

# WHAT'S AILING PAKISTAN'S ECONOMY? UNDERSTANDING THE FOUNDATIONS OF INSECURITY

TUESDAY, OCTOBER 18, 2011  
WASHINGTON, D.C.

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Transcript by Federal News Service  
Washington, D.C.

ASHLEY TELLIS: Well, good afternoon, everyone. Welcome to the Carnegie Endowment for International Peace. I'm Ashley Tellis. I'm a senior associate here at the endowment working on a variety of South Asian issues.

And today we have the special pleasure with us to have Akbar Zaidi, who is a nonresident fellow of the endowment and has actually published two policy briefs with us so far, with two more to come sometime over the next year. I believe you'll have seen copies of Akbar's papers; we've put them outside. There's also a formal bio that should be on your chairs, so I'm not going to spend an inordinate amount of time introducing him formally. But I do want to say that Akbar has some very specific qualifications to speak to us on the issue that we're going to discuss today, which is Pakistan's economy and how Pakistan's economy affects its long-range trajectory.

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Akbar Zaidi is a professional economist. He understands the discipline and is the author of, I believe, at last count, 12 books?

S. AKBAR ZAIDI: Right.

MR. TELLIS: (Chuckles.) He's being modest. Twelve books published in Pakistan not just on dry academic economics but economics as understood within the milieu of Pakistan society. And so, in that sense, Akbar does justice both to the economics of Pakistan and to the political economy of Pakistan.

What I asked him to do this afternoon was to speak on the broader question of the Pakistani economy writ large because what happens to the Pakistani economy in the context of the changes taking place in Pakistani society, of course, will determine Pakistan's long-term trajectory and its success as a state. And what happens to the Pakistani economy, to my mind, is far more important for Pakistan's success over the longer term than overcoming many of the immediate and more transient issues that dominate the headlines, particularly insofar as they bear on U.S.-Pakistan relations. So I thought we'd take a step back from all the crises of the moment and look at something that is really fundamental and important, which is Pakistan's economic trajectory, its strength and its weaknesses, and what is it that we can expect as this country evolves in the years ahead.

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So without further ado, I will yield the microphone to Akbar Zaidi, welcome him on your behalf, welcome all of you back to the endowment. So over to you, Akbar. Thank you.

MR. ZAIDI: Thank you very much, Ashley. I've been associated with Carnegie as a visiting scholar for a year and a half. This is the first time I've seen where Carnegie is, so I'm glad that that's happened and I've finally seen the institution which has published two of my policy briefs.

It's also a very great pleasure to have Ashley here – and I can say this in his presence as well, that there are very few people whom I respect as much as Ashley, not just on South Asia but also on Pakistan. And I'm always intimidated by his insight and in his presence, so I know that everything that I'm going to say, whether he agrees or disagrees, is going to – he's going to challenge me in some way or the other, and I think that's a very healthy relationship that he and I have. So thank you, Ashley, for inviting me.

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So the ailing Pakistani economy – it's ill; is it dying – terminal illness? Does it just need some vitamin? I mean, we started with the metaphor of an ill, ailing economy.

What is the illness? How prolonged has it been? Is there any way out? Does it – you know, does it require further U.S. assistance for it to survive? These are some of the questions which I hope to look at.

But I think, on the one hand, if you talk about an ailing economy, Pakistan's economy and crisis, (I mean ?), every day when you look at the Pakistani newspapers, you hear about some economist writing about Pakistan's economic crisis. I disagree with that and I don't – I think, you know, crisis is a word that we use in Pakistan three times a day, so it's lost its impetus and its meaning.

But the general conventional wisdom is that Pakistan – not just – the country we know has collapsed. I mean, forget about that; it's done and over. That's – no one talks about that anymore after the 2<sup>nd</sup> of May and then the Mehran base and – so that's done with.

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So is the economy still surviving? That's something that I hope to look at.

But let me just sort of step back a moment and say that, OK, how ill is Pakistan's economy? Is this a recent illness? Is it close to collapse? Did it start just in the last two years when General Musharraf left, leaving an economy well – sort of in place and progressing well?

