7	-4.6	5.6	5.8
1996-97	6.4	3	9.1	7.1
1997-98	4.7	2.5	6.3	5.2
1998-99	4.3	4.5	4.4	4.2
1999-2000	6	1.2	9.7	6.9

Source: World Bank, World Development Indicators CD-ROM, 2000.

Table 4.26 Macro-economic indicators			
			(% of GDP)
Year	Budget deficit	Trade balance	Current account balance
1990-91	-11.6	-11.1	-5.4
1991-92	-7.3	-10.8	-4.5
1992-93	-8.4	-11.1	-3.8
1993-94	-10	-13.3	-6.5
1994-95	-9.6	-11.6	-4.9
1995-96	-8.9	-9.5	-3.9
1996-97	-7.9	-8.1	-2.6
1997-98	-9.2	-6.9	-1.4
1998-99	-7.5	-8.7	-3.6
1999-2000	-9.8[a]	-10.8[a]	-6.4[a]

a: denotes provisional data
Source: Central Bank of Sri Lanka, Annual Report 2000.

considerable instability in the economy. The high trade deficits were a result of poor performance of agricultural exports. While globalisation had helped the growth in exports of the garments and other industrial products, the agricultural exports had increased slowly. The imports, however, had increased much faster than the exports leading to a worsening of trade deficits. The current account deficits were smaller than the trade deficits due to remittances and other invisible receipts.

Fiscal deficits had remained high during the period 1990-91 to 1999-2000, never falling below -7.3 per cent of GDP. Fiscal deficit in 1999-2000 was -9.8 per cent. The extra expenditure related to ethnic conflicts as well as revenue losses from reduced rates of taxes explain the high fiscal deficits. The requirement of keeping the budget deficit in check to meet the conditions imposed by the donors has meant a drastic cut in capital expenditure (see table 4.27).

Table 4.27 Functional classification of capital expenditure					
					(% of GDP)
Expenditure	1994	1995	1996	1997	1998
Total capital expenditure	7.5	7.4	5.7	5.7	6.8
Economic services	5.1	5.1	4.1	3.6	4.4
Agriculture and irrigation	0.9	0.9	0.6	0.4	0.6
Transport	2.5	2.8	1.6	1.5	1.9
Energy	1	0.7	0.8	0.8	0.9
Social services	1.3	1.5	1.3	1.3	1.5
Education	0.5	0.5	0.6	0.5	0.6
Health	0.3	0.3	0.3	0.3	0.4

Source: Central Bank Annual Report 1998 as cited in Economic Review, April-May 2000.

The proportion of tax revenue in GDP has fallen from 17.8 per cent in 1995 to 14.5 per cent in 1998. The increasing defence expenditure during the 1990s was financed not from the increased level of tax revenues but by cutting essential economic and social expenditures. While the expenditure on social services has stagnated, the expenditure on economic services has fallen drastically. It is not surprising that there was no major acceleration of growth rate in agriculture. The government capital expenditure did not provide enough support to even the private sector.

Impact on human development

In South Asia, Sri Lanka was well-known for its commitment to social welfare. Larger allocations for human development and social programmes had brought substantial income equality and poverty alleviation in the country during the early decades after independence. Despite the commendable long-term trend in poverty reduction, however, a large part of the population remains vulnerable to income fluctuations. The rate of poverty reduction has fallen during the 1990s. The recent adverse impact on poverty is attributed to deterioration in terms of trade during the 1990s and slower growth performance. The ongoing ethnic conflicts, drought in 1996, decline of agricultural productivity, and labour unrest probably explain the low growth in agriculture. The statistics on poverty show that the percentage of households below the poverty line had declined from 31 per cent in 1985-86 to 20 per cent in 1990-91, but poverty rose again to 25 per cent in 1995-96.

Income poverty remains high in Sri Lanka with at least one-fourth of the population living below the poverty line. Southern province is the poorest in terms of per-capita income and has the highest unemployment rate. In rural areas, poverty is high among both agricultural and non-agricultural households. Most farm families are poor, surviving on less than two acres of land and deriving over 40 per cent of their income from off-farm sources. The inhabitants of rural areas also live without access to safe water and sanitation (30-50 per cent), and electricity (65-75 per cent). The poor suffer most from low-quality social services, with acute disparities in the rural areas where health, education, housing and safe water and sanitation services are far below the national average.

Despite numerous poverty alleviation programmes in the country the growing poverty in Sri Lanka shows that poverty cannot be reduced or overcome by the poor themselves. The poor have to be provided with opportunities to link their productive activities with the wider economy. If the government believes that the poor should benefit from the market economy, then anti-poverty programmes have to be linked with the productive employment plans.

The continued persistence of poverty is explained by high unemployment rates which stood at 14.1 per cent in 1987, 14.7 per cent in 1993 and 11.3 per cent in 1998. The employment growth rate during 1987-96 was 1.7 per cent per year while the growth rate of real wages has been –0.4 per cent per year during 1990-98. It is not surprising that unemployment and poverty has not been reduced much due to declining real wages and weak employment creation.

Since the onset of globalisation policies, negative trends have also been observed in the pattern of income distribution. In 1995, the share of poorest 20 per cent in consumption was 8 per cent while that of the richest 20 per cent was 42.8 per cent. This ratio has deteriorated for the poorest 20 per cent relative to the situation in the 1970s.

In brief, Sri Lanka is the most market-oriented economy in South Asia. The reforms in Sri Lanka have a long history. The impact of reforms on economic performance has been positive but not as high as some countries in East Asia or South East Asia. The impact on human development in terms of poverty reduction and employment generation has been negated during the post-reform era due mainly to internal strife. The security related expenditure has squeezed the expenditure on capital expenditure and social sectors. The agricultural sector has performed in an unsatisfactory manner as its growth rate has been reduced considerably during the 1990s.

Conclusions

The previous sections have described the reforms that the South Asian countries had undertaken in the 1990s to integrate with the global economy and have assessed the major impacts on growth, macro stability and poverty and employment—the two key components of human development. As the discussion of these issues was carried out sequentially for the five countries, this concluding section attempts to identify the commonalties and differences in the globalisation experiences in South Asia. The future prospects and promises of globalisation conclude the discussion.

With the exception of Sri Lanka, which started its reform process in 1977, all other South Asian countries are still in mid-stream of comprehensive reform programmes of liberalisation and stabilisation The conclusions on the pattern and results of reform are therefore preliminary. However, the inter-country comparisons are still useful.

The pace, sequencing and timing of reforms has varied between countries but the decade of the 1990s has proved to be a turning point in South Asia for the reform movement. Sri Lanka has gone through a second wave of reforms while all other countries have shown a strong consensus and commitment to reforms. India has led the reform process with the introduction of wide-ranging reforms in 1991 and extending the scope of such

Economic performance during the reform era varies considerably both between countries and over time

reforms throughout the decade. The sequencing of some reform measures has been defective as it has added to the difficulties in other interrelated policy areas. The obvious case in this regard has been the reduction of tariffs before reforming the tax systems to widen the base and improve tax collection. The revenue loss from the tariff reforms has been a major contributor to high fiscal deficits. Similarly, financial sector reforms relating to the curtailment of government borrowings from the banking system at low costs were introduced before any meaningful restructuring of the public-sector expenditure. This has increased fiscal deficits in Pakistan and India. While the reform of the financial sector was needed, the sequencing of financial sector reforms was not appropriate. The recent efforts at tax and expenditure reforms in all countries are expected to correct the earlier policy failures. It is interesting to note that, in line with the neo-classical perspective, the content of reforms in all countries had over-emphasised the role of price incentives and market orientation. The institutional innovations and the role of non-price factors in the reform programmes were given a low priority.

The economic performance during the reform era varies considerably both between countries and over time for each of the countries in South Asia. India has been a star performer. From only negligible growth in 1991-92, it has attained high growth of over 7 per cent in GDP for three consecutive years between 1994-95 to 1996-97. There has been a loss in the growth momentum but, with reforms, it is expected that India can grow at a higher rate. Bangladesh has not seen much acceleration in growth rates during the 1990s. Nepal's growth rate at 3.6 per cent per annum has been lower than that of Bangladesh but it has shown a slight acceleration over its own growth rate of the previous decade. In the case of Pakistan, the growth rate during the 1990s has fluctuated between 1.9 per cent and 7.8 per cent in 1996-97 and 1991-92, respectively. Fluctuations notwithstanding, there has been a definitive slow-down in growth due primarily to lack of implementation of reforms, political instability, external shocks including adverse changes in weather and sanctions. Sri Lanka's growth rate in the early 1990s has improved as a result of the second wave of reforms. However, the growth in Sri Lanka has faltered in the second half of the 1990s due primarily to the ongoing civil strife.

In terms of the contribution of different sectors to growth, agriculture has performed poorly in all countries in the 1990s. Adverse weather shocks do not explain the slow growth. The lack of emphasis on agricultural reforms and reduced allocations of funds for agricultural and rural development provide a better explanation to the dismal performance of agriculture in South Asia. Industrial sector and some of the service sub-sectors, especially information technology in India, have done extremely well in the 1990s.

Macro instability has been a major concern in South Asia. All countries have experienced high fiscal deficits as a proportion of GDP. Contractionary fiscal measures have reduced the fiscal deficits in all countries, except Sri Lanka. Limited revenue mobilisation and lack of expenditure control have been the major causes of continuing high fiscal deficits.

Balancing external accounts is crucial for stability as well as to build capacity to continue implementing the reform programmes. Trade and current account balances have remained negative for all South Asian countries during the 1990s. India's position has been relatively more comfortable and Nepal's has been the most difficult one throughout the decade. Despite increased FDI flow to Sri Lanka and India, South Asia has not been a preferred region for attracting major FDI flows. Regional conflict and weak reform efforts probably explain the sluggish inflows of foreign capital to South Asia.

The impact of reforms on human development in South Asia has been mixed. The allocation of funds to social sectors has seen no major upward revision. The employment expansion in none of the countries has been significant. The rates of unemployment and/or underemployment remain high. With the slow down of growth in Pakistan and no major acceleration in the growth rates in other countries except India, poverty rates in South Asia have remained high. In Pakistan, the poverty rates have almost doubled during the 1990s. In India and other South Asian countries, the earlier progress in poverty reduction has been halted in the 1990s.

The setback to growth and human development in South Asia in the 1990s is a matter of serious concern. However, the prospects of rapid improvement in human well-being are bright. It requires, among many other things, a rethinking of the globalisation process so that the short-term costs of economic reforms are not borne mainly by the poor who do not have a voice in decision-making. Acceleration of growth with human development and poverty reduction is a realistic expectation in all countries. Peace in the region and cessation of internal strife could make South Asia an attractive region for foreign investors. With increased trade orientation and FDI flows, South Asia can get access to foreign markets, resources and technologies. There is also a need to increase the intra-regional trade in South Asia. The existing large cross-border illegal trade between some countries in South Asia is an abundant proof of the untapped potential of intra-regional trade. With progressive legislation of this trade, political friction between countries can be reduced drastically. The next chapter addresses this issue of regional cooperation.

BLANK

5

South Asia and Regional Cooperation

SAARC leaders should agree on a number of concrete measures to open up their markets to each other and to the rest of the world…(And) SAARC should call on the international community to assist their efforts by providing much larger access to world export markets, greater inflow of foreign private investment, and larger external assistance. The SAARC leaders should offer the world their own plan for human development and poverty reduction which can then become the basis for a viable global compact.

– Mahbub ul Haq

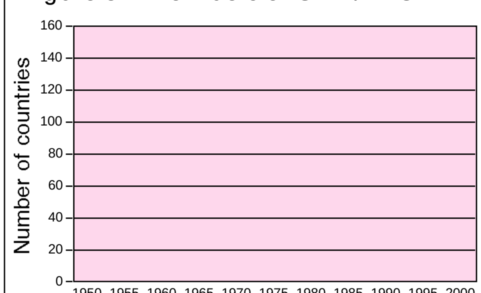
Chapter 5

South Asia and Regional Cooperation

Two dominant forces have been shaping the world economy during the last quarter of the 20th century—globalisation and regionalisation. Regional economic integration has occured simultaneously and is linked to the process of globalisation. The General Agreement on Tariffs and Trade (GATT) and its successor organisation, World Trade Organization (WTO) had recognised the role of Regional Trade Agreements (RTAs) in the world economy. Multilateral trade liberalisation had led to an exponential growth of the world economy, benefiting many nations, yet it became clear from the protests by the civil societies from both North and South in Seattle and in other places that increasing trade openness was imposing tremendous short-term costs to developing as well as some sectors of the developed countries. Regional cooperation is seen by the participating countries as a countervailing power in trade negotiations with the countries outside the region, besides providing opportunities to benefit from trading with the neighbours.

The question that the developing countries, including South Asia, face is the precise role of regional cooperation in the rapidly globalising world. In view of the large gains from multilateral trade liberalisation, South Asia needs to continue on the trade liberalisation front; this does not stand in the way of enhanced regional cooperation. In this chapter, we try to look at the nature and the extent of current regional cooperation in South Asia, and how should we strengthen this in order to enhance the collective bargaining power of South Asia in global forums.

Figure 5.1 Members of GATT/WTO



Source: WTO and MHHDC staff calculations.

World trade has grown at an average rate of 6 per cent over the past decade or so, at twice the growth rate of world GDP. On January 1, 1995, the WTO replaced GATT, which dealt only with trade in goods, and included in its mandate to monitor and implement agreements on commodities, services, and intellectual property rights, and a mechanism for dispute settlement. Now with more and more countries becoming members of the GATT/WTO (see figure 5.1), global trading order is what WTO rules make it to be. In 1999, more than two-thirds of the 140 members (as on 30 Nov. 2000) of the WTO were developing countries with having approximately a 20 per cent share of world exports. This has wide-ranging implications for the global economy.

Regional trading groups

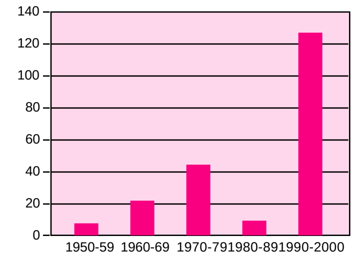
Looking at the current trend in forming regional trading blocs, we see that nearly all of the WTO's 140 members have notified participation in one or more Regional Trade Agreements (RTA)—customs unions, free trade areas or other preferential arrangements. In the period 1948-1994, the GATT received 124 notifications of RTAs (relating to trade in goods), and since the creation of the WTO, 90 additional arrangements covering trade in goods or services have been notified. Out of the total of 214 agreements and/or enlargements so far notified to the GATT/WTO, 134 are deemed to be currently in force. The network of RTAs throughout the world is now highly complex and many countries are members of several agreements, sometimes with very differing rules.

The unprecedented rise in the number of Regional Trade Agreements in the last decade (see figure 5.2) has led to a critical analysis of the merits of regional trading agreements in relation to the unbridled push towards a multilateral trading system. It is important to acknowledge the obvious gains in terms of trade volume and welfare effects for both developing and developed countries in extending their trade to the markets worldwide. In India, a new middle class has emerged that is ready and able to purchase goods from the developed countries. While the global market is still not entirely competitive, many developing countries are now able to expand their exports to developed markets. In addition, other ostensible gains, such as productivity gains, due to the applications of research and technology, mostly developed in industrial countries, are highly important in an open world. A study shows that a net increase in output of US$ 25 billion was observed in 77 countries that could be attributed to international R&D spillovers (Coe *et al*. 1997). This suggests that gains from this factor would be even greater as trade barriers come down worldwide. Yet the case for forging regional alliances is gaining new ground: witness the formation of Free Trade Association of the Americas (FTAA), set for 2005, which will be the largest trading bloc, with 34 member countries, in the world. Global trade will no doubt be the dominant driving force of the global economy. But the question is what kind of complementary role the regional trading groups could play in this trading regime? And what will be the impact of this on the vast majority of poor people around the world?

There are, in general, four main motivating factors for forging regional alliances. These are: (i) to promote economic cooperation among the members of the group by increasing efficiency and exploiting economies of scale; (ii) to achieve international competitiveness during globalisation; (iii) to build a sense of security and to facilitate political harmony within a region; and, (iv) to forge a collective bargaining position in global negotiations. During the last two decades there was a proliferation of regional alliances around the world. In Asia, there is the Asia-Pacific Economic Cooperation forum (APEC), the Association of South-East Asian Nations free trade area (ASEAN), and a pact between Australia and New Zealand, ANZCERTA. In the mid-1980s, South Asian Association for Regional Cooperation (SAARC) was formed. In the Americas, apart from the North American Free Trade Area (NAFTA), we have seen the creation of the Southern Common Market in the South America (MERCOSUR), and now a Free-Trade Area of the Americas (FTAA). Outside Asia, the most advanced is the European Union (EU). At the moment, the EU is second to APEC with a 35.5 per cent share of total world exports in 1998. APEC, with a share of 45.3 per cent of world exports is the largest trading bloc with 21 member countries including the United States, Japan and China.

There is considerable debate over the nature and future of these regional alliances under the auspices of the WTO. As to their future role, it is not certain whether their recognition in the WTO framework, via Article XXIV, is to attract existing regional blocs to enter the WTO membership, or merely to promote the existence of such regional (preferential) trading blocs as a complementary instrument to the working of WTO. Another view is that the Article XXIV of the WTO may, at a later date, translate into a phasing out mechanism for these regional blocs. And as to their nature, some insist on calling these alliances

Figure 5.2 The number of RTAs notified to GATT/WTO each decade



Source: WTO and MHHDC staff calculations.

Table 5.1 Direction of exports as a % of total exports in 1998

	EU	USA	Japan	Industrial Countries	SAARC
Bangladesh	46	36	2	87	2.7
Bhutan	-	-	-	-	-
India	27	21	5	57	5.6
Maldives	24	34	9	68	18.4
Nepal	33	26	1	61	36.5
Pakistan	31	22	3	60	5
Sri Lanka	29	38	5	76	2.6
SAARC	29	24	5	42	5.3

Source: IMF, Direction of Trade Statistics 1999.

'preferential' rather than 'regional' or 'free' trade agreements. It is also argued whether they are 'building blocks' or 'stumbling blocks' towards a more integrated trading world. As America considered embracing regionalism in the early 1980s, the threat of such a move led EU to enter the GATT talks. The same thing happened in the 1990s when the rise of APEC persuaded the EU to bring the Uruguay Round to a close. Furthermore, it is also argued that preferential trade agreements within a region could be counterproductive, by eliminating tariffs on imported goods from some countries but not from all others in a region. Preferential trade agreements also create a 'spaghetti bowl' of overlapping Rules of Origin that are sure to distort some investment decisions. A recent survey concluded that regional arrangements 'seem to have generated welfare gains for participants, with small, possibly negative spillovers onto the rest of the world' (World Bank 1999c).

South Asia's trade outside the region

A host of economic and political factors have so far limited trade within the South Asian region. Although informal trade between India and Pakistan is said to be over the one billion US dollar mark, official trade among SAARC countries accounts for less than 4 per cent of their total trade volume. The trade policies pursued in these countries have tended to discourage intra-regional trade on the one hand and encouraged trade with the developed world on the other. The region's principal export destinations are the United States, the European Union, and Japan (see table 5.1).

For South Asia as a whole, the EU and the USA are very important as an export market. Both EU and the US absorb the bulk of the textiles and garment exports from South Asia. Studies have shown that any trade diversion of textiles and garment exports to the US market due to the formation of NAFTA will be minor, and this will be more than offset by the new trade created by the abolition of the Multi Fibre Arrangement (MFA) in 2005 and the US tariff reductions under WTO (Safadi and Yeats 1993) (see box 5.1). However, it is also argued that the use of non-tariff barriers can limit the market for South Asia.

At present, Japan's formal relationship with South Asia is primarily one of official aid. SAARC has been receiving

Box 5.1 Will progress within EU and NAFTA affect SAARC?

In 1993, the single market became a reality for the European Union. Six years later the Euro, a single currency for the region, came into being. Over in the Americas, the entry of Mexico, a developing country, within NAFTA was also witnessed. As these two regions combine to form a significant part of South Asia's export markets, such developments in these regions cannot be ignored.

