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PAKISTAN@100 GOVERNANCE & INSTITUTIONS

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GLOSSARY

AGP	Auditor General of Pakistan
BISP	Benazir Income Support Programme
BPS	Basic Pay Scale
CAPP	Connected Agriculture Platform of Punjab
CCI	Council of Common Interests
CFM	Citizen Feedback Model
CGA	Controller General of Accounts
CST	Central Sales Tax
FATA	Federally Administered Tribal Area
FBR	Federal Board of Revenue
FIA	Federal Investigation Agency
FMIS	Financial Management Information System
GCI	Global Competitiveness Index
GDP	Gross Domestic Product
GST	General Sales Tax
HRM	Human Resource Management
IMF	International Monetary Fund
I-SAPS	Institute of Social and Policy Sciences
KP	Khyber Pakhtunkwa
LG	Local Government
LGA	Local Government Act
LGO	Local Government Ordinance
ICT	Information and Communication Technology
MDAs	Ministries, Departments, and Agencies
MoF	Ministry of Finance
NAB	National Accountability Bureau
NADRA	National Database and Registration Authority
NAP	National Action Plan
NEC	National Economic Council
NFC	National Finance Commission
OECD	Organization for Economic Cooperation and Development
OGP	Open Government Partnership
PER	Performance Evaluation Report
PFCs	Provincial Finance Commissions
PIIE	Peterson Institute for International Economics
PFM	Public Financial Management
PPRA	Public Procurement Regulatory Authority
PTC	Parent Teacher Committee
SBP	State Bank of Pakistan
SDPI	Sustainable Development Policy Institute

SECP	Securities and Exchange Commission of Pakistan
SOE	State-owned Enterprise
TSA	Treasury Single Account
WASH	Water, Sanitation, and Hygiene
WDI	World Development Indicators
WGI	Worldwide Governance Indicators

EXECUTIVE SUMMARY

Governance is the most important constraint to Pakistan's progress toward achieving high-income country status. Pakistan's aspiration to be a high-income economy by 2047—when the nation will turn 100 years old—will depend on the quality and performance of its governance institutions. Because governance affects investment, citizens' trust, and human capital development, together with improving the quality of institutions and policies, innovating the Government's business processes, and improving service delivery to citizens, it is critical in supporting Pakistan's accelerated economic transformation**.**

The next three decades will be definitive, as Pakistan will experience several major changes. There is likely to be a more decentralized system of governance as provinces and the federal government continue implementing the constitutional provisions on devolution. With an increasing population and proliferation of technology and connectivity, the distance between the state and citizens will narrow, with networked communication channels defining the nature of accountability between government and ordinary Pakistanis. As a result, the state will no longer be able to ignore the expectations and aspirations of common citizens for improved service delivery and quality governance.

The public sector is likely to be under pressure from citizens and businesses. Increasing population, the complexity of service delivery challenges, and the modernization of citizen feedback systems will require the state to sharpen its focus on regulation and reduce its direct service-delivery role. While still retaining its primary role of a provider of public goods, the state will be expected to provide strong regulatory and quality assurance standards to ensure that non-state actors can provide quality services.

Existing patterns of state ownership will be constrained and the public sector will be expected to justify the continued dominance of state-owned enterprises (SOEs) in the market. This pressure will not only come from the private sector calling for a level playing field, but also from users of services interested in better service delivery. These new challenges, and the ability of the state and public sector to successfully deal with these challenges through modernization and capacity enhancement, will require Pakistan to redefine the social contract between the state and its citizens by 2047.

The public sector will have to respond to internal pressures for change in line with global norms. The shape and outlook of the state bureaucracy will need to transform and develop new skills sets, enhanced and technology-driven business processes, modern performance management systems, and enhanced transparent and accountable governance systems. Civil servants will need to be familiar with a modern ethos of good public sector governance, including professionalism, innovation, technological sophistication, and strategic decision-making. The Government will need to respond to the new and emerging demands for efficient and effective institutions.

Building strong and transformative institutions is only a first step for Pakistan. The challenge of sustaining institutional quality and reaping the benefits will be even more demdaning, given the history of institutional reforms in Pakistan. For example, a large proportion of public sector employees has low skill levels; full devolution of functions and resources has not yet been achieved as envisaged in the 18th Amendment to the Constitution, limiting the realization of full development and accountability at the local level; and revenue mobilization and expenditure are still being undermined by the lack of a modern public financial management (PFM) regime.

There is already a path toward an efficient and accountable public administration system. This includes the openings provided by devolution, the resolve by stakeholders encapsulated in Pakistan's Vision 2025, and the emergence of 'islands of effectiveness'—public sector institutions that have demonstrated the ability to deliver high-quality services. Similarly, the increased assertiveness of accountability institutions is an important opportunity to improve transparency and accountability. Finally, renewed trust in Pakistan's institutions generated by the recent alternation in power—a first for Pakistan—provides important signals for a reorientation of Pakistan's institutional quality.

ABOUT THIS POLICY NOTE

This policy note makes the case that governance is the most important obstacle to Pakistan's economic development. Governance obstacles undermine Pakistan's ability to translate its existing assets into opportunities for growth and development. The note identifies several governance failures organized around three main challenges: inefficient public administration system; incomplete devolution; and the dominance of the state in the market. These three obstacles are merely aggregates of an array of challenges that citizens and firms experience at all levels in their interaction with the state.

The policy note acknowledges that behind the technical complications lie strong political-economy pull factors that have hindered progress on reform over the years. Three such issues include elite interests and capture, the urgency of geostrategic and geopolitical priorities that distract successive governments from commitment to administrative reforms, and Pakistan's patronage-based politics.

The challenge of reforming the state to be transformational is not new. A plethora of recommendations already exists.[1] What is needed is renewed political will and the support of the bureaucracy to instigate and accelerate far-reaching reforms, undertake the necessary actions to shift the character of the public sector into an efficient and effective structure, and generate citizen demand for improved services. To reach this point, citizens and firms on the one hand, and politicians and bureaucrats on the other, will need to move beyond kinship and network ties to make difficult choices about the nature of the state needed to boost Pakistan's prospects. The citizens and firms will need to actively call for improvements in the quality of services, while the politicians and bureaucrats will need to set the standards and be accountable for delivery.

The road to 2047 will be long and uneven. This policy note offers three pathways to position immediate structural and functional reforms to ensure that Pakistan's institutions are redesigned to support development. These include improving administrative efficiency, deepening devolution, and rethinking the role of the state, briefly discussed below.

Improving administrative efficiency. Public administration is an instrument of national integration. In the era of collaborative and digital governance, strengthening the technical competencies of the public administration is necessary to improve the quality of the bureaucracy and service delivery (for example, revamping the current structure of public administration, which is skewed toward generalist employees with inadequate skills required by a 21st century civil service). The bureaucracy should be improved by raising the level of technical skills and functions. This will mean new skills sets, new business processes, adaptability, and a new ethos of public service.

Deepening devolution. Devolution offers immense promise for economic transformation and progress, but lingering shortcomings, including capacity gaps at the local level, recentralization of

[1] Examples include: The report of the "National Commission for Government Reforms on Reforming, the Government in Pakistan," Prime Minister's Secretariat, Government of Pakistan.

functions by the central and provincial governments, and incomplete decentralization, especially weak autonomy for local governments (LGs), must be addressed in the short to medium term. Strengthening LG systems with fiscal decentralization is the best guarantee for ensuring the effective decentralization of decision-making and accountability, and unhindered and quality service delivery for citizens. Both federal and provincial governments should support decentralization systems for improving citizens' well-being.

Redefining the role of the state. The state remains a dominant player in the market through control of several SOEs. Redefining the role of the state in creating a conducive environment for private sector participation and improving citizen-centric service delivery could provide opportunities for better utilization of state resources through improved regulation. Further strengthening of institutions (including those in charge of regulation) could strengthen the investment climate and create opportunities for citizen participation, better access to public services, and increased trust in the state. A greater role for the private sector in social service delivery and leadership of the private sector in economic development could augment the state's effort in service delivery and create development opportunities.

In the short to medium term, this policy note offers the following key recommendations.

Modernize the public administration to position it to develop, interpret, and implement government policies designed to promote growth and development to achieve high-income country status by 2047 by:

- Modernizing systems and revising processes to reduce human interface;
- Automating administrative processes to improve efficiency;
- Improving coordination and collaboration within and between different levels of government;
- Reskilling the civil service with new skills sets to improve design and implementation of policy; and
- Implementing a government-wide performance management framework and enforcing accountability.

Modernize PFM to generate sufficient resources and efficiently appropriate those resources for development by:

- Developing a legal framework to support the efficient use of public resources;
- Introducing information and communication technology (ICT) systems in financial management;
- Ensuring fiscal transparency in the use of public finances to improve accountability and trust;
- Enabling competition in the market through open bidding and grievance redress mechanisms; and
- Integrating the budget process with planning to align spending with priorities of the Government.

Expand the tax base to generate resources for development by:

- Revamping the Federal Board of Revenue (FBR) and provincial tax authorities to improve autonomy, oversight, and efficiency;
- Adopting a medium-term resource mobilization strategy and assigning well-informed revenue mobilization targets to the FBR and provincial tax authorities and enforcing accountability for compliance;
- Removing all instances of distortionary exemptions and enforcing tax compliance;
- Strengthening capacity for, and the practice of, evidence-based tax projections and policy decisions projection;
- Streamlining federal and provincial governments' roles in the collection of the General Sales Tax (GST) on Goods and Services; and
- Establishing a National Tax Council.

Further devolve functions and financing to lower levels of government to maximize the benefits of devolution without undermining macroeconomic stability by:

- Aligning devolved functions with financing to empower LGs for better service delivery;
- Strengthening the key devolution organs, for example, the National Finance Commission (NFC) Secretariat, the Council of Common Interests (CCI), and Council of Ministers to effectively support devolution;
- Revising the current NFC formula to account for changes in population and make the NFC relevant for intergovernmental fiscal transfers; and
- Developing service delivery standards for the federation and provinces, and monitoring adherence.

Establish a single entity to manage the portfolio of SOEs by:

- Vigorously implementing the existing corporate governance rules;
- Excluding government officials from all boards managing SOEs;
- Recruiting managers from the private sector and assigning performance targets; and
- Divesting the Government's interest from the current SOE portfolio.

Improve the quality of delivery of social services at all levels of government by:

- Expanding provincial government spending on health, education, and water and sanitation services;
- Establishing strong performance-monitoring systems for service delivery;
- Streamlining the regulatory framework for private provision of services; and
- Expanding the coverage of social services for poor and vulnerable populations.

INTRODUCTION

Pakistan is a resilient state. It has weathered both internal and external shocks, and survived in a geopolitical context. Underpinned by a strong military bureaucracy, strong elite networks, and sometimes external anchors (for example, the United States of America and the Kingdom of Saudi Arabia), the characteristics that underpin Pakistan's progress are inadvertently the same ones that seem to slow it down: a large and educated population; a well-organized civil service with a functioning bureaucracy, strong kinship and familial ties; and strong military and national pride. For this reason, the titles of the following recent academic works on Pakistan are predictably unequivocal in their pessimism: 'A Hard Country' (Lieven, 2011), 'Power Failure' (Hussain, 2015), 'Governance Deficit' (Qureshi, 2016), and 'Governing the Ungovernable' (Husain, 2018). Yet, Pakistan's state structures have remained resilient in the face of both internal and external shocks (Cohen, 2005; Lieven, 2011).

Even under these circumstances, Pakistan has experienced some growth episodes. These growth episodes occurred during those periods marked by a strong focus on governance, including growth-enhancing economic reforms and political stability (Husain, 2018). In the past decade, for example, Pakistan has managed to reduce the poverty headcount. The decade also coincides with two election cycles during which an elected government has completed a full term without interruption. Nevertheless, growth has not been transformational because of the weak institutional structures that underpin the Pakistani state. This 'growth without development', as Easterly (2001) refers to it, is the result of persistent governance failures.

Pakistan's growth performance has been lower than its potential for several decades. Average gross domestic product (GDP) per capita growth has been between 1 and 2 percent annually over the past 40 years. This compares with average annual per capita GDP growth of between 6 and 7 percent in China over the past 50 years, 4 percent in Malaysia, and 5 percent in Vietnam more recently. Pakistan's public investment rate, at around 5 percent of GDP, and private investment rate, at around 10 percent of GDP, are low and around half of South Asia's average.

Pakistan aspires to become a high-income economy by 2047—the year when the Republic will turn 100. By all measures, this seems to be an ambitious prospect given the challenges that Pakistan faces. Over 20 million children are out of school, hence reducing the opportunities for robust human capital formation. Limited fiscal space undermines growth and investment, and policy inefficiencies and an unfavorable investment climate contribute to low foreign investment. Inefficient public administration practices and policy ineffectiveness undermine the full participation of the private sector in the economy. And, Pakistan's relations with some of its neighbors also constrain its potential for productive partnerships.

The world over, countries that have invested in improving their governance environments are the ones that have also seen massive transformation, not only in the quality of life for their citizens, but also gains in economic growth. Countries such as the Rep. of Korea, Indonesia, Malaysia, and Singapore boast better human development records because of their focus on strengthening governance institutions. Pakistan has also experienced most of its growth episodes in periods of political stability that provided the opportunity to focus on economic reforms (Husain, 2018).

The rationale for improved governance in Pakistan is pertinent given the strong link between development and institutional quality in Pakistan (Naveed, 2016).

Consider the following:

- In Khyber Pakhtunkwa (KP)—one of Pakistan's poorest provinces—parents choose not send their sons to schools because of teacher absenteeism. They prefer to send their children (especially daughters) to private schools because public schools are of poor quality (Sustainable Development Policy Institute [SDPI] survey, 2014).

- The top five most problematic factors for doing business in Pakistan require effective government interventions: businesses cite corruption (17 percent), tax rates (11 percent), government instability (8 percent), crime and theft (7 percent), and inefficient bureaucracy (7 percent) (Global Competitiveness Report, 2017-18).

- Pakistan is ranked 147 (out of 190 countries) on the WBG's Ease of Doing Business rankings for 2018, far below other comparator countries (World Bank, 2018).

To achieve high-income status, Pakistan will need to improve its institutions. Strong institutions would contribute to the emergence of a strong investment climate by removing inefficiencies and attracting foreign investors; they would also improve the delivery of services, such as education and health, and support a reduction in the number of out-of-school children, the development of skills for the future, and the narrowing of the opportunity gap for girls, and the gap between rural and urban, and rich and poor, segments of Pakistani society. Strong institutions would also enhance trust in the state, especially at the local level. The effect would be a capable state whose institutions are dedicated solely to improving citizens' well-being and supporting the transformation to a high-income economy. For now, Pakistan is outranked by its regional and aspirational peers in most indicators of governance (Figure 1).

However, Pakistan will also require a new approach. It will need new institutions with a new ethos, a different caliber of public sector officials with different tools and capacities, and a stronger and active citizenry supported by local-level mechanisms for participation and accountability. This forward-looking approach will require better commitment to reform, improved coordination of the government apparatus to deliver the Government's agenda, and cooperation of both citizens and firms to support the Government's programs.

This policy note discusses three main pathways through which Pakistan can improve the effectiveness of the state to be a catalyst for growth and development.

Improving administrative efficiency. Public administration is an instrument of national integration. In the era of collaborative and digital governance, strengthening the technical competencies of the public administration is necessary for improving the quality of the bureaucracy and service delivery (for example, the current structure of public administration is skewed toward generalist and unskilled employees). The bureaucracy should be enhanced through improvements in technical skills, as well as in functions—this will mean new skills sets, new business processes, adaptability, and a new ethos of public service.

Deepening devolution. Devolution offers immense promise for economic transformation and progress, but lingering shortcomings, including capacity gaps at the local level, recentralization of functions by the central and provincial governments, and incomplete decentralization, including especially weak autonomy for local governments (LGs), must be addressed in the short to medium term. Strengthening LG systems with fiscal decentralization is the best guarantee for ensuring effective decentralization of decision-making and accountability—and unhindered quality service delivery for common citizens. The federal and provincial governments should support the decentralization agenda for improving citizens' citizen well-being.

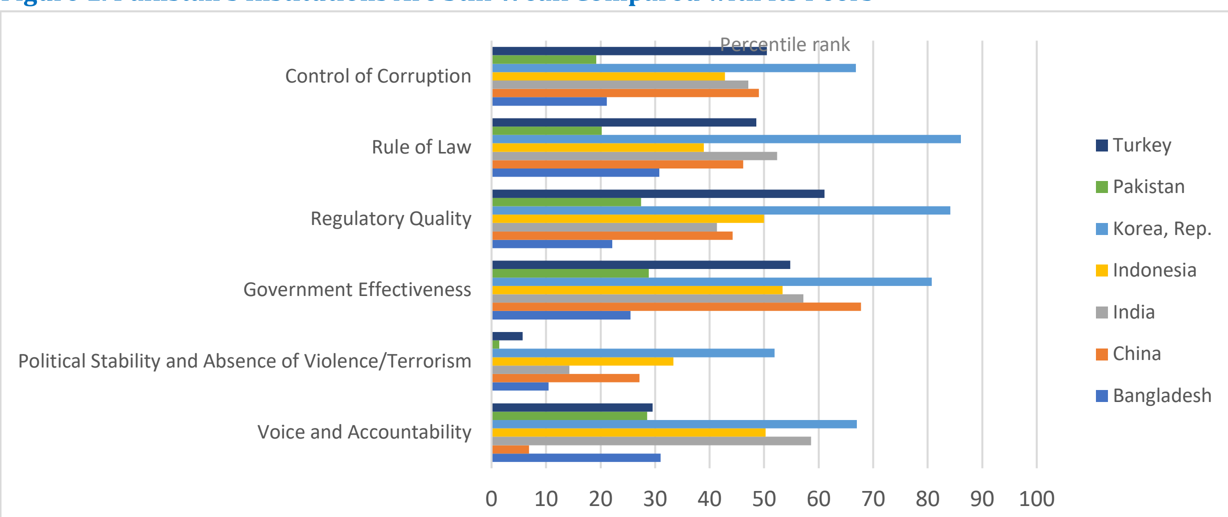
Redefining the role of the state. The state remains a dominant player in the market through full control of several state-owned enterprises (SOEs). The state also plays a substantial role in the financial markets, crowding out private investment in these areas. Redefining the role of the state in creating a conducive environment for private sector participation and improving citizen-centric service delivery could provide opportunities for better utilization of state resources through improved regulation. Further strengthening of institutions (including those in charge of regulation) could strengthen the investment climate and create opportunities for citizen participation, better access to public services, and increased trust in the state. A greater role for the private sector in social service delivery and leadership of the private sector in the challenges of economic development decreases the role of the Government, and could reduce and lighten the Government's burden.