If you look at the 60 years of Pakistan's economy, the surprising thing is that the growth rate has been above 5 percent, which is not bad, you know, not bad – 5 percent over the 60 year period. And if you look at the last 12 years, the per capita income has doubled from about 525, 530 to about a thousand-plus today. That's also – that's not an ailing economy. But anyway, that's a – that's a sign that things seem to be doing well in some places; at least some people are making some money.

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Sixty-five percent of Pakistan's population has mobile phones. For a population where, on the one hand, you read that 40 percent is below the poverty line, you suddenly get these figures of 65 percent having mobile phones where you have to pay maybe 2,000 (rupees) or 3,000 (rupees) or even, you know, 1,500 rupees to get a phone, it's sort of – it's odd; there are some statistics which don't match up. How can 65 percent have mobile phones?

It's a predominantly urban country now. You know, estimates suggest that maybe 55 percent urban – very unlike the rest of South Asia. I think this is something else that – there are people say that it's Bangladesh and India; I think India's urbanization is about 30 percent? Yeah. Pakistan's is maybe double that, almost double that. So very different sorts of indicators when we look at South Asia.

If I were sort of a technocrat from the World Bank or the IMF, and perhaps there's some of you here, I'd have a very long list of things that need to be done, OK? You know, do this, this, this, this, this, and everything will work.

I'm not going to do that. I think one needs a slightly different approach to understanding Pakistan, its economies, and how it functions, and the problems within.

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So I'm going to use a political economy approach, which I won't explain because, you know, I'm hoping that you'll just allow me to get away with whatever I mean by political economy. But I'll explain certain things about it, which I'm – which I'm going to look at.

So I'm going to use a political economy approach to explain, to understand, to highlight some of the features of Pakistan's economy, and to answer the question whether it's ailing, whether, you know, it causes insecurity, what are the sort of structural reasons for this, if any. So these are some of the things that I'm going to look at.

But I think the first issue which we need to address is, when we say an economy is not doing well or that it's ailing or that it's collapsing, what are we comparing it to? What's our measure of – how can we say that?

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One very obvious example, comparison, is, OK, let's compare it with Pakistan's neighbors. India is doing well; since 1991, it has a growth rate of 6 ½ (percent), 7 ½ (percent), 8 ½ percent. China, we don't talk about anymore because it's doing so well.

Even Bangladesh now is doing better than Pakistan in terms of the economy, and I think in terms of a lot of other indicators as well; the “basket case” of South Asia, Pakistan's basket case, is now sort of the marvel for Pakistan. And I wrote an article some time ago saying that Mr. Jinnah's Pakistan is now ironically Bangladesh, and Pakistan today is Mr. Jinnah's worst fear and worst nightmare. So I think Bangladesh has actually emerged as a secular state, as an economic – as, at the moment, a democracy, and an economy which is – which is maturing. So even Bangladesh has done better.

So at least Pakistan is not as bad as Afghanistan, because when we're looking at neighbors, that's a neighbor too. Or is it? I mean, one – you know, there are some people who feel that Afghanistan might have a better future in the longer term and Pakistan is going to implode and the economy is not doing well and there is – you know, at least the Americans are going to bail out Afghanistan; maybe not Pakistan. So is Pakistan doing better than Afghanistan? I think probably so.

But (so there's ?) – one way of looking at how bad or how well Pakistan is doing is to compare it with its neighbors. And it seems that India, Bangladesh, even Sri Lanka now are on – are on a higher trajectory and a better economic map where human capital and social development is taking place. (Well, ?) Pakistan, there are largely problems. So that's one way of looking at it.

The other is, the potential. OK, I just told you that GDP per capita almost doubled in about 12 years – 1999, 2000 to 2012, it doubled from about five and a half hundred to about a thousand-plus. So it's one way – it's done fairly well.

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But potential: Is Pakistan – was Pakistan's potential – should it have been Malaysia today? Should it have been South Korea? There is one story which I have read in every book, including mine, which has not been sort of confirmed by anyone, is that the South Koreans in 1961 or '62 came to Pakistan and stole the second-year – five-year – second five-year plan and that they emulated it in their country. So I've seen a lot of people write about that, but, you know, I'm not sure if that's correct or not.