Greater tariff escalation as a consequence of the *Single Market Programme* of the European Union in some industries such as leather, textiles and clothing has placed South Asia at a disadvantageous position in the EU market. The preferential removal of trade barriers for Mexico, within NAFTA, will result in a diversion of South Asia's exports particularly textiles, clothing and leather, in favour of Mexico. Moreover, the liberalisation of cross-border trucking by NAFTA will reduce transportation costs, which will favour Mexican products over non-NAFTA products in the US market.

However, it is argued that Mexico's ability to displace third country imports in North America is limited. The import penetration ratios of Mexico in the areas of textile and clothing are much smaller than the countries of South Asia. Also, a relatively large portion of the Mexican MFA quota remained unfilled indicating supply side constraints that limit the ability of Mexico to displace third country exports.

Source: Khan and Mahmood 2000.

approximately US$ one billion annually in the form of bilateral aid since the second half of the 1980s. A SAARC-Japan Special Fund has also been established to stimulate support for SAARC economic cooperation.

Trade: SAARC vs. other regional blocs

Among all the regional groupings, SAARC ranks very low in terms of intra-regional trade (see table 5.2). Trade within the region is very low and insignificant, averaging around 4 per cent during the past three decades. This indicates limited trade complimentarities within the region. The region constitutes a small market for the products of SAARC member countries. In ASEAN, in contrast, trade complimentarities are greater as intra-regional exports form over 20 per cent of the region's total exports.

In terms of global trade too, SAARC ranks very low among regional groupings (see table 5.3). As a percentage of global exports, SAARC accounted for only one per cent in 1999 compared to 38.9 per cent by EU, 18.8 per cent by NAFTA, 1.3 per cent by MERCOSUR, and 6.5 per cent by ASEAN. These figures have hardly changed compared with the pre-SAARC era. Obviously, SAARC's economic cooperation has not been translated into any impressive results in the global context.

There are many reasons for such insignificant trade within the SAARC region. On the political side, the main obstacle to greater trade integration has been the tension between India and Pakistan, and to a lesser degree, fear of Indian trade domination by her smaller neighbours. For example, Bangladesh has a sharply rising trade deficit (as percentage of GDP) with India since 1993. This is due to India's non-tariff barriers, such as, local government rules and regulations that become major obstacles to the exports of Bangladesh. In the case of Sri Lanka, which has a free trade agreement (FTA) with India, the trade balance is believed to be 13 to 1 in favour of India. On the Indian side, the obstacles have not been removed, whereas Sri Lanka has facilitated the entry of Indian goods under the FTA. While intra-regional trade is not growing, SAARC member states are making free trade pacts with other regions.

On the economic side, perhaps the main inhibiting factor has been a lack of complimentarity in the exports of SAARC member countries. The four major South Asian nations export a similar basket of commodities, and often compete directly in third markets, especially for textiles. Furthermore, India's economic pre-ponderance and comparative advantage in a range of products have resulted in asymmetric trade relations with her neighbours, hindering regional integration. Regional trade has also perhaps not taken off because all the countries in the region have been pursuing, until the late eighties, import substitution policies aimed at promoting domestic industries. Lastly, low technological growth and demand within the region itself, and historical trade links with the developed countries, have resulted in extra-regional patterns of trade.

It is important to stress the fundamental importance of a regional trading bloc to enhance the capacity of its members, both individually and collectively, to cope with the challenges of globalisation. It is also important to use this vital instrument of cooperation to consolidate the region's gains from the globalisation process.

Table 5.2 Exports within the regional trade blocs (as % of total exports)

	1970	1990	1995	1999
APEC	57.8	68.3	71.9	71.9
EU	59.5	65.9	62.4	62.6
NAFTA	36.0	41.4	46.2	54.6
MERCOSUR	9.4	8.9	20.3	20.5
ASEAN	22.9	19.8	25.4	22.2
SAARC	3.2	3.2	4.4	4.7

Source: World Bank, World Development Indicators 2001.

Table 5.3 Total exports by regional trade blocs (as % of world exports)

	1980	1999
APEC	33.7	46.9
EU	41.0	38.9
NAFTA	16.6	38.9
MERCOSUR	1.6	1.3
ASEAN	3.9	6.5
SAARC	0.7	1.0

Source: World Bank, World Development Indicators 2001.

SAARC and economic cooperation

Recognising the value of regional cooperation in both economic and non-economic spheres, and despite being confronted with some of the most intense political issues, the seven South Asian countries formally launched the South Asian Association for Regional Cooperation (SAARC) on 7th December 1985. It was a historic event and signified the culmination of the process that began as early as 1978-79 with the late President Zia-ur-Rahman of Bangladesh initiating consultations in the matter with his counterparts in South Asia.

The main objectives laid down in the SAARC Charter adopted at the first Summit are to promote the welfare of the peoples of South Asia; accelerate economic growth and social progress; promote active collaboration in the economic, social, cultural, technical and scientific fields; strengthen cooperation in international forums on matters of common interest; and cooperate with international and regional organisations with similar aims and purposes. Decisions on all matters of SAARC are taken on the basis of consensus. Article X (2) of the SAARC Charter excludes bilateral and contentious issues from the ambit of SAARC.

Ten SAARC Summits have been held so far (see box 5.2). Since its inception, SAARC has been involved in several programmes and projects. The first SAARC Summit held in Dhaka (1985) focussed on non-economic areas for regional cooperation. The twelve agreed areas of cooperation in the Integrated Programme of Action (IPA) were: agriculture; education and culture; environment; health and population; meteorology; prevention of drug trafficking and drug abuse; rural development; science and technology; communications; tourism; transport; and women in development. It was not until the seventh Summit in Dhaka in 1993 that a framework agreement on SAARC Preferential Trading Arrangement (SAPTA) was signed. The eighth Summit in New Delhi in 1995 directed that all necessary steps should be taken to facilitate the ratification by all member states and operationalise SAPTA by the end of 1995.

The ninth SAARC Summit, held in Male (May 1997), established an important body, the Group of Eminent Persons (GEP). The GEP was to undertake a comprehensive appraisal of SAARC, identify measures to further enhance the effectiveness of the Association and formulate a long-range vision and perspective plan of action, including a SAARC Agenda for 2000 and beyond. They submitted their report 'SAARC Vision Beyond 2000' to the tenth SAARC Summit held in Colombo (July 1998). The GEP's recommendations focussed on three areas: (a) regional economic integration, including negotiation of a treaty for a South Asian Free Trade Area (SAFTA); (b) the adoption of a Social Charter for SAARC; and (c) the reform of SAARC institutions. It also envisaged a SAARC Customs Union, with harmonisation of external tariffs by 2015, and a SAARC Economic Union, with harmonisation of monetary and fiscal policies by 2020. The group also suggested a South Asian Development Fund (SADF) to finance development activities in the least developed member states.

At the tenth SAARC Summit, SAARC leaders accepted two of the three GEP's main recommendations. These are: (i) negotiation of a Treaty for SAFTA, and (ii) the adoption of a SAARC Social Charter. The leaders agreed to set up a Committee of Experts for drafting a comprehensive treaty for SAFTA by 2001. The first meeting of the Committee of Experts was held on July 15-17, 1999 in Kathmandu. An intergovernmental Expert Group is to be set up to commence work on the Social Charter. There was, however, no consensus on the long term goals of a SAARC Customs Union by 2015 and SAARC Economic Union by 2020.

SAPTA

On April 11, 1993, the SAARC Preferential Trading Agreement (SAPTA) was signed. In the economic sphere of SAARC, this was the most prominent achievement. It formally came into existence in December 1995, well in advance of the date stipulated by the sixth Summit in Colombo in 1991. The main objective of SAPTA is to expand trade and economic cooperation amongst the member states through reciprocal exchange of concessions or preferences for both tariff and non-tariff restrictions on imports from member countries, with a view to distribute benefits equitably among all South Asian states (see box 5.3). It is believed that such preferences will lead to an increase in such imports and promote mutual trade, and thus contribute to the economic development of the member countries.

The Agreement, which took effect in December 1995, was very cautious and was based on product-by-product tariff reductions. In the first round of trade negotiations (SAPTA-I), a 10-25 per cent preferential reduction in tariffs was agreed upon on only 226 items by all countries. Indeed, members even reserved the right to withdraw concessions at any time. For most countries, the intra-regional trade in the commodities on which they offered concessions initially was not more than 5 per cent of their total exports. Besides barring some offers made in favour of the least-developed member states, the preferential margins were very small.

The second round of trade negotiations (SAPTA-II) saw the number of commodities for concession rise to 1868 and after SAPTA-III the number almost doubled to 3456. The fourth round of trade negotiations plans to look at deeper tariff concessions on actively-traded products, removal of discriminatory practices and non-tariff barriers on items which have been granted tariff concessions.

Despite these efforts, South Asia's intra-regional trade has not picked up. Why is that?

Box 5.2 SAARC: A calendar of events

1981 – Colombo	First formal meeting of the foreign secretaries of the region for venturing into institutionalised regional cooperation was held.
1983 - New Delhi	The second stage towards regional cooperation was marked with the convening of the meeting of the foreign secretaries. The Integrated Programme of Action (IPA) was launched here through the declaration of the South Asian Regional Cooperation (SARC).
1985 – Dhaka	The first SARC Summit was held and the heads of state or government decided to establish South Asian Association for Regional Cooperation (SAARC). For the first eight years of its existence, hardcore economic issues, such as trade, industry, money and finance were to be kept outside the scope of cooperation under SAARC.
1991 – Colombo	An Inter-Governmental Group (IGG) was set up to formulate an agreement to establish a SAARC Preferential Trading Agreement (SAPTA) by 1997.
1993 – Dhaka	The framework agreement on SAPTA was finalised. SAARC and UNCTAD signed a Memorandum of Understanding too.
1995 - New Delhi	SAPTA formally came into existence, well in advance of the date stipulated by the Colombo Summit. The SAPTA provided for a transition to a South Asian Free Trade Area (SAFTA). Earlier it was envisaged that SAFTA would be achieved by the year 2005. Three rounds of negotiations have taken place under SAPTA. In the last round of negotiations, a total of 3456 commodities were offered for tariff concessions.
1997 – Male	At the Summit, the heads of state or government decided to bring forward the date of achieving SAFTA to 2001.
1998 – Colombo	The tenth Summit decided that deeper tariff concessions should be extended to products which are being actively traded or are likely to be traded among members, in order to accelerate the progress in the next round of SAPTA negotiations.

The Reality of trade under SAPTA

Intra-regional trade within the SAARC countries is affected by a number of economic as well as non-economic factors, such as:

• *Similarity of products and process*. As most of the economies are based on agriculture and their technological advances as regards production processes are not very different, they produce very similar items. Thus the preferential trade agreement may not necessarily lead to higher volumes of intra-regional trade within SAARC.

Box 5.3 SAPTA principles in a nutshell

- Overall reciprocity and mutuality of advantages.
- Step-by-step negotiations and periodic reviews so as to improve and extend the preferential trade arrangement in stages.
- Inclusion of all products, raw, semi-processed and processed.
- Special and favourable treatment to least-developed countries (Bangladesh, Bhutan, Maldives and Nepal).

• *Consumer demand*. Some of the goods produced on a large scale in certain SAARC countries do not appear to meet the required consumer demand of the importing SAARC country. For example, as Pakistan is not a tea producer, it offers a large market for tea exports of Sri Lanka, India and Bangladesh. However, a large part of Pakistan's tea requirement is imported from outside the SAARC region, such as Kenya, because the kind of tea required by Pakistan is not produced in adequate quantities in the SAARC region.

• *Product quality*. Sometimes it is the lower quality of products produced within the region that leads some countries to import goods from outside the region, even though the prices outside the region may be higher.

• *Market limitation*. Sometimes this becomes a major obstacle. Intra-regional trade can suffer because of political and/or geographical considerations. For example, geography limits the markets for Nepal and Bhutan, being land-locked countries they have to trade mostly with India. On the other hand, political differences between India and Pakistan have kept the trade between these two countries at a very low level.

However, if all trade in South Asia is fully liberalised and tariff levels are lowered, then preferential trade agreements under SAPTA become less meaningful and would not particularly help in enhancing intra-regional trade. In this context, it is important to note that preferences given from a low tariff regime are less meaningful and significant than those from a high tariff regime. For example, a 50 per cent preference for a 60 per cent tariff level will bring down the preferential tariff level to 30 per cent, whereas a 50 per cent preference on a 12 per cent tariff level will bring the new tariff level down to 6 per cent. Clearly the effect on prices of the latter preference is less than the former. Similarly, if imports have few restrictions, the question of preference does not arise.

Transportation and communication links within SAARC

Within the South Asian region, service industries in the sub-sector of transportation and communication are still quite primitive and in their technological infancy, and tend to be restricted by their time-old practices, and restrained by lack of investment. In the transport sector, there are direct flights from Colombo to Europe, Middle East and South East Asian countries, but within SAARC at least one change-over is required for flying from Colombo to Bangladesh or Nepal. The high costs of airfreight also hinder the free flow of cargo by air. On the telecommunication sector side, there is over-usage and congestion during business hours. A letter can take about two weeks to go from Sri Lanka to Nepal.

The slow port facilities are another impediment to free flow of trade. An average Indian port takes about twenty-two days to deal with the cargo ships, whereas the average for other East or Southeast Asian ports is about twelve days. It takes over ten days to clear cargo from the port of Colombo, but in Dubai ships are cleared within five hours after arrival. Airfreight cargo in Dubai is cleared in three hours! Thus, the geographical proximity of SAARC member countries is negated by inefficiency, delays, lack of proper facilities and inadequate flights, air and sea routes and shipping services.

Pros and cons of preferential arrangements

Of the various existing preferential trading arrangements on the international scene, the most meaningful have been the arrangements within the Latin American countries. The regional agreements within Africa and Middle East in recent years have not been very successful. In the case of ASEAN, the intra-regional trade as a share of world trade declined among the ASEAN countries before 1990, at a period when the items under the tariff preferences were increased to over 20,000 by 1990. It is because of the slow progress of the ASEAN preferential trade arrangement that the countries decided to move towards the establishment of a free trade area during the Summit meeting in January 1992.

The Bangkok Agreement, encompassing Bangladesh, Sri Lanka, India, Laos and Republic of Korea, emerged in the early 1980s, but over the last fifteen to twenty years intra-regional trade has declined as a share of their world trade. In fact, the very imports that had been granted tariff preferences declined in value during the period 1981-86, and for almost half of the preferential items there was no record of imports from their member countries. The reason cited for the low level of trade was that there was no political will. This apparently seems to be the case with the SAARC as well.

What really has to be identified is whether the preferential trade arrangements within South Asia are themselves an effective tool for creation and growth of intra-regional trade, or whether historic relations, religious differences, political attitudes and issues of sovereignty play the deciding role? Furthermore, preferential trade arrangements focus on market access via tariff reductions. Markets can be accessed more easily if tariff reductions are not followed by interim ancillary duties or para tariffs. Also the existing non-tariff barriers (NTBs) stand in the way. On the other hand, the removal of NTBs is only worthwhile if they are applied frequently and to the actively-traded goods within the region.

Custom duties and tariffs generally do not include various other charges such as landing, port and warehousing charges and surcharges. Sometimes these are fairly significant and negate the lower or no tariffs, thus neutralising the effects of tariff removals. As a result, the business community within SAARC tends to lose confidence in the tariff reductions under SAPTA.

Rules of Origin need to be an integral part of preferential or free trade arrangements. They determine that no agreements are violated by geographical location of industries to bring their products within the preferred regions. If the Rules of Origin decree that at least 40 per cent of a product must be from the country selling the product then it eliminates or reduces the misuse of location by the stronger producing countries to infiltrate through SAPTA into large and concessional markets.

Due to the existence of a fairly substantial amount of illegal trade within the SAARC region, lowering of tariff barriers may not immediately make a major impact on the volume of official trade. The incidence of illegal trade on regular trading is a problem for most preferential trading arrangements. In ASEAN, there is a substantial amount of illegal trading, such as most exports from Indonesia to Singapore find their way through the informal sector, and these are not reflected in the various annual trade statistics. Even if the informal trade sector is diverted to the formal sector it will not denote fresh and increased trading but will only show up as part of the existing trade. The strength of a preferential trade agreement lies in new trade creation and not merely in creating trade diversion.

Due to the existence of a fairly substantial amount of illegal trade within the SAARC region, lowering of tariff barriers may not immediately make a major impact on the volume of official trade

Some policy issues for SAPTA

Trade preferences include both tariff and non-tariff preferences. Most preferential trade agreements established in the world have worked on tariff reductions on specific goods that do not face non-tariff barriers. Large tariff concessions are meaningless if the import of the item is severely restricted on other grounds. In fact, this is one of the reasons for hindering trade within a preferential trade grouping. The countries, while providing each other tariff preferences with one hand, restrict their imports with the other hand. In any preferential trade agreement if tariff concessions are combined with

There are enough economic reasons for advancing intra-regional trade and cooperation in South Asia

non-tariff concessions, it will be more effective in facilitating mutual trade. However, even under such a framework the following two conditions should be met: (a) tariff cuts should be significant so as to make a marked impact on the imported price, and (b) trade preferences should cover a large number of items of current and potential trade value in order to cover a reasonably large area of trade.

Preferential trading arrangements could be stimulated by applying two strategies. One strategy could be to first work bilaterally within a regional framework on a selected group of commodities and then extending the system to the entire region. This approach is known as 'gradualism', and was first advocated by the father of economics, Adam Smith. The Australian-New Zealand Closer Economic Relations Trade Agreement is an important model where all tariff and quantitative restrictions affecting bilateral trade for a large list of commodities were eliminated gradually during the 1983-1990 period. In this Agreement, trade liberalisation was based upon the principle of a 'negative list' whereby reciprocal concessions were extended across-the-board to all the commodities, with the exception of an initial list of sensitive items to be liberalised eventually. The bilateral free trade area thus created between Australia and New Zealand proved to be very effective in increasing trade.

The second strategy could be adopted by a region that could attract external funding and investment. For example, in the case of ASEAN, despite slow progress in trade under the preferential trading arrangement, the stimulant that enhanced regional trade to a level of 16 per cent, was extra-regional investment and support from Japan. Japanese investment and support invigorated the dormant economies in the region. This in turn stimulated trade under the preferential trading arrangement.

There are enough economic reasons for advancing intra-regional trade and cooperation in South Asia. Direct trade in such products as steel and aluminium, textile machinery, chemical products, and dry fruit, currently being diverted through third countries, will benefit all countries quite substantially in terms of price, quality, and time. Besides, many goods being imported at high costs from other countries can be made available from within SAARC. Specific trade complimentarities need to be created in order to foster greater intra-regional trade in South Asia. Promising prospects for immediate intra-SAARC trade expansion exist in such products as tea and coffee, cotton and textiles, natural rubber, light engineering goods, iron and steel, medical equipment, pharmaceuticals, and agro-chemicals.

In the context of SAFTA, policy makers of member countries are going to face a tough time. First, they are going to come under a tremendous pressure from various private sector lobbies. Importers of a product will support tariff liberalisation while producers may lobby against it. Secondly, some items will be included in the negative list purely for revenue considerations. Thirdly, the negative list must be justifiable on good grounds to other member countries. Given the fact that the size of the negative list is not well defined in the SAPTA agreement, a likely scenario is that of a very large negative list being submitted by member countries and consequently having only a few products under free trade with zero tariffs. Such a scenario will not help in moving quickly towards a custom union or a common market.

Benefits of regional cooperation

The history of policymaking in the region implies that often pure trade levels and flows are less central to decisions than other issues such as income distribution and poverty alleviation. With this in mind, the debate then turns to what should be the optimal trade policies for South Asian countries with regard to each other, and the rest of the world.