CHAPTER 1: HOW GOVERNANCE AFFECTS GROWTH

Governance—the process through which the state and non-state actors interact to design and implement policies, within a given set of formal and informal rules that shape and are shaped by power (World Bank, 2006)—is now accepted as an important growth accelerator. Countries with a weak governance environment also tend to be those with weak prospects for the economic development necessary to foster structural transformation. This is because the interactions among citizens, the state, and firms are mediated by institutions—the rules of the game—that determine how these relationships are manifested. Weak institutions undermine growth and strong institutions support growth.

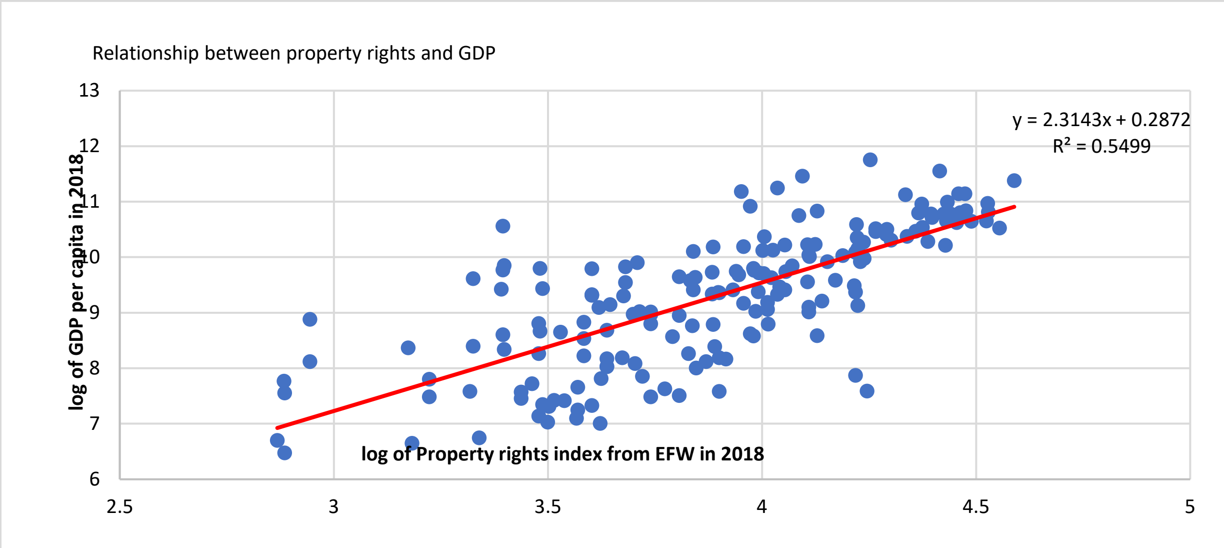
It is now well-recognized that institutional strength forms the backbone of the economic and social development of any country (Figure 2). Without participatory, transparent, accountable, and justice-manifesting institutions, including those that guarantee property rights, policy-making can remain paralyzed, constraining countries' abilities to optimize their economic and human development capacity. Acemoglu and Robinson (2012) and Rodrik, Subramanian and Trebbi (2004) show the practical significance of strong and effective institutions to bring about transformative economic progress.

Figure 1. Pakistan's Institutions Are Still Weak Compared with Its Peers



Source: Worldwide Governance Indicators (WGI), 2018.

Figure 2. Growth Increases as Institutions Strengthen



Source: Worldwide Governance Indicators (WGI), 2018

Institutions represent the formal structures and laws, informal values, and norms that shape and govern the behavior and expectations of different actors in each setting (Luiz, 2009). Institutions condition choices and moderate expectations of other people's behavior (Lin and Nugent, 1995). Institutions support markets, property rights, regulations, macroeconomic stabilization, social insurance, and conflict management (Rodrik, 2000). In fact, institutions explain the difference between failure and progress among nations (Acemoglu and Robinson, 2012); they condition the behavior of actors in the policy arena—signaling the 'rules of the game' (North, 1990) and, more generally, determine economic performance and variations across countries. Restructuring institutions is an instrument of adjustment to changes in the socioeconomic environment at the national, regional, or local levels to increase their effectiveness and efficiency in achieving their mission, performing their roles, and carrying out their functions.

Strong institutions constrain the actions of the political elite and public officials, while also creating the incentives for private investment (Acemoglu and Robinson, 2012). Thus, institutional arrangements determine how public functions are carried out, how resources are allocated, and the direction government interventions take. Institutions determine the level of development in an economy. Where institutions are weak, the political elite can use resources for their own personal gain, disregarding the interests of the public and prolonging the status quo in society.

Weak institutions create incentives for the elite to entrench the politics of kinship and patronage. As Andrews, Pritchett and Woolcock (2012) note, in countries with weak institutions, such governance and institutional weaknesses are manifested at both structural (the design of organizations) and functional (how the organizations perform their mandates) levels. Consequently, the state fails to provide basic services, such as health and education, to its citizens because of a misallocation of resources and ill-formed priorities. Resource inequality also enables the elite to subvert the political, regulatory, and legal institutions for their own personal gain. The elite may also oppose institutional reforms that threaten their political power (Acemoglu and Robinson, 2012; Khalid, 2016; Khalid, 2017) and influence policy formulation to win favors. This leads to the persistence of inefficient and low-quality institutions.

1.1 GOVERNANCE IN PAKISTAN – THE BALANCE SHEET

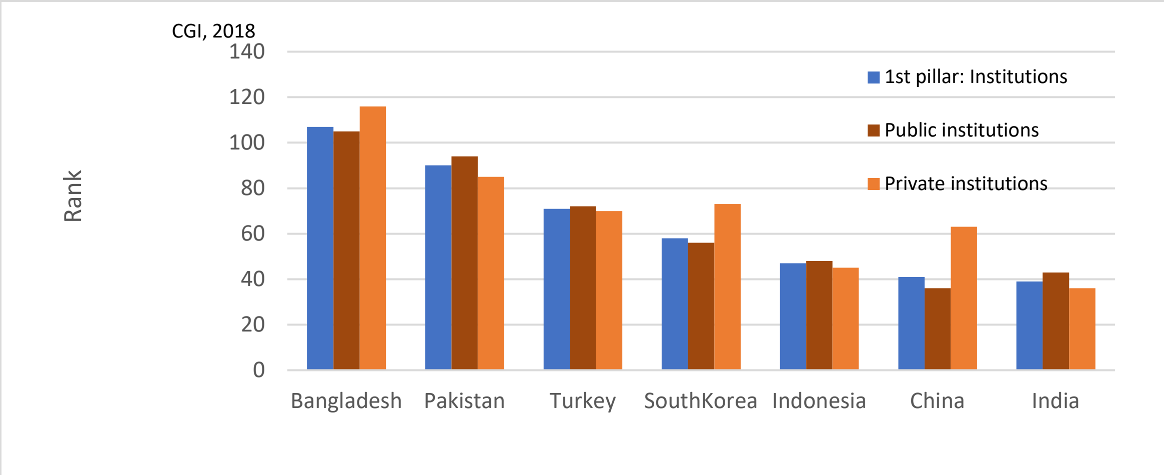
There is no question that governance matters for Pakistan. Indeed, as a recent publication (Kugelman and Husain, 2018) declared, regarding Pakistan's institutions, "we know they matter, but how can they work better?" The question of why institutions matter for Pakistan is still important, if only to amplify how strengthening the governance environment, building better institutions, and implementing citizen-centric policies could multiply Pakistan's development prospects.

The paradox of Pakistan's growth shows how poor governance has undermined Pakistan's development. Although Pakistan has benefited from episodes of economic growth, these have tended to be less robust, as they have been accompanied by frequent reversals. Pakistan only managed to progress from a low-income country to the status of a low middle-income country after more than 70 years of independence.[2] While well-known challenges—for example, unstable policy environment, energy crises, and security challenges—have affected growth, several other aspects related to public-sector governance have also contributed. A weak institutional apparatus for producing high-quality and skilled manpower; slow and costly judicial procedures (contract enforcement); market rigities (land, labour, and capital); and political risk, have all constrained the space for transformational growth. These governance deficiencies have undermined the private sector, reduced market efficiency, and hampered the overall macroeconomic environment.

The global ranking of Pakistan on key indicators of institutional quality is low compared with its peers. Pakistan's poor rankings on the institutions pillar, and in its quality of public and private institutions on the Global Competitiveness Index (GCI), underscore the ineffectiveness of the governance structure and the inability of the country's institutional framework to sustain an investor-friendly environment (Figure 3).

[2] From 1960 to 2016, Pakistan's GDP per capita (constant 2010, US dollar) only increased marginally from US$304 in 1960 to US$1,178 in 2016.

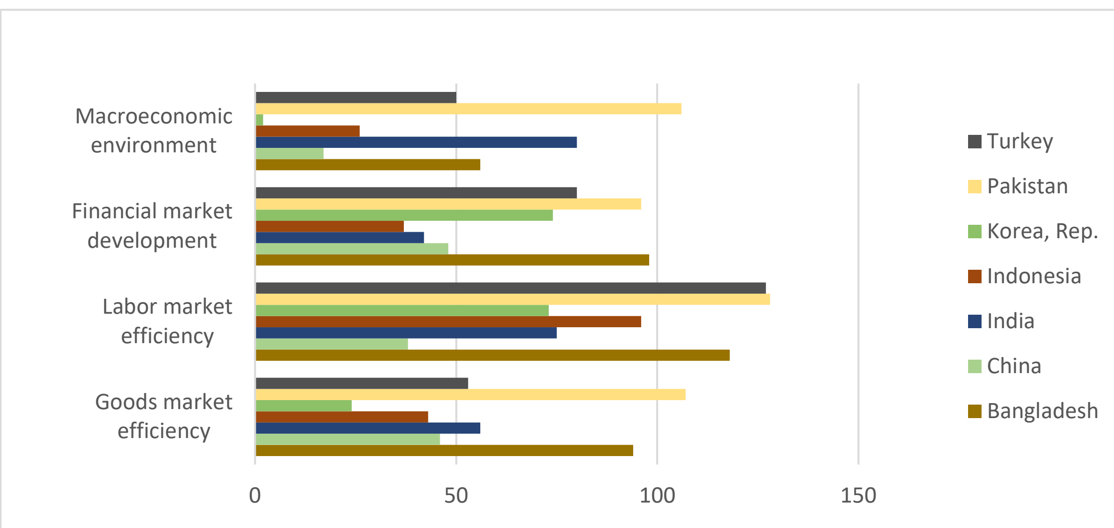
Figure 3. Uniform Pattern of Weak Institutional Performance across Governance Indicators



Source: Global Competitiveness Report (GCI), 2018.

The poor quality of governance institutions has affected Pakistan's competitiveness. In Pakistan, the inefficiency of both the goods market and the labor market demonstrates this situation. The financial market, which is crucial for economic growth, has equally suffered. Pakistan is ranked the lowest among its peers on all the indicators except for financial market development, in which it is ranked slightly higher than Bangladesh (Figure 4).

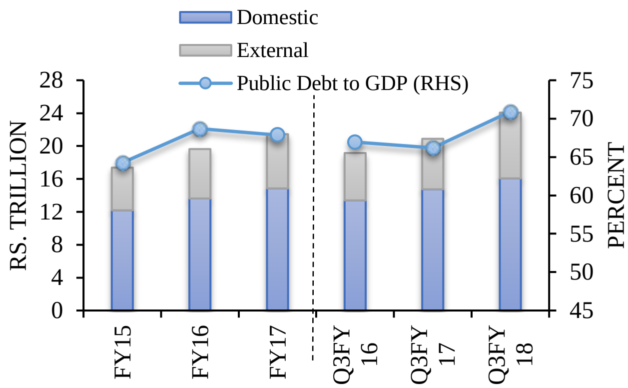
Figure 4. Weak Institutional Quality Has Eroded Market Efficiency and the Macroeconomic Environment

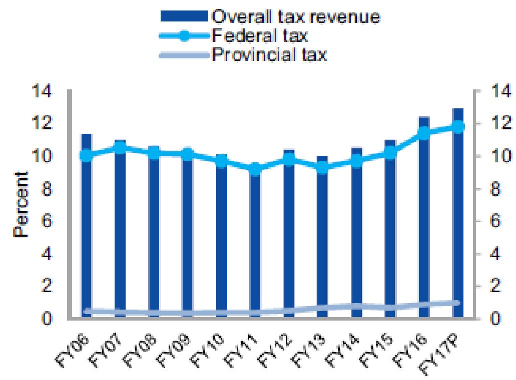


Source: Global Competitiveness Report (GCI) 2018.

Pakistan carries a heavy and growing fiscal burden, and requires improvements and greater transparency in the management of public finances. Pakistan has routinely endured high fiscal deficits. This calls for improving the management of public finance, both at the policy and operational levels. A stronger commitment to efficiency in the use of resources and an effective tax-collection system, both at the federal and provincial levels, are critical. Combining better prioritization of public spending and strengthening the legal environment for public financial management (PFM)—including strengthening public procurement and domestic resource mobilization—could ensure better value for money, improvements in the revenue base, and better targeting of public expenditure.

Figure 5. Revenue Collection Has Not Kept up with Government Debt

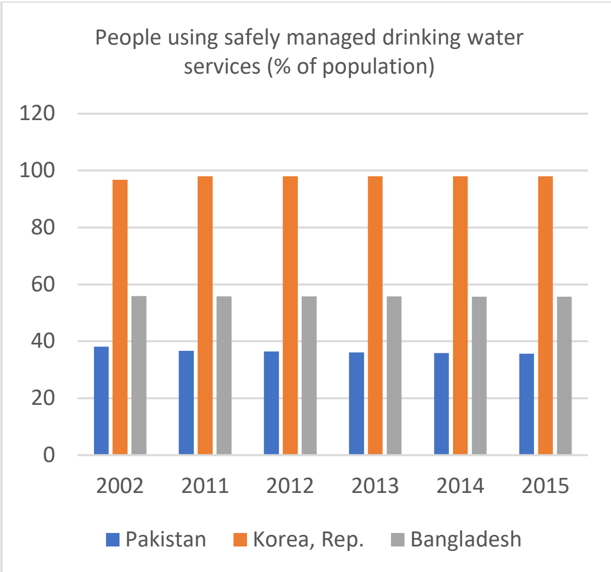




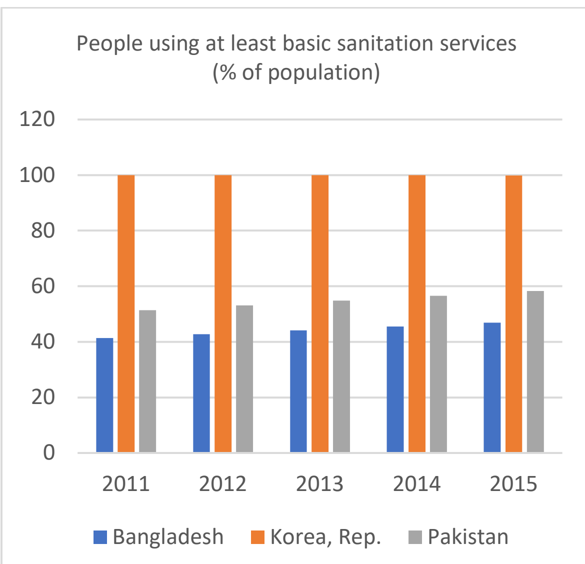
Sources: SBP, MoF, IMF, and WBG staff calculations.

Pakistan needs to provide more citizen-centric service delivery to meet the increased demands of a growing population. The population of Pakistan has grown rapidly, and currently stands at 208 million (2017), resulting in a large youth bulge, growing urbanization, and an expansion of the middle class. The youth bulge and increasing urbanization are already placing significant pressure on social services. Persistent water shortages and electricity cuts suggest that the number of users now far exceeds the volume of services provided (Figure 6). The demand for improved service delivery could also strengthen the Government's accountability for service delivery and improve the availability of social services. Alternatively, it could create opportunities for only a small segment of the population that can afford privately provided services, leaving behind a large number of people. The potential market failure requires that Pakistan strengthens its service delivery mechanisms to ensure that citizens have access to social services such as education, health, water and sanitation, electricity, and secure neighborhoods.