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But it's – this gives us a sense that in the early 1960s, Pakistan was seen economically as a model for other countries to follow. The New York Times – I write in one of my briefs here – The New York Times, the London Times in 1964 and 1965, wrote that, you know, Pakistan is one country which is the envy of the rest of the world. On January 18, 1965, The New York Times wrote, Pakistan may be on its way towards economic success that so far has been reached by only one other populous country, which is the United States. This is 1965.

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Is that the potential that we are talking about? Should Pakistan have developed to that extent that it could have been, you know, a role model for the rest of the world? So that's the potential. So when I say, we need to see where Pakistan – how does one compare Pakistan? How does one look at it and say that it's done well or not done well? There are at least these two areas: One is comparisons with other countries and the other is its possible potential.

I've argued that, you know – having said that, 5 percent of GDP over 50 years is impressive – 60 years is impressive, but the main thing that one sees in this pattern is what I call a roller coaster economy: high growth for five or six year; then very low growth – 3 percent for – 2 percent for four to five years; then, again, high growth for seven years.

And I shouldn't say this, but perhaps, you know, this high growth seems to coincide when there's a military general in power in Pakistan and when there's a Republican government in power in the United States and when somebody invades Afghanistan. You know, these three things seem to happen 1979, 1980: You have Reagan, you had General Zia-ul-Haq and you have the Soviets invading Afghanistan; you have 7 percent growth rate for 10 years in Pakistan. Under Musharraf, you have Bill Clinton, then you have George Bush, then you have the Americans invading – is that what – is that how one says it? – the Americans taking over Afghanistan, and you have a military general in Pakistan as well. So again, for a few years, high growth. This is a roller coaster economy; it goes up and down, up and down. And for the most part, the high rates of growth have taken – coincided when a military general has been in power, when a Republican administration has been in the United States and when someone has invaded Afghanistan.

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The problem is that, you know, the main – the main sort of – the gap in all this is that there's been no long-term consistent economic growth. If you look at India, up to about '88, '89 – some people say that the – in 1985, the reforms took place; others say that it was 1991 – but, say, late 1980s, India's growth rate was 2 ½ (percent), 3 percent, but it was consistent, it was long term, it was stable – it was low but it was stable. Throughout – up to about the end of the 1990s, Pakistan used to boast and compare itself with India and say, we've had growth over 5 percent, 6 percent; India is at 2 ½ (percent), 3 percent. But now, after 1991, and then again in late 1990s, there's been this point of inflection in India's growth rate, where again it's been stable and it's been very, very high, much higher than Pakistan.

So I think one of the main differences in Pakistan and other countries is this trend, long-term trend; in Pakistan, it's up and down, five years up, four years down, five years up and down. (Inaudible) – what we call a roller coaster economy. I think that's something that needs to be identified.

So what are the reasons for this? You know, why has it been not consistent? Why has it – why – why has it not been growing 2 percent, 4 percent, 5 percent over 50 years? Why has it had these ups and downs?

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I think there are numerous reasons, but I'm going to focus on three and talk about – highlight three of them, and then later on talk about, you know, how – what has changed over the last few years.

And as I said, I'm going to talk about the political economy perspective, not just, you know, technocratic reforms, not just World Bank, IMF policies, not just what we think is right but why certain things don't work.

The three areas: One is what I would call the political economy of defense.