A study establishing the link between tariffs and transport costs for neighbours considering trade liberalisation found that increasing intra-regional trade can avert large transport costs associated with internal trade in the larger countries and with partners outside of the region (Srinivasan 1993). This will benefit all trading partners unambiguously. It also found that new trade in goods and services can be generated that could have a significant growth-enhancing effect. It is pointed out however, that multilateral liberalisation would be much more beneficial to each of the individual countries. It further revealed that while regional liberalisation would benefit all countries, the effect would be largest for the smaller economies of the region.

In South Asia, there are some sectors which have traditionally been seen as areas of potential cooperation that could very well be strengthened by regional integration as opposed to multilateral liberalisation. India has a clear revealed comparative advantage in iron ore and Pakistan in vegetable and fruits, for example. Furthermore, there is no doubt that cooperation in sectors such as energy and electricity could be substantial. It is evident that during periods of high price inflation of energy resources, energy imports lead to negative effects on output, terms of trade, debt and even income distribution. The benefits of alleviating this dependence on foreign energy sources by regional trade are unambiguous. In addition, there is potential for trade in manufactured inputs that would dampen energy price shocks. There is also enormous potential for hydropower cooperation given that the Himalayan rivers flow through Bangladesh, Bhutan, Nepal, India, and Pakistan.

There can be significant gains both from increasing intra-regional trade as well as from trade outside the region. While economic gains would result from either policy, it is perhaps more important to recognise that the major benefits from intra-regional trade and cooperation would be political. According to a study, a political agreement that reduces tensions and hostilities in the region, thereby releasing resources for development and poverty alleviation may very well be more important than multilateral liberalisation initiatives (Thakur 1994). Therefore, a preferential trade arrangement, either initially between India and Pakistan or as a regional effort, can be mutually beneficial, not only in its direct economic effects but also in tackling non-economic barriers. It also needs to be pointed out that rough estimates of the value of smuggled and third-country goods imported from India into Pakistan approach US$ one billion and that similar Pakistani imports into India could well push the value of trade up to US$ 2-3 billion.

There is every reason to believe that a preferential trading agreement in the region at a pace suited to all the countries could secure welfare gains and increase trade flows at least until it is clear that multilateral liberalisation as a commitment of all WTO members is being practised by all members. After all, it is true that regional agreements exist in all parts of the world: NAFTA and the EEC, among others, are coexisting peacefully amidst calls for globalisation.

If South Asian countries remain aloof in a world of trading blocs, they stand to lose tremendously. In a world that is headed towards free trade, regional agreements would facilitate the entry of smaller nations in the multilateral trading system on a preferential basis. It is important for South Asian countries to acknowledge the welfare gains from their own regional arrangement which would at the same time prepare the domestic producers for the rigours of multilateralism.

Clearly it has been the political tension in the region that has been the main stumbling block to trade and cooperation—the history and current trade and cooperation in South Asia is testament to the long-standing mistrust that has dominated the post-war era (see box 5.4).

There can be significant gains both from increasing intra-regional trade as well as from trade outside the region

There is no question that a regional arrangement that addresses economic issues while removing political hostility is beneficial to all. There is also a need to shield the poor masses of the region from the rigours of globalisation.

Policy implications

In view of the lack of mutual trust, ethnic and religious conflicts, and the magnitude of bilateral disputes in South Asia, it is unrealistic to believe that any substantial growth of regional cooperation is possible without first easing political tensions. Any realistic assessment of the prospects for the growth of economic cooperation and interdependence in South Asia has to address several of the following issues.

The first issue relates to the role of the state in promoting regional cooperation in South Asia. Given limited political contacts and mutual security concerns, a state-directed approach to economic cooperation is better suited to this region. Any prospect of enhancing regional economic cooperation exclusively by the market forces appears bleak. Conscious efforts at the political level and demonstration of political will by the South Asian leaders are absolutely necessary for the growth of regional economic cooperation in South Asia.

The second issue concerns the development of a pragmatic approach to economic cooperation in South Asia. Given the extensive heterogeneity in the levels of economic development of South Asian countries, how can they proceed to achieve such a strategy? Clearly, the approach should be gradual and based on the economic capability of each state.

Box 5.4 Regional trading blocs and South Asia

The various economic groupings joined by the South Asian countries have not met with great success. South Asia, during the last fifteen years, has witnessed four major attempts at regionalism, via various trading blocs such as Economic Cooperation Organisation (ECO), Indian Ocean Rim Association for Regional Cooperation (IOR-ARC), Bangladesh, India, Myanmar, Sri Lanka, and Thailand Economic Cooperation (BIMSTEC) and SAARC.

ECO, at present consists of Islamic nations of Central Asia, Islamic nations of Eastern European countries (Turkey), West Asia (Iran), and South Asia (Pakistan). Intra- ECO trade during the first five years of the 1990s stagnated between 2-5 per cent of its total trade. The member states of ECO signed a Preferential Trade Agreement in 1992 that provided for a 10 per cent import tariff reduction on specified commodities. It was further proposed that expansion of the list of concessions and increase in the depth of tariff reductions to 25 per cent will take place but no action was taken. This lack of commitment has therefore not translated into any significant increase in intra-ECO trade.

The IOR-ARC was formed in the mid-1990s when India's 'Look East' policy coincided with Australia's 'Look West' policy at the time when South Africa was attempting to assert its regional space and gain recognition in global affairs. In 1999, there were 19 member countries that formed IOR-ARC including India, Sri Lanka and Bangladesh from South Asia. India has blocked Pakistan's entry to the IOR-ARC, as Pakistan is not offering MFN status to Indian exports.

Cooperation among the Indian Ocean countries has also not been a great success. The countries are vastly different and they have their political allegiances with non-IOR-ARC countries. Above all, economic co-operation in the IOR-ARC is based on the 'open regionalism' arrangement, which is a very vague concept. The prospects for South Asian countries to establish stronger links with Australia, Africa, and the Gulf via IOR-ARC do not seem to be bright.

South Asia's attempt to form a corridor to ASEAN and Japan, via BIMSTEC was a Thai initiative stemming from Thai government's 'Look West' policy in late 1997. BIMSTEC is viewed by some as the revival of the old Bangkok Agreement, which is reaching a point of natural disintegration. Given the commitments for preferential trade agreements in ASEAN and SAARC, reductions in tariff among BIMSTEC members could take place only in the wider Asian context under the Bangkok Agreement. Any other new initiative in preferential tariff among BIMSTEC countries may not be possible at this point in view of the national commitments to WTO and also due to the existing preferential trading arrangements.

The fact that SAARC member countries are looking at forming other regional alliances in the presence of SAARC reinforces their frustration about SAARC. As is suggested by the failure of these attempts at forming regional alliances, South Asia has to concentrate more on SAARC and adopt an attitude of rational economic behaviour and understanding.

Regional cooperation should not replace, but only complement the existing bilateral trade and economic transaction between the South Asian countries. The growing interest in operationalising a South Asian Free Trade Area (SAFTA) should not obscure the importance of the extra-regional and global economic cooperation that most of the South Asian countries are currently engaged in. For instance, it would be detrimental to the economic interests of India, Pakistan and Sri Lanka, if they do not seek access to the markets in Central Asia, Southeast Asia, the Gulf region, and the OECD countries. The key to the development of a pragmatic strategy to increase economic cooperation among the countries is to promote intra-regional trade by lowering tariffs without de-linking from inter-regional and global economic relations.

Third, to begin with SAARC countries should pursue modest trade objectives and seek joint development projects of modest scale. Only after the benefits from the modest cooperation have been reaped, and are visible, that the tempo of cooperation be increased.

Fourth, conservation of the natural resource base should constitute an integral part of any economic development strategy. In order to meet their growing needs of energy and alleviate health risks, South Asian countries should give top priority to an efficient use of the natural resource base and conserving the environment.

Finally, a South Asian Development Fund (SADF), as suggested by the Group of Eminent Persons (GEP) should be established in order to provide financial support to regional projects (GEP Report 1998). The aim of the proposed fund is to undertake regional infrastructure, environmental, poverty alleviation, and human resource development programmes; assist in financing joint ventures; and to extend support for intra-regional and inter-regional trade. A successful SADF will be able to provide the much-needed economic support to regional projects and thereby strengthen interdependence among the South Asian countries.

What South Asia needs is regional identity and rationality

What South Asia needs is regional identity and rationality. No one country can unilaterally level the ground for making SAARC an efficient organisation. A consensus needs to be developed and agreed to by all SAARC member countries about the place of South Asia within Asia and also internationally.

South Asia can learn a few lessons from ASEAN. The success of ASEAN has been attributed to three factors: Each country must build up its own resilience and other countries must help that country to this end; the low-key approach of its biggest member, Indonesia; and the habit of working together. Seen in this context, India has a clear responsibility to be magnanimous to other members of SAARC, and other smaller countries in the region should also modify their attitudes to make SAARC an efficient body.

BLANK

6

Institutions of Global Governance and Globalisation

Global markets cannot achieve justice for all nations or all people. Global institutions are needed to set rules, to monitor 'global goods' and 'global bads', to redress widening disparities. Paradoxically, the global institutions are weakening just as global interdependence is increasing.

– Mahbub ul Haq

Chapter 6

Institutions of Global Governance and Globalisation

While the world economy has been evolving towards an integrated system, the mechanisms for managing the system in a stable and sustainable way for the benefit of all people have lagged behind

In the wake of globalisation, growing economic interdependence of countries poses enormous challenges for global governance. A global economy has emerged but the institutions of global governance, i.e., the governmental functions that need to be performed at the global level, are not performing either efficiently or equitably. While the world economy has been evolving towards an integrated system, the mechanisms for managing the system in a stable and sustainable way for the benefit of all people have lagged behind. The globalisation process is expanding global opportunities without distributing them equitably. There are enormous differences in the relative power and influence of different actors at the global level: there are nations of different size and power, international institutions of different degrees of influence, private firms of different size and power, and international NGOs of different degrees of influence.

Among the most powerful of the multilateral economic institutions are the Bretton Woods Institutions (BWI), i.e., the International Monetary Fund (IMF) and the World Bank, and the World Trade Organization (WTO), in which the representation of the majority of world's population is particularly weak. Decision-making in these global forums, as perceived by many analysts, is neither representative nor transparent. As such, much of the criticism of globalisation has been directed at these institutions for failing to address the inequities and adverse effects borne by the poor nations and poor people. The previous chapters have analysed the national policies and their impact on people in South Asia. In this chapter we look at these three institutions of global governance that have been most responsible for framing the policies of globalisation in order to integrate the developing world into the global market.

Bretton Woods Institutions: A brief history

The Bretton Woods Institutions were created to serve as global institutions for maintaining financial stability and for promoting development and trade. While the intentions of the founding fathers were noble, these institutions are currently experiencing a crisis of confidence as there is a growing perception that they have failed to achieve the objectives for which they were created.

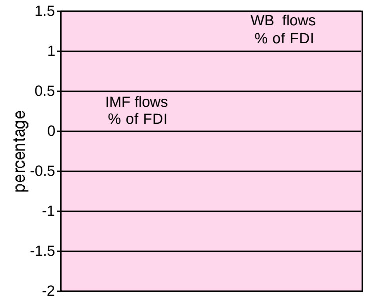
After the Great Depression of 1930s and the Second World War, the famous British economist, John Maynard Keynes, became convinced of the imperative of setting up institutions of international economic management that would protect the world from another economic catastrophe. Keynes' ideas, embodied in the 1942 Memorandum, were based on four pillars. The first pillar was to provide global macroeconomic monetary and financial stability. The original idea was of a World Central Bank which would maintain full employment and provide the liquidity for this purpose by expanding the supply of 'bancors', the proposed world reserve currency. This would mainly serve to finance the balance of payments deficits of countries. In 1942, Keynes wrote, 'We need a system possessed of an internal stabilising mechanism, by which pressure is exercised on any country whose balance of payments with the rest of the world is departing from equilibrium in *either direction* (italics by Keynes), so as to prevent movements which must create for its neighbours an equal but opposite want of balance'. The second pillar was what ultimately emerged as the World Bank, or International Bank for Reconstruction and Development. In the 1942 Memorandum, this was suggested to be an investment fund for relief and development of war-torn Europe. The third pillar was the International Trade Organisation whose primary function was to stabilise prices of primary commodities. The main idea was to prevent the collapse of prices of primary commodities which had been a marked feature of the Great Depression. The fourth pillar of the system was meant to be a soft aid programme linked with the United Nations (Singer 1995).

The Keynesian vision for the Bretton Woods Institutions was greatly diluted in actual implementation (M. Haq 1995).

- In the place of a World Central Bank with access to resources equal to one-half of world imports, as was proposed by Keynes, the IMF was established with control over less than 3 per cent of world imports. The reserve currency of IMF (Special Drawing Rights) constitutes only about 3 per cent of global liquidity. And with the introduction of floating exchange rates in 1971, the main function of IMF, i.e., maintaining exchange rate stability, was also lost. So the IMF reinvented itself by undertaking surveillance, providing technical assistance and short-term resources to tide over balance of payments difficulties of developing countries. Keynes placed the burden of adjustment on both surplus and deficit countries; in actual practice, deficit nations, mainly developing countries, bear the burden of adjustment.
- Similarly the World Bank, which was supposed to stand between the global capital markets and the developing countries and to recycle surplus resources to poor nations for promoting development, is now a minor player in global capital markets. The dominant role in recycling funds is now played by multinational corporations (MNCs) with home base, in most cases, in developed countries, and investing in a handful of developing and former communist bloc countries, with the aim of making profit and expanding their market share. In 1999, of the total net financial flows (FDI) in the world, World Bank accounted for only one per cent and IMF provided minus 1.4 per cent (see figure 6.1a), whereas in South Asia, World Bank accounted for 31 per cent and IMF for minus 2.7 per cent of the net financial flows to that region (see figure 6.1b). It is a sad commentary on the current institutions of global governance that despite being such minor providers of resources for development, they exercise so much influence on the economic policies of developing countries!
- Keynes envisioned an international trade organisation which would not only maintain free trade but also help stabilise world commodity prices. But as there was no consensus for creating a world trading body, a General Agreement on Tariffs and Trade (GATT) was set up which excluded primary commodities altogether from its purview. Finally in 1995, at the last round of Uruguay trade negotiations, the World Trade Organization (WTO) was established. This new institution provides for a dispute settlement mechanism to ensure a rule-based trading system. It also deals with the commodities trade.

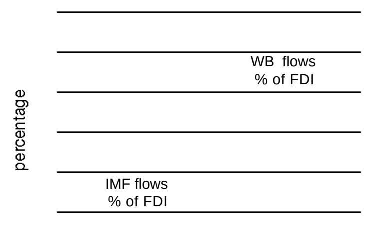
The impact of policy conditionalities of these global institutions of governance has fallen disproportionately on the poor, both socially and economically. Organisations such as the UN and international NGOs have tried to respond by playing a supportive and partnership-oriented role in addressing the concerns of the poor. Nevertheless, the fact that global private corporations, driven mainly by the profit motive and mostly unconcerned about social issues, control a large proportion of global GDP is a matter of serious concern to many poor people and poor nations (see figure 6.2).

Figure 6.1a Net financial flows from multilateral institutions as a % of FDI flows 1999 (world)



Source: World Development Indicators 2001.

Figure 6.1b Net financial flows from multilateral institutions as a % of FDI flows to South Asia (1999)



Source: World Development Indicators 2001.

Experience of South Asian economies has shown that during the period of structural adjustment, poverty has increased and income distribution has deteriorated

Recent policies of IMF and World Bank in South Asia

While the early policies of the global institutions of governance were designed in the spirit of building the capacity of the state, over time there has been a trend towards reducing the role of the state and moving towards liberalisation and privatisation in South Asia as well as in other developing countries. The reason for this shift is partly due to inefficient economic management in the public sector in most countries of South Asia.

In our 1999 report on *Human Development in South Asia*, we underscored the governance failure as one of the most critical challenges that South Asia faces today in promoting economic growth and reducing poverty. The South Asian states have fallen back on their essential tasks, even though their involvement in the socio-economic lives of the people is pervasive. They are unable to deliver the most basic public goods—sound macroeconomic management, basic social services, and internal law and order. As a result of these failures, during the 1980s and 1990s debt burden kept on rising, trade and budgetary deficits widened, and poverty increased. This was the situation which led the South Asian governments to seek IMF and World Bank help. Short-term relief was sought from the IMF to tide over the short-term financial crisis; the Bank was approached to provide medium to long-term development finance to revive economic growth and reduce poverty.

Most South Asian countries have been implementing the IMF and World Bank stabilisation and structural adjustment programmes during the 1990s. While the IMF loans are useful as a certificate of creditworthiness for accessing other multilateral and bilateral loans, grants and investment, the conditionalities attached to these loans make it impossible for countries to get out of the debt trap and on to a higher growth path. Experience of South Asian economies has shown that during the period of structural adjustment, poverty has increased and income distribution has deteriorated. In early 1990s, unsustainable balance of payments and fiscal deficits, among other variables, compelled India and Pakistan to take loans from the IMF and the World Bank which carried the usual conditions for stabilisation and structural adjustment, including cuts in public expenditure. As shown in chapters 3 and 4, while India's growth rate had increased to over 6 per cent, income inequality had increased, poverty had been reduced at the national level and in urban areas whereas in the rural areas it had gone up. In Pakistan, on the other hand, growth rate had declined and both poverty and inequality had increased.

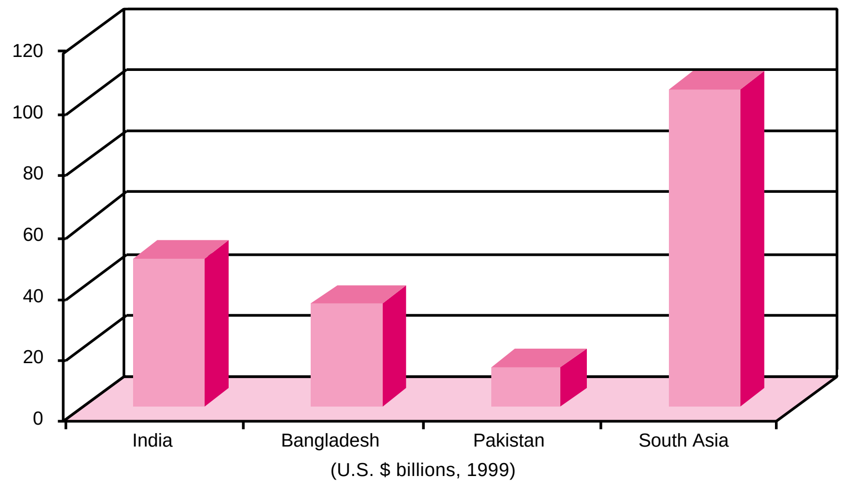
Impacts of stabilisation and structural adjustment

The most debated IMF/World Bank instruments have been the stabilisation and structural adjustment programmes (SAPs) which countries must implement in order to have access to funds for achieving higher growth with stability. These programmes include wide-ranging reforms and restructuring in many areas, including contraction of demand through fiscal and monetary policies, and improving productivity and competitiveness through privatisation and liberalisation of markets. While such funds are intended to provide relief from both short-term balance of payments deficits as well as long-term funds for development purpose, fiscal balance has generally been achieved at the cost of social services including cuts in expenditure for education, health and food subsidies targetted mainly at the vulnerable groups in the society. While policy decisions to allocate funds to social sectors is a responsibility of national governments, the policymakers in South Asia, however, are finding it increasingly difficult to allocate more resources for social programmes. The servicing liability of past debts is perhaps the single most serious constraint in this regard. In order to make an assessment of the usefulness of IMF/World Bank programmes in South Asia, we need to briefly look at five critical areas of concern.