Figure 6. Half of Pakistan's Population Does Not Have Access to Safe Drinking Water or Basic



Sanitation

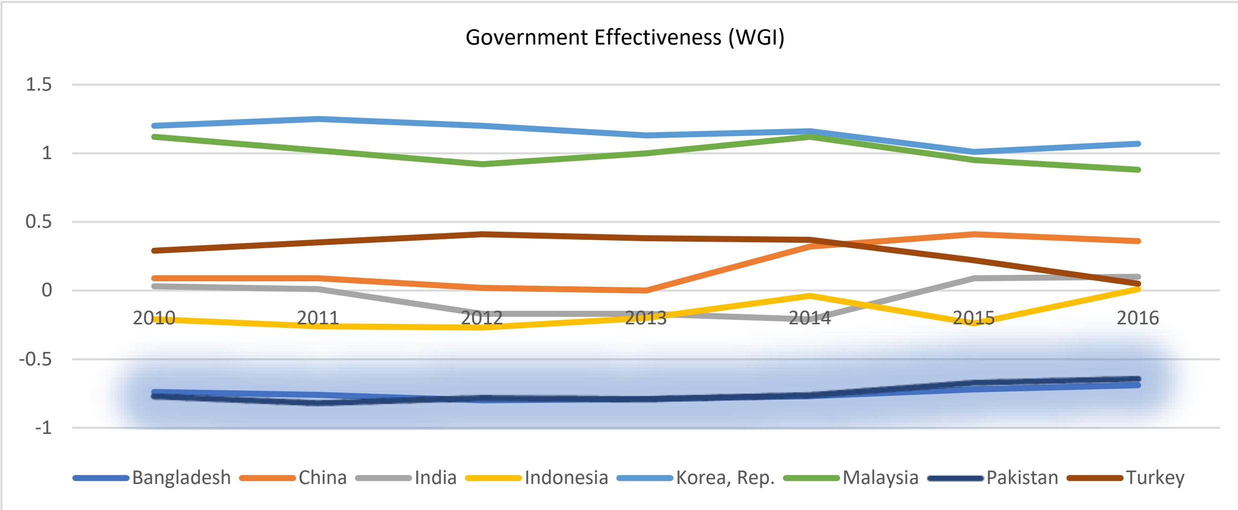


Source: World Development Indicators.

Pakistan needs to address the lingering regional inequalities and gaps between urban and rural regions. Strengthening governance could also help Pakistan deal with this phenomenon. Reforming how provincial governments target the poor and the formula for intergovernmental fiscal transfers are critical in improving the availability of the Government to reach the poor. While the 18th Constitutional Amendment has provided opportunities for devolved governance, coordination problems still undermine the national government's ability to develop strong systems for monitoring the provinces' performance in the delivery of national development priorities. As a result, while some parts of the country have done well in reaping the benefits of devolution, others seem to have been left behind. There are striking differences in the availability of services in different parts of the country.

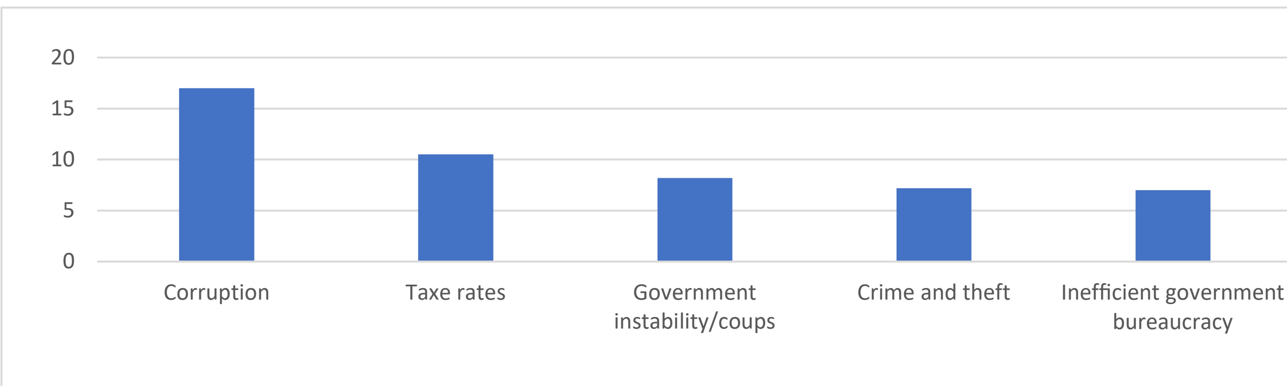
There are variations across institutions, with some performing much better than others. However, the overall picture is far from ideal. Pakistan performs below its regional peers on various governance and institutional indicators. Pakistan has the lowest percentile ranking among its peer countries on four out of the six WGI indicators: Voice and Accountability, Political Stability, Rule of Law, and Control of Corruption. The situation is hardly less gloomy in the Governance Effectiveness and Regulatory Quality indicators: only Bangladesh is ranked below Pakistan (Figure 7). Similarly, governance factors feature prominently among the obstacles cited by Pakistani businesses (Figure 8).

Figure 7. Pakistan Ranks Lower Than Most of Its Peers in Government Effectiveness



Source: Worldwide Governance Indicators (WGI), 2017

Figure 8. Governance-Related Issues Rank at the Top of Investor Complaints on Doing Business In Pakistan



Source: Global Competitiveness Report (GCI), 2016-17.

However, there are pockets of effectiveness, or so-called 'candles in the dark' (Ayub and Husain, 2016), with isolated cases of success. For instance, the same public administration that has not been able to produce results in some areas, nonetheless helped manage functions that resulted in the reduction of the poverty head count from 64.3 percent in 2002 to 24.3 percent in 2016 (World Bank, 2018c). Among the reasons for this success is the Government's concerted effort and strong focus to target the poor and expand social protection services across Pakistan. Initiatives such as the National Database and Registration Authority (NADRA), the Benazir Income Support Programme (BISP), or the Motorway Police, have succeeded despite the challenging institutional context in which the public sector operates. The main success factors in these institutions could easily be replicated in other institutions.[3]

1.2 WHY ARE THINGS THE WAY THEY ARE IN PAKISTAN?

Politics and political systems are key to determining any country's policy outcomes, given that those who rule typically play a large role in determining policy. A dysfunctional political system or politics can easily undermine delivery of public services and policy outcomes. Several factors undermine reforms, and these factors may also undermine Pakistan's economic growth path.

1.2.1 Elite Capture: How the Squeezing of Democratic Governments Works

Institutional reforms in countries with an unequal distribution of power may be hindered by the elite, who benefit from the existing economic and political institutions (Acemoglu, Johnson and Robinson, 2005). Such elites oppose institutional reforms that threaten their political power. In this way, low-quality economic and political institutions can persist (Acemoglu and Robinson, 2012). They oppose measures that prevent corruption and protect the public. Resource inequality also enables the elite to subvert the political, regulatory, and legal institutions for their own benefit, and leads them to favor established institutions over new and more efficient ones (Glaeser et al., 2003).

Pakistan's complex history and its geopolitical location have given rise to several elite factions with their own agendas. However, the Pakistani elite configuration is far from homogenous. It includes the military, the bureaucracy, the industrial houses, the businesses, together with the feudal and the religious players. Given the fluidity of these categories, some elites straddle all the clusters. Each category of elite is strong in its own right and affects development in a different way.

These elites also behave differently depending on the nature of their interests and the bargains they seek. The securitization of public policy and the overarching role of the military in Pakistani politics is the result of the desire to sustain the military's position of influence (Dwyer, 2016). The subsequent capture of the state through a combination of the military, politicians, businesses, and bureaucratic maneuvering leaves no space for far-reaching reform. Political players continue to hold strategic positions in parties in Pakistan, while elections are viewed by urban power-brokers and regional elites as an extension of age-old systems of kinship and intertribal rivalry, as well as a chance to gain access to government largesse (Lieven, 2011). The landowning class still dictates much economic direction for its own benefit, through political channels (Lieven, 2011). Rural landowners in some areas still dictate the political choices of their tenants, and key elites, including business houses with their deep pockets use, all means to influence election choices.

What does this mean for Pakistan? High inequality in economic and political power perpetuates the existence of predatory institutions, creating further inequalities and hindering economic growth.

[3] They include clear goals and objectives, attracting and retaining skilled staff, financial sustainability, vision and continuity of leadership, managerial autonomy and political support, adaptability, and monitoring and evaluation.

Key institutional reforms that could have been undertaken, such as those involving tax reform, civil service reforms, or land reforms, are largely derailed or scrapped altogether if they go against perceived interests. Important changes that could introduce the much-needed efficiency and new skills into the bureaucracy are undermined for fear that they could disrupt the existing order. Discretionary exemptions from tax obligations and the Government's continued engagement in loss-making SOEs point to the pervasiveness of elite influence within the Government.

1.2.2 Regime Switches and Political Instability

Pakistan has been a sustained democracy for the past 10 years. With two democratic governments in succession, Pakistan is witnessing a full electoral term of 5 years for the first time in the country's 70-year history. Two overarching factors have characterized Pakistan's political system. The first is regime instability, in terms of the switches in power from democratic to military governments and back, and the uncertainty that accompanies these switches. The second is political instability during democratic regimes. The underlying regime instability in Pakistan and, to an extent, the underlying political instability, is the dominance of the military as the country's most powerful institution, and the tug of war between the civilians and the military for power in handling the perceived national interests. Power shifted from civilian governments to the military in 1958, 1977, and 1999. Each shift led to a sustained period with the military at the helm—1958 to 1971, 1977 to 1988, and most recently 1999 to 2008, although for some years in each of those time periods Pakistan was a hybrid authoritarian-democratic state with a military leader but an elected parliament.

The periods of democratic rule in Pakistan have been marred by speculation following intense conflict between the main political parties and power politics. The first type pf speculation is the fear that the military might take over at any time. The second type of speculation is that the government of the day might be dissolved and fresh elections held—even in the past 10 years of sustained democracy—on the orders of the military. This uncertainty has affected the policy decisions of the civilian governments while in power, both at the federal and constituency levels. While the army no longer seeks overt control of government, it has asserted its power by commanding control over security and foreign policy, thwarted recent attempts at making peace with India, and bristled at civilian assertions of power. Still, the past 10 years have been a democratic period far more politically stable than the 1990s. The excuse for dissolution of government was always poor governance or corruption, but there was also the perception that the military was working 'behind the scenes' in these instances to destabilize the civilian governments. This instability is correlated with growth.

1.2.3 Incumbency Disadvantage

Another feature that characterizes Pakistani politics is an 'incumbency disadvantage'—that is, in each election, incumbent politicians of equal quality as nonincumbent politicians are less likely to win. This contrasts with the typical incumbency advantage found in other political contexts such as the United States, where incumbent politicians of equal quality as nonincumbent politicians are more likely to win elections.

There is a causal incumbency disadvantage at the constituency level in Pakistan (Afzal, 2013). For the four elections between 1988 and 1997, candidates who barely won a National Assembly seat were, on average, between 13 and 16 percent less likely to win the next time than candidates who barely lost. This incumbency disadvantage was limited to those incumbent legislators who belonged to the party in power at the center or the majority party. For those legislators belonging to other parties, there was no incumbency effect. This implies that voters specifically punish legislators who belong to the party in power at the center, perhaps because they consider them to be complicit in the corrupt activities of the federal government, or in other failures associated with it.

Politicians behave differently when they are uncertain about their reelection prospects. They are less inclined to put in place policies that benefit their constituents in the longer term. The incumbency disadvantage dictates that candidates who win by small margins in an election are unlikely to win the next time around; if they take their defeat for granted, they are more likely to engage in extractive behavior and benefit only some of their constituents in terms of patronage. They are also more likely to invest in projects that are easily visible—such as roads, village electrification, gas (which legislators end up spending most of their development funds on) rather than those that are less tangible, such as investing in improving the quality of schools.

1.2.4 Party Switching

Another common political practice in Pakistan is switching parties, or horse-trading. This partially derives from the incumbency disadvantage that parties face at the macro level—that is, a majority of parties face the likelihood of being voted out of parliament—thus incentivizing opportunistic legislators to jump ship to join the opposition party, which is on the rise. This makes it more difficult for voters to hold politicians and parties accountable, because voters are voting for a candidate-party package when they go to the polls in their constituencies. This undermines individual accountability. As a result, the incumbent's incentive to support growth-enhancing reforms is low.

1.3 WHY HAVE PAST INITIATIVES FAILED AND WHAT WILL IT TAKE TO CHANGE?

Several recommendations, and indeed reforms, have been attempted, with mixed results. Some reforms were considered illegitimate by elected governments, having been introduced during military governments. For example, the Local Government Ordinance (LGO) 2001, although it was seen as an important reform for deepening decentralization and providing a greater role for local authorities, was deemed illegitimate. As a result, it was scrapped in 2013 and replaced by the Local Government Acts (LGA) 2013. In addition:

- The changing priorities of development partners have, on occasion, led to some unintended consequences. Development partners have occasionally shifted focus from some areas of engagement (for example, civil service reforms) to areas on service delivery reforms, especially in health and education, and this too with varying degree of eagerness for difficult and fruitful reforms. "Low-hanging fruit" is the buzz phrase.

- Vested interests of the bureaucracy have, on occasion, led to weak commitment to reforms that have directly threatened the interests of the bureaucracy. The entire reform effort has been loosely structured and its primary focus has been the higher civil service (the Central Superior Services) and, in particular, one cadre—the Civil Service of Pakistan (later the District Management Group, and today the Pakistan Administrative Service). Obviously, this cadre has resisted the reforms.

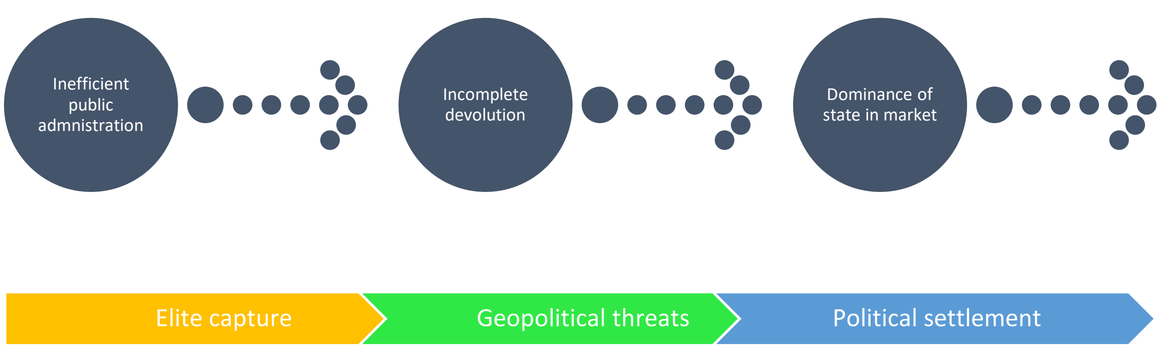
- Weak ownership of reforms has also undermined the ability of key stakeholders to support difficult choices related to the reforms. The bureaucracy, for instance, has sometimes seen reforms as impositions from political actors, while politicians have sometimes used reforms to target the bureaucracy.

Chapter 2: Three Governance Challenges for Pakistan's Transformation

There are three main pillars of governance challenges that undermine the effectiveness of the state (Figure 9). These obstacles reinforce each other and will continue to confront Pakistan's policymakers over the next 30 years in the country's quest toward achieving high-income country status. The first is an inefficient public administration system, the second is incomplete devolution, and the third is the dominance of the state in the market. The prospects for Pakistan's development over the next 30 years could be enhanced if Pakistan makes its public administration system more efficient, takes advantage of its nascent devolution and expands its reach, and reviews the role of the state in the market and in service delivery.

Overlaying these technical problems is a legacy of political-economy factors. These must be addressed to clear the way for a consensus on difficult reforms. The first of these is vested interests and elites that resist and/or capture the proposed reforms and therefore undermine their success. This is seen in the number of unsuccessful attempts that have been made to improve the functioning of the Pakistani state. Second, security and regional geopolitical problems have reduced the salience of growth-enhancing reforms and moved the focus of successive governments away from administrative reforms toward immediate national security and geopolitical threats. And third is the nature of Pakistan's political settlement, which allows short-term patronage-based dividends to trump long-term investments in transformative policies.

Figure 9. Three Governance Obstacles to Growth and Development for Pakistan



2.1 Challenge 1: Inefficient Public Administration

Pakistan's public sector is an extension of colonial-era bureaucratic structures. The Pakistani public sector was designed during the British colonial era to enforce compliance with state policies and encouraged little public participation. These tendencies shaped the whole spectrum of bureaucratic structures and systems, including recruitment processes, training, mobility systems and, most importantly, the role of the bureaucracy in higher-level policy formulation and implementation systems.

The public sector is plagued with both political and technical problems. The political problems have created structural weaknesses that can only be resolved through a political process. These include the design of the public administration, and the relationship between the various categories and hierarchies in the various parts of the civil service. The technical problems, on the other hand, have created functional weaknesses that could be addressed through technocratic responses. The choices and sequencing of reforms must therefore be appropriately calibrated to suit the respective realities of Pakistan's public administration.

Pakistan has made several attempts to understand what plagues its public administrative system. However, proposals have not been fully implemented. Where they have been implemented, they have faiuled to change the system because reforms have focused on the structure of organizations (form) rather than on the functioning of these institutions. In some cases, they have been driven less by technocratic considerations and more by political motivativation. In this sense, the rules—the traditions that have supported poor performance—have largely been left intact as layers of the bureacracy are changed, replaced, or discarded altogether. In recent times, government institutions have become more aware of these challenges. For instance, the Public Service Commission has acknowledged that rules for recruitment, poor motivation, and the lack of incentives, are among some of its major challenges.[4] The following pargraphs detail these challenges.

Human Resource Management System

The absence of strong human resource management (HRM) systems, including a functional HRM planning system, undermines staff allocation and management. The HRM system is manual and staff records are kept in individual files, maintained at different levels/with different competent authorities in the departments. Even basic staffing data (number of sanctioned and filled positions, titles, grade levels, qualifications, training obtained, years in service, etc.) are not available in electronic form at the department level. This has created inefficiency and opportunities for opaqueness in personnel management, including in the filling of vacant positions. The absence of data and a weak monitoring system for human resource planning means that estimating staff strength can be a challenge. This has led to two main problems. First, in the absence of human resource planning to estimate needs, it is possible to hire more staff than are needed (e.g., hiring at lower levels for basic functions, rather than at important technical/specialist levels), leading to an increase in the wage bill. Second, without human resource planning, several vacancies exist in various departments due to the difficulty of establishing staff movements (e.g., by promotion or transfer) at any given time.

