

Editors' Introduction

The Lahore School's Third Annual Conference on the Management of the Pakistan Economy, in May 2007, reflected on the economic reforms that have been implemented since the 1990s and on the prospects for additional reforms in both the near and long-term. A number of respected economists and other experts provided evaluations of the government's past efforts, and offered advice on the direction that future reform efforts should take. The Conference focused on a few key areas which included Governance Reforms, Industrial Competitiveness, Monetary, Fiscal and Financial Sector Policies, Exchange Rate and Trade Policies, and Female Labor Force Participation. The key findings of the papers were as follows:

Governance Reforms: Ishrat Husain presented a view of long-term governmental reform in Pakistan to take place over a period of 10 to 20 years. The need for such reform is great, given the demands of the "globalized world" that all economies, including Pakistan, increasingly face. He drew lessons from other developing countries that have been successful in their modernization efforts. He also reviewed recent developments in Pakistan that highlighted the need for change, including: i) the lack of equitable distribution of the benefits of economic growth and dysfunction in the delivery of public services, ii) the implications of public enterprise privatization for government ministries, iii) the devolution of powers and public finances to the provinces and districts, iv) the shift in the responsibilities of federal ministries toward policy making and monitoring and evaluation, v) the burgeoning of public-private and public-NGO partnerships, vi) uncertainty about the future of the civil service, and vii) developments in e-government. Mr. Husain discussed the broad principles that should underpin reforms in the civil service, the structures of federal, provincial and district government, and business process re-engineering. He concluded with suggestions regarding the timing and sequencing of reforms that would be most conducive to long-term change.

Industrial Competitiveness: A.R. Kemal began by pointing out that Pakistan is currently internationally competitive in only a few products, demonstrating the need for dramatic improvements. He continued by examining in detail Pakistan's performance in the various dimensions of the Global Competitiveness Index, in addition to a brief analysis of total factor productivity measures. Dr. Kemal concluded with suggestions on how Pakistan can increase its productivity and therefore competitiveness, in particular by attracting investment via a more favorable business environment, adapting and adopting new technologies, using industrial clusters to foster technological up-gradation, improving education, streamlining business regulation and dispute resolution mechanisms, and improving infrastructure (especially transport).

Shamyla Chaudry also examined the ratings of Pakistan in various surveys of global competitiveness and compared Pakistan's position in these rankings to that of India and China, two neighbors and competitors. She found that Pakistan has stagnated by most measures of industrial competitiveness, and is particularly weak in health and education and human capital development.

Monetary, Fiscal and Financial Sector Policies: Shahid Kardar evaluated Pakistan's recent performance in monetary and fiscal management of the economy. While admitting that macroeconomic stability has been maintained, he argued that the situation remains precarious, given the level of inflation, current account deficit, and fiscal deficit. The economy has benefited from inflows from donors post-9/11, increased remittances of overseas Pakistanis, and privatization receipts, but the country may not be able to rely on these sources indefinitely. More recently, the government tightened monetary policy. Mr. Kardar also looked at the fiscal policies of the government. The government had been financing expenditures through borrowing from the State Bank, but changes were needed in order to reduce the inflationary pressures that this borrowing had created. With this view, the article presented suggestions for reforming both government expenditures and revenues.

Shakil Faruqi began with a summary of the financial reform efforts that began in Pakistan in the early 1990s, in particular the privatization and consolidation of the banking sector. He assessed the current state of the banking system with regards to soundness, non-performing loans, intermediation costs and efficiency (spreads), profitability, banking and exchange rate risks, and sensitivity to shocks. Despite an impressive performance in several areas, he noted that shortcomings remain; among these is lack of credit access for large segments of the population, and lagging levels of financial intermediation as compared to other countries at similar stages of development.

Muhammad Arshad Khan and Sajawal Khan also looked at financial sector reforms. The paper begins with a framework for the three major stages of financial sector reform. They divided Pakistan's past reform efforts into three phases, starting in the late 1980s. They evaluated the effects of these sustained reform efforts by looking at the impacts on interest rates, bank solvency, credit and indicators of financial deepening, bank profitability, privatization, and corporate governance. Suggestions for a second generation of reforms were given, including a focus on macro-stability, governance, institutional capacity building and property rights, development of venture capital and private equity, and the legal infrastructure for finance.

Exchange Rate and Trade Policies: M. Ashraf Janjua analyzed trends in Pakistan's real exchange rate (REER) over the period 1978 to the present, and identified the domestic policies and events in the external environment that contributed to REER movements. The article also included an econometric analysis of the *equilibrium* real exchange rate (ERER), based on macroeconomic fundamentals. The estimated equilibrium real exchange rate was then compared to the actual REER to identify exchange rate misalignments over the last three decades.

Naheed Zia Khan turned the discussion to international trade, by providing a detailed overview of the history of trade negotiations through GATT and the WTO. Given the current (stalled) round of trade negotiations in Doha, she paid particular attention to the issue of agriculture, focusing on Pakistan's modest support policies toward agriculture and contrasting them with the strong agricultural support offered by the US, EU and other developed nations.

Samina Shabir and Reema Kazmi gave a detailed account of the history of economic cooperation between Pakistan and China, describing the many agreements signed since 2001 by the two countries on tariff reductions, investment, defense, energy, infrastructure, and other areas. These agreements (and future planned agreements) are intended to create a free trade area between Pakistan and China. The paper also took a detailed look at Pakistan's exports and its trade deficit with China, and examined the recent performance of some key sectors of the Pakistani economy that will continue to receive protection under the FTA, including textiles, garments, engineering, automobiles, and consumer durables.

Female Labor Force Participation: In the last paper of the special edition, Mehak Ejaz used recent data from the Pakistan Social and Living Standards Measurement Survey (PSLM) to conduct an empirical analysis of the determinants of female labor force participation. Using a limited dependent variable approach, she found that women were more likely to work outside the home when they belonged to a nuclear family, had greater education, were unmarried, and had access to a vehicle, and were less likely to work when there were a large number of children in the household and had access to home appliances.

This Special Edition of the *Lahore Journal of Economics* has been compiled from the papers presented at the Third Annual Conference on Management of the Pakistan Economy. This Special Edition is meant to disseminate the findings of this conference more widely at both the national and international levels.