DEBT BURDEN: Although South Asia has been the second largest (Africa is the largest) regional recipient of concessional lending from the Bank's soft-loan affiliate, IDA (see figure 6.3), yet the region has accumulated a huge level of debt. In addition to mounting military expenditure, debt servicing is a major constraint to increased development investment in South Asia. Unsustainable and high debt servicing levels consume significant portions of some countries' GDP. In terms of total debt, of the top 15 debtor countries, India is ranked as 8th, with a total external debt of 94 billion, with Pakistan at 34 billion, Bangladesh at 18 billion, Nepal at 3 billion and Sri Lanka at 9 billion US dollars (WB, WDI 2001). The debt burden is particularly heavy in the case of the least developed countries in South Asia which are Maldives, Nepal, Bhutan and Bangladesh. While debt is being rescheduled and/or written-off in many nations of sub-Saharan Africa, through new initiatives and donor commitments, the least developed nations in South Asia have so far not been able to get much relief from these initiatives.

POVERTY: Both IMF and World Bank are now committed to poverty reduction in developing countries. Although IMF strictly adheres to its macroeconomic stabilisation policies, in 1987 it created the Enhanced Structural Adjustment Facility (ESAF) in order to make IMF financing less expensive for the low-income countries. However, in view of the harsh criticisms emanating both from professional analysts as well as from the civil society groups concerning the adverse impact of IMF policies on poverty, in 1999 IMF announced its commitment to poverty reduction and replaced ESAF with Poverty Reduction and Growth Facility (PRGF). Developing countries are now required to prepare

Figure 6.3 Cumulative inflows of IDA in South Asia



Source: World Bank, World Development Indicators 2001.

Poverty Reduction Strategy Papers (PRSPs) to access this facility.

Studies commissioned by the World Bank have also shown that the Bank's poverty assessments failed to address the link between poverty reduction and macroeconomic and sectoral policies. The Bank's poverty assessments also gave limited attention to local dimensions of poverty reduction and to the role of debt in poverty creation. Thus, the Bank has also joined IMF with a sharper focus on poverty reduction as an essential element of the strategy for accelerating economic growth. PRSPs have become an important policy document of governments in their negotiations with the IMF and World Bank. Without an acceptable PRSP, a country can have little access to external assistance since the funding by other donors also depends on the acceptance of PRSP by the IMF and the World Bank. But a typical PRSP includes all the stabilisation and structural adjustment policies that are considered essential by IMF/World Bank to facilitate the country's entry into the global markets for goods, finance and services (see box 6.1).

PRIVATISATION: While the World Bank policies were initially intended to assist developing-country governments in their development initiatives, the policies during the late 1980s have seen the

Box 6.1 Are the new Poverty Reduction Papers really new?

The Poverty Reduction Strategy Papers (PRSPs) have drawn criticism for being little more than reworked versions of standard IMF policy papers that mandate structural adjustment programmes as preconditions to accessing IMF assistance. A policy dilemma results from the PRSPs in many cases as the implied methods of implementation directly conflict with elements of Structural Adjustment Programmes. For example, how will subsidies, social safety nets and social sector spending be protected from cuts prescribed by SAPs? There is a need to balance social sector needs with those of economic revival. A satisfactory solution to this dilemma holds the key to the high pro-poor growth.

In the Poverty Reduction Growth Facility framework, the 'success' of a poverty reduction strategy is based on government's macroeconomic and structural reform policies. While a PRSP might even yield some useful information about how poverty should be addressed, it is vague as to how poverty elimination measures will be linked to the standard array of macroeconomic and structural adjustment conditionalities that continue to remain the mainstay of the IMF-World Bank reform programmes. Evidence from the interim PRSPs already undertaken in Africa, Latin America, South Asia and Southeast Asia shows striking similarities with the conditionalities that accompanied earlier Policy Framework Papers. There has been no transformation nor examination of historic causes of poverty while achievement of social goals is relegated to social safety nets, regardless of government capacity to provide them.

activities of the Bank shifting towards empowering the market and private sector. Furthermore, rather than use such development efforts to build up the strength of local firms, the lion's share of development contracts have gone to foreign firms.

In order to facilitate the region's integration into the global economy, the Bank has encouraged private sector participation in the funding and management of infrastructure projects such as power, telecommunications, natural gas, and transport. Urban development projects that strengthen urban planning, finance and improve transport infrastructure, and improve service delivery in areas other than the ones just noted, have also involved the private sector. Lately, there have been increased efforts to privatise oil and gas development, distribution of power, telecommunications, infrastructure development, as well as institutional and regulatory reform as reported in Pakistan, India, Bangladesh, Sri Lanka and Nepal.

A serious problem arises from such rapid privatisation. In many South Asian countries there is a weak domestic base of investors, so with increasing foreign investment in public assets, ownership and control is transferred to outsiders. This can have adverse social consequences if the asset in question, for example, a well-networked bank with many linkages to rural areas and providing small credit, falls into foreign hands and undergoes a strategic restructuring with respect to its mandate and its functioning. It is quite probable that this type of restructuring may go against its original purpose of serving the poor people in distant areas.

Privatisation has yielded mixed results as regards actual improvements in efficiency. Furthermore, many South Asian firms are not globally competitive. In order to improve competitiveness, the World Bank and IMF often recommend closing down and/or privatising many such firms, resulting in layoffs and increased unemployment.

Increased privatisation is forcing hundreds of small and medium-sized enterprises, for example, textile mills, battery manufacturers, ceramic units, small machinery and makers of spare parts that employ mainly the poor, to shut down due to foreign competition. Closures due to privatisation in India have pushed a large number of working women (11 per cent of the public sector labour force) to work under dismal conditions in the informal sector.

LIBERALISATION: Liberalisation policies are supposed to create a global market environment where resources can be allocated free from the inefficiencies and distorting policies of state interventions. But in the real world of South Asia where management and labour skills are limited, finance is not readily available, infrastructure is poor and rules of business are not properly developed or enforced, the policies for trade, financial and investment liberalisations that have been designed to encourage the best allocation of resources do not really result in increasing investment and accelerated growth. Volatile private capital flows and highly protectionist export markets have threatened the fragile economies. The stabilising state regulatory control measures are being undermined by international agreements. In recent years the developing countries have run greater current account deficits as a proportion of GDP than in the past, without achieving higher growth rates. These growing current account deficits have been primarily due to widening trade deficits, as export earnings have generally been unable to keep pace with the rapid import expansion. Evidence from many countries shows that trade liberalisation is followed by a combination of large capital inflows, currency appreciation and mounting trade deficits mainly due to import surges being unmatched by sluggish export responses. The chain of events often ends with a crisis involving a reversal of capital inflows, collapse and overshooting of exchange rates, sharp cuts in imports and a strong economic contraction (UNCTAD 1999b).

The liberalisation policies have also promoted the corporatisation of large agricultural farms and has indirectly promoted the entry of large agro-MNCs. The World Bank funding to Indian agriculture has supported the fertiliser industry, groundwater pumping, high-yield seeds and setting up of banking institutions to finance capital-intensive agriculture. However, there has been little examination of how such liberalisation policies will affect the sustainable livelihoods of subsistence farmers who make up the majority of the agrarian sector. It is feared that the structural adjustment programmes comprising subsidy elimination, establishment of agro-corporations, removal of trade restrictions on agricultural commodities, and an overall unification of local with global prices will leave the poor farmers in a most vulnerable situation.

While state inefficiency and artificial low pricing of agricultural commodities have led to decreased agricultural productivity and rural income, there has been little discussion on how improved governance could ensure the provision of better infrastructure, tenancy rights, reform of land ownership and protection for small farmers. The policy initiatives in these areas have been few in South Asia.

EMPLOYMENT: On this front the concerns that stem from globalisation policies are both positive and negative. Liberalisation involves opening up of markets to foreign competition and investment while reducing government intervention and protection. Market liberalisation policies are lowering barriers to opportunity for the educated and skilled labour force of South Asia leading to increased employment, investment and growth of the information technology and telecommunications sector. IT-enabled sectors, such as data-processing and teleworking, have not only created direct employment for thousands of men and women mostly in India, but in other South Asian countries as well (250,000 jobs for women over past four years as quoted in ILO World Employment Report 2001). On the other hand, barriers to opportunity exist for a broad segment of South Asians who are uneducated and unskilled and thus cannot benefit from the new technology-created jobs. Furthermore, unemployment is rising as a result of massive layoffs by the privatised state financial institutions and utility companies. Most importantly, the marginalised people who rely on the state for employment and social support (education and healthcare) to remain above the poverty line are the ones most exposed. These groups find it most difficult to adjust.

There has been little examination of how such liberalisation policies will affect the sustainable livelihoods of subsistence farmers

IMF in Latin America, East Asia and Russia

In the 1980s, the Latin American countries had experienced huge financial and fiscal crises because of huge government deficits, loose monetary management and runaway inflation. The situation called for tight fiscal and monetary policies to stabilise the economies. The policies that the IMF had prescribed to governments in Latin America covered wider concerns than merely achieving fiscal and monetary balance. It included achievement of macroeconomic stability through control of fiscal deficits, opening up the economy to foreign competition, and reducing the role of the state through privatisation and deregulation. In the case of Latin America, the IMF/World Bank medicine worked. The region's economic health was restored (Burki 2001).

Many developing countries have been critical of the IMF restructuring policies that have exacerbated the divide between the rich and the poor

But when the IMF was called in to help with the East Asian crisis, it did not look at the different underlying factors that had caused the crisis in East Asia. Unlike Latin America, the East Asian countries were running budget surpluses, had kept money supply under control, and the inflation rate was low. The genesis of the problem was created in the 1990s by international pressure, including that of the IMF, on the governments of East Asia to open up their financial and capital markets. With savings rates of around 30 per cent these countries did not need to attract additional funds. The deregulated financial and capital markets had led to inflows of short-term hot money that comes in as quickly as it goes out, in search of instant profit. These flows of hot money in East Asia had led to real estate boom. Its outflow was instrumental in real estate bust. Instead of focusing on the recklessness of the private sector, the Fund had used the Latin American recipe of tight monetary and fiscal policies to control the public sector. The inappropriate policies had aggravated the crisis in East Asia and was instrumental in spreading the contagion far and wide, including Russia.

As Russia did not have a sufficiently-developed institutional infrastructure to allow a free market economy and uncontrolled capital flows to work well, the rapid liberalisation and privatisation imposed upon Russia by the IMF, at the insistence of the US, had allowed a small group of oligarchs to gain control of state assets and plunder the country. Thus when the East Asian contagion spread, the corrupt money flew out of the country, leaving a devastated economy behind. The GDP was cut by half, poverty rates rose to almost 50 per cent, with more than half of Russia's children living below the poverty line (Stiglitz 2000).

Many developing countries have been critical of the IMF restructuring policies that have exacerbated the divide between the rich and the poor. Many claim that the IMF had aggravated the Asian Flu by compounding capital flight with harsh conditionalities that had made things worse. IMF's shock therapy—currency devaluation and increased interest rates—squeezed the domestic economy and transformed the financial crisis in each country into an economic and social crisis.

IMF in South Asia

The underlying economic situation—poor economic management, large fiscal and current account deficits, and low tax to GDP and saving to GDP ratios—was almost the same in each South Asian country. When these countries approached the IMF for assistance, the IMF prescribed the same Latin American medicine of tight monetary policy and demand contraction, complemented by privatisation, liberalisation of trade and reduced role of governments in the economy. The IMF did not take account of the fact that these countries were at a very different stage of economic development with lower human development indicators, higher poverty levels and lower levels of infrastructure development than those prevailing in Latin America. However, it is important to note that while India had managed to achieve the results as required under the IMF programme, its prescription in other countries was not very satisfactory.

India's stabilisation and structural reform programmes implemented in the

1990s, had all the usual attached terms and conditionalities. However, the Indian government formulated its own strategies with targeted objectives and deadlines to achieve the required results. As a result of the government's self-imposed discipline, the stabilisation measures succeeded in bringing the deficit to a safer level and giving a greater role to monetary policy. Foreign exchange reserves went up considerably, and the IMF loan was paid back within a few years. The engine of Indian economy's remarkable turnaround was the IT sector. The facilitating role played by the structural reform programmes needs to be highlighted in this context.

On the other hand, although Pakistan had started the IMF programme before India, its economic situation started deteriorating further so that Pakistan, till recently, was not able to complete any of the IMF programmes. During the 1990s, the period of stabilisation and structural adjustment, growth rates fell, debt burden rose sharply, and poverty intensified. The reforms undertaken under IMF/World Bank policies and direction have not so far delivered the promised results. The standard stabilisation programmes have focused primarily on stabilising the economy and not on reviving growth. The timing as well as the design of the programme was inappropriate as it was introduced when the economy was decelerating, public confidence sagging and income inequality between the rich and the poor widening. The recessionary component in the IMF programme had made the bad situation worse.

Sri Lanka, another country under the IMF standby arrangement, has also experienced low growth, an import surge, export stagnation and capital flight. Admittedly, many of the causes of the weak economic situation are due to the ongoing civil strife. But if the IMF assistance comes with the conditionalities that worsen the situation further, where could the countries go for help in times of economic crisis?

World Trade Organization

WTO is the newly-established global institution that provides a solid foundation of the new multilateral rule-based trading system. The scope of its activities includes trade in goods including agricultural commodities, services and intellectual property. A dispute resolution mechanism has also been established under WTO to provide power to the organisation to keep the signatory states within the boundaries of the trading system they have established themselves.

The predecessor of WTO, the General Agreement on Tariffs and Trade (GATT), did not acknowledge the importance of primary commodities to Southern countries. So the inclusion of primary commodities in trade negotiations has been of great importance to developing countries. However, as we will discuss below, agricultural trade is still being protected in developed countries, contrary to WTO aims and objectives of free trade. The WTO, on the other hand, has been accused of overloading agreements with a built-in agenda and terms that are too harsh for developing economies to adhere and adjust to. While the WTO mandates a 'one country one vote' policy, it is argued that its agenda is shaped, paced and driven by the US, EU and other developed countries based largely on negotiating capabilities and economic strength.

The pace of negotiations at the WTO has been set by the resource-rich Northern countries, leaving the rest to struggle with the outcomes of secretive meetings and swift agreements. Since the Uruguay Round, developed countries have failed to implement agreed-upon commitments and tariff reductions under the regular and Special and Differential Treatment (SDT) clauses. As tariff barriers have fallen in developing countries, the world has been further divided along income lines, separating the global rich from the global poor. It is argued that political pressures in the North have resulted in developing

Agricultural trade is still being protected in developed countries, contrary to WTO aims and objectives of free trade

countries reducing their tariffs to levels lower than what is required by the WTO agreement.

Trade in goods

Most of South Asia's manufacturing industries, long protected by subsidies and import substitution policies, are not competitive to face the challenges of the global market. Prior to moving towards complete liberalisation, South Asia needs first to introduce competition-inducing policies in all sectors to improve their sectoral efficiency and productivity. This requires closer cooperation between the government and the private sector. The main improvements in exports for South Asia have been in the traditional sectors with low wages. India's software industry also depends on its relatively cheap skilled labour. The need for export diversification has been acknowledged for many decades, but success has been slow in coming. And now the traditional export sectors are also facing the new rules of the game (see box 6.2).

So far, market liberalisation has been one sided. While developing economies have been forced to drastically reduce their tariff rates, their Northern counterparts have not delivered the promised tariff reductions on goods of key interest to poor countries. With respect to the dispute resolution process, the majority of cases filed in the dispute settlement arena of the WTO have been by the developed countries.

Trade in services

The importance of services in the exports of developing countries has been growing rapidly in the recent past. Exports of services is currently more than 20 per cent of the total exports of developing countries (Martin & Winters 1995). In view of the rapid expansion of trade in global services, the General Agreement on Trade in Services (GATS) has important implications for the development prospects of South Asia. When services were first included in the Uruguay Round in the mid-1980s, there was a general resistance to it in developing countries. However, the provisions of GATS do not provide for an across the board liberalisation of the services sector. Each country is free to decide the extent of its own market access to other countries for services of interest to it. Under the Agreement, the developed countries have offered market access commitments to only 50 per cent of their services market. In fact, the GATS involves no commitment to reduce the levels of protection. It involves only a standstill commitment that the protection of the services sector will not be increased.

In view of the large potential gains from a comprehensive liberalisation of services of all kinds (travel, transport, labour and financial services, etc.) to the developing countries, it is crucial that future negotiations in the services sector open the services market in developed countries for the benefit of developing countries. The surplus low and unskilled labour in South Asia—the vast majority of South Asian population—has virtually no access to opportunities in the North. The protectionist nature of Northern policies is perhaps most evident in this case.

Box 6.2 Clothing and Textiles

As per the Uruguay Round, Southern nations have reduced tariffs only to find an aggregate reduction mechanism employed by the North, which enables them to selectively keep tariffs high on items of interest to the South. The high tariffs on such items are being felt by South Asia's clothing and textiles sector, due to which exports to the US have not risen. If South Asia improves its competitive efficiency, the Multi Fibre Arrangement abolition may bring benefits in terms of increased exports but will also leave the once protected quotas exposed to free market competition. Value-added goods need to be a part of the strategy to benefit export interests, for example, the products of raw cotton, textiles, raw leather, leather goods and agricultural products (cotton, wheat and rice). The backward linkages between this sector and the poor elevate its socio-economic importance to South Asian policymakers interested in poverty eradication. Tariff escalation, a traditional tactic of the North also needs to be dismantled so that processed products may be exported from the South with greater ease and may encourage the demand for skilled labour. For example, EU and US tariff behaviour places a lower tariff on raw leather than it does on leather goods. This practice does not encourage export of South Asia's value-added products.

Source: MHHDC staff.

Intellectual property rights

Developed countries have long recognised the evolution of the global marketplace from a capital to a knowledge-based system. This foresight forged the Intellectual Property Rights (IPRs) Agreement long before the establishment of WTO. The institution that manages the IPRs is the World Intellectual Property Organization. Developed-country research and development investments have driven the protective movement as over 90 per cent of the patents owned globally are in the hands of the EU or US innovators, while 90 per cent of biological resources and life forms are indigenous to developing nations. While the mechanisms, policies and legal frameworks are lacking in Southern nations, the Northern ones continue to file for licenses and patents.

While the WTO's dispute settlement process and TRIPS agreements heavily favour the negotiating expertise of the North, there are signs of success in South Asia, where MNC applications for patents for cases such as Basmati rice (in conflict with the Convention on bio diversity), are being withdrawn due to public pressure from both North and South.

Article XXVII:III(b) of TRIPS at present calls for patents or *sui generis* rights on plant varieties developed by the 'breeder'. This interpretation undermines the rights of South Asia's indigenous farmers who may be forced to pay for traditionally natural inputs through fees to agro industry, global patent owners of plant life in essence 'owning all of the by products' of harvest. The effects of such a TRIPS-oriented patent system would result in the monopolisation of indigenous knowledge (medical, agricultural) by MNCs leading to higher prices of medicines and seeds/fertilisers at the expense of poor farmers and consumers.

Outside of agriculture, TRIPS will reduce the availability of copied or pirated products, particularly software, that has fertilised the growth of the IT-enabled service sector in South Asia. Increased costs will reduce access to skills and therefore further erode the position of the South Asian labourer. This is not to say that protection of intellectual property rights is a one-sided affair. Indeed, it is in everyone's interest to provide the inventor with some protection for the investment of resources in research and development. In the case of India, for example, lack of protection of intellectual property rights in the 1980s is blamed for low investment and lack of modernisation of the chemical and pharmaceutical sectors. However, a balance must be achieved that protects indigenous knowledge and makes provisions for less-developed economies that are clearly at a disadvantage.

The growing concern in the case of the health sector is of course, that the WTO offers opportunities as well as threats. The fear stemming from the inability of the poor in developing countries to afford essential drugs or vaccines for newly-emerging diseases such as AIDS is a looming threat. Already, the sharp increase in the price of drugs for diabetes is creating concern. Import/export and industrial policies to encourage the manufacture of medical equipment again influence the ability of the system becoming more equitable and efficient.

The inability of the poor in developing countries to afford essential drugs or vaccines for newly-emerging diseases such as AIDS is a looming threat

Trade in agricultural commodities

The most fundamental problem in agricultural trade lies with the domestic policies of developed countries. Agriculture in most developed countries is sheltered behind high tariff walls, farm subsidies, loan guarantees and non-tariff barriers that place those developing countries that are heavily dependent on agricultural exports at a great disadvantage. Agricultural trade is not being liberalised as fast as trade in manufactured goods. In developed countries, tariffs on agricultural products have remained at 40-50 per cent range; Japan had a tariff of 1000 per cent on rice last year (2000).