[4] See: Public Service Commission. *Annual Report*, 2015. Islamabad: Public Service Commission, page 7.

The human resource functions are dispersed. There are no human resource units, equipped with trained personnel (in HRM) in departments to handle personnel matters in collaboration with other relevant departments (for example, the Establishment Division, the General Administration Department, the Public Service Commission, the Finance Department, the Accountant General's office, and training institutes).[5] The elements of a good HRM system, such as job descriptions or key performance indicators, are generally missing.[6] During the annual budget preparation process, information on sanctioned positions is collected from field offices or directorates. However, at provincial or federal levels, there is no consolidated database of public sector employment, potentially leading to overstaffing (Table 1).

Table 1. Public Sector Employment in Pakistan

	2002	2011	2015
(i) General government	**2,782,100**	**2,924,285**	**3,251,391**
(a) Civilian central government	429,500	449,964	357,374
(b) Subnational government	1,765,600	1,857,321	1,958,217
(c) Armed forces	587,000	617,000	935,800
(ii) SOE employees	**382,800**	**369,285**	**385,939**
Total public sector employees (i + ii)	**3,164,900**	**3,293,570**	**3,637,330**

Note: Above data exclude LG and provincial SOEs' employees.
Sources: Data for 2002 & 2011: National Commission for Government Reforms (NCGR), 2008
Data for 2015: (a & b) Controller General of Accounts, Audited Financial Statements for FY2016.
(ii) Government of Pakistan, Establishment Division (various years)
(c) Index Mundi, NA

Recruitment, Performance Management and Promotion

Recruitment to the All-Pakistan Service and 11 occupational groups of the federal service is through a nationally-held competitive examination. The selection examination does not prioritize technical qualifications. A premium is placed on skills in English language and expertise in subjects of a generalized nature (English essays, English composition, general knowledge, and everyday science). To qualify in these competitive programs, prospective candidates need to excel in generalized academics rather than specialized or modern aspects of public sector management skills. Thus, leadership for policy implementation in core technical areas suffers. While these professionals have been able to develop managerial qualities, the lower levels of the civil service have been hollowed out as a result of the lack of attention given to furthering core technical skills at the lower levels.

Performance management is not designed to nurture responsive and optimally performing institutions. The system prioritizes adherence to rules rather than performance based on objective criteria. There are no continuous rewards for superior performance, thus undermining the incentives

[5] There exist administration or establishment wings/units in the departments, however, they do not have trained personnel and their functioning is not clear, as majority of the functions/roles of HR unit are delegated to competent authorities, and there are no rules that require regular reporting/sharing of HR related information with a central HR unit of the department. Hence, there is no consolidated staffing database in departments.
[6] There are service rules for each post, but no formal job descriptions.

for improvements in performance. The absence of job descriptions for most jobs makes it difficult to review the performance of staff and propose remedial measures. Where performance appraisal is conducted, it is usually superficial and not used to support further development of staff. For instance, it is not rare to see a performance evaluation report (formerly called as Annual Confidential Report) that provides glowing tribute in all areas, only to recommend training in the very same areas. In addition, the completion of performance evaluations is not regularly monitored. It is the staff's responsibility to ensure completion of the annual performance evaluation record (and personal file) when his/her promotion becomes due. There is no clear management accountability for the same.

Box 1. Public Sector Employment at the Federal and Subnational Levels

Following the 18th Constitutional Amendment, the federal government devolved 17 federal ministries in three phases. A total of 60,578 employees of devolved ministries and their related departments have been adjusted. According to the annual employment report of the Establishment Division of FY11, 17,115 employees were transferred to provincial governments, and 29,736 employees were adjusted within different ministries of the federal government. In addition, 403 employees were transferred to Federally Administered Tribal Areas (FATA)/GB/AJK.

According to the available data, the actual strength of federal government ministries and attached departments reduced slightly from 449,964 in 2011 to 444,521 (actual positions) in 2014. However, the actual employment in SOEs increased from 369,285 in 2011 to 385,939 in 2014. Latest public sector employment data for all provinces are not available. However, data on sanctioned provincial positions in Punjab show an average increase of 5 percent during FY10-FY15. The actual or filled positions are usually fewer than the sanctioned positions, although the budget is allocated according to the sanctioned positions (for example, at the federal government level, actual or filled positions are about 89 percent of the sanctioned positions, or 500,382, while in federal SOEs the ratio is 86 percent of sanctioned positions, or 450,338).

Table: Punjab provincial sanctioned positions

	FY10	FY11	FY12	FY13	FY14	FY15
Punjab						
BS 1–15	340,558	357,735	369,321	382,030	389,376	418,441
BS 16	11,322	11,981	11,986	13,058	14,724	16,233
BS 17–22	33,430	35,166	35,798	36,455	40,336	44,046
Unclassified/special grade	1,315	1,743	903	1,006	1,703	5,859
Total	**386,625**	**406,625**	**418,008**	**432,549**	**446,139**	**484,579**
% increase		5	3	3	3	9

Source: Punjab Bureau of Statistics (various years).

Federal employment

Overall at the federal level, there has been a nominal impact of devolution on the employees in Basic Pay Scale (BPS) 1–16 (in terms of decline in actual strength), due to a ban on new appointments and normal retirements, whereas BPS 17 and above showed an increase due to the transfer of officers from Balochistan and non-applicability of a ban on fresh recruitment. A majority of the employees are in BS 1–16, while around 5 percent of employment was occupied by officers in BPS 17–22.

Division-wise, the Interior Division was the largest administrative unit because of the civil armed forces—about 41.13 percent of the actual federal government strength (444,521), followed by the Railways Division (17.96 percent), Communications and Postal Services (7.77 percent), Kashmir Affairs and Gilgit Baltistan (5.60 percent), and Revenue Division (4.92 percent).

At the provincial level, the majority of the federal employees are assigned in Punjab and Khyber Pakhtunkwa (KP) (73 percent of total).

State-owned enterprises

Employment in SOEs has increased due to new projects, the regularization of services of daily wages/contract employees, the creation of new posts and fresh recruitment in few departments, such as Utility Stores Corporation of Pakistan (Pvt) Ltd., Pakistan Electric Power Company (Pvt) Ltd. and its sister organizations, including Water and Power Development Authority, Karachi Port Trust, State Life Insurance Corporation of Pakistan, Sui Northern Gas Pipelines Company Ltd., and other corporations/bodies, and so on.

The majority of staff are in BS 1–16 (about 83 percent of total strength 385,939) and there are 66,910 officers (BS 17–22) employed by 208 federal SOEs in FY14.

About 60.74 percent of the total SOE employees were working in seven corporations/bodies in FY14. These included the Pakistan Electric Power Company (Pvt) Limited with its distribution companies (36.32 percent), followed by WAPDA with 4.56 percent, the National Bank of Pakistan with 4.23 percent, and Utility Stores Corporation of Pakistan, and Pakistan International Airlines with a collective 4.22 percent. Pakistan Steel and Capital Development Authority also have a sizeable strength (7.19 percent).

Female participation

Female participation in the workforce remains low at all levels in the public sector. The quota of 10 percent female employment is not fully implemented. At the federal government level, there were 20,428 female employees (actual), which was about 4.60 percent of the total federal government strength in 2014. About 21 percent of female employees are at BS 17–22 positions.

Among the provinces, Punjab has highest share of female federal government employees (61 percent), followed by Sindh (13.87 percent), KP (9 percent), and Balochistan (4.02 percent).

In federal SOEs, females represent only 4.46 percent of the total SOEs employee strength (385,939).

Sources: Establishment Division, Annual Statistical Bulletin of Federal Government Employees (FY11 and FY14); Annual Statistical Bulletin of Employees of Autonomous/ Semiautonomous Bodies/Corporations under the Federal Government (FY11 and FY14).

Note: Data in this box may be slightly different from the above actual employees' data sourced from CGA based on annual financial reports. However, the discussion is relevant.

Promotions are largely based on seniority and the confirmation of staff on probation following appointment to the federal government on the basis of their ranking in the final passing-out examination. Staff on probation are allowed four attempts to qualify for promotion. Because the majority of employees achieve satisfactory ratings on their Performance Evaluation Report (PER), the PER has little practical value in identifying the top performers. In addition, the grade (BPS) spread at senior management level (BS 19–21) is too narrow to provide for regular turnover, meaning that staff tend to serve in the same grade for a long time before promotion. The absence of a policy on job rotation or transfers at other levels makes transfers to departments in some districts less attractive.

Leveraging Technology for Improved Public Sector Performance

The recent efforts to improve public sector performance show some promise. Specific federal-level institutions have also innovated in ways that have improved the quality of the services they offer. The public sector-run social safety program (BISP), worth billions of dollars, is an important example of the public sector's capacity to be transformational. Managed with unusual levels of transparency, the success of this program is attributable to the joint efforts of federal-, provincial-, and district-level officials in Pakistan. The NADRA, Immigration and Passports, Higher Education Commission, and Motorway Police have also shown innovative ways of improving service delivery (Ayub and Hussain, 2016).

Technology now offers new ways for improving processes. Pakistan could expand the use of information and communication technology (ICT), and harness digital dividends for service delivery and public sector management; revenue mobilization; collecting and curating data on citizens' behavior and needs; and investing in new technologies across the service delivery value chain, for example, for accounting, performance management, measuring outcomes, and communicating with citizens. Pakistan is gradually using ICT innovations to improve service delivery at all levels of government. Recent successes in curbing violence and terrorism have only been possible thanks to concerted efforts of the rule-of-law and public-safety institutions in Pakistan.

Some district governments have also experimented with innovative technologies for improving service delivery. Technology solutions have been used in diverse areas such as land revenue record digitization, disease surveillance, service delivery monitoring, and citizen feedback and satisfaction systems. The ICT-mediated Citizen Feedback Model (CFM) is established in the office of Punjab's Chief Minister in Punjab for monitoring the performance of district-level government service providers. Punjab has also launched the Connected Agriculture Platform of Punjab (CAPP) to provide agriculture-related advisory services. In the case of KP, a District Performance Monitoring Cell in the Chief Secretary's office has significantly improved the quality of service delivery at the local level through ICT-based, real-time monitoring of several key services of imminent relevance for citizens.

Improving the PFM System

Pakistan has a fairly developed infrastructure for PFM. At the policy level, Parliament has a key role in authorizing revenues, expenditures, and debts. The Ministry of Finance (MoF) plays a pivotal role in budget preparation and expenditure control. Ministries, departments, and agencies (MDAs) have well-defined roles in implementing budgets and submitting accounts for expenditures incurred. The Controller General of Accounts (CGA), with an extensive network of offices, makes payments, maintains accounts, and prepares annual financial statements. The Auditor General of Pakistan (AGP) has an extensive organization for conducting financial compliance and performance audits.

Pakistan needs to address a number of core challenges in the country's path to achieving high-income country status by 2047. These challenges are related to budget execution, cash management, external audit, and fiscal transparency. Additional problems include those related to procurement and domestic resource mobilization.

Financial Management

Budget execution still presents challenges. Pakistan does not have an Organic Budget Law. Instead, the PFM system is regulated by various sets of rules (for example, General Financial Rules, Treasury Rules, and the National Accounting Manual), which contain contradictions and gaps. For example, there is no clear requirement for budget funds to be held in the Treasury Single Account (TSA), nor any limit on in-year re-appropriations. Nor are there any fiscal transparency requirements. The MoF and most provinces do not publish in-year budget execution reports. Likewise, there is no provision for recording new commitments, cash management, or internal audits. These functions are not performed, except in some provinces on a pilot basis.

Despite the existence of a sophisticated Financial Management Information System (FMIS), payments are not automated. Instead, spending units need to provide the relevant documentation to the CGA, who then issues the payments. This process, which is known as 'pre-audit' and dates from the British colonial administration, is cumbersome and open to discretion. It also creates opportunities for unofficial payments. Expenditure reporting is incomplete, as municipal expenditures are not included in the FMIS, and development expenditure is reported as a one-line item (by project code) without a breakdown along economic categories.

The cash management regime is not sufficiently developed. The absence of a cash management system means that the various government entities have accounts in commercial banks. For example, at the end of calendar year 2017, hundreds of entities at all levels of government had accounts in commercial banks with a combined cash balance of PKR 2.3 trillion (around US$20 billion), or 7.2 percent of GDP. The number of these accounts exceeds 450,000, which makes them all but impossible to audit. These accounts are not linked to the TSA and their balances are not shown in any fiscal reports, although they appear in the State Bank of Pakistan's data on the banking sector. This practice has several negative impacts: it artificially overstates the reported expenditure, thereby inflating the fiscal deficit and leading the Government to overestimate short-term borrowing needs. Also, funds flow out of the TSA primarily when government entities transfer funds from their development budgets into their bank accounts.

Fiscal transparency remains limited, although Pakistan has declared its intent to join the Open Government Partnership (OGP) with commitments on fiscal transparency. The Government of Pakistan declared this intent in 2016, but it is yet to submit a National Action Plan (NAP). The federal and provincial budgets are published, but supplemental budgets are disclosed only at the end of the fiscal year. The federal government does not prepare in-year budget execution reports; only Sindh province does so. In the absence of accrual accounting, financial statements produced by the CGA do not include data on assets or liabilities, such as outstanding public debt and government cash deposits held outside the Treasury. Neither contingent liabilities nor government arrears are reported.

Public Procurement

There are Public Procurement Regulatory Authorities (PPRAs), as well as procurement legislation, at both the federal and provincial levels. Reports by the Auditor General review procurement practices and identify instances of violations. Overall, legal procedures are observed, not least due to the propensity of bidders who resort to the courts. Government officials are often reluctant to sign procurement documents due to a lack of relevant training and the fear of being accused of irregularities, which results in delays and frequent cancellations of procurement tenders. There are no e-procurement systems in place (except for petty purchases in Punjab province), but no procurement statistics are compiled. As a result, it is not possible to use procurement data to make strategic procurement decisions.

The federal PPRA is under-resourced and lacks the leadership to drive the necessary procurement reform activity. The lack of PPRA resourcing means poor accountability for the delivery of procurement results include meeting cost-saving targets; no center-led collaboration across federal and provincial agencies; and no oversight and support for agency procurement. Improving governance, monitoring, and oversight requires capacity within the PPRAs and a common understanding and harmony among the audit, procurement, and accountability institutions.

Domestic Resource Mobilization

Pakistan's tax system is riddled with legal loopholes that facilitate tax evasion. Government prize bonds are both anonymous and tax exempt, so they are the instrument of choice for investing funds of unexplained origin. Likewise, funds brought into the country as remittances are tax exempt and are widely used to repatriate illegally exported capital. The Benami Law—which prohibits anonymous transactions—itself remains to be implemented after passage in 2016, as secondary regulations remain to be approved. Low taxation of immovable property also provides opportunities for tax avoidance and money laundering. The recently enforced Finance Act 2018, including a tax amnesty, would likely result in substantial revenue losses. The Act offers a tax amnesty for repatriated capital, abolishes property valuation tables for capital value tax, introduces several distortionary exemptions for specific industries, and reduces income tax rates to 15 percent.

Pakistan has only 1.5 million registered taxpayers who file corporate or personal income tax returns. Despite some improvements in taxpayer information (for example, the use of a national identification number for all individual taxpayers, which allows cross-checking with databases on property transactions), such information is not used for risk-based tax audits. Instead, taxpayers to be audited are selected randomly. The lack of collaboration between the Federal Board of Revenue (FBR) and provincial tax authorities also enables tax evasion and instances of double taxation. None of the provinces levies the agricultural income tax based on income, which would hurt the interests of large landowners who are well-represented in provincial assemblies across political parties. Instead, provinces collect negligible amounts from a nominal tax on land. On the positive side, advances in automation (for example, electronic invoices for property tax in Punjab) are helping to reduce rent-seeking opportunities, while increasing compliance.

Overlapping Mandates and Weak Coordination

Poor coordination and collaboration around systems and processes inevitably result in unnecessary 'turf' issues, and hamper their effectiveness. There is a national-level anticorruption agency, the National Accountability Bureau (NAB), and four provincial anticorruption entities, which function under respective laws and rules, and report to respective provincial authorities. In addition, the Federal Investigation Agency (FIA) also investigates certain economic crimes.[7] There is a threshold (by amount) defined for the handling of corruption cases by the federal or provincial agencies (four provincial anticorruption establishments). However, the division of authority is generally unclear, and sometimes jurisdictional overlap is reported between these entities, whereby multiple authorities are sometimes found working on one case, leading to unhealthy competition. Ultimately, the federal authority takes the lead in such cases. However, under weak coordination this may lead to inefficiency and a lack of effectiveness in enforcing the law (Husain, Rana and Touqeer, 2013).

Institutional fragmentation or weak coordination is also reflected in the functioning of the country's tax system. Pakistan has one federal and three tax authorities in each province, while some taxes or fees are also collected by the respective LGs. There are multiple taxes and jurisdictional overlaps, which increase compliance and administrative costs. These overlaps also provide opportunities for rent-seeking. For instance, the implementation of GST on services in its current form leads to double taxation and potential tax conflicts. Some provincial governments tax the service at the place of the business (origin), while the same service is taxed at the place where it is used in the current form, leading to double taxation and potential tax conflicts.[8] Some provincial governments tax the service at the place of the business (origin), while the same service is taxed at the place where the customer resides (destination) by another province. In some cases, confusion (and double taxation) may arise when some supplies are treated as goods by the federal authority, while provinces treat them as services.

2.2 Challenge 2: Incomplete Devolution

Devolution has been used for political ends. Successive regimes have attempted to shape the nature of local-level governance in Pakistan (Figure 10). Pakistan's military governments have viewed LGs strategically—they relied on them for legitimacy—and used them as a countervailing force against provincial- and federal-level politicians who were associated with democratic regimes. According to Afzal (2018) democratic governments, on the other hand, have viewed LG politicians as a threat to the power of their provincial and federal elected officials. Predictably, the LGAs have recentralized power at the provincial level (other than in KP to some degree). This has undermined the full operation of the LGs, without the authority to direct service delivery, assess local needs, and ensure accountability through better monitoring by voters.