Now, by that, I don't mean military expenditure. In most countries, when you say political economy defense, you'll say, OK, the military gets 4 percent of resources of GDP, so which means that there's 4 percent less for development. In the case of Pakistan, the military has received about 6 percent, 6 ½ percent of GDP in the 1980s. And now, according to different calculations, it's about 3.2 percent or 3.4 percent. Musharraf did a very – I mean, I didn't know he was an accountant, but he did a very interesting accounting exercise. What he did was, each year, when the budget is announced, a very large chunk of military expenditure was under the heads – under the head of military pensions because that takes a large amount of military expenditure. So what Musharraf did was that he removed the military pensions head and put it in the civilian account. So that suddenly saw the military defense budget fall. So that's why I'm saying that there are different calculations about it, that 3 ½ percent of 3.6 percent –

But nevertheless, that's not what I mean by the political economy of defense. I'm more concerned about the persistence of the military in the political economy of Pakistan – the persistence of the military, its priorities, its justification for being in power and how that has an impact on Pakistan's insecurity, on other regions – on other countries in the region, on the defense budget, on a lot of other things, on civilian government and so on and so forth. So I'll explain that a little bit.

Out of 64 years, the numbers are 37 military, about 37 civilian. If you look at the civilian further, I think there are far more years where one can count those years in the military basket, especially, from '99 – from '88 to '99, the so-called “civilian mistake interregnum,” the – you know, the “lost decade” – whatever you want to call it. You know that the military controlled the civilian process, the democratic process, the political process of Pakistan. So I'd actually put those 11 years in the military basket as well. So we know that the military has ruled Pakistan for far more than any dispensation of any kind of civilian government – elected, unelected, technocratic.

Now, authoritarianism is not necessarily a bad thing when it comes to government. We've got South Korea as a – as a fairly good example of economic development taking place, but then we've also got North Korea across the border, which is a different story. So, you know, authoritarianism can be – have different outcomes.

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So it's not just the authoritarianism. It's not that the military has ruled for so long that it's caused these problems. But it's more that the military has sort of taken over the state. It's begun to determine what direction, what policy Pakistan should have. Whether it's today's democratically elected – and I do consider Pakistan – and I can say this for once in my lifetime, that – in my adult lifetime – that Pakistan is still, regardless of what you think of Mr. Zardari, a democratically – a democratic government. It's a democratic country today. It will not be next week, but that's a different story. Today, it certainly is. Since 2008, I think it has been.

But even in a democratic elected government – under a democratic government – even when there has been a great deal of public support in 2008 after the assassination of Benazir Bhutto, when the present government came into

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power, the civilian government has not been able to control a number of key areas which the military controls: nuclear policy, Kashmir, Afghanistan, probably U.S. relations and perhaps a lot more as well. So the way the military has taken over institutions of the state, even under when a civilian is power – is in power, I think it's had an impact on how – which direction the country goes in.

And I think India is very important in this whole story that I'm going to talk about, because I'm going to end at India. And I think that one of the – for those of you who are familiar with Pakistan – and I can see faces who are very familiar with Pakistan, who've studied Pakistan, including Ashley – we know that the military uses the idea of Kashmir or India to justify its presence in the public sphere, to justify its presence as an economic predator, to – it requires a large army; it requires the 6 percent of GDP, even when civilian – even when it's not at war, even when there seems to be a partial settlement with India or – to keep forces away from the border – to let the issue of Kashmir simmer, there is still a high domestic defense expenditure borne by the military – borne by the economy.

But it's not simply that. I think it's determining which countries the businessman can trade with. It's determining the sort of policies that a certain country is a friendly country because the military determines it to be; certain countries (are ?) unfriendly, and there is some sort of cold war taking place, and – whether it's in the form of the ISI or other institutions acting upon it.

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But there is an underlying, simmering war, which allow – which does not allow trade to take place, which does not allow economic relations to improve. This is all part of the political economy of defense. If my argument is correct, that's it's the military which determines a large chunk of policy in its key areas, which does not allow – which not only drains the economy but which does not allow economic actors to act freely, then that's what I would call a political economy of defense.

And I think this has been one of the problems throughout the last 65 years, that the military has intervened and created an environment which is not necessarily good for trade, which is not necessarily good for Pakistan's development, for its image, whatever else you want to call it. (I mean, there are ?) a number of things which impact upon the economy. So that's one box which I'll (keep ?) for the moment.