From human development perspective, institutional policies of multilateral organisations have resulted in increased deprivation of the poor, rising unemployment and unsustainable development practices

This is one of the most important reasons for developing countries' lack of trust in the workings of the WTO. While South Asian countries are reducing tariffs and domestic support on a whole range of products, the United States, European Union and Japan continue to subsidise and enable their farmers and multinational corporations to sell agricultural products at lower prices, while maintaining higher costs. The farm subsidies in developed countries hurt developing countries on three counts: first, it keeps the world prices low; secondly, it excludes developing countries from the food markets of rich countries; and finally, developing-country food producers suffer due to dumping of cheap food imports from developed countries (UNDP 1997). The labour-intensive Southern farmers are at a disadvantage in terms of the economies of scale realised by the capital-intensive Northern farmers. Few measures have so far been taken to protect the subsistence farmers and fishermen in the new Agreement on Agriculture (AoA).

South Asian agriculture needs to be treated differently in view of the dependence of most people on agriculture as well as the widespread rural poverty in South Asia. 'India's most recent proposal to the WTO recommends that any support aimed at alleviating poverty, rural development or the diversification of agricultural products be exempted from WTO-sponsored commitments to reduce domestic support' (The Economist, June 9, 2001).

New issues

Environment and social issues are increasingly being pushed onto the trade agenda along with the process and production methods (PPMs). PPM-based restrictions should not be imposed on resource-strapped Southern economies in which some sectors utilise out of date, and perhaps, polluting technology out of necessity. As far as labour and environmental linkages are concerned, there are national and international mechanisms designed to address these problems. A trade regime dealing with export-related activity is neither an appropriate forum nor an effective device to achieve these objectives, as they will be used by countries to raise non-tariff barriers and, as some studies suggest, make the situation of child labour and poverty worse.

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Across the institutions of global governance, there is an urgent need to reassess their current policies in view of the socio-economic constraints of poor nations. From human development perspective, institutional policies of multilateral organisations have resulted in increased deprivation of the poor, rising unemployment and unsustainable development practices.

In view of the adverse impacts that globalisation has had on human development, the civil society and UN agencies have sought to mitigate them through independent activities and/or partnerships with government institutions and machinery to improve service delivery and community development. Such movements have been able to cushion the adverse impacts that globalisation and the existing institutions of global governance have had on the poor and the marginalised.

Globalisation is wiping away national borders and weakening national policies. For the weak and the vulnerable countries and people, there is need for a stronger role for national governing institutions for providing goods, services and protection that are not available in the marketplace. There is also a need for compassionate institutions of global governance that would truly help developing countries to create a better future for billions of people living in the developing world. The rising criticism against the IMF and the World Bank has recently prompted these institutions to review their policies as well as to institute a consultative process with academics, NGOs and other civil society groups to review their policies and programmes. These are important steps forward. But if these consultations were to go beyond window-dressing, these institutions need to rethink and reform their own governance structures. We turn to this subject in the next chapter.

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Towards Humane Globalisation

What is crucial for poor nations is an equitable access to global market opportunities, not charity…What we must insist today is a comprehensive package from rich nations for imposing immigration controls since free labour flows were supposed to be an essential component of a liberal economic system which would equalise global opportunities.

– Mahbub ul Haq

Chapter 7

Towards Humane Globalisation

Positive effects of globalisation on economic growth as well as human development depend on how the globalisation process is managed nationally and internationally

Globalisation has become an increasingly dominant feature over the past decades as more countries are getting integrated into the global economy through trade and capital flows, and information and communication technologies. It is an inevitable process in the efforts of each nation to accelerate economic growth and modernise their societies. Although there are debates about the benefits that poor nations can reap from globalisation, there is no doubt that if some countries choose to opt out, the potential costs of becoming marginalised from the global economy in terms of lost efficiency, technology and growth could be huge. But the positive effects of globalisation on economic growth as well as human development depend on how the globalisation process is managed nationally and internationally. Through sensitive management of the globalisation process, poor developing countries can leapfrog several decades of development without putting heavy burden of costs on the poorer section of their population.

We recognise that the social impact of globalisation is more directly linked to national policies and strategies. Although the policies of global institutions have a major influence on national policy-making, the extent of their influence depends on the commitment and capacity of governments at all levels, from national to local, to manage their economic and social development policies and programmes in a socially-responsible way. It is true that the South Asian governments need to improve their governance systems in order to enhance their productivity, efficiency and competitiveness. It is also true that the stabilisation and structural reform programmes of the IMF and World Bank, though necessary, can sometimes become a hand-maiden of policies that negate the promises of globalisation to increase economic development and reduce poverty.

The 1999 Report on *Human Development in South Asia* underscored the importance of improving governance in South Asia. Many of the negative impacts of globalisation on growth and human development are due to governance failures at national as well as global levels. In this chapter we explore how the globalisation process can be humanised at both national and international levels to promote growth with human development.

National imperatives

Through the UNDP Human Development reports, Mahbub ul Haq kept on reminding us that growth *per se* does not lead to human development. Growth is important but the nature of growth, its character and distribution are just as important. A link between growth and human lives has to be created consciously through deliberate public policy, such as public spending on social services and fiscal policy to redistribute income and assets. This link may not exist in the automatic workings of the markets. This is particularly true in the context of South Asia as this region is the home of the highest number of poor and illiterate people and malnourished children, with huge deprivations in all other indicators of social development.

The globalisation process erodes the sovereignty of nation states, particularly their role in economic decision-making. But in developing countries, the role of government in economic and social development is vital. In South Asia, however, the governments continue to play a dominant role in economic and social sectors, with poor outcomes. Yet an exclusive focus on the market may leave the poor out in the cold. The challenge is to balance the goals of economic growth with those of human development. What will it take for South Asia to develop policies that increase its benefits from globalisation while improving the lives of the vast majority of the people. South Asia needs to make sustained efforts in four broad policy areas. These are: (a) accelerating human development, particularly education; (b) reducing poverty; (c) enhancing integration with the regional and global economic system and; (d) improving economic management.

Accelerate human development

Education and skill training is the most important component of this. Knowledge and technology rules the global market. Without underestimating India's recent success as being one of the high-technology centres of the world, South Asia's education indicators, even at the primary and secondary levels, lag behind most developing regions. South Asia as a region produces very few people with technical skills to produce goods and services of higher quality and productivity to compete with the global market. The limited number of IT-trained people that South Asia produces each year is lost to the region because of their demand in developed countries. The region needs to improve both the quantity and quality of education at each level, from primary, secondary to tertiary. This is critical for developing relevant skills for adapting to a changing world market demand.

Of course the first essential step is universal primary education. This is the foundation on which the secondary and tertiary education and skill training can be built. But as we have seen in chapter 3, during 1995-99, 46 per cent of children in South Asia did not complete primary education. Of the secondary school-age children, less than half—44 per cent—enrolled for secondary education in 1996. In 1998, the combined enrolments at all three levels were only 51 per cent; and only 22 per cent of tertiary enrolment was for natural and applied sciences. While the competition in the global marketplace demands higher levels of education and skill training, the quantity and quality of education in South Asia have a long way to go, despite islands of highly-skilled people and institutions.

South Asia must prepare its labour force to face the global competition. Central to this is the strategy to provide quality primary education to all school-age children, provide them skill-training, and also cater to the needs of the higher levels of education in new technologies. While the governments should allocate sufficient resources for primary and secondary education, private sector should be mobilised to set up technical institutions for imparting training for the new market demand.

South Asia must prepare its labour force to face the global competition

Public funding of education has to be increased on primary and secondary education, while leaving the technical and higher levels of education to the private sector, with liberal scholarships for the financially-needy students. But the education budget, both as a percentage of GDP and of the total central and state/provincial government budgets, has to be increased in order to provide better access to and improve the quality of education.

Reduce poverty

In the wake of globalisation, poverty in South Asia is either rising or stagnating. This underscores the urgency of mainstreaming the governments' commitment to reduce poverty. For macro-economic policy, this means much more than just promoting economic growth. Poverty reduction strategies must be built into the macro and micro policies. Globalisation policies to focus on cash crops instead of food crops, and capital-intensive rather than labour-intensive industries need to be analysed

Governments must prioritise the needs of the poor to overcome mass human deprivation

to assess their impact on the poor, the rural areas, food security and employment generation.

Recent evidence suggests that India's decade-old economic reforms have increased economic growth but have not made much progress in reducing poverty. The economy grew at over 7.5 per cent a year in the mid-1990s, but the proportion of people living in poverty dropped by one percentage point from 1993-94 to 1997. In rural areas where most Indians live the poverty reduction was even less. The rate of poverty reduction in pre-reform era was faster. Despite the fact that there is some confusion about the two sets of data used to calculate poverty, consumption of the poor has declined due to higher food prices as a result of economic reforms. Food prices have played an important role in determining the absolute poverty in India , along with the availability of productive employment opportunities. Non-agricultural employment generation has been lower over the 1990s than it was in the previous decade. In Pakistan, all evidence points towards low growth in the 1990s, accompanied by rising levels of poverty in both urban and rural areas.

Governments must prioritise the needs of the poor to overcome mass human deprivation. The backlog of such deprivation is huge, as we present in this report (see table 9 on page 171). A realistic human development agenda should be designed and implemented by each country. The minimal aim of South Asian governments should be to protect those who get bypassed by the markets and crushed by the reform programmes. This requires social safety nets that are not only efficient in their reach but also adequate in their coverage.

While the state should look after the welfare of the poor, the real focus should be on empowering people. But the poor may not benefit from the market if they have no access to productive assets, such as land and credit. In South Asia such assets are highly skewed. An effective land reform policy is the best answer to such a situation. The impact of land reforms in reducing poverty is decisive, one-tenth of the reduction of poverty in India between the period 1958-92 has been attributed to the implementation of land reforms. Another practical way of empowering the poor is through the provision of micro-credit. Many micro-credit programmes are being implemented in South Asia by the public sector and the NGOs.

Enhance integration

Continued export growth is essential to benefit from globalisation. This requires diversifying into goods and services for which demand is sufficiently elastic, namely those with higher technological content. But from the point of view of employment generation, South Asia needs to continue in more traditional labour-intensive, low technology exports, as well as diversify into more high-technology goods and services. India's success in establishing a niche for itself in the fast-growing global software and information technology market demonstrates that such diversification can be achieved, but requires increasing investments in human capital to develop appropriate factor endowments.

A source of huge potential benefit for sustaining trade integration in the region lies with increasing the share of official intra-regional trade. As pointed out in chapter 5, the level of such trade is very low, and the potential gains from greater intra-regional trade are large, not only in terms of economic gains, but also in terms of deepening regional economic and political cooperation. In this respect, more attention needs to be focussed in fostering regional trade links, particularly in India, which, despite much progress in liberalisation, remains relatively protected, with a low level of import penetration from other countries in the region.

A key to sustain and increase capital flows to the region, is to maintain a favourable macroeconomic environment. Sound economic fundamentals, such as low inflation, stable exchange rates and low fiscal deficits, are crucial for attracting foreign investors and increasing access to private capital markets. A major challenge will be to increase South Asia's share of such flows. As shown in chapter 2, South Asia's share of the developing-country total has stagnated during the 1990s.

Policies to sustain economic growth and increase export orientation will be necessary, as well as making national investment regimes more open and transparent. Careful attention needs to be focussed on the exact nature of FDI inflows. Those directed to the manufacturing and export sectors are likely to bring the most benefits than those based on mergers and acquisitions stemming from privatisation programmes.

To sustain economic integration, simply increasing the level of trade and capital flows to the region, however, is not enough. Reduction of the risks inherent in greater economic openness is also fundamental to any such efforts. The existing composition of exports in most countries of South Asia is highly concentrated in terms of products as well as geographic regions. Thus, diversifying export products and markets are essential steps to reduce the vulnerability of export earnings.

Short-term volatility of capital inflows can seriously destabilise the economy and society. Greater attention, therefore, needs to be paid to the composition and maturity of capital flows, with the aim of decreasing the region's reliance on short-term debt and portfolio investment flows. Minimising such risks also requires strengthening prudential regulations and effective bank supervision to avoid irresponsible exposure to excessive external borrowing. In most countries, such safeguards remain weak.

Improve economic management

The globalisation process in South Asia has been initiated and facilitated by a series of economic reform programmes undertaken under the umbrella of the IMF and World Bank. Although these reforms have made South Asia a more open and less distortionary region, the record of reform has not been an unqualified success. Several governance and institutional failures have diluted the efficiency of the reform programme.

First, economic reforms remain incomplete and their implementation remains slow and hesitant. Governments continue to play a dominant role in major economic activities. Also, external liberalisation has not been accompanied by internal or regional liberalisation. While trade with the outside world is getting freer, trade within the region is still very limited. Domestic financial sector reforms are incomplete. Public sector banks are still burdened with a large stock of non-performing loans. Deficit reduction is slow. There has been a relatively higher emphasis on reducing development expenditure and subsidies meant for the poor than on mobilising additional resources by taxing the rich and cutting non-development expenditure. Sometimes progress made by the central governments is negated by a lack of performance at the state/provincial and lower levels.

Reduction of the risks inherent in greater economic openness is also fundamental

Secondly, the institutions needed to assist the economic transition are either missing or remain weak. Market regulations to protect the poor and the vulnerable are either weak or non-operative. There have been limited legal reforms to aid the economic transition. The judicial system is also weak in protecting private property rights and enforcing business contracts.

Thirdly, in many parts of South Asia the burden of structural adjustment has fallen mostly on the poor. Whenever government tries to balance the budget, social expenditures are the first victims, and within social expenditures primary education, primary healthcare and food subsidies to the poor are the worst hit.

Fourthly, economic reforms have only touched the price structures, not the structures of economic and political power. Markets may discriminate against the poor, if productive assets like land and capital are badly distributed, and if a powerful rentier class has access to all economic opportunities. If economic adjustment has to be meaningful, it must be accompanied by social adjustment. Countries must spend as much time on correcting social fundamentals as on correcting economic fundamentals (MHHDC 1999). The globalisation process itself does not consider these issues, hence the backlash by civil society groups at the meetings of the global economic managers.

Current global economic management is failing to eliminate large fluctuations in economic activities, prevent huge surpluses and deficits from arising, and stop speculative capital movements

Global imperatives[1]

Can globalisation be better managed internationally? This is an issue that deserves the kind of intellectual ferment that Keynes generated about global governance in the 1940s when the globalisation process was not as pervasive and strong a phenomenon in the global economy as it is today. Despite excellent work done by several scholars including Hans Singer, Mahbub ul Haq, Nobel Laureate James Tobin and many others, powerful nations are giving very little thought to the necessity of reforming the existing institutions of global governance or creating new ones.

As discussed in chapter 6, during the last fifty years while globalisation has become stronger, the role played by the institutions of global governance is increasingly becoming marginal. The current global economic management is failing to eliminate large fluctuations in economic activities, prevent huge surpluses and deficits from arising, and stop speculative capital movements. At the Bretton Woods conference in 1944, Keynes had intended for the institutions to perform these functions. But the institutions, the IMF and World Bank, that were created at Bretton Woods, do not almost in any way fulfil their intended role. As private capital flows dominate the development finance, the IMF and World Bank have been marginalised. Yet they exercise overwhelming influence on the macro and micro economic policies of developing countries.

At present, several forums perform the role of global economic governance in one form or another, often with overlapping mandates:

- Group of 8, composed of the most powerful nations, set the tone for the global financial and monetary policy in their annual summits. But the issues that the G-8 normally considers fall within a narrow range of macroeconomic management. The issues of pressing concern to developing countries fall, in general, outside the purview of G-8 although in recent summits of G-8, poverty and debt of the least developed countries have attracted some attention. But meaningful actions on these fronts are yet to be taken on a scale that would make a difference to the people in these countries.
- Development and Interim Committees of the World Bank and IMF represent both industrialised and developing countries. But these forums do not enjoy the power and the clout of G-8, and their agendas are more narrowly focused on issues of concern to the World Bank and IMF.
- The Economic and Social Council of the UN (ECOSOC) deliberates on many of the socio-economic issues that are at the top of the global agenda. But the forum has neither the financial resources nor the technical capacity to be taken seriously by the global financial managers.

To humanise globalisation, it is important to consider ways to either reform the existing institutions of global governance, or to create new ones. We believe the world community is ready now, in view of massive demonstrations at the meetings of G-8, IMF, World Bank and WTO, to think seriously about creating two new institutions—(a) a World Central Bank, (b) an Economic Security Council, and (c) an innovative

[1] Arguments in this section have been drawn from Mahbub ul Haq's writings see e.g., M. Haq 1995, M. Haq *et al*. 1995 and 1996.

mechanism to control the volatility of short-term financial flows.

(a) The world has no credible lender of last resort at the global level which can bail out countries from short-term liquidity crisis, without inflicting long-term economic damage. Central banks perform this role at the national level. There is a need today for a World Central Bank to maintain steady growth of world output, prevent emergence of massive imbalances, recycle funds from surplus countries to deficit countries and avoid large exchange rate fluctuations. These functions have to be performed without making the poor countries sacrifice either growth or human development.

(b) Globalisation has also led to a series of serious threats to human security ranging from new diseases, drugs, crime, environmental degradation, unemployment to rising poverty. While global political issues are discussed at the UN Security Council, there is no global forum to discuss the economic and social issues, although ECOSOC and various UN agencies deal with these issues in a fragmented manner. The proposal to establish an Economic Security Council offers an opportunity to design a new framework for addressing global economic and social issues to serve the interests of all nations. The imperatives of global human security can only be addressed by such a council. Many global issues need global strategies and global actions. Global macroeconomic coordination, particularly monetary and financial, cannot be left to G-8 as it does not represent the voices of the poor nations and poor people. In 1945, the US Secretary of State said in the report to the US President on the establishment of the United Nations, '*No provisions that can be written into the Charter will enable the Security Council to make the world secure from war if men and women have no security in their homes and their jobs.*' (as quoted in M. Haq 1995).

An Economic Security Council can fill the following gaps: first, it can provide leadership in tackling the shared global concerns such as poverty and environmental insecurity; second, it could help establish an early warning system and the modalities for global assistance in conflicts within nations; third, it could provide policy leadership on macroeconomic management.

(c) Finally, in view of excessive volatility of short-term capital, Prof. James Tobin's proposal to levy a small tax on speculative currency transactions deserves special attention of the international community. The aim of Tobin Tax is to slow down speculative, short-term capital flows. This has the potential to increase the autonomy of national authorities for monetary and macroeconomic policies, with a bit more independence from the effects of international money markets. This will be particularly valuable to developing countries since their economies adapt less easily to external shocks and their thinner financial markets are more vulnerable to the impact of external capital inflows and outflows. National tax authorities could collect the tax, and proceeds could be shared between the national and global institutions of governance for promoting human development and reducing poverty.

The world has no credible lender of last resort at the global level which can bail out countries from short-term liquidity crisis

Role of civil society and private sector

Civil society, comprised of the media, trade unions, professional associations such as lawyers, doctors, teachers associations, and NGOs, can serve a watchdog function by monitoring activities and development policies on human development and poverty alleviation of national and international institutions of governance. While NGOs in South Asia have been able to target and access groups better than government or international actors, their record of cost effective service delivery has been mixed. In order for the NGOs to be effective in counterbalancing negative impacts of globalisation, cost effectiveness of their operations is important. It is, however, critical that active government and civil society cooperation

Civil society movements present perhaps the best method of guarding against disproportionate burdens being placed on the poor

take place in South Asia in all spheres of activity, from rural support to policy research to covering multilateral negotiations and WTO meetings.

At the global level, civil society forces have been active in organising demonstrations at the meetings of multilateral institutions. Their voices have been drowning the official deliberations at each meeting. However, it remains to be seen how beneficial these meetings are going to be for the poor people in poor nations.