Pakistan's decentralization agenda is incomplete. The 18th Constitutional Amendment is an important first step in a series of reforms to create responsive, responsible, fair, and accountable multi-order governance in Pakistan. However, over time, critical reforms that were needed to ensure that the public sector serves the public interest and secures a common political and economic union were either not deepened or ignored altogether.

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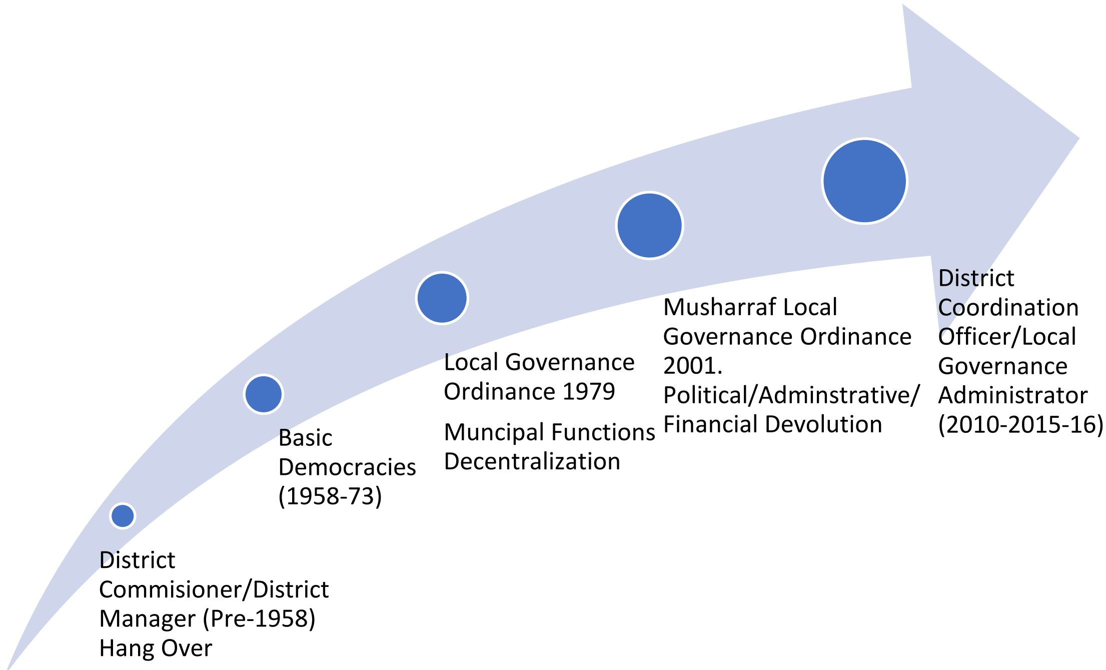
[7] In 2005, the Economic Crimes wing of FIA was merged into NAB to avoid overlap and duplication. However, later this decision was reversed. This has strained the relationship between the two institutions and weakened the process of making public office holders accountable.

[8] GST is split between goods and services, with goods being taxed by the FBR and services by provinces.

Figure 10. Pakistan's Devolution Time Line



The 18th Amendment to Pakistan's Constitution reasserted the federalist character of the Pakistani state. Among others, the amendment transferred hitherto federal functions, including responsibility for education, health, environment, and agriculture, to provinces and expanded the mandate of the Council of Common Interests (CCI) to coordinate intergovernmental relations; assigned taxing authority for sales taxes on services to the provinces; and provided the provinces with borrowing authority. Taxes on agricultural income, immovable property, estate and inheritance, and *zakat* and *usher* (religious taxes) were returned to the provinces for levy and collection. These recent efforts set the stage for provincial governments to improve local-level participation in governments and gave them a mandate to further decentralize to locally-elected representatives.

These reforms were also an opportune moment for the federal government and the four federating units to take a fresh look at their roles and mandates. For instance, the amendment not only changed the composition of the CCI but also entrusted the CCI with decision-making, monitoring, supervision, and control over matters included in the Federal Legislative List Part II[9] and related institutions. It also made the National Economic Council (NEC) more responsive to provincial needs. The NEC is expected, under the Constitution, to meet twice a year with the mandate to formulate plans on financial, commercial, social, and economic policies.

[9] This list was expanded through the 18th Constitutional Amendment to include railways; minerals; oil and natural gas; hazardous materials; industrial policy; electricity; major ports; federal regulatory authorities; national planning and economic coordination; supervision and management of public debt; census; provincial police powers beyond provincial boundaries; legal; regulation of legal, medical, and other professions; standards in education and research; interprovincial coordination; and conflict resolution.

Pakistan's LG system has been even more unstable than its central regimes. Pakistan is now in its fourth wave of decentralization, yet it is the first time that the LGAs have been passed in quick succession. However, elections were held only after a Supreme Court ruling—in Baluchistan in 2010, and in Punjab, Sindh, and KP in 2013 (Figure 10). For this same reason, while the structure for a devolved governance arrangement exists, the implementation of devolution has been sporadic, with the depth of devolution varying from one province to another in the three areas of administrative, fiscal, and political decentralization.

Administrative Decentralization

Under a system of administrative decentralization, the local levels have the responsibility to plan, finance, and manage functions decentralized by the central government. This usually includes the power to employ functionaries working at the local level and owning the overall responsibility for local-level HRM. In addition, administrative decentralization allows local levels to pass bylaws applicable within the respective territory. Here, these civil servants are expected to be accountable to the elected local leaders and citizens.

The reallocation of functions to the provinces occasioned by the 18th Amendment was expected to support the further strengthening of administrative decentralization. The reality in Pakistan has been different. In some cases, initially devolved functions have been recentralized to the provincial level. For example, in Punjab, education and health are now centrally managed at the provincial level through the District Education and Health Authorities. Without the full transfer of fiscal, political, and administrative functions to the lower levels, provinces continue to hold significant implementation powers. Provincial governments still retain powers of appointment of LG officials, the election of local-level officials along party lines, and the powers to determine district boundaries. For instance, in KP the provincial government has powers to supervise local councils, budget controls, and audits. They may also suspend council officials.

The legal environment for the operation of LGs undermines their proper functioning. All four provinces have adopted the LGAs with little consultation among provinces or direction from the federal government. These Acts tend to subordinate the LGs to the provincial governments, despite Article 140-A, which requires the provinces to establish LG systems and devolve administrative, fiscal, and political authority. The Chief Minister of the various provinces can dismiss the LG or the head of the local council. The Chief Minister also has appointing powers, thus restricting the autonomy of LGs. Stronger autonomy for LGs is needed to ensure that they are more accountable to local councils, and only in certain cases to provincial authorities.

All four provinces contain LGs that have been deprived of their constitutional powers. The mechanisms for generating revenue and the system for intergovernmental fiscal transfer through the Provincial Finance Commissions (PFC) have not been effective in resource allocation**.** Administrative powers remain subject to the discretion of provincial leaders, who remain possessive over key service delivery areas. The general inclination of provincial authorities as Shafqat (2014) notes, is to "centralize for the purposes of political expediency, rather than acting in the true spirit of the 18th Amendment and empowering local government structures".

The institutions and individuals that were to be reformed have not owned and supported reforms consistent with the spirit of the 18th Amendment. Political parties and their leaderships have done little to build faith in strengthened local-level structures. For this reason, the 18th Amendment's potential for changing the direction of the civil service has not been fully realized.

Fiscal Decentralization

Fiscal devolution in Pakistan has been elusive*.* Without fiscal devolution, LGs remain dependent on higher-tiered governments for budget allocations because they cannot adequately raise their own funds (although LGs charge business registration fees), thus largely limiting the effectiveness of devolution. The 7th National Finance Commission (NFC) and the 18th Amendment form the basis for Pakistan's fiscal decentralization. Together they significantly increased the overall share of subnational governments in the country's revenues and reestablished fiscal autonomy of the provinces in taxing and spending decisions.

The system for intergovernmental fiscal transfers was established before the 18th Amendment. The latter therefore outlined the functions to be devolved to the provinces, well after the system for fiscal transfers had already been established, i.e., the functions followed the resources. This has complicated Pakistan's fiscal decentralization. The 7th NFC Award also introduced a multifactor formula for horizontal distribution of resources to the provinces, which was amended to include not just the population share but also factors such as poverty, underdevelopment, and inverse population density criteria.

The revenue-sharing arrangement in the 7th NFC Award has complicated fiscal policy-making and changed incentives at the federal level. The Constitution now fixes the federal revenue share at a ceiling of 42.5 percent of federal tax revenues.[10] The federal share can go down, but it cannot be increased. Moreover, at around 10 percent of GDP, Pakistan is characterized by a low rate of tax revenue mobilization. This further narrows the range and effectiveness of fiscal policy instruments. Furthermore, several big-ticket vertical programs[11] within the devolved subjects (for example, the Higher Education Commission) continue to be funded by the federal share. This has not allowed provincial Higher Education Commissions to take off or function smoothly. There is a need to devise procedures for consultation between the federal and provincial Higher Education Commissions.

Political Decentralization

There are some variations across provinces in terms of further decentralization to LGs. In KP, by far the only province where progress has been made, local bodies have greater control. In KP, significant powers have been devolved down to the village council and neighborhood council levels. KP also devolves significant powers of financial management to the local levels, and empowers village and neighborhood councils to supervise officials of the LG in their jurisdiction (Shafqat, 2014). In

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[10] The federal government's share goes down even if we look at 1 percent of the net proceeds of divisible pool taxes which are assigned to the Government of KP to meet the expenses on war on terror. Second, the share of the provinces exceeds 47.5 percent when grants to the provinces, electricity and agriculture subsidies (fertilizer), and resources allocated to provincial development schemes funded under the Public Sector Development Programme are included.

[11] These programs focus in the areas of health and population planning according to the CCI decision of April 28, 2011.

comparison, Punjab and Sindh have significantly restricted the autonomy of LGs. For example, Punjab can disband the LG before the completion of its term, while in Sindh successive LG elections are not guaranteed.

These uncertainties continue to undermine the potential benefits of decentralization. Given the history of reversals and variations in implementation, LGs lose out on opportunities to strengthen local-level structures. For example, in Punjab it took 4 years between the passage of the LGA (2013) and the transfer of the budget to the newly elected LGs, which occurred only on January 1, 2017.

Devolution - A Window of Opportunity for Governance Innovations

Devolution has provided an opportunity for innovative solutions in service delivery. Some noticeable examples include enhanced participation of political decision-makers from the local level (for example, in KP), enhanced understanding of governance challenges in the local context, and a guaranteed financial allocation through the NFC. In the case of health and education, newer approaches to improving service delivery have been introduced.

Punjab has achieved results by outsourcing of the management of basic health facilities to an external operator.[12] Local-level participation in service delivery has also improved because of devolution. For instance, Parent-Teacher Committees (PTCs), critical for improving primary education outcomes, are active in several provinces. Similarly, localized development has increased through the platform of Citizen Community Boards, for example, in several districts of Punjab province. [13]

Innovations for service delivery monitoring and quality assurance have also been introduced through several versions of local governance systems in Pakistan. For example, Punjab has pioneered systems to monitor the field activities of service delivery workers (immunizers, teachers, and agriculture extension workers) through smartphones. Formal monitoring committees comprising locally-elected public representatives have played a very meaningful role in ensuring public accountability, with visible service delivery dividends.

The Right to Information in Punjab and KP Act gives citizens the opportunity to hold the Government accountable for its key functions, while related systems provide citizens with the opportunity to give feedback on service delivery. The Citizen Feedback Model (CFM) is yet another arena in which elected LG systems have proved their worth in bridging the state-citizen gap substantively. KP has also collaborated with Punjab to introduce a monitoring system for schools. Balochistan and Sindh are also using comparable systems to monitor, including teacher presence, the condition of school facilities, and community feedback.

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[12] Chief Minister's Initiative of Primary Healthcare: http://www.prsp.org.pk/Projects/Projects.aspx.
[13] http://siteresources.worldbank.org/PAKISTANEXTN/Resources/Publications-and-Reports/PakDevolutionSummary-English.pdf.

2.3 CHALLENGE 3: DOMINANCE OF STATE IN THE MARKET

The proper role of the state is to provide an enabling environment for the delivery of basic social services and for the efficient functioning of the private sector. This involves strengthening market institutions and the regulatory framework for service delivery to citizens. For Pakistan, the challenge of ensuring a positive environment for the participation of the private sector, including the strong corporate governance of SOEs, is an important element of the growth agenda. Citizens and firms bear the burden when the public sector is unable to deliver quality services on time.

The challenge for Pakistan is clear. To expand its potential for transformation, Pakistan needs to consider minimizing the presence of the state in the market, strengthening regulatory systems for private sector participation, and improving the governance of service delivery. The delivery of social services depends to a great extent on how the Government arranges priorities, including those concerning infrastructure spending. This depends, to a large degree, on the availability of proper systems for centralized planning, both at the federal and provincial levels, for devolved functions such as education and health. The public depends on the state for the provision of basic services. However, even when the private sector is involved in the provision of health, education, or water and sanitation services, the state remains a key player. As such, defining the proper role of the state is critical for maximizing the benefits to citizens.

Minimizing the Presence of the State in the Market

The federal government owns 197 SOEs,[14] with a combined output of 10 percent of GDP and combined assets valued at 43.4 percent of GDP in FY16. The portfolio includes both natural monopolies (for example, railways) and interest in sectors typically the domain of the private sector.[15] Financial support to underperforming SOEs is a major driver of the fiscal deficit and a source of substantial fiscal risks (Figure 11). In FY16, for instance, subsidies, loans, and grants to federal SOEs accounted for 32.7 percent of the budget deficit and 1.5 percent of GDP. In addition, sovereign guarantees for the SOE debt reached almost 3 percent of GDP in FY17. This support finances operational losses of SOEs, while some large SOEs that report net profits also feature among the largest recipients of subsidies and grants, most notably distribution companies and generating companies.[16] This means that, even in the fiscal years when the SOEs posted an aggregate profit, the SOE portfolio resulted in a net cost to the budget. For example, in FY15, the SOEs posted a net profit, but the Government's receipts from SOE dividends covered only 28.6 percent of the subsidies to the SOEs.

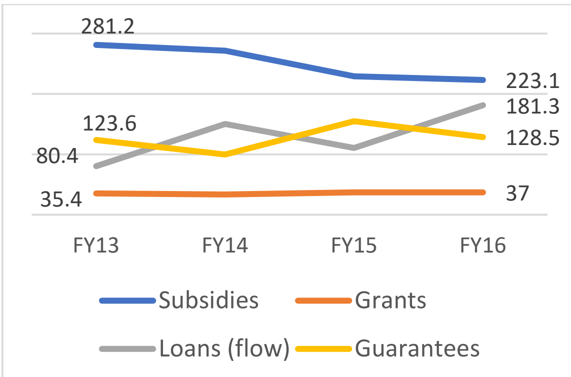
In the past 4 years, the federal government has accumulated increased contingent liabilities related to SOEs. According to data reported by the central bank, the State Bank of Pakistan, the stock of government guarantees increased by more than 80 percent in the past 5 years to reach PKR 937

[14] These include SOE subsidiaries and 45 not-for-profit entities. The SOEs have different legal structures, with public sector companies established under the Companies Ordinance being the largest with 179 enterprises. There are also 10 federal authorities and 8 development finance institutions. Only 13 federal public sector companies are listed on the stock exchange.
[15] Pakistan Steel Mills is one of the largest SOEs in the industrial sector and among the SOEs with the highest losses.
[16] See: Ministry of Finance, *State-owned Enterprises: Performance Review*, FY14, FY15, and FY16.

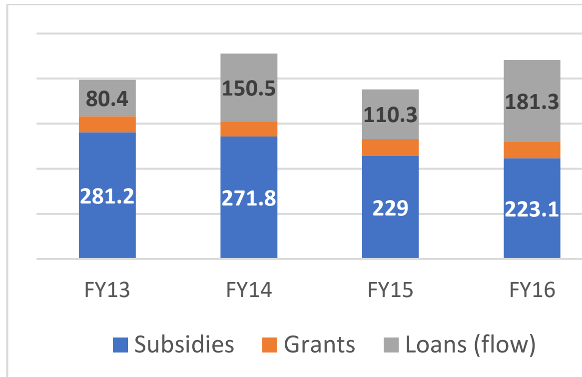
billion (2.9 percent of GDP) in FY17. The Government guarantees to cover 84.7 percent of the outstanding SOE debt liabilities, thereby providing a strong incentive for banks to issue loans to SOEs rather than to private companies. As a result, two-thirds of the credit issued by commercial banks in Pakistan goes to the public sector, depriving the private sector of the financing it needs to grow.

Figure 11. Government Financing of SOEs

Government financial support to federal SOEs (PKR, billion)



Financing from the federal budget (PKR, billion)



Source: MoF, SOEs: Performance Review, FY14, FY15, and FY16.

Pakistan's growth requires stronger market institutions, including the effective management of SOEs. Despite improvements in the regulatory framework with a new corporate governance system, the lack of a law to regulate the activities and performance of SOEs undermines effective corporate governance. Similarly, there is no policy framework on the parameters of state ownership, its role in the corporate governance of SOEs, and how the Government will implement its ownership policy. The absence of a policy framework for SOE governance has perpetuated an ad-hoc approach to the ownership and oversight functions of SOEs—as opposed to a portfolio-based approach.