The acute problems facing labour worldwide, as a result of globalisation, have been brought up by trade unions and other labour organisations at the international level. The spread of technology has allowed networks to develop across borders. These networks lobby for labour rights and have actively opposed the negative effects of globalisation. Similarly, media organisations and journalists across the world have an invaluable role to play to promote humane globalisation.

The problem, however, is in creating a critical mass of support and awareness amongst the larger public for the issues that affect them at local, national, regional and global levels. There is a need to link struggles for social justice together. In India, Bangladesh and Sri Lanka, people's movements have developed that draw on all these civil society actors to resist aggressive actions from private and state-level actors. In a globalising world, such civil society movements present perhaps the best method of guarding against disproportionate burdens being placed on the poor. However, it is important for civil society to strengthen itself sufficiently and also to look beyond national borders. In much the same way that South Asian states need to work together to mitigate the impacts of new trade regimes, civil society in South Asia must work together on issues of common concern.

The business community is acknowledged as one of the chief players in providing jobs and generating income. While the private sector needs adequate incentives to expand and fuel economic growth, its market power and political influence necessitates regulations and guidelines in order to promote humane globalisation. In this regard, two following initiatives will be useful:

- A new framework for government-business cooperation to increase incentives for private sector innovation, transparency and accountability. A healthy expansion of South Asia's private sector requires greater trust and cooperation between the government and the business community. Policies that would address the concerns of both private sector and the people could only be achieved through mutual consultation. Such a process would lead to consensus-building and greater public-private partnerships in implementing policies.
- Guidelines for corporate social responsibility. Corporate social responsibility extends beyond organisational operations and encompasses the community where a business operates, as well as the region which it serves. Voluntary guidelines for corporate social responsibility, prepared collectively or individually by businesses, could encourage the private sector to take civic action on issues ranging from business ethics and environmental responsibility to social development. For their part, governments could offer incentives to those corporations that invest a certain percentage of their profits in social responsibility programmes (MHHDC 1999).

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We started this report by raising some issues that needed to be addressed in the context of globalisation and human development. At the end of our analysis, we conclude that

- Participation and benefits of globalisation have so far been limited to a small segment of educated and skilled population and private-sector entrepreneurs.

- South Asian countries and their people do not have full access to the opportunities of trade as non-tariff barriers and agricultural subsidies in the developed countries stand in the way of optimising benefits from trade. Also, labour is not fully mobile, except the highly-trained professional class.
- New technologies have expanded the choices of professionals, researchers and students to improve their knowledge and job opportunities. New technologies have also tended to reduce gender disparities by enhancing women's education, training and job opportunities in IT-enabled sector.
- Economic expansion, associated with globalisation, is creating jobs in narrow fields—in high technology such as information/communication, and in low technology such as garment factories. All other areas of economic activity, like traditional manufacturing, agricultural and non-farm activities, are not experiencing any increase of jobs. Globalisation-led growth has, in most cases, not been job-led growth.
- Markets have been free in the negative way, in raising prices of goods and services, hurting the poor without providing any opportunity for them to earn more income. Also, imports are rising without the simultaneous increase of exports, consumption patterns are changing from traditional food and beverages to fast foods and drinks.

The proponents of globalisation would argue that if China can gain so much from globalisation, why can't South Asia, especially the smaller countries. China had the social fundamentals in place before it started opening to the world economy. More importantly, we are not arguing against globalisation, we only want to underline its pitfalls, as the East Asian experience has pointed out (see box 7.1), and to ensure the sustainability of globalisation by enhancing and protecting human development in South Asia.

South Asian countries are at a crossroad, well placed to accelerate globalisation and growth, but lagging behind most other developing regions. The unexploited potential for greater integration and growth in South Asia is large, and the future may well bring faster growth from globalisation. The degree to which it will be able to take full advantage depends on the commitment of South Asian countries to reduce regional hostilities and continue integrating, while paying closer attention to minimising the associated risks.

Box 7.1 Globalisation: Lessons South Asia could learn from the East Asian crisis

There are several lessons for South Asia from the recent East Asian crisis:

- Trade liberalisation is good for an economy. However, financial liberalisation should only be undertaken cautiously and after proper sequencing.
- If 'hot flows' of capital are to be allowed, they should be monitored carefully and managed properly. As demonstrated by the Tequila and East Asian experiences, rapidly expanding short-term debt financed by 'hot flows' can harm domestic economies.
- The exchange rate system followed, whether fixed or flexible, should reflect the economic fundamentals of the country.
- Transparency, absence of politicisation and prudential regulation must exist in the financial sector.
- Proper data reporting is a must—if only to accurately assess the financial state of an economy.
- Industrialisation should be diversified, decentralised and rural oriented, not urban concentrated.
- An active and free domestic media is a necessity. A more realistic picture of an economy can only be of benefit to all parties—whether domestic or foreign. If the media highlights deficiencies in a national economy, it should be viewed not as a threat, but as an opportunity to correct mistakes and weaknesses.

Source: MHHDC 1999.

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Chapter 4 draws on the following: Abdelati, Nagaoka, Sidgwick, Lonnberg and Zveglich 2000; Acharya, Thapa and Sharma 1998; ADB 1997; ADB 1998; Adhikari; Ali and Tahir 1999; Amjad and Kemal 1997; Arif 2001; EIU 1999; EIU 2000; ESCAP 1999a; ESCAP 2001; Ghosh 1998; GOB 1996; GOB 1998; GOP 1977; GOP 1988; GOP 1994; GOP 1999c; GOS 2001; Gupta 1999; HMG Nepal 2000; Hasan 1998; Husain 1999; IMF 1999a; IMF 2001a; Irfan and Amjad 1983; Irfan 2001; Khan 2000; Mahendra 2000; Malik 1988; Mujeri 2001; Qureshi and Arif 1999; Rijal 2000; Sarvekshana; Shand 1999; World Bank 1985; World Bank 1988; World Bank 1989; World Bank 1996; World Bank 1998; World Bank 1998a; World Bank 1999d; World Bank 2000; and World Bank 2001;

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Chapter 7 draws on the following: Haq, M. 1995a; Haq, M., Streeten, Jolly and Haq, K. 1995b; Haq, Kaul and Grunberg 1996; and MHHDC 1999.

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Contents

Note on Statistical Sources for Globalisation Tables

The special globalisation data for this report have been collected from various international sources. Principle international sources include the UN system and the World Bank. For instance, data on trade, foreign direct investment, GNP and debt have mostly been collected from the World Bank. Indicators for environment and information flows were compiled mainly from the UNDP and International Telecommunication Union's reports respectively.

Since regional international comparability is limited for data obtained from national sources, serious effort has been made to use international data wherever available. Even though data in international sources is not as current as the one available in national sources, preference was given to the former due to the nature of the data required. There is however, a scarcity of international and national data for both Bhutan and the Maldives.

Extra care has been taken to ensure that the information provided in the tables is both reliable and consistent.

Certain data have been specifically compiled for the purpose of this report such as the data on trade flows, resource flows and information flows. It should be noted that weighted average for South Asia has been computed using country population figures as weights. It is hoped that such a compilation of data for South Asia would be useful for policy-makers, researchers, and students interested in globalisation issues.

Often, the latest reliable data remain unavailable for several important globalisation indicators such as the loss or gain resulting from reduction in tariffs, subsidies and customs duties, labour remittances and labour movements. There is an urgent need for up-to-date and accurate data on globalisation in order to analyse globalisation issues as objectively as possible.

1. Trade Flows

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)
Total trade								
Trade/GDP ratio (PPP adjusted level, %) 1990-98	3.6	9.1	5.6	6.6	15.7	21.5	34.9	4.7
– annual average change (%) 1990-98	1.4	-1.3	4.8	3.9	5.5	-0.6	0.8	1.3
Exports of goods and services 1999								
Total (US$ millions)	54047	8838	6031	1150	5566	120	...	42952.3
– as a % of GDP	12	15	13	23	35	31	...	13
Imports of goods and services 1999								
Total (US$ millions)	67250	11688	8527	1496	6717	160	...	53614
– as a % of GDP	15	20	19	30	43	42	...	16.6
Mean unweighted tariff rates (%) 1999								
– all products	32.2	46.5[a]	22	17.7	20.1[b]	…	…	32
– primary products	30.5	42.7[c]	22.4	12.9	23.9[d]	…	…	30
– manufactured goods	32.4	46.9[e]	22	18.9	19.7[f]	…	…	32
Export structure								
Food exports (% of total exports)								
– 1990	3	17	19	15	19	23	…	6.6
– 1999	9	17	15	12	15	…	…	10.5
Agricultural raw materials (% of total exports)								
– 1990	4	4	5	7	2	8	…	4.1
– 1999	3	6	5	7	1	…	…	3.5
Manufactures (% of total exports)								
– 1990	51	54	56	67	65	40	…	52.3
– 1999	54	53	69	42	77	…	…	55.4

Notes:
a, c & e: year 1998; b, d & f: year 1997.

Source: Row 1: World Bank 2000c; Rows 2, 3, 4 & 5: World Bank 2001.

2. Resource Flows

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)
Net foreign direct investment flows (US$ millions)								
– 1990	162	244	0	6	43	…	1	128.4
– 1999	2169	530	225	4	177	…	7	1738.7
Net portfolio investment flows (US$ millions)								
– 1990	252	0	0	0	0	0	0	198.6
– 1998	4462	0	3	0	71	0	0	3421
Net bank and trade related lending (US$ millions)								
– 1990	14538	-63	67	-14	10	…	-3	11463
– 1999	-532	-521	15	-13	-74	-2	7[a]	-460
Net official development assistance (ODA) or official aid (US$ millions) 1999	1484	732	1203	344	251	56[b]	25[c]	1338
– aid per capita 1999	1	5	9	15	13	…	…	2.6
– aid as a % of GNP 1999	0.3	1.2	2.5	6.7	1.6	…	…	0.7
External debt 1999								
– US$ millions	94393	34423	17534	2970	9472	120	180[d]	77665
– present value of debt as % of GNP	16	43	23	32	45	32.1[e]	58.1[f]	20.1
Total debt service 1999								
– percentage of GNP	16	43	23	32	45	…	…	20.1
– percentage of exports of goods and services	104	252	140	122	104	…	…	122.9

Notes:
a, b, c, d, e & f: year 1998

Source: Row 1&6: World Bank 2001; Rows 2: UNDP 1999, UNDP 2000; Rows 3, 4 & 5: World Bank 2001, UNDP 2000.

3. Information Flows

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)
Main telephone lines (per 1,000 people) 1999	27	22	3	11	36	9[a]	57[b]	24
Fax machines (per 1,000 people) 1999	0.2	2	…	0.4	…	1.7[c]	14.3[d]	0.4
Personal computers (per 1,000 people) 1999	3.3	4.3	1	2.7	5.6	4[e]	…	3.2
Internet hosts (per 10,000 people) 2000	0.32	0.4	0	0.35	0.91	…	…	0.31
Internet users (thousands) 1999	2800	80	50	35	65	…	…	2157
Mobile telephones (per 1,000 people) 1999	2	2	1	0	12	…	…	2
Public payphones (per 100,000 people) 1996-98*	0.4	0.2	…	…	0.2	…	…	0.3
Televisons (per 1,000 people) 1999	75	119	7	7	102	…	40[f]	72
Cable subscribers (per 1,000 people) 1999	37.1	0.1	…	2.9	0	…	…	28.4
Daily newspapers (per 1,000 people) 1996	30	21	9	11	29	…	10	27
International tourism departures (thousands) 1997-98	3811	…	992	110	518	…	37	3029.9
Patent applications filed 1998								
– Residents	2111	16	32	…	81	…	…	1623.8
– Non-residents	7997	782	184	…	34974	…	…	6735.2

Notes:
* data refer to the most recent year available during the specified period
a & b: year 1997; c: year 1996; d: year 1995; e: year 1996-98; f: year 1997.

Source: Rows 1, 2, 3, 5, 6, 8, 9: ITU 2000, UNDP 2000, UNDP 1999 & MHHDC 1999; Rows 4 &12: World Bank 2001; Rows 7 & 11: UNDP 2000; Row 10: MHHDC 1999.

4. Selected Economic Indicators

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)
GNP per capita (US$) 1999	440	470	370	220	820	510	1200	438
GNP per capita (PPP$) 1999	2230	1860	1530	1280	3230	1260	…	2118.3
GNP per capita average annual growth rate (%) 1997-98	4.3	0.5	4.2	0.3	3.3	2.4	4.4	3.8
Tax revenue (% of GDP) 1999	9.1	13.1	…	8.5	14.9	…	…	8.7
Average annual rate of inflation (%)								
– 1990-98	8.9	11.1	3.6	8.9	9.7	9.7	8.2	8.6
– 1998	8.9	7.8	5.3	3.3	8.8	5.9	0.8	8.3
Agriculture (as a % of GDP)								
– 1993	31	25	30	43	25	42	…	30.4
– 1998	29.3	26.4	22.2	40.5	21.1	38.2	16	28.4
Industry (as a % of GDP)								
– 1993	27	25	18	21	26	27	…	25.8
– 1998	24.7	24.7	27.9	22.2	27.5	36.5	…	25
Services (as a % of GDP)								
– 1993	41	50	52	36	50	31	…	43
– 1998	45.9	48.9	49.9	37.3	51.4	25.4	…	46.5
Percentage labour force employed 1997								
– agriculture	60.1	45.5	60.1	93.8	46.3	94	20.2	59
– industry	18.1	21.5	21.8	0	22.9	0.5	32.7	18.5
– services	21.8	33	18.1	6.4	30.8	5.5	48.1	22.4

Source: Rows 1, 2, 3 & 4: World Bank 2000 & 2001; Rows 5: UNDP 2000; Rows 6, 7 & 8: UNDP 1996 & UNDP 2000; Row 9: ILO 1998.

5. Environment and Globalisation

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)
Average annual rate of deforestation (%)[a]								
– 1980-90	-1.1	3.1	1.8	0.9	1	0.6	…	-0.4
– 1990-2000	-0.1	1.1	-1.3	1.8	1.6	0.3	…	-0.06
Carbon dioxide emissions 1997								
– total (millions of metric tonnes)	1065.4	98.2	24.6	2.2	8.1	0.3	0.3	829.7
– share of world total (%)	4.2	0.4	0.1	…	…	…	…	3.3
– per capita (metric tonnes)	1.1	0.8	0.2	0.1	0.4	0.2	1.1	0.95
Annual fresh water withdrawals 1987-97 *								
– as a % of water resources	39.7	183.6	13.9	14.6	19.5	0	11.2	55.3
– per capita (cubic metres)	588	1269	134	1397	573	13	17	678.2
Annual internal renewable water resources (cubic metres per capita) 2000[b]	1244	542	813	8282	2656	44728	105	1345.6
Printing and writing paper consumed (kilograms per capita) 1997	2.2	1.4	1.1	0.1	2.8	0	3.8	1.9

Notes:

* data refer to the most recent year available during the specified period
a:a positive number indicates a loss of forest area, a negative number a gain
b:these annual averages disguise large seasonal, interannual and long-term variations

Source: Row 1: World Bank 2001 & UNDP 2000; Row 2: World Bank 2001; Rows 3, 4 & 5: UNDP 2000.

Human Development Indicators for South Asia

Contents

Note on Statistical Sources for Human Development Indicators

The human development data presented in these annex tables have been collected with considerable effort from various international and national sources. For the most part, standardised international sources have been used, particularly the UN system and the World Bank data bank. The UNDP and World Bank offices made their resources available to us for this report.

Countries in the indicator tables are arranged in descending order according to population size. While most data have been taken from international sources, national sources have been used where international data have been sparse. Such data have to be used with some caution as their international comparability is still to be tested.

Several limitations remain regarding coverage, consistency, and comparability of data across time and countries. The data series presented here will be refined over time, as more accurate and comparable data become available. In particular, policy-makers are invited to note the following deficiencies in the currently available statistical series and to invest sufficient resources to remedy these shortfalls:

(a) Generally the latest data are not available for several indicators. Some statistical indicators date back ten years or more. Analysis of the current economic and social situation is greatly handicapped in the absence of up-to-date data.

(b) Time series are often missing for even the most basic data as population growth, adult literacy, or enrolment ratios. An effort must be made to build consistent time series for some of the important indicators.

(c) In certain critical areas, reliable data are extremely scarce: for instance, for employment, income distribution, public expenditure on social services, military debt, foreign assistance for human priority areas, etc.

(d) Information regarding the activities of NGOs in social sectors remains fairly sparse.

It is time for policy-makers to make a significant investment in the collection and analysis of up-to-date, reliable, and consistent indicators for social and human development. If development is to be targeted at the people, a great deal of effort must be invested in determining the true condition of these people.

It is hoped that the various gaps visible in this annex will persuade national and international agencies to invest more resources and energy in investigating human development profiles.

1. Basic Human Development Indicators

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Total estimated population (millions) 2000	1014	138	129	24	19	2.1	0.3	1326	4867
Annual population growth rate (%) 1995-2000	1.7	2.6	1.6	2.7	1.1	3.1	3.7	1.8	1.8
Life expectancy at birth(years) 1999	63	65	59	58	74	62	65	62.9	63
Adult literacy rate (%) 1999	56.5	45	40.8	40.4	91.4	42	96.2	53.9	72.9
Female literacy rate (%) 1999	44.5	30	29.3	22.8	88.6	30[b]	96.2	42	65[c]
Combined 1st, 2nd and 3rd level gross enrolment ratio (%) 1999	56	40	37	60	70	33	77	52.6	61
Infant mortality rate (per 1000 live births) 1999	70	84	58	75	17	80	60	69.6	63
GNP per capita (US$) 1999	440	470	370	220	820	510	1200	437.9	1240
GNP average annual growth rate (%) 1998-99	6.9	3.6	5	4.6	3.8	5.5[d]	7.1[e]	6.3	2.9
GNP per capita average annual growth rate(%) 1998-99	4.9	1.2	3.3	2.2	2.7	2.4[f]	4.4[g]	4.3	-0.5
Real GDP per capita (PPP$) 1999	2248	1834	1483	1237	3279	1341	4423	1997.4	3530
Human development index (HDI) 1999[j]	0.571	0.498	0.47	0.48	0.735	0.477	0.739	0.554	0.647
Gender-related development index (GDI) 1999[k]	0.553	0.466	0.459	0.461	0.732	0.444[h]	0.735	0.535	0.634[i]

Notes:

a: Population figures for 2000 are taken from UN: World Population Prospects: The 1998 Revision. (Medium variant). Population figures for Pakistan have been calculated using 1998 Population Census, GOP. The population growth rate has been calculated by using the formula {[(new value/old value)^1/n]-1}*100

b, c, h, i : year 1998

d, e, f, g : year 1997-98

j: The Human Development Index (HDI) has three components: life expectancy at birth; educational attainment, comprising adult literacy, with two-thirds weight, and a combined primary, secondary and tertiary enrolment ratio, with one-third weight; and income. Any significant difference in the HDI for the South Asian countries is due to the change in methodology for calculating the index. Please refer to UNDP's Human Development Report 2000.

k: The Gender-related Development Index (GDI) adjusts the HDI for gender equality in life expectancy, educational attainment and income.

Source: Rows 1, 2: UN 1999, GOP 1998; Rows 3, 7: UNICEF 2001; Rows 4, 5, 6, 11, 12, 13: UNDP 2001, UNDP 2000; Row 8: World Bank 2001; Rows: 9, 10: World Bank 2000c & World Bank 2001.

2. Trends in Human Development

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
GNP per capita									
– 1973	130	130	80	90	230	…	…	126	880[a]
– 1999	440	470	370	220	820	510	1200	437.9	1240
Real GDP per capita (PPP, US$)									
– 1960	617	820	621	584	1389	…	…	648	790
– 1999	2248	1834	1483	1237	3279	1341	4423	2123.3	3530
Human development index (HDI)									
– 1960	0.206	0.183	0.166	0.128	0.475	…	…	0.204	…
– 1999	0.571	0.498	0.47	0.48	0.735	0.477	0.739	0.554	0.647
Life expectancy at birth									
– 1960	44	43	40	38	62	37	44	44	46
– 1999	63	65	59	58	74	62	65	62.9	63
Gross enrolment ratio for all levels (% age 6-23)									
– 1980	40	19	30	28	58	7	…	37	46
– 1999	56	40	37	60	70	33	77	52.6	61
Adult literacy rate(%)									
– 1970	34	21	24	13	77	…	91	32	43
– 1999	56.5	45	40.8	40.4	91.4	42	96.2	53.9	72.9
Infant mortality rate (per 1000 live births)									
– 1960	144	139	151	212	90	175	158	144	137
– 1999	70	84	58	75	17	80	60	69.6	63
Fertility rate									
– 1960	6	7	6.7	6	5.4	6	7	6.1	6
– 1999	3	4.8	3	4.3	2.1	5.3	5.2	3.2	2.9
Underweight children (% under 5)									
– 1975	71	47	84	63	58	…	…	69	40
– 1995-2000	53	26	56	47	34	38	43	49	29
Daily calorie supply (as % of requirement)									
– 1986	100	97	83	93	110	…	80	98	107
– 1997[b]	118	110	96	109	101	…	82	114	117

Notes:
a: year 1979, b:1995 has been used as base year for required calorie supply

Source: Row 1: World Bank 2001, World Bank 1995b; Rows 2, 3, 5, 6, 9: UNDP 2001, UNDP 2000, UNDP 1994; Row 4: UNICEF 2001, UN 1996; Rows 7, 8: UNICEF 2001, UNICEF 1998; Row 10: UNDP 2000, UNDP 1990.

3. Education Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Adult literacy rate (%)									
– 1970	34	21	24	13	77	…	91[a]	32	43
– 1999	56.5	45	40.8	40.4	91.4	42	96.2	53.9	72.9
Male literacy rate (%)									
– 1970	47	40	47	22	86	…	…	47	55
– 1999	67.8	58.9	51.7	58	94.3	58[b]	96.3	65	80.3[c]
Female literacy rate (%)									
– 1970	19	5	9	3	68	…	…	17	32
– 1999	44.5	30	29.3	22.8	88.6	30[d]	96.2	42	64.5[e]
Primary enrolment (%) gross									
– 1970	73	40	54	26	99	…	…	68	76
– 1997	100	74[f]	92[g]	113	109	73[h]	131	97	107
Secondary enrolment (%) gross									
– 1970	26	13	…	10	47	2	…	25	…
– 1997	49	26[i]	19[j]	42	75	5[k]	49[l]	44	59
Combined enrolment for all levels (%)									
– 1980	40	19	30	28	58	7	…	37	46
– 1999	56	40	37	60	70	33	77	52.6	61
Pupil-teacher ratio (primary level) 1997-99*	48.29	48.43	59.31	38	30	41.4	23.43	49	33[m]
Percentage of children dropping out before grade 5 (1995-99)	48	50	30	56	3	14	2	45.8	27
Tertiary natural and applied science enrolment (as % of total tertiary) 1995-97	25	…	25	14	29	…	…	22.3	…
R&D scientists and technicians (per 1000 people) 1990-96	0.3	0.1	…	…	0.2	…	…	0.3	0.4
Public expenditure on education (as % of GNP)									
– 1960	2.3	1.1	0.6	0.4	3.8	…	…	2	2.5
– 1995-97	3.2	2.7	2.2	3.2	3.4	4.1	6.4	3.2	3.8
Children not in primary schools (in millions) 1997	27	7	4.5	0.596	0	0.22	0.001	39	…

Notes:
a:year 1985; b, c, d, e: year 1998; f: year 1996; g, i, m: year 1995; h, j, k, l: year 1993; * latest available year

Source: Rows 1, 6, 11: UNDP 2001, UNDP 2000, UNDP 1999 & UNDP 1994; Rows 2, 3: UNDP 2001, UNDP 1999, UNICEF 1997; Rows 4, 5: World Bank 2001, World Bank 1998, World Bank 1997b; Row 7: MHHDC 1999; Row 8: UNICEF 2001; Row 9: UNDP 2001, UNDP 2000; Row 10: UNDP 1999; Row 12: MHHDC 2000.

4. Education Indicators in India by State, Rural/Urban, and Gender

	Adult literacy rate (%) 1997	Female literacy rate (%) 1997	Male literacy rate (%) 1997	Primary net enrolment ratio (%) 1997	Female primary net enrolment ratio (%) 1997	Male primary net enrolment ratio (%) 1997	Primary gross enrolment ratio (%) 1997	Female primary gross enrolment ratio (%) 1997	Male primary gross enrolment ratio (%) 1997
All India	57.7	43.9	70.5	60.3	48.8	71	90.3	81.5	98.5
Rural areas	49.4	34	64	60.7	47.7	72.8	90.8	79.6	101.1
Urban areas	80.4	72.1	87.7	59	52	65.5	89	86.8	91
Andhra Pradesh	46.6	35	58	52.3	46.4	57.9	89.6	86.8	92.3
Arunachal Pradesh	52.9	39.9	64	69.7	52.2	89.6	97.2	82.1	114.5
Assam	72.1	60	83	85.4	74.9	95.4	109.1	104.3	113.8
Bihar	44.3	27	60	50.2	28.2	70.1	76	59.5	90.9
Goa	83.6	74.9	92	68	59.4	78.1	86.1	76.8	97.1
Gujarat	63.4	49	77	90.3	80.8	97.6	117.6	114.5	119.9
Haryana	57.1	41	71	56.9	56	57.6	83.9	84.9	83.1
Himachal Pradesh	73.7	63	84	74.1	66.4	83	90.1	82.7	98.6
Jammu & Kashmir	50.6	35	65	35.9	23.7	49.4	67.2	53.4	82.7
Karnataka	53.2	43	63	89	77.3	100.4	113.2	120.7	105.5
Kerala	91.4	88	95	69.6	67.4	71.7	90.1	88.8	91.3
Madhya Pradesh	49.6	32	66	79.2	60.5	96.8	102.4	89.4	114.5
Maharashtra	68.9	56	81	80.1	75.1	84.9	112.9	110	115.7
Manipur	71.4	57.9	84.1	77.1	64.1	92.3	85.9	74.1	99.7
Meghalaya	68.2	64	72.1	52.7	49.4	56.5	93.4	86.1	101.9
Mizoram	94.9	93.9	95.8	88.2	77.6	99.1	113.6	104.6	123
Nagaland	82.5	71.9	91.9	44.4	39.9	49.7	94.3	86.3	103.6
Orissa	47.2	32	62	67.2	49	84.9	90.5	76.1	104.5
Punjab	60.4	53	67	59.3	59.3	59.3	81.6	83.1	80.4
Rajasthan	48.9	27	69	56.4	31.8	78.5	97	81	111.3
Sikkim	76.2	66.2	85	64.3	58.2	70.7	113.3	110	116.7
Tamil Nadu	65.6	54	77	84.8	82.1	87.3	108.6	107.3	109.8
Tripura	71.2	65	77	81.4	65.2	99.9	88.4	75.3	103.4
Uttar Pradesh	49.1	32	64	30.8	18.4	41.8	62.3	49	74.1
West Bengal	69.6	58	80	46.4	40.2	52.3	92.2	85.6	98.6
A & N Islands	96.6	93	100	71.9	61.4	84.4	86.9	76.2	99.6
Chandigarh (UT)	80.2	67.8	89.9	52.1	47.7	56.6	79.5	73.2	85.9
D & N Haveli	47.7	30.2	64.3	71	49.3	92.7	73.2	111	96.2
Daman & Diu	81.5	67.5	95.1	79.6	70	90.5	99.1	88.8	99.1
Delhi	81.8	72	90	68.4	63.9	73.2	89.1	81.6	97.2
Lakshadweep (UT)	95.1	90	100	91.7	82.3	101.1	104.5	96.3	112.8
Pondicherry (UT)	86.9	81.8	92	84.9	72.8	99.1	93.5	83	105.8

Notes:
— UT is Union Territory. — A person is literate if he or she can read and write with understanding in any language. — Official primary school age is 5/6 years to 9/10 years in India.

Source: GOI 1999b.

5. Education Indicators in Pakistan by Province, Rural/Urban, and Gender

	Adult literacy rate (%) 1998	Female literacy rate (%) 1998	Male literacy rate (%) 1998	Primary net enrolment ratio (%) 1998	Female primary net enrolment ratio (%) 1998	Male primary net enrolment ratio (%) 1998	Primary gross enrolment ratio (%) 1998	Female primary gross enrolment ratio (%) 1998	Male primary gross enrolment ratio (%) 1998
All Pakistan	45	32.6	56.5	49.2	40.2	57.6	81.3	66.6	95
Rural areas	34.4	20.8	47.4	…	…	…	…	…	…
Urban areas	64.7	55.6	72.6	…	…	…	…	…	…
NWFP	37.3	21.1	52.8	56.1	39.2	71.7	66.5	50	81.7
Punjab	47.4	35.3	58.7	50.4	45.7	54.8	54.4	47.9	60.5
Sindh	46.7	35.4	56.6	42.3	30.7	52.9	47.5	34.5	59.3
Balochistan	26.6	15	36.5	41.6	31.3	50.1	52.8	40.8	62.7
Islamabad	69	58.2	77.9	89.2	85.2	93.1	100.4	95.5	105.2

Note:
— Official primary school age is 5-9 years.

Source: GOP 1999a.

6. Education Indicators in Bangladesh by District, Rural/Urban, and Gender

	Adult literacy rate (%) 1998	Female literacy rate (%) 1998	Male literacy rate (%) 1998	Primary net enrolment ratio (%) 1998	Female primary net enrolment ratio (%) 1998	Male primary net enrolment ratio (%) 1998	Primary gross enrolment ratio (%) 1998	Female primary gross enrolment ratio (%) 1998	Male primary gross enrolment ratio (%) 1998
All Bangladesh	55.9	48.1	63.1	81.4	82.9	80.0	96.5	94.5	98.4
Rural areas	51.7	44.9	58.3	81.1	82.7	79.6	86.5	94.5	98.4
Urban areas	75.5	64.0	84.3	82.9	84.0	81.8	96.5	94.5	98.4
Dhaka	58.8	49.2	67.6	79.9	81.8	78.1	97.2	95.6	98.7
Rajshahi	47.3	36.8	56.9	80.2	82.7	77.7	96.5	93.5	99.4
Khulna	55.1	46.2	63.4	85.8	88.6	83.1	100.0	98.2	101.8
Chittagong	57.9	53.4	62.0	81.4	80.9	81.9	95.3	92.2	98.3
Sylhet	49.6	45.6	53.2	78.6	79.8	77.6	94.8	95.1	94.5
Barisal	75.2	74.9	75.5	88.4	89.1	87.7	93.7	95.4	92.1

Notes:
— Definition of literacy used is reading, writing and simple numeracy skills.
— Official primary school age is 6-10 years.

Source: GOB 1999c.

7. Education Indicators in Nepal by Region, Rural/Urban, and Gender

	Adult literacy rate (%) 1997	Female literacy rate (%) 1997	Male literacy rate (%) 1997	Primary net enrolment ratio (%) 1997	Female primary net enrolment ratio (%) 1997	Male primary net enrolment ratio (%) 1997	Primary gross enrolment ratio (%) 1997	Female primary gross enrolment ratio (%) 1997	Male primary gross enrolment ratio (%) 1997
All Nepal	44.8	27.7	62.5	69.6	59.9	78.9	122.1	103.7	139.6
Eastern Region	44.6	26.9	62.7	70.7	62.9	78.3	120.3	106.5	133.8
Central	39.1	21.5	56.2	68.8	56.9	79.9	116.9	94.5	138
Western	55.7	39.7	74.7	76.8	72.9	80.5	141.9	135.5	147.9
Mid-Western	33.9	14.4	53.1	66.3	51.9	81.1	115.1	88.9	140.7
Far Western	35.1	14.9	56.8	57.9	45.3	70.2	111.8	81.6	141.1
Mountain	38.	19.7	55.6	79	64.9	92.8	141.6	108.9	173.6
Hill	49.1	30.7	69.7	81.2	73.8	88.4	148.7	133.1	164.1
Terai	36.6	20.6	51.8	57.4	45.3	69	94.2	73.6	113.7

Notes:
— The definition of literacy used is self-nomination (by sampling).
— Official primary school age is 6-10 years.

Source: HMG Nepal 1999a.

8. Health Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Population with access to health services (%) 1995	85	55	45	…	93	65	75	78	80
Population with access to safe water (%)									
– 1990-96	81	60	84	44	46	58	96	82	71
– 2000	88	88	97	81	83	…	…	88.5	79
Population with access to sanitation (%)									
– 1990-96	16	30	35	6	52	70	66	22	29
– 2000	31	61	53	27	83	…	…	36.9	52
Population per doctor									
– 1984	2520	2910	6730	32710	5520	23310	20300	3720	4590
– 1992-95	2083	1923	5555	20000	4348	5000	5263	2273	1282
Population per nurse									
– 1980	4674	5870	14750	7783	1262	2990[a]	600[b]	4162	…
– 1993	3323	3330	11549	2257	1745	6667	…	4091	4715
Daily calorie supply per capita 1997	2496	2476	2085	2366	2302	…	2485	2379	2663
Maternal mortality rate (per 100,000 live births) 1990-99	410	340[c]	440	540[d]	60	1600[e]	202[f]	405	…
Women using contraception (% age 15 - 49)									
– 1970	12	4	22	1	8	…	…	12	18
– 1990-99	41	17	49	30	66	19	17	39	…
Public expenditure on health (as % of GDP)									
– 1960	0.5	0.3	…	0.2	2	…	2.4	0.5	0.9
– 1990-98	0.6	0.9	1.6	1.3	1.4	4	5.3	0.8	1.9
Pregnant women aged 15-49 with anaemia (%) 1975-91	88	37	53	65	39	30	…	84	…

Notes:
a, b: year 1984
c, d: year 1990-98; e: year 1993; f: year 1995.

Source: Row 1: UNDP 1998; Rows 2, 3: World Bank 2001, UNDP 1998; Row 4: UNDP 2001, UNDP 1992; Row 5: MHHDC 1999; Row 6: UNDP 2000; Row 7: World Bank 2000c, World Bank 2001, MHHDC 1999; Row 8: UNDP 2000, MHHDC 1998; Row 9: World Bank 2000c; Row 10: UNDP 1999, UNDP 2000.

9. Human Deprivation Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Population below poverty line (%)									
– $1 a day (1993 PPP U$) 1989-1998	44.2	31	29.1	37.7	6.6	…	…	40.7	…
– national poverty line 1984-1999	35	34	35.6	42	25[a]	…	…	32	…
Population without access to health services 1995									
– number (millions)	143	63	68	…	1.3[b]	0.6	0.1[c]	276T	910T
– as a % of total population	15	45	55	…	7[d]	35	25[c]	22	20
Population without access to safe water 2000									
– number (millions)	121.7	16.6	3.9	4.6	3.2	0.8[f]	0.01[g]		1067T
– as a % of total population	12	12	3	19	17	42[b]	4[i]	11	21
Population without access to sanitation 2000									
– number (millions)	699.7	53.8	60.6	17.5	3.2	0.6[j]	0.09[k]	835T	2439T
– as a % of total population	69	39	47	73	17	30[l]	34[m]	63	48
Illiterate adults 1999									
– number (millions)	432	74	75	14	1.7	1.12	0.01	598T	1372T
– as a % of total adult population	43.5	5.5	59.2	59.6	8.6	56[n]	3.8	46	27[p]
Illiterate female adults 1999									
– number (millions)	266	45	43	8.7	1.1	0.7	0.01	365T	881T
– as a % of total adult female population	55.5	70	70.7	77.2	11.6	70[q]	3.8	58	35[r]
Malnourished children under 5 1990-98*									
– number (millions)	59	9	8	2	0.54	0.1	0.002	79T	167T
– as a % of total population	53	38	56	47	34	38	43	51.1	31
Under-five mortality rate (per 1000 live births) 1999	98	112	89	104	19	107	83	97.6	90
Daily calorie supply 1997									
– quantity	2496	2476	2085	2366	2302	…	2485	2447.2	2663
– as a % of total requirements	118	110	96	109	101	…	82	114	117
People with disabilities 1992									
– number (millions)	1.8	6.5	0.9	0.6	0.07	…	…	9.92T	110T
– as a % of total population	0.2	4.9	0.8	3	0.4	…	…	0.9	2.6

Notes:
a: year 1987-97, b, d: year 1985-95, c, e: year 1991; f, g, h, i, j, k, l & m: year 1990-96; n, p, q, r: year 1998;* latest available year

Source: Row 1: UNDP 2001, UNDP 2000; Row 2: MHHDC 1998; Rows 3, 4: World Bank 2000c, World Bank 2001; Rows 7, 9: UNDP 2000, Row 8: UNDP 2001; Rows 5, 6, 10: UNDP 2001, UNDP 2000, UNDP 1999, UNICEF 2001.

10. Gender Disparities Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Female population (2000)									
– number (millions)	491	66	63	12	9.5	1.05	0.14	642.7	2395
– as a % of male	93.9	91.7	95.5	100	102.2	98.1	93.3	94.1	96.9
Adult female literacy (as % of male)									
– 1970	41	35	35	12	80	…	…	40	…
– 1999	66	51	57	39	94	52[a]	100[b]	63	81[c]
Female primary school gross enrolment (as % of male)									
– 1970	64	37	48	20	92	6	107	60	79
– 1995-99*	82.8	69.6	96.9	74.2	98.2	75.6	97.6	83	89.8
Female 1st, 2nd and 3rd level gross enrolment ratio (as % of male) 1997	75	50	75	71	103	71	101	74	87
Female life expectancy (as % of male)									
– 1970	97	99	97	97	103	104	95	97	103
– 1999	102	103	100	98	107	103	96	102	105
Real GDP per capita (PPP$) (female as % of male) 1999	37	29.9	57.6	52.8	50.9	50.8[d]	59	39	50[e]
Earned income share (female as % of male) 1995	34	26	30	50	55	48	55	33	48
Economic activity rate (age 15+) (female as % of male)									
– 1970	43	11	6	52	37	52	35	37	53
– 1999	50	40.5	76.2	67	55	65	79	52	66.1[f]
Administration and managers (% female) 1992-97	2.3	4.3	4.9	…	17.6	…	14	3	10
Share of females in parliament (%) 1999	8.7	2.6	12.4	7.9	4.9	2	6.3	7.3	10
Gender Development Index (GDI) 1999	0.553	0.466	0.459	0.461	0.732	0.44[g]	0.735	0.535	0.634[h]
Gender Empowerment Measure (GEM) 1997	0.24	0.176	0.304	…	0.321	…	0.342	0.236	…

Notes:
* latest available year.
a: year 1997; b, c, d, e, f, g, h: year 1998

Source: Row 1: UN 1999; Row 2: UNESCO 1994, UNDP 2000; Row 3: UNICEF 2001, World Bank 1997b; Rows 4, 6, 11 & 12: UNDP 1999, UNDP 2000, UNDP 2001; Row 5: UNICEF 2001; UN 1994; Row 7: UNDP 1998; Row 8: UNDP 2001, MHHDC 1999; Row 9: UNDP 1999, UNDP 1998; Row 10: IPU 1999, GOP 1999b, GOI 1999a, GOB 1999a, GOS 1999, HMG Nepal 1999b.