The state's ownership and oversight function is currently exercised under a decentralized institutional arrangement. Legal ownership of the SOEs lies with the Government of Pakistan, but in practice the line ministries exercise the ownership and oversight function over the SOEs in their sectors. Line ministries exercise this function by appointing their own officials to SOEs' Boards of Directors—despite regulatory requirements that mandate the appointment of independent Board members (SECP, 2013). The Directors are removed at will. This arrangement gives rise to conflicts of interest between line ministries' policy and regulatory functions on the one hand, and their interests as de facto owners of the SOEs in their respective sectors on the other hand. In some instances, the ministry combines the roles of regulator, owner, and main customer of an SOE (for example in the cases of the Ministry of Communications and the National Highway Authority, or the Ministry of Housing and Works and the National Construction Ltd.).

The Government is cognizant of the need to improve the corporate governance of SOEs, but compliance remains an issue. The corporate governance rules and their enforcement by the Securities and Exchange Commission of Pakistan (SECP) have begun to put pressure on SOEs, which appear to be moving toward better overall governance practices. The recently compiled corporate governance report on Observance of Standards and Codes 2017 found that corporate governance was making progress, despite the generally low awareness of its importance. However, the SECP needs to dedicate more resources to monitor and enforce compliance with the corporate governance rules. It is estimated that less than half of all the SOEs submit declarations of compliance to the SECP and actual compliance is likely to be even lower.

Strengthening Regulatory Standards and Improving Oversight and Quality Assurance

Another important enabler for stronger private sector participation is competition regulation. The Competition Commission of Pakistan is mandated to enforce the Competition Act of 2010. The Commission, however, has been more successful in enforcing the Act's provisions on consumer protection and misleading advertising than those related to abuse of market dominance or collusion to stifle competition. Its efforts to investigate cases of suspected anti-competitive practices have been constrained by a lack of legal authority to force companies to disclose information or political influence, while its ability to enforce decisions has been suppressed by long delays in the courts' adjudication of appeals. While some economic sectors such as telecommunications are highly competitive, others such as insurance and power distribution are highly concentrated among a few operators, especially the SOEs. Anti-competitive practices are prevalent in agricultural markets, especially those dominated by large estate owners, such as in the sugar industry. These producers also benefit from extensive tax exemptions and tariffs on imported products.

Regulatory strengthening is also important, because the private sector now delivers a large proportion of social services (especially in the health and education sectors). These services were traditionally the domain of the public sector. Between 2000 and 2008, the number of private educational facilities increased by 98 and 137 percent, respectively, at a middle and high level (Table 2). During the same period, mid-school level public educational facilities expanded by 32 percent, while those at the high-school level expanded by 17 percent. At the primary level, the increase in the number of private facilities was modest, but still exceeded the increase in public services at this level.

Table 2. Number of Public and Private Educational Institutions, 1999 To 2008

Level	Type	1999–2000	2005	2007–08	Percentage of total in 2007–08	Change since 2000 (in %)
Middle	Private	12,550	24,115	24,847	61	98
	Public	12,085	14,334	15,982	39	32
	Total	24,635	38,449	40,829	100	66
High	Private	5,940	13,484	14,053	59	137
	Public	8,509	9,471	9,911	41	17
	Total	14,449	22,955	23,964	100	66
Total	Private	33,238	54,510	56,150	25	69
	Public	152,373	143,653	165,235	75	8
	Total	185,611	198,163	221,385	100	19

Source: Institute of Social and Policy Sciences (I-SAPS), 2010

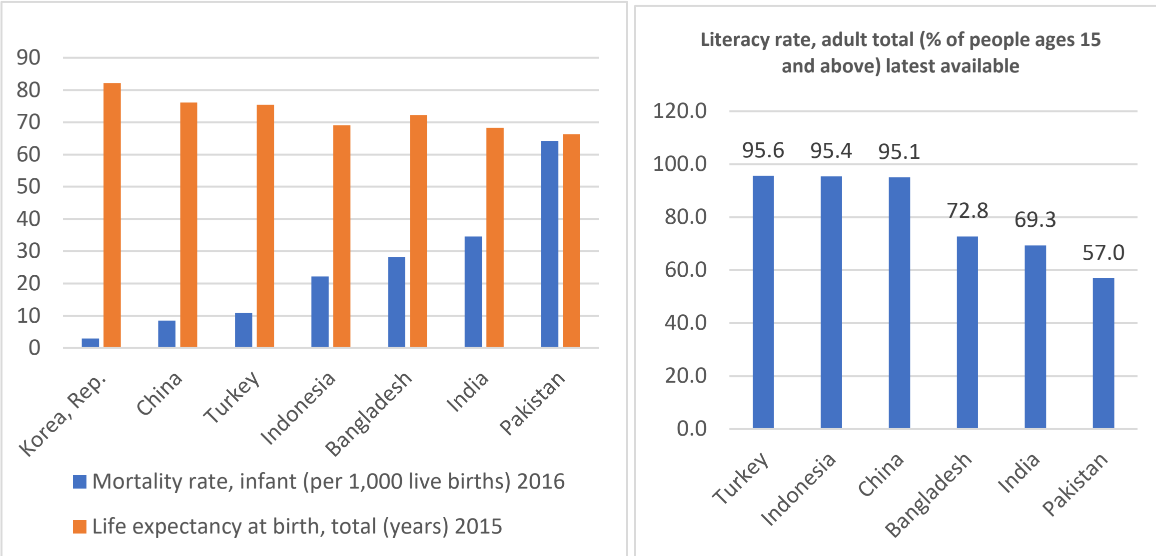
Regulation can support corporate social responsibility, and reduce inequality and conflict. Given the disparities in opportunities across the country, strong regulatory standards for the private sector and non-state providers are important. Various sections of Pakistani society are disadvantaged compared with somemore developed sections; many sections are poor in terms of natural resource endowments and solid industrial or economic growth. There is a wide range of implicit and explicit vulnerabilities, which act as a major arbiter of power-distribution and resource-allocation decisions at political and administrative levels. A new role for the public sector must be fully informed by, and sensitive to, these systemic and manifest inequalities.

The role of the state as a regulator demands strong oversight. This will also entail ensuring a level playing field for all private sector actors, operationalizing quality assurance systems, and promoting cultures of corporate social responsibility and public accountability. All of these factors will be crucial for protecting and promoting the interests of less privileged sections of Pakistani society, in view of the larger presence and role of private and commercial sectors in matters of service delivery. The Government should not undermine the positive role of private sector actors for quality and improved service delivery. At the same time, it will need to perform its central role as a regulator to minimize the vulnerability of poor segments of society and to ensure affordability and quality in the performance of private and corporate sector service providers.

Citizen-centric Service Delivery

There is no question that social services such as education, health, safety nets, water, and sanitation are essential in advancing overall human development, and a critical driver of economic growth and prosperity. Increasing investments in priority social sectors (especially health and education) can have a positive impact on the overall levels of human development in Pakistan. Pakistan has made substantial investments in education and other areas of human development, but the outcome of these investments has not been promising. Indicators of health and education outcomes remain modest. Compared with aspirational peers, such as the Rep. of Korea, Turkey, and Indonesia, Pakistan ranks poorly on infant mortality rates, life expectancy, and literacy rates (Figure 12).

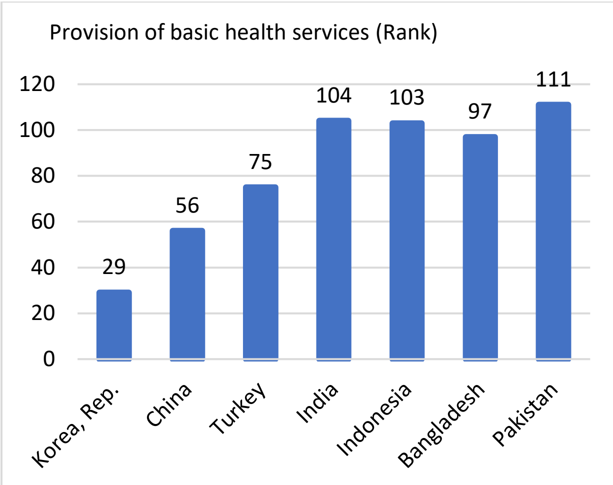
Figure 12. Human Development Indicators Are Low Compared with Its Peers



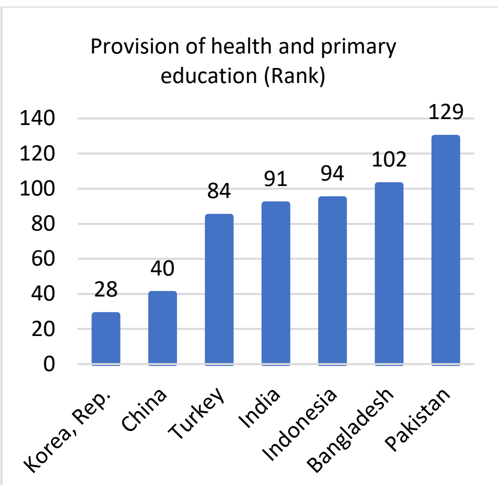
Source: World Development Indicators.

The poor quality of education and healthcare systems also adversely affects Pakistan's competitiveness. This is reflected by its ranking on the education and health indicators—known as the 'basic requirements' provided by the GCI (Figure 13). On both indicators, Pakistan is ranked worst among its peers and poorly in the world. Out of 137 countries for which the data are available, Pakistan is ranked 111 on health provision (basic requirement) and 129 on health and primary education (efficiency enhancers). These numbers call for immediate action on the Government's part to reform its institutional and governance framework to improve service delivery, either directly or through alternative service delivery methods, such as public-private partnerships (PPPs).

Figure 13. Pakistan Ranks Low on The Provision of Basic Services and Services That Enhance



Efficiency



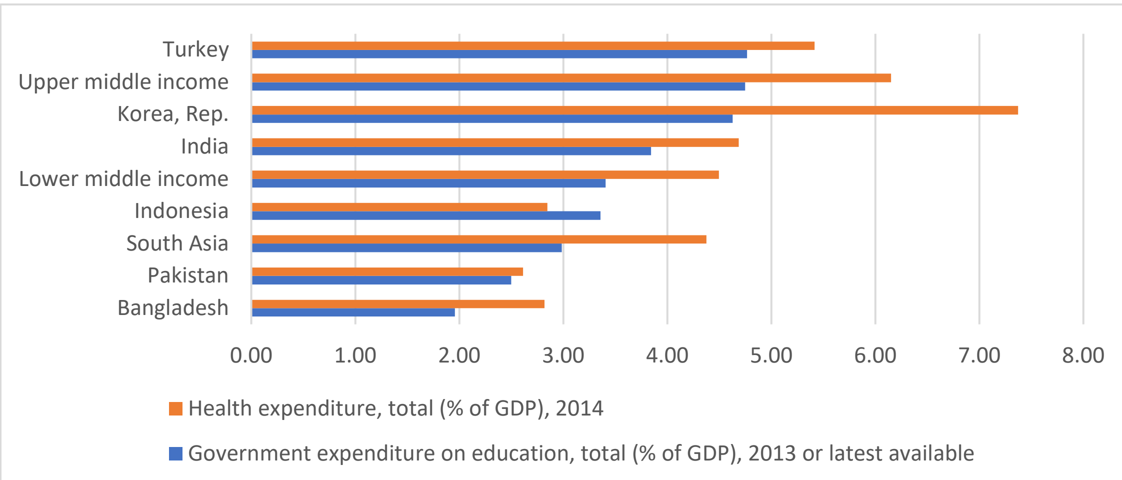
Source: Global Competitiveness Report (2018).

Governance issues are at the core of the lack of satisfactory outcomes in investments in social service delivery. The governance challenges in the delivery of education and health services are similar to the challenges in other areas of service delivery, such as water and sanitation. Governance issues include accountability, financing and expenditure decision-making, together with accountability for service delivery, equity, quality, and efficiency. Poor prioritization in spending—that is, a preference for large infrastructure and defense overspending in social services—is both because of political-economy factors (for example, relations with India and regional security) and an accountability system that prioritizes patronage over efficient policy-making. Pakistani politicians prefer to spend on visible projects such as roads over investments in social services, whose results take longer to demonstrate.

Financing and Expenditure

In FY16, Pakistan spent about 1 and 2 percent of its GDP on health and education, respectively (Figure 14). In this area, Pakistan compares unfavorably with other countries in terms of spending. This is perplexing given that, at the political level, at least as captured by the Constitution, there is agreement on the need to provide education for all children (Shah, 2012). The Government's target of 4 percent of GDP has been elusive (Malik and Rose, 2015). Factors contributing to low expenditure in the social sectors are several, including squeezing fiscal space and greater emphasis on physical and infrastructure development, among others.

Figure 14. Education and Health Expenditure for Pakistan And Comparators



Source: World Development Indicators.

The situation is not much different in the health sector. Public sector facilities are not capable of providing the requisite level and quality of health care to most ordinary citizens. Pakistan's overall performance on key healthcare indicators is low. The burden of disease and other allied health sector challenges appear to be beyond the capacity of what the public sector can handle. Added to these are a plethora of governance challenges in running primary and secondary healthcare facilities, such as: delayed procurement; the paucity of essential medicines; weak links with public health and water, sanitation, and hygiene (WASH) sectors' systemic inefficiencies; and corrupt practices.

The utilization and expenditure of allocated resources is also a concern. Of the total education budget allocated to the provinces, the expenditure ranges from 79 to 96 percent. Furthermore, the major share of the allocated education budget for all provinces goes to a recurrent budget. All provinces allocate over half of their education budgets to recurrent spending, leaving only a small portion for the development budget. Of the development budget, the percentage spent against allocation is relatively low in all provinces other than KP.

Table 3. Total Education Budget by Province

Province	Education budget allocation (% of total budget)	Total education budget (allocation); million rupees	Total education budget (expenditure %)
Punjab	20	286,505	79
Sindh	20	147,877	82
KP	25	119,721	96
Balochistan	20	48,345	95

Source: Provincial budget documents.

The landmark 18th Amendment, among other things, declared health and education an exclusive domain of provinces by abolishing the concurrent list from the Constitution. Alongside this functional reallocation pertaining to the social sectors, the 18th Amendment in FY11 also resulted in the expansion of the resource envelope for provinces. However, these positive constitutional developments appear to have not reversed the trend of assigning a lower priority to health and education sector spending from the Government's own resources.

Management and Accountability

Absenteeism is an important governance challenge in service delivery in both the health and education sectors. In KP, for instance, a survey by SDPI (2014) found that teacher absenteeism affects the decisions of parents to send children to government schools. Similar problems are reported with regard to healthcare facilities. Citizens reported the absence of health workers and long queues in hospitals—largely due to absenteeism. Teacher absenteeism has an impact on student absenteeism and learning outcomes, and is also a factor in the number of school dropouts. Similarly, doctor and healthcare staff absenteeism leads to lower demand and utilization of healthcare facilities, and leads to poor health outcomes. Other factors that adversely affect learning and health outcomes include: the high turnover rate of the service delivery providers at the implementation level, as well as turnover at the management level; a lack of staff, especially in remote or rural areas; and management/leaderships that are not familiar with service delivery.

Private Provision of Social Services

Given the earlier scenario, the role of the public sector in social service delivery is important. The private sector is assuming an increasingly pertinent role in service delivery in both the education and health sectors, given increasing population, public sector inefficiencies, weak institutional framework, political uncertainties, and weak devolution regime (at the district level). Vast numbers of privately run schools and private healthcare facilities have spread throughout Pakistan, both in urban and rural areas.

In a country where school participation remains low, Pakistan's private schools play a prominent role in accelerating participation in education. Private school provision of education has seen a momentous shift in the overall increase in school participation. It is especially high among students ages 6 to 10, and 11 to 15, where one-fifth of children in this age group attend private school. This is one-third of all the children who go to school in Pakistan (Nguyen and Raju, 2014).

Participation has also improved among students in Punjab, KP, and Sindh. The implications of private sector provision of school education are enormous for women and low-income families, as higher education has become readily accessible (World Bank, 2018b).

This desire for private provision of education and health care is indicative of the inability of the public sector health and public education facilities to cater to the basic needs and demands of citizens. It also reflects the Government's unwillingness or inability to continue making the necessary investments in these crucial social sectors. It is therefore no surprise that, despite several sector improvement programs in health and education, conditions in most of these facilities remain far from satisfactory. School infrastructure is still far from ideal and coverage remains minimal (World Bank, 2018d). The education sector faces the challenges of missing facilities, insufficient day running resources, gaps in teachers' capacity, and weak governance systems for monitoring and accountability.

The reality of the quality of service provision and the availability of resources for improved investment in education and health, and in their management systems, call for rethinking the Government's role in providing social services. It is also a reality that the complexity of demographic challenges in Pakistan and the highly contested political-economy of resource allocation decisions will make social service delivery increasingly challenging in the coming years. The Government cannot abdicate its duty to provide public goods such as education and health services. However, it can create an enabling environment to facilitate private providers, without disadvantaging citizens who cannot afford such services. The Government will need to find a balance between public and private sector rationales for satisfying the ever-increasing, high-quality service delivery aspirations and expectations of citizens. In this respect, the Government will need to ensure that such a system does not exarcebate existing inequalities.