11. Child Survival and Development Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Population under 18 (1999)									
– number (millions)	398	68[a]	56	11	6.2	1.01	0.14	427.3	1857.5
– as a % of total population	40.4	51.9	44.1	47	32.6	49	48.3	42	38
Population under 5 (1999)									
– number (millions)	115	19	15	3.4	1.6	0.34	0.04	154.4	538
– as a % of total population	11.8	14.5	12	14.8	8.5	16.5	14.3	12.1	11
Infant mortality rate (per 1000 live births)									
– 1960	144	139	151	199	83	175	180	144	138
– 1999	70	84	58	75	17	80	60	69.6	63
Under 5 mortality rate (per 1000 live births)									
– 1960	236	226	247	297	133	300	300	235	216
– 1999	98	112	89	104	19	107	83	97.6	90
One year olds fully immunised against tuberculosis (%)									
– 1980	14	9	1	43	63	9	8	13	…
– 1995-98	79	66	91	86	90	94	99	79.2	81
One year olds fully immunised against measles (%)									
– 1980	1	3	2	2	0	18	30	1	…
– 1997-99	55	54	66	73	95	77	97	57	70
Births attended by trained health personnel (%) 1995-2000	34	19	13	9	94	15	90	30.9	52
Low birth weight infants (%) 1990-97	33	25	50	…	25	…	13	33	18
Child economic activity rate (% age 10-14) 1999	13	16	29	43	2	55[b]	6[c]	15	16
Child labour (millions) 1994	100	19	15	…	…	…	…	134	…

Notes:
a: includes age groups 0-19; b and c: year 1995

Source: Rows 1, 2: UNICEF 2001, GOP 1998; Rows 3, 4, 5, 6, 7: UNICEF 2001, UNICEF 1984; Row 8: UNDP 1999, UNDP 2000; Row 9: World Bank 2000b, MHHDC 1998; Row 10: UNICEF 1995.

12. Profile of Military Spending

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Defence expenditure (US$ millions, 1993 prices)									
– 1985	7207	2088	308	22	214	…	…	9839T	189727
– 1998	10600	2810	450	40	730	…	…	14630T	164700
Defence expenditure annual % increase (1985-98)	3	2.3	3	4.7	9.9	…	…	3.1	-1.1
Defence expenditure (as a % of GNP)									
– 1985	2.5	5.1	1.3	0.7	2.6	…	…	3	7.2
– 1998	2.5	4.6	1	0.8	4.8	…	…	2.6	2.9
Defence expenditure (as a % of central government expenditure)									
– 1980	19.8	30.6	9.4	6.7	1.7	…	…	21.3	…
– 1998	17.1	20.7	…	0.7	18.6	…	…	15.5	…
Defence expenditure per capita (US$, 1993 prices)									
– 1985	9.4	22	3.1	1.3	14	…	…	9.9	52
– 1998	10.8	21.5	3.6	1.7	39.2	…	…	11.4	33
Defence expenditure (as a % of education & health expenditure)									
– 1960	68	393	…	67	17	…	…	113	143
– 1995	57	181	46	22	100	…	…	71	…
Armed forces personnel (no. in thousands)									
– 1985	1260	484	91	25	22	…	…	1882	16027
– 1998	1175	587	121	46	113	…	…	2042	14200
– % increase (1985-97)	-7.2	17.5	24.8	45.7	80.5	…	…	7.8	-12.9
Number of soldiers									
– per 1000 population (1998)	1.18	4.5	0.98	2	6.1	…	…	1.9	2.8
– per 1000 doctors (1990)	4000	9000	6000	35000	25000	…	…	5594	18500
Employment in arms 1998 production (000's)	250	50	…	…	…	…	…	300	3810
Military holdings[a] 1998 index (1985=100)	178	151	193	40	889	…	…	170	106
Aggregate number of heavy weapons 1998	10510	5310	390	10	240	…	…	16460	210200

Notes:
a: military holdings include combat aircrafts, artillery, ships & tanks that a country possesses. The index is a calculation based on the aggregate number of heavy weapons.

Source: Rows 1, 2, 7, 10: BICC 2000, BICC 1997; Row 3: BICC 2000, BICC 1997, UNDP 2000; Row 4: BICC 2000; BICC 1997; UNDP 1999, World Bank 1995a; Row 5: BICC 2000, UN 1999, GOP 1998; Row 6: MHHDC 1999; Row 8: BICC 2000, UN 1999, GOP 1998; Rows 9, 11: BICC 2000.

13. Profile of Wealth and Poverty

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Total GDP (US$ billions) 1999	447.3	58.2	46	5	16	0.4	0.4	573T	5,827T
Real GDP per capita (PPP$) 1999	2248	1834	1483	1237	3279	1341	4423	2123.3	3530
GNP per capital (US$) 1999	440	470	370	220	820	510	1200	438	1240
Income share: ratio of highest 20% to lowest 20% (1987-98*)	5.7	4.3	4.9	5.9	5.4	…	…	5.5	…
Population below poverty line (%)									
– $1 a day (1993 PPP US$) 1989-1998	44.2	31	29.1	37.7	6.6	…	…	41	…
– national poverty line 1984-1999	35	34	35.6	42	25[a]	…	…	321	…
People in poverty (%) 1990									
– urban	38	20	56	19	15	…	…	37	…
– rural	49	31	51	43	36	…	…	47	…
Social security benefits expenditure (as % of GDP) 1993	0.3	0.2	…	…	2.5	…	…	0.4	…
Public expenditure on education and health (as % of GNP) 1995	4.2	3.6	3.7	4.3	4.5	…	13.3	4.1	…
Gross domestic investment (as % of GDP) 1999	23	15	22	20	27	47.3[b]	…	22	23
Gross domestic savings (as % of GDP) 1999	20	10	17	13	20	37.9	…	18.6	25
Industry (as % of GDP) 1998	24.7	25	27.9	22	27.5	36.5	…	25	34.1
Tax revenue (as % of GDP) 1998	8.6	12.6	8.4[c]	9	14.5	7.8	21	9	…
Exports (as % of GDP) 1999	12	15	13	23	35	31	…	13	28
Debt service ratio (debt service as % of exports of goods and services) 1999	15	30.5	10.1	7.9	7.9	4.8	3.9	16	22.3
Total net official development assistance received (US$, millions) 1999									
– quantity	1484.4	732	1203.1	343.7	251.4	66.6	30.7	4112T	33026T
– as % of GDP	0.3	1.3	2.6	6.9	1.6	15.1	…	0.8	0.6
Total external debt 1999 (US$, billions)	94	34	18	2.6	8.5	…	…	157T	2572T

Notes:
* data refer to most recent year available
a: year 1987-1997
b: year 1998
c: year 1997

Source: Rows 1, 2, 4, 5, 14 & 15: UNDP 2001; Row 11: UNDP 2000; Row 3: World Bank 1999a; Rows 9, 10, 13: World Bank 2001, UNDP 2000; Row 6: UNDP 1996; Row 7: MHHDC 1999; Row 8: WHO 1999; UNDP 1999, World Bank 1997b; Row 12: UNDP 1999, GOB 1999b; Row 16: World Bank 2001.

14. Demographic Profile

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Population (in million)									
– 1960	442	50	51	9	10	1	0.1	563T	2,070T
– 2000	1014	138	129	24	19	2.1	0.3	1,326T	4,867T
Population growth rate (annual) (%)									
– 1960-70	2.3	2.8	2.6	2	2.4	1.8	2	2.4	2.5
– 1970-80	2.2	2.6	2.8	2.6	1.7	2	2.7	2.3	2.2
– 1980-90	2.1	3.6	2.1	2.6	1.6	2.2	3.2	2.3	2.1
– 1990-95	1.9	2.7	2	2	1.1	3.7	2.6	1.9	1.8
– 1995-00	1.7	2.6	1.6	2.7	1.1	3.1	3.7	1.8	1.6
Population doubling date (at current growth rate) 1995	2036	2022	2039	2021	2058	2018	2014	2034	2039
Crude birth rate (per 1000 live births)									
– 1960	43	49	47	44	36	42	41	44	42
– 1999	25	35	28	34	18	37	35	26.4	25
– % decline (1960-99)	42	28.6	40	23	50	11.9	15	40.9	40
Crude death rate (per 1000 live births)									
– 1960	21	23	22	26	9	26	21	21	20
– 1999	9	7	9	10	6	9	7	8.8	9
– % decline (1960-99)	57	69.5	59	61.5	33	65.3	67	57	55
Total fertility rate									
– 1960	6	7	6.7	6	5.4	6	7	6.1	6
– 1999	3	4.8	3	4.3	2.1	5.3	5.2	3.2	2.9
– % decline (1960-99)	50	31.4	55.2	28.3	61.1	11.6	25.7	47.5	51.6
Total labour force 1999 (in millions)	441	50	67	11	8	…	…	577T	2,460T
Male labour force 1998 (in millions)	293	35	37	6	5	…	…	376T	1447T
Female labour force 1998 (in millions)	138	14	27	5	3	…	…	187T	969T
Percentage annual growth in labour force									
– 1980-99	2	2.8	2.6	2.3	2.2	…	…	2.1	2
– 1999-2010	1.9	3.2	2.3	2.5	1.7	…	…	2.1	1.6
Unemployed/Underemployed labour (as a % of total) 1993	22	13	12	43	16	6	1	21	…
Employed labour force (%) 1997									
– agriculture	60.1	45.5	60.1	93.8	46.3	94	20.2	59.1	…
– industry	18.1	21.5	21.8	0	22.9	0.5	32.7	18.5	…
– services	21.8	33	18.1	6.4	30.8	5.5	48.1	22.4	…
Real earnings per employee annual growth rate (%) 1980-92	2.5	…	-0.7	…	1.4	…	…	2.2	…

Source: Rows 1, 2: UN 1999, UN 1994; Row 3: UN 1999; Rows 4, 5, 6: UNICEF 2001, UNICEF 1997; Rows 7, 10: World Bank 2001; Rows 8, 9: World Bank 2000; Row 12: ILO 1998; Rows 11, 13: MHHDC 1998.

15. Profile of Food Security and Natural Resources

	India	Pakistan	Bangladesh	Nepal	Sri Lanka	Bhutan	Maldives	South Asia (weighted average)	Developing Countries
Food production per capita 1998 (1989-91=100)	120	142	112	118	114	107	115	121.4	132[a]
Food imports per capita 193 (1980=100)	46	114	86	137	553	…	…	68	…
Cereal imports per capita (1,000 tons) 1994 (1980=100)	2	195	33	79	87	…	…	68	70
Food aid in cereals per capita (1,000 tons) 1994-95 (1980=100)	46	23	91	33	126	…	…	57	63
Food aid (US$ million) 1992	99	190	240	6	63	3	1	602T	3,130T
Land area (1000 ha) 1997	297319	77088	13017	14300	6463	4700	30	412,917T	7,494,675T
Percentage of land area under 1997									
– forest and woodland[b]	22	2	8	35	28	59	3	19	26
– cropland	57	28	63	21	29	3	10	54	11
Irrigated land (as % of cropland) 1997	34	81	45	38	32	25	…	40	20
Deforestation (1000 ha per year) 1980-89	1500	9	8	84	58	1	…	1106	866
Annual rate of deforestation (%) 1990-95	0	2.9	0.9	1.1	1.1	0.3	…	1	…
Reforestation (1000 ha per year) 1980-89	138	7	17	4	13	1	…	103	797
Production of fuel wood and charcoal (1000m^3 per year)									
– 1980	201956	16683	22941	13732	7305	1027	…	263,644T	1,253,900T
– 1996	279350	276470	32020	20718	9780	1381	…	370,889T	1,669,840T
Internal renewable water resources per capital (1000m^3 per year) 1998	1896	1678	10940	7338	2341	49557	…	2937	6055
Annual fresh water withdrawals[c]									
– as % of water resources	21[d]	63	2	2	15[e]	0	…	…	63
– per capita (m^3)	612[f]	1269	217	154	503[g]	13	…	538	496

Note:
a: year 1997
b: Data refers to the year 1995; c: Data refer to any year between 1987-96 unless otherwise stated.
d & f: year 1975; e & g: year 1970

Source: Rows 1, 13: UNDP 1999, UNDP 2000; Rows 2, 3, 4,: World Bank 1997b; Rows 5: World Bank 1995a; Rows 6, 8: FAO 1998; Row 7: FAO 1998, UN 1997. Rows 9, 11: UN 1990/91; Rows 10, 14: WRI 1998/99; Row 12: FAO 1996.

Selected definitions

Aggregate net long term resource flows are the total resource flows with original maturity of loans greater than one year.

Aggregate net short term resource flows are the total resource flows of original maturity of loans of less than one year.

Balance of payment account is a double entry record of all real and financial transactions between one country and the rest of the world. It shows all flows of goods and services into and out of an economy and all transfers of real resources or financial claims provided to or by the rest of the world without a *quid pro quo.*

Current account balance is the sum of net exports of goods and services, income, and current transfers.

Gross fixed capital formation refers to total outlays on additions to the fixed assets of a country including net changes in the level of inventories.

Institutional Investor Credit Rating measures the chances of a country's default. The ranking ranges from 0 to 100. The higher the rating, the lesser the chances of default for that country.

Portfolio equity flows refer to purchases of shares by foreign investors on domestic stock markets.

Net financial flows include net inflows of investment, net portfolio equity flows, net portfolio debt flows and bank and trade-related lending.

Merchandise exports show the f.o.b (free on board) value, in US dollars, of goods provided to the rest of the world.

Merchandise imports show the c.i.f (cost plus insurance and freight) value in US dollars of goods purchased from the rest of the world.

Real per GDP capita is the gross domestic product (GDP) per capita of a country converted into US dollars by the Atlas Method as used by the World Bank. GDP measured at purchasing power parity (PPP) is GDP converted into US dollars by the PPP exchange rate.

Real effective exchange rate is the exchange rate of a country in terms of the exchange rate of other countries with trading volumes used as weights and with an adjustment made for inflation.

Trade balance refers to the excess of merchandise trade exports over merchandise imports.

Trade to GDP ratio is the trade balance as a percentage of the gross domestic product.

KEY TO INDICATORS

Indicator	Indicator tables	Original source
A, B, C		
Agriculture (as a % of GDP	4g	UNDP
as % of total exports	1g	WB
Armed forces personnel	12	BICC
Bank and trade related		
lending	2g	WB; UNDP
Bangladesh education		
indicators	6	GOB
Births attended by trained		
health personnel	11	UNICEF
Cable connections per 1000		
people	3g	ITU
Calorie supply (daily)	2,8,9	UNDP
as % of total requirement	2	UNDP
per capita	8	UNDP
Cereal imports per capita	15	WB
Child economic activity rate	11	UNDP; WB
Child labour, total	11	UNESCO
Co2 emissions, total	5g	WB
share of world total	5g	WB
per capita	5g	WB
Computers, personal, per		
1000 people	3g	ITU; UNDP
Crude birth rate	14	UNICEF
Crude death rate	14	UNICEF
D		
Daily newspapers	3g	MHHDC
Debt, total external	13,2g	WB
(PV as % of GNP)	2g	WB
Debt servicing		
% of GNP	2g	WB
% of exports of goods		
and services	2g	WB
debt service ratio	13	UNDP
Defence expenditure, total	12	BICC
annual % increase	12	BICC
as % of GNP	12	BICC; UNDP
as % of govt. exp.	12	BICC; UNDP
per capita	12	BICC; UN; GOP
as % of education &		
health expenditure	12	MHHDC
Deforestation, total	15	UN
% annual rate	15,5g	WRI; WB; UNDP
Drop out rate of children		
(before grade 5)	3	UNICEF
E		
Earned income share	10	UNDP
Economic activity rate	10	UNDP; MHHDC
Employment in arms		
production	12	BICC
Enrolment, primary level	3	WB
female	3	UNDP; UNICEF
Enrolment, secondary level	3	WB
2nd & 3rd level	1,3	UNDP
Enrolment ratios, gross	2	UNDP
Exports, total	1g	WB
% of GDP	1g	WB

Indicator	Indicator tables	Original source
F, G		
Fax machines per 1000		
people	3g	ITU; UNDP
FDI flows	2g	WB
Female administrators &		
managers	10	UNDP
Fertility rate, total	14	UNICEF
Food aid, total	15	WB
cereals per capita	15	WB
Food exports, % of total		
exports	1g	WB
Food imports per		
capita	15	WB
Food production per capita	15	UNDP
Fresh water withdrawals		
as % of water resources	5g	UNDP
per capita	5g	UNDP
Water resources, internal		
renewable	5g	UNDP
Fuel wood & charcoal		
production, total	15	FAO
Gender Empowerment		
Measure	10	UNDP
Gender-related Development		
Index	1,10	UNDP
GDP, total	13	WB
GDP, real per capita	1,2,13	UNDP
GNP, growth rate	1	WB
GNP per capita	1,2,13,4g	WB
GNP per capita growth rate	1,4g	WB
Gross domestic investment	13	WB; UNDP
Gross domestic savings	13	WB; UNDP
H, I, J		
Health expenditure, public		
(as % of GDP)	8	WB
Health services, % with		
access	8	UNDP
% without access	9	UNDP
Human Development Index	1,2	UNDP
Illiterate adults, total	9	UNDP
female	9	UNDP
Immunisation against		
measles	11	UNICEF
tuberculosis	11	UNICEF
Imports, total	1g	WB
% of GDP	1g	WB
Income poverty, 1 $ a day	9,13	UNDP
national poverty line	9,13	UNDP
Income share: ratio of top		
20% to bottom 20%	13	WB
India education indicators	4	GOI
Industry (as % of GDP)	13,4g	UNDP
Infant mortality rate	1,2	UNICEF
Inflation, growth rate	4g	UNDP
Internet hosts per 10,000		
people	3g	WB
users	3g	ITU

Indicator	Indicator tables	Original source
K, L		
Labour force, total	14	WB
female	14	WB
male	14	WB
% annual growth	14	WB
% unemployed/underemployed	14	MHHDC
% employed	14	WB
% employed, agriculture	4g	ILO
% employed, industry	4g	ILO
% employed, services	4g	ILO
Land area	15	FAO
irrigated land	15	FAO
Life expectancy at birth		
total	1,2	UNICEF
female	10	UNICEF
Literacy rate, total	1,2,3	UNDP
female	1,10	UNDP
male	3	UNDP
M, N, O		
Malnourished children under five	9	UNDP
Manufactures, % of total exports	1g	WB
Maternal mortality rate	8	WB
Mean tariff rates		
all products	1g	WB
primary products	1g	WB
manufactured goods	1g	WB
Military holdings index	12	BICC
Mobile phone subscribers per 1000 people	3g	ITU
Nepal education indicators	7	HMGN
Number of soldiers	12	BICC; UNDP
ODA received, total	13,2g	UNDP; WB
as % of GNP	13	UNDP

Indicator	Indicator tables	Original source
P, Q, R		
Pakistan education indicators	5	GOP
Paper, printing and writing consumed	5g	UNDP
Patent applications filed		
resident	3g	WB
non-resident	3g	WB
Portfolio investment flows	2g	UNDP
Public payphones per 100,000 people	3g	UNDP
Pupil-teacher ratio	3	MHHDC
S		
Safe water, % with access	8	UNDP; WB
% without access	9	WB
Sanitation, % with access	8	UNDP; WB
% without access	9	WB
Services (% of GDP)	4g	UNDP
T, U, V		
Telephone mainlines, per 1000 people	3g	ITU; MHHDC; UNDP
Televisions, per 1000 people	3g	ITU
Tertiary, natural & applied sciences enrolment	3	UNDP
Tourism, international departures	3g	UNDP
Underweight children (under 5)	2	UNDP
W, X, Y, Z		
Water withdrawals, fresh	15	WRI
Water resources, per capita	15	UNDP

Note: 'g' is added to table numbers that appear in Profile of Globalisation in South Asia.

Key to source abbreviations

BICC	Bonn International Centre for Conversion
FAO	Food and Agriculture Organization
GOB	Government of Bangladesh
GOI	Government of India
GOP	Government of Pakistan
GOS	Government of Sri Lanka
HMGN	His Majesty's Government of Nepal
ILO	International Labour Office
IPU	Inter-Parliamentary Union
ITU	International Telecommunication Union
MHHDC	Mahbub ul Haq Human Development Centre
UN	United Nations
UNDP	United Nations Development Programme
UNESCO	United Nations Educational Scientific and Cultural Organization
UNICEF	United Nations Children's Fund
WB	World Bank
WHO	World Health Organization
WRI	World Resources Institute