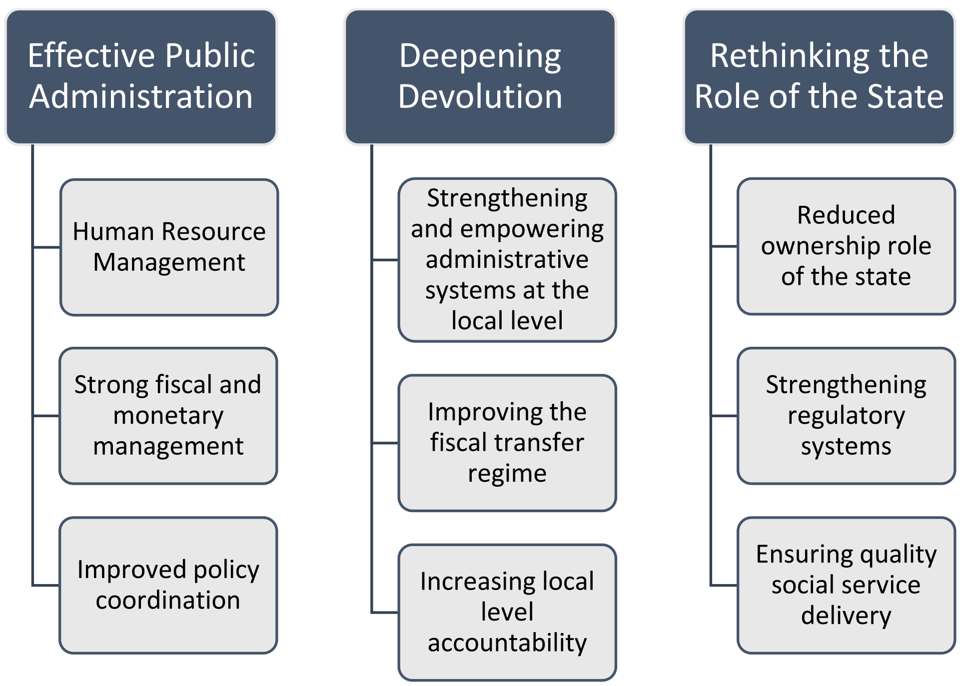
Oversight and Quality Assurance

The state is obligated to ensure quality service delivery and set the quality standards to maintain quality control of both state and non-state providers of services. The proliferation of private providers of education and health services necessitates a greater need for stronger quality control and standardization of the delivery of social services. Devolution of the health and education functions to provinces now make this issue even more prominent. It is also a reality that resource constraints and competitive resource demands from multiple sectors have greatly reduced the Government's ability to invest in health and education sector facilities across the country. The Government's regulatory role has assumed extra importance, with most provincial governments taking over several of the hitherto devolved functions in service delivery. Independent and professional regulatory and quality monitoring systems and institutions are placed as part of the Government to oversee service delivery standards both in public and private sectors. These may include the development of, and monitoring adherence to, minimum service delivery standards, citizen feedback systems, and public accountability and transparency dispensations.

CHAPTER 3: POLICY DISCUSSIONS – HOW TO ADDRESS THE CHALLENGES

To prepare Pakistan for high-income country status, a new ethos of public service will need to be established. This will require a shift in the behavior of civil servants, organizational culture, the tools of trade, and the aspirations of government employees. In this sense, three pathways are applicable (Figure 15). The first is a revamping of the public administration system to make it more effective and efficient, the second is deepening devolution to strengthen administrative and fiscal structures that support devolved functions, and the third is reassessing how the state can function to support the market and improve service delivery. The following pargraphs detail these three pathways.

Figure 15. Three Governance Pathways to Growth and Development of Pakistan



3.1 Pathway No. 1: Improving the Performance of the Public Administration System

Modernizing Public Administration Systems

Policymakers need to conceive and implement a program of rejuvenating the public administration system in Pakistan. This will entail restructuring the federal government and rationalizing the tier management levels to improve efficiency. There is also a need to modernize the way in which bureaucracy works—from policy formulation, coordination, implementation, and execution to service delivery roles. These changes in the working of the public sector will need to be catalyzed through increased reliance on IT and modern technology for facilitating informed decision-making and quality service delivery. Capacity-building measures for civil servants should be designed to cater to skills that are currently missing in the public sector, including those that could enable the development of a digital economy, climate change and adaptation, data analytics, and robotics. In addition, the Government could consider introducing lateral-entry intake for senior-level government positions to allow for the recruitment of outside professionals with specialized skills. This would have to be done carefully to manage internal resistance.

Strengthening Human Resource Management (HRM)

A related area is the revamping of the HRM system to respond to the needs of a 21st century civil service. The entire HRM apparatus, including recruitment, in-service training to career progression, remuneration systems, performance management, and accountability, will need to be transformed in line with the aspirations of Pakistan to become a high-income economy. This will entail strengthening the Public Service Commission at the federal and provincial levels in terms of appointment of their members (highly professional and qualified in human resources selection, rather than number of years of service or political favorites) and support staff, and making them more independent in functional and financial matters. For example, to improve performance management, the Government could consider revising the system of annual confidential Performance Evaluation Reporting by introducing a modern, IT-based performance assessment and appraisal system for civil servants, with the possibility of introducing performance-based contracts.

Reskilling the Civil Service through Targeted Training

Training programs will need to be restructured to introduce tailor-made improvements in technical capacities among various cadres and work streams of civil services. The bureaucracy (federal, provincial, and local level) would need to become more professional, innovative, and fully capable of taking strategic- and evidence-based decisions to resolve public sector performance and service delivery challenges. Intra-service rivalries and turf wars among various cadres of civil servants will need to be eliminated through a system of positive reinforcement and the right incentive structure, and by introducing competitive examinations for all services for grade 21–22 jobs.

Revisiting Training and Capacity-building Approaches

Rethinking in-service training and capacity-building programs for civil servants will be needed to realign the skills sets of government employees with the demands of the economic transformation. One way to improve training for better public administration is to strengthen the federal civil service's specialized training institutes to offer domain-related training to enhance technical knowledge and skills. This includes provision of qualified trainers and the development of domain-related, demand-based training courses, making the completion of some courses mandatory requirements for promotion. To improve training, the Government could consider redesigning the pre-service and in-service training regime for civil servants by linking performance in training institutions to rapid career progression. Training should focus on government officials who are at grade levels BS 16 and below, given the largest concentration of staff with lower capacity. Training should inculcate technical capabilities among civil service cadres on the use of technology in management and decision-making in the public sector, and emphasize on-the-job training for continuous learning.

Bringing in New Skills for Economic Transformation

The Government could consider reskilling the civil service to be a driver of economic transformation. The program could be based on the requirements of a government program aimed at economic transformation in partnership with the private sector. Such a reskilling program should be designed to address at least three additional capacity gaps that typically exist in most civil service cadres in Pakistan. These include the 'technology and IT skills gap', the 'skills gap to complement economic transformation', and the 'skills gap on people-centric service delivery outlook'. Taken together, these three systemic, capacity gaps are largely to blame for below-par performances among public-sector functionaries. They have a role to act as catalysts and agents of economic transformation to fast-track equitable growth and citizen-centric social development in Pakistan. To do this, the Government will need to focus on investment in strategic skills and tools for a new economic paradigm.

Expanding the Use of Technology in Public Administration

Expanding the use of technology to improve the performance of civil servants and engage citizens is a priority. In this process, recent experience in the provinces provides a useful template for further mainstreaming technology and emerging digital tools (for example, artificial intelligence and machine learning) into the practice of public sector management. ICT could be expanded to: harness digital dividends for service delivery improvement and efficient/smarter public sector management; for collecting and curating data on citizens' behavior and needs; and for investing in new technologies across the service delivery value chain, for example, for accounting, performance management, measuring outcomes, and communicating with citizens. The Vision 2025, drawn up by the Government of Pakistan, emphasizes a focus on the procedures and rules, which are at the core of any effective e-governance program. It is crucial to address issues of sustainability, interactivity, and standardization of e-governance activities, if the public sector in Pakistan intends to modernize the systems and procedures of governance through modern technology. The approval of the Digital

Pakistan policy provides a new opportunity for scaling up new initiatives in the use of technology for the business of government.

Modernizing PFM

A modern PFM system is required to efficiently allocate resources. To begin with, there is need for a legal framework with sufficient guidelines to support the efficient collection and use of public resources. Such a framework would also make provisions for the use of ICT to improve efficiency and value for money, especially in procurement and PFM. To improve transparency, efficiency in public procurement, and the predictability of public expenditures (by aligning planning systems with expenditure), the Government should consider introducing e-procurement systems. The National Financial Management System is already available and could be used as a platform for e-procurement. To drive a step-change in procurement performance, each of the PPRAs should be given a stronger leadership role for procurement. Without a center-led procurement function, coordination of long-term procurement reform, and the resulting benefits, will remain fragmented and ineffective. The procurement expenditure-to-GDP ratio in Pakistan is estimated as 19.8 percent (PIIE, 2016). Therefore, the potential of procurement reform as a growth driver is significant. Harmonization of procurement rules and procedures, both federally and provincially, including future proofing of the legal framework to support technological innovation, will improve transparency and competition, and reduce transaction costs. Making use of e-procurement technology such as e-Procurement, FMIS, open data, and big data (consolidated category management across the Government) that is interoperable will improve procurement oversight and the overall efficiency and economy of the procurement function. Without such systems, the ability to identify and coordinate strategic procurement opportunities is limited. Recently, the Agriculture Department of the Punjab has launched a web-based procurement management information system which, if successful, could be replicated in other procuring agencies, and provincial PPRAs can consolidate this information to produce an annual report.

Expanding the Tax Base

A growing Pakistan will need to expand its tax base to raise the resources required to finance the increased demand for social services and infrastructural investments. Pakistan collects its tax from a very small tax base. To improve revenue collection, the Government needs to prepare and adopt a medium-term revenue mobilization strategy. Such a strategy will need to include important policy directions regarding the rationalization of exemptions, which distort the tax regime. The Government will also need to enforce tax compliance to ensure that all eligible taxpayers meet their obligations. A related and important aspect of improving the tax base is the urgent need to restructure the FBR to align its structures with a devolved environment and provide it with the relevant organizational strength to meet the agreed revenue targets. This could include further strengthening of the FBR’s autonomy and oversight, assigning revenue targets, and establishing a National Tax Council. Further actions to streamline the tax collection mandates of the federal and provincial governments would help to clarify the jurisdictional conflicts around General Sales Tax on goods and services (GST).

3.2 PATHWAY NO. 2: DEEPENING DEVOLUTION

Revisiting the 18th Constitutional Amendment

International experience emphasizes that decentralization fails when it lacks a clearly stated overarching objective. While Pakistan might have followed the implicit objective of assigning a dominant role to provinces in service delivery and bringing decision-making closer to its citizens to enhance accountability under the 18th Constitutional Amendment, these objectives need to be made explicit. The design of any decentralized system, including expenditure, tax and revenue assignments, as well as the transfer of functions and tax instruments, depends on the agreed objective of the reform process.

The 18th Constitutional Amendment provided a new opening for strengthening local-level participation in governance. Additional efforts are necessary to expand the opportunities provided by the 18th Amendment is the next most important policy measure. Devolved governments tend to ignore different sets of stakeholders at the cost of politically-driven prioritizations, which is something that needs to be hedged against, by identifying innovative avenues of engaging multiple stakeholders—urban population, rural communities, entrepreneurs, small-scale farmers, and private sector leaders—to ensure equity. Further devolution could provide avenues for prompt and more informed responses to the challenges of social and municipal service delivery, such as infrastructure and service delivery investments. This will, in turn, provide the enabling environment for attracting large-scale investments for growth and development in the country.

Further Devolution of Functions and Financing

In the short to medium term, a few areas of concern will be critical. First, the balance of powers and authority between the federal and provincial governments will need to be carefully calibrated. Political agenda-setting, macroeconomic policy-making, and implementation roles need to be creatively conceived and agreed upon, so that the functions are placed at the most appropriate level of government and supported by proper financing. Under this arrangement, the federal government will need to play its role in ensuring equitable development and balanced growth for the collective and inclusive benefits of all sections of the citizenry and geographical regions.

Strengthening Capacity of Provincial Employees

There is a need to rethink public sector processes and the capacities of civil servants at all levels. It is important to align these processes with the mandated roles of the various tiers and sections of the Government. Civil servants will need to look toward democratically elected political leadership for strategic agenda-setting and policy formulation, while performing their constitutional mandates of offering policy options and ensuring smooth and high-quality execution of political vision and manifestos. Related to this is the need to ensure constitutional protection of tenure and conditions of service for civil servants, as provided under the 1956 and 1962 Constitutions. In addition, there is need to establish district and provincial cadre services to cater to career management of staff employed by provinces and districts. This also calls for civil service reform at all levels of federal, provincial, and local governments.

Strengthening the PFCs

Strengthening the Provincial Finance Commissions (PFCs) and articulating their relationship with LGs will help to strengthen local-level autonomy. The PFCs must empower LGs in matters of finance, resource allocation, and revenue collection. In this vein, strengthening devolution will require greater emphasis on financial autonomy of LGs, both through a determined mechanism of transfer from the top (provincial government) and through expanding their capacity to generate funds locally. In addition, efforts must be made to ensure effective coordination (across all tiers of government) on key areas such as taxation, regulatory environment, agreement on national standards, and strengthening the role of LGs as the primary agent for service delivery. The new PFCs would ensure that decentralization and equalization of fiscal resources go beyond the provincial level, and reach the poor and marginalized areas within their jurisdictions. Thus, there is an immediate need to update the PFC Awards across all provinces.[17] The new criteria should be based on the most recent national population census and the distribution criterion expanded to include other relevant indicators, such as poverty. Poverty data should also be updated on a regular basis—at least every 2 years to capture variations in and changes over time.

Improving Local-level Accountability

Local-level accountability will be useful in strengthening the social contract by giving citizens an opportunity for voice and participation. This could be achieved by training locally-elected officials to improve their awareness of how the Government functions. The existing training institutions of provincial governments could be streamlined and their curriculum and modes of training be upgraded and modernized for this purpose. Additional opportunities could be used to create openings for local-level deliberation to promote community-based democracy through consultation, deliberation, and participation in decision-making (e.g., through feedback mechanisms). Furthermore, the Government should focus on establishing a binding legal framework of fiscal responsibility that ties all levels of government to macroeconomic stability targets and eliminates arbitrary powers of the executive to adjust taxes and duties. This should come together with minimum service delivery standards at the local level, and the introduction of output-based financing that ensures monitoring of results, compliance with minimum standards, and performance accountability to citizens.

Strengthening the Key Organs of Devolution for Improved Coordination

To make decentralization useful for Pakistan, a key step should be to develop a common vision of decentralization to be achieved through improved coordination (at all levels of government). The Council of Common Interests (CCI) is the main coordinating forum under the 18th Amendment to the Constitution. It generates regular interactions between the provinces and federal government on an equal footing. However, it must be strengthened to establish its leadership role in

[17] Provinces redistribute revenues among lower tiers of the government, through a revenue-sharing formula known as the PFC.

not just resolving intergovernmental disputes arising from the devolution process, but also in shaping the decentralization agenda. As the national dialogue must be an ongoing exercise, it is crucial that the constitutionally prescribed permanent secretariat of the council is established.

Revising the Fiscal Transfer System

The current NFC Award system should be revised so that it is more aligned to the changing development needs of the provinces and population dynamics. The design of any decentralized system, including expenditure, tax and revenue assignments, and the transfer of functions and tax instruments, depends on the agreed objective of the reform process. For Pakistan, having agreed on the vision for decentralization outlined in the 18th Amendment, the next step should be to outline clear and mutually agreed upon principles for the division of responsibilities, and to rethink how funding arrangements through tax devolution, grants, and subnational revenue collection will address this division of responsibilities. Such a process would also delineate how the burden of financing joint responsibilities will be shared between the provincial and the federal levels, to ensure that decentralization does not undermine macroeconomic stability. This will require revision of the current NFC Award system and a road map for assigning functional responsibilities for the implementation of decentralization.[18]

3.3 PATHWAY NO. 3 RETHINKING THE ROLE OF THE STATE IN THE MARKET AND SERVICE DELIVERY

The Government must identify SOEs that should be privatized and ensure the completion of the privatization process in a transparent manner within the assigned timeframe. Corporate governance reforms are no substitute for privatization; they should serve to improve the prospects of the entity to be privatized. To build public confidence, privatization needs to be transparent. Given the complex stakeholder map, meaningful dialogue and communication are key between all the relevant stakeholders (MoF, Privatization Commission, line ministries, regulators, employees, unions, media, judiciary, citizens, and so on) to create the necessary buy-in and understanding. Equally important is the need to understand and integrate the privatization of selected SOEs within the broader reform agenda of the sector in which they operate. The quality of the pipeline is also significant and needs to be prepared strategically.

[18] This tug of war over resources leads to zero-sum games and the resulting swings in the balance of powers within nations is a perpetual feature of dual federalism model. Pakistan manifests these tendencies as is evidenced by the past negotiations on NFC Awards (Shah 2012).

Establish a Legal Framework for Government Ownership

It is crucial to have a clear, coherent, and modern legal and regulatory framework for the state as the owner and shareholder of the SOEs. A State-owned Enterprises Act, or an equivalent law, is needed to clearly establish an ownership policy that defines how the state, as owner, governs its SOEs, thereby laying down clear criteria for subsidizing SOE activities and extending financial support to SOEs.[19] A more centralized institutional arrangement for SOE portfolio management is necessary for consistent policy implementation. For the best results, the entity responsible for the SOE portfolio should have a strong mandate to make decisions based on commercial criteria to maximize portfolio value and return-on-equity for the Government.

To bring down fiscal costs, the Government needs to continue efforts to corporatize the SOEs. The SOEs should be required to prepare business plans. Restructuring will reduce fiscal costs if the newly appointed boards and management are effective and if corporatization brings the entities under the same law (the Companies Ordinance) and under one regulator (SECP), thus ensuring a level playing field for the private sector. These measures are in line with OECD guidelines recommending that governments simplify and streamline the operational practices and legal form under which SOEs operate.

Establish an Entity to Manage SOEs

Designating a central entity to manage the SOE portfolio is a key step toward implementing a portfolio approach to SOE ownership. This could be an existing or a new ministry, government agency, or—under the centralized model—a holding company. The mandate of this entity could include the following functions:

- Monitoring and reporting on the financial performance of individual SOEs and aggregate reporting on the financial performance of the SOE portfolio.
- Monitoring fiscal risks associated with SOEs' explicit and implicit liabilities; monitoring SOEs' compliance with relevant laws and regulations.
- Developing a performance framework for SOEs in collaboration with line departments. Such a framework would include indicators of financial and operational performance and could be implemented through annual performance agreements/Memoranda of Understanding signed by the Government and SOEs' management, and so on.

Appoint Independent Management Boards for SOEs

It is imperative to separate the Government's role, as owner, from its role as policymaker, coordinator, and regulator. The Government should refrain from becoming involved in the day-to-

[19] Typically, an SOE Act requires the SOEs to be commercially oriented; the SOEs to be forbidden to expand or contract the scope of their activities without government approval; the SOE obligations to provide timely financial and management information; guidance on dividends; clear delineation of the roles and responsibilities of the government, boards, and management; and processes for appointing Boards of Directors.

day management of SOEs and should allow SOEs full operational autonomy to achieve their objectives by professionalizing SOE boards and holding them accountable through the development of a proper performance monitoring and evaluation system. Appointing and monitoring the boards is integral to monitoring ownership. As the owner, the Government is accountable to Parliament, and it needs to appoint directors capable of meeting the owner's expectations, following a skills-based appointment process with majority of independent directors. Anything less—such as patronage or representation—diminishes the skills on the board. There should be a well-structured and transparent board-nomination process. The boards, once appointed, should be allowed to exercise their responsibilities independently.

Strengthened Market Institutions for Private Sector Participation

To create the enabling environment, the Government will need to enforce adherence to improve transparency and adherence to the rule of law. This will require enforcement of property law and contractual rights, the control of corruption, and the development of an appropriate regulatory framework. A strong legal framework will also increase the ability of prospective private suppliers to compete fairly for tender biddings in public procurement. A stronger environment for business will also require improvements in bureaucratic quality to ensure the availability of administrative capacity to draw up, negotiate, and monitor contracts in an impartial and non-corrupt manner, and to ensure that they operate in the public interest, while maintaining independence and avoiding conflicts of interest or regulatory capture. In the long term, a well-designed consultation program can be set up with the private sector based on a sound policy on PPPs. The Government would still retain a supervisory role in ensuring that the private sector continues to meet its social obligations.

Improving Social Service Delivery

To improve the confidence of citizens in the state, the Government will need to strengthen service delivery. This will require expanding spending in health and education, and ensuring equitable distributions of resources to cover hard-to-reach areas. To improve performance, the Government could introduce a performance monitoring system for service delivery, while using targets to hold managers and providers accountable. The introduction of technology for service delivery in the provinces provides a good template for rolling out ICT for service delivery across the rest of the public sector. For this to be successful, civil servants will need to be encouraged to adjust to innovative modes of service delivery. Innovative partnerships with the private sector will be needed to augment public sector financing for service delivery. This could be completed with new modes of service delivery, such as PPPs, outsourcing, and contracting delivered with high quality and efficiency. It is critical to clearly demarcate how much the private sector can be involved in the provision of services. This would have to be supported by a strong regulatory framework to ensure quality assurance. To improve service delivery, an additional remuneration package could be introduced for key positions, and remuneration should be pegged to performance in service delivery.

Developing Service Delivery Standards

To meet Pakistan's human development challenges, minimum service delivery standards (at least for key sectors) need to be established, while acknowledging the substantial variation in development outcomes across provinces. Such standards are more likely to be accepted if they are jointly negotiated and agreed between provinces and the center (for example, as in Australia), whereas unilaterally imposed service standards have often proved to be unrealistic or unaffordable. Pakistan could thus establish intergovernmental councils at the sectoral level under the umbrella of the CCI to set such standards; ensure coordination between the policy formulation, budgetary, and implementation processes; and allow for flexibility to reflect the differences in devolution across sectors (for example, as in Germany). Following the development of service delivery standards, a technocratic body should monitor development outcomes and validate compliance with service delivery standards. Monitoring of performance in relation to the agreed targets (for example, Human Development Indicator goals) can act as an incentive, even if transfers to the provinces are not directly tied (for example, as in Australia) by building healthy competition between provinces. A suitable body for this endeavor would be a non-political council consisting of technical experts to monitor human development outcomes in relation to the agreed goals, and bring biannual monitoring reports into the public domain, for example, through presentations to Parliament.

Strengthening Performance Monitoring Data

Ensuring that compliance with service delivery standards and sustainable improvements to service delivery are facilitated through the availability of reliable statistics. Key data requirements include information on fiscal flows from the center to the provinces, provincial fiscal and economic statistics, and information on service delivery performance. Such data allow for monitoring, benchmarking, and estimating service delivery costs. In addition, it facilitates citizens' ability to hold service providers and local as well as provincial governments accountable. Improving the data environment for service delivery statistics could begin by strengthening Pakistan's Bureaus of Statistics and provincial bureaus of statistics by broadening their mandate to include data collection related to provincial fiscal, economic, and service delivery performance and their staffing. Strengthening these departments' capacities and ensuring their cooperation throughout the data-generating process ensures that statistics are collected using a common methodology, and that the statistics and results are made available in a common layout.

Social Accountability, Voice, and Participation

There are three relationships around the delivery of public services. These include between the poor and vulnerable and providers, between the poor and policymakers, and between policymakers and providers (World Bank, 2004). Increasing poor clients' choice and participation in service delivery will help them monitor and discipline providers. Raising poor citizens' voice, through the ballot box and widely available information, can increase their influence with policymakers, and reduce the diversion of public services to the non-poor for political patronage. By rewarding the effective delivery of services and penalizing the ineffective, policymakers can ensure that providers serve poor people better.

Information-sharing and Grievance Redressal

Information-sharing, transparency, and grievance redressal are key aspects of social accountability. With better information, the community and citizens can demand better performance. Transparency in government processes, budget allocation, and actual expenditure allows citizens and the state to make more informed decisions. Along with improved information-sharing and transparency, the mechanism for grievance redressal must be strengthened, together with legal, economic, and political space for people to raise their demands and grievances. Immediate measures that could be implemented to strengthen transparency and accountability include, for instance, the development of Right to Information legislation at the federal level obligating mandatory disclosure of certain kinds of information held by the Government.[20] The Government could also establish a requirement to share information with the public about the performance of key service delivery sectors, such as education and health, and measures to hold poor performance accountable. And to improve fiscal transparency, the Government could facilitate the timely disclosure of budget information, including quarterly budget execution reports; annual financial statements, including data on public debt and contingent liabilities from sovereign guarantees; external audit reports by the AGP; and audited financial statements of SOEs.

Quality Assurance and Monitoring

Private schools remain self-governing and unregulated. The existing regulations[21] on private schools do not define the terms and conditions for geographic distribution or establishment in any specific area and, therefore, the infrastructure and fees determine the location. Nguyen and Raju (2014) find that although the existing legal and regulatory frameworks include registration, curriculum, academic standards, length of school year/days, and recordkeeping/reporting tuition and fees, teacher employment terms (including pay), teacher qualifications, and availability and quality of facilities, these regulations are not enforced.

Given the multiple governance challenges in service delivery, there is a need for a holistic approach with key elements complementing each other. The Government has to provide a strong legal and regulatory framework, within which the private sector can perform, while the clients or the citizens receiving the services have to be empowered with information and avenues for addressing their demands and grievances. The involvement of the private sector in service delivery is a given. However, without proper oversight and quality assurance, and a regulatory framework provided by the state, the quality and reach of service delivery will be hampered. Citizen monitoring and involvement can improve service delivery—no matter who is delivering the service.

There is a need for an overarching institutional improvement. The state's capacity to regulate and provide quality assurance is lacking. Institutional capacity building at the federal, provincial, and

[20] Several provinces in Pakistan now have a Right to Information legislation.

[21] Islamabad Capital Territory Private Educational Institutions (Registration and Regulation) Act 2013; KP Registration and Functioning of Private Educational Institutions Ordinance 2001 and Amendment 2002; Punjab Private Educational Institutions (Promotions and Regulations) Ordinance 1984; Sindh Private Educational Institutions (Regulation and Control) Ordinance 2001, and Rules 2005.

district levels is essential, especially with regard to financial management. Own-source revenue generation is needed, together with better management and coordination of external resources.

3.4 Addressing Political Economy Challenges: Elite Capture, Geopolitical Threats, and Political Settlement

Governance failures are of two major types in Pakistan. The first set of challenges result from political factors—both internal and regional. Geopolitical factors, for example, relations with India, affect the choices Pakistan must make such as whether to prioritize investments in pro-poor policies or defense. On the other hand, internal political economy factors, such as the relationship between the provinces and the federal government undermine a drive toward greater efficiency, meritocracy, and innovation. The second set of challenges result from technical decisions and should be more amenable to technical solutions. For example, the structure and workings of the civil service and the inefficiencies in the PFM systems could be addressed by applying technical solutions. Nevertheless, both types of challenge require some form of political will and strong endorsement by political actors.

Pakistan is familiar with these circumstances. Several recommendations have been highlighted to address governance deficiencies without successes. The next few years will require a new approach to ensure that growth-enhancing reforms are initiated and fully implemented. To ensure that the proposed reforms are implemented and that the Government sustains its journey on the reform path, it will need to address key political economy factors that consistently undermine reforms.

Building a Coalition of Reformers

Thoroughly diagnosing the problem, quick implementation, and learning-by-doing have been identified as good practice principles in the design of public sector reforms (World Bank, 2012). In designing of new engagements in Pakistan, greater focus should be on jointly diagnosing the problem with a coalition of reformers. Such an approach would consider the views of political actors regarding the kind of institutions that they would like to see emerging in Pakistan. The coalition of reformers need not be one group assembled for this purpose, but could be developed to target various constituencies using various platforms, including the media. An important aspect in the diagnosis of a problem in the protracted governance context is the broadening of the coalition of reformers, by bringing in hitherto disparate voices to the discussion about the problems that affect development. Tailor-made responses that are imported from other contexts are unlikely to be useful in Pakistan, given its history and experience with reforms. It is through the development of a coalition of reformers that it can be apparent whether sufficient salience can be generated among influential actors at both the technical and political levels to propel the reform efforts.

Transparency and Information-sharing

The provision of real-time public information on the performance of key political actors is required for voters to hold politicians accountable. This should be the focus during electoral campaigns and during politicians' terms in office. With this information, voters should reward legislators for activities that support growth-enhancing policies. Airing sessions of Parliament on television, and making public the votes in Parliament—as they are in developed democracies, including the United States—would also help equip voters with the knowledge they need to keep politicians accountable. Truly empowered LGs could be an avenue for effective canvassing of information about important reforms and their implications for citizens, and also help increase accountability. However, information alone is not enough. Both the citizens and political actors need to act on the information they receive, for that information to have any substantive impact on the nature of the reforms being contemplated.

CHAPTER 4: CONCLUSION – THE CHALLENGE OF IMPLEMENTATION

WHAT WILL IT TAKE: PULL AND PUSH FACTORS

There is a desire across Pakistan to move the country onto a new developmental path. This is evidenced by the emphasis placed on several strategic documents, including Vision 2025. While there may be clarity in where Pakistan wants to see itself, how to use the public sector to cause this transformation is far from certain. Efforts to reform the public sector and civil services in Pakistan have a long history of mixed results; often more failures than success stories.

This has been the case from the 1973 reforms associated with the Bhutto regime, to the more recent constitutional amendments mainstreaming devolution associated with the Musharraf regime. Whether one looks at the administrative reforms of 1973, or the devolution experiment of 2001, some recurrent themes can be traced as inevitable pull and push factors. Maintaining the status quo, the ascendancy of group or cadre interests over common improvement objectives, a lack of public debate on reform directions, and ambivalent political will for sustaining long gestation are the main obstacles. The painstaking civil service reform agenda appears to have frustrated even the best-designed efforts in the past. Any future efforts for public sector rejuvenation and civil service reforms will, therefore, need to be carefully hedged against these historical and recurrent pitfalls—the pull and push factors—that appear to have become the norm in public sector reforms in Pakistan. These factors include:

- Elite capture and vested interests;
- Structural weakness of institutions;
- Citizen demand-side pressure;
- The private sector; and
- Peer pressure.

Elite Capture and Vested Interests

Elite capture and vested interests seem to be the most pernicious of the pull factors. Various kinds and categories of elites will always tend to oppose public sector reform efforts in an effort to preserve their vested interests. The list of such elites is long, including politicians (especially in the context of local politics), civil service cadres and groups (embroiled in issues of interservice rivalries), private and professional entities (doctors and engineers trying to stick to unprofessional practices), and other state actors (media, judiciary, and security establishment), each viewing the public sector reform process from the prism of their institutional interests. To successfully confront these pull factors, Pakistani stakeholders could employ both big-bang approaches, and incremental and opportunistic strategies.

Weak Coordinating Institutions

The structural weaknesses of institutions and of the society at large is yet another pull factor. Pakistani institutions are too weak to midwife the kind of transformation needed to overhaul the existing ethos and replace it with a growth enhancing one. Insecurity deepens the sense of individuals' and institutions' fear of change. This has in turn been highly counterproductive for public sector reform efforts at various times in Pakistan's history. Overall institutional inertia works against any efforts to energize public sector governance solutions. Breaking variants of inertia has been one of the most daunting tasks in the process of introducing new innovative solutions to complex governance problems in Pakistan. Lastly, unclear, misplaced, and ambiguous priorities (both overall and institution specific) for a future vision have also acted as a negative element in earlier reform efforts. A whole-of-government approach is needed to provide assurance to key stakeholders, including the bureaucracy, that reforms provide an opportunity for transformation.

Nevertheless, amid the difficult context are opportunities that could work in Pakistan's favor.

Citizen Demand-side Pressure

These include an increasingly well-informed and motivated citizenry, **which has seen other countries make fast-track progress on the path toward growth and development**. The expansion of the middle class, buoyed by rapid urbanization and the youth bulge, provides increasing opportunities for citizen groups to organize for better service delivery. Of late, an extremely vibrant and rights-conscious civil society has been one of the salient and notable features of Pakistani citizenry. It has nurtured and augmented sustained dialogue for the long-awaited public sector and service delivery reforms in Pakistan. A confident media is yet another ingredient of stronger citizen voice for lasting reforms and transformational growth in Pakistan.

Private Sector

The private and corporate sector in Pakistan can also bolster public sector reform efforts. The private sector in Pakistan has provided ample evidence of its inherent strength and willingness to play a central role in taking Pakistan forward on the path of fast-track growth and viable development in the coming years and decades. If the Government can settle for its policy formulation and regulatory role, firms and the private sector in Pakistan can take a big lead in improving service delivery and promoting entrepreneurship by mobilizing corporate and private sector resources, and taking the initiative in pursuing a transformational agenda.

Peer Pressure

Finally, peer pressure could energize both the state and citizens to confront the challenges that are likely to be faced in transforming Pakistan into a high-income economy. By reforming the public sector and balancing the roles of various actors and pillars of the state, Pakistan could be poised to seize a historic opportunity that lies ahead on the road to 2047. By identifying peer groups and pro-reform constituencies within the state, and by fully and optimally benefiting from inherent advantages (natural endowments, geostrategic location, the youth bulge, and the proclivity to innovation) Pakistan can respond to the spirit of the times in a proactive manner and achieve win-win outcomes for all members of Pakistani society. A reformed public sector, based on modern best practices; a high calibre civil service structure employing modern and IT-driven problem-solving behavior; and a dedicated and committed leadership that is fully cognizant of national priorities, can readily complement and steer the transformational development agenda—leading to a prosperous Pakistan by 2047.

TOWARD 2047—SELECTED DRIVERS OF CHANGE IN INSTITUTIONAL REFORM FOR GROWTH AND TRANSFORMATION

As Pakistan heads to 2047, the nature of the state is expected to change. These changes will be triggered through the interplay of two crucial realities. To begin with, at the present rate of population growth, Pakistan will have become one of the most populous countries in the world by 2047. If service delivery fails to transform and respond to the needs of a burgeoning population, dissatisfaction among the masses will only be compounded. A related issue pertains to devolution. The course of devolution and the ability of the federal and provincial governments to redefine their role with enhanced localized empowerment will have a huge impact on the nature of service delivery, and redefine the social contract: governments will be closer and citizens can demand accountability more easily. The three factors detailed in the following paragraphs will be important.

The Nature and Roles of the Public Sector

Pakistan is certain to open a debate about the nature and role of the public sector in the changed context of 2047. Will the state continue to make unsuccessful efforts to try to retain hegemony over the service delivery mandate, or will it be able to take the leap of faith and allow the private sector a more visible and enhanced role as a provider of essential services? That, in turn, will lead to the next challenge regarding recalibration of state institutions for effective regulatory and enforcement roles, instead of trying to do everything by itself. For any structural transformation in Pakistan to work, the federal and provincial governments will need to strengthen their roles as regulator and facilitator to ensure quality and equity in service delivery for citizens and firms in Pakistan. The course and direction of such a transformation in roles of the Government will define the ultimate success of Pakistani society in coping with emerging social and developmental challenges in the coming decades in a successful manner.

The ICT Revolution and ICT-mediated Public Sector Management

The ICT revolution will be another driver of prospective changes in public sector performance. The speed at which the state structures embrace the inevitable delivery through ICT-enabled systems will ultimately decide the effectiveness of the Government's responsiveness to future challenges. ICT solutions can be successfully employed for enhancing the performance levels and quality across the public sector in Pakistan. Pakistan is already distinguishing itself as a technology and innovation hub, yet the use of technology in governance systems is still modest.

The Skills of the Future

The interplay of emerging governance and developmental challenges, and ability to benefit from upcoming opportunities, will depend on the new shape of public sector institutions and actors in Pakistan in the coming years. How efficiently the public sector in Pakistan can make use of public sector employees with technical capabilities and the calibre to respond to the challenges of transformational growth and development will be central to Pakistan's bright future by 2047. In fact, the final shape and contour of the new social contract in Pakistan will ultimately be decided by the efficiency of the public sector in adopting modern and technically sound capacities for resolving the challenges of underdevelopment and inequitable growth in Pakistan. This will require new skills sets, which are available in abundance in the Pakistani market, but which the civil service has not adequately tapped into.

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