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The second is – and not just to blame the military; it's the civilian elites who are equally at fault, I think. So it's – it's the absence of what I would call a long-term contract off the Pakistani elite – civilian, military, bureaucratic, technocratic elite – with the people of Pakistan, that there is no long-term contract. I mean, you – as I said, you can have authoritarian governments; you can have military governments which are forward-looking, which are development-oriented, developmental authoritarianism – China – people call China developmental authoritarianism. There are numerous other examples from the – from the '70s and '80s where there was developmental authoritarianism. I think Ayub Khan was one example of developmental authoritarianism in Pakistan.

But I think that it's not authoritarianism alone; it's not the military alone, you know, which is – which is a very important actor in all this, but I think that civilian elites in Pakistan, whenever they have been part of the military – and that's another very interesting example – you know, sort of a comparison with Latin American military, with the – with the – with the military in Latin America – a large number of even civil society, a large – a number of businessmen, members of the bureaucracy, they all support – they have supported military governments in Pakistan. So they're equally implicated. The civilian and the military elites are equally implicated in having a long-term social contract and economic contract with the people of Pakistan.

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So I think – you know, this roller coaster relationship, I think it's been accidental rather than, you know, something that has been planned out. (And I ?) – there have been economic policies, particularly in the 1960s, I think that's one period, but which had damaging consequences in the sense that East Pakistan was discriminated against, which led to – led to it being – led it to it breaking away and forming Bangladesh. But – and again, in the early 1970s, a lot of people had very strong views about Mr. Bhutto. But there was a social contract of a different nature where social welfare and – call it socialism or some form of social-democratic economic principles were applied.

But after that, I think, you know, this – the absence of an elite – civilian, military, other elite – coming to an agreement about where it wants to go has been one of the major problem for a failing economy. And that's why, if you look at economic growth in Pakistan, I mean, it's very easy to see how that takes place. Under the Zia period, for example – Zia ul-Haq, 1988 to '99? – no, the other way, '77 to '88, '77 to '88 – with, as I said – you know, not jokingly, but the invasion of Afghanistan by the Soviet Union helped bail out Zia, helped the economy a great deal. A lot of aid came into (it ?) – a different kind of arrangement as compared to what we have now, but it was a lot of military aid coming in, a lot of civilian aid coming in, development taking place in the – in the what is now (Khyber Pakhtunkh ?) high area, so there was development, roads and infrastructure being built by Fazle Haq, the – (inaudible) – general Fazle Haq who was the governor of the NWFP at that time. So there was development which took place. A lot of NGOs started being formed.

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So you see the – you see a military government being helped by U.S. and Saudi money, especially – (inaudible) – it's very interesting that in Pakistan, when we often criticize the Americans for everything that they do, good and bad, people don't criticize the Saudi government. And I think the Saudi sort of ideological trend there, backed up with their money, has caused perhaps a larger amount of problems than the Americans have, and certainly, under Zia's Islamic structure, Islamic arrangement, the Saudis were very prominent. They were very important in funding the mujahedeen as well, as I think they are now in a different sense.

So the 1970-80s, when we see high growth, it's closely linked to the Soviet Union being in Afghanistan – military aid, other types of aid coming into Pakistan. After that, once the Soviet regime falls, everybody withdraws from the region; you go back to a normal scenario where you – where the governments in Pakistan turn to the IMF. They're trying to struggle and – from the '88 period to the '99, they're trying to struggle to deal with some sort of structural changes, the debt that has been created under Zia.

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And then, again, in the 1990s, '99, when Musharraf takes over, for the first few years, it was very – a lot of people – Aisha (sp) was just asking me – she's going to have General Musharraf on her – she works for the Voice of America and she was saying, I will have Musharraf on my television show on Monday, and he's going to say his economic reforms were fantastic.

What's interesting is that – Musharraf takes over in '99 – from '99 to 2001, the economy is far worse than it was under Benazir and Nawaz Sharif, and it was very bad at that time. It was far worse in this period. What saved Musharraf was bin Laden and 9/11 onwards, and the Bush-Mush relationship, which, you know, went – which worked very effectively.

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So the Musharraf period that we see, from – to 2001, 2002 to 2007 was very high growth, 7 percent again. This is a roller coaster going up, largely backed by U.S. aid, largely backed by money coming in on the account of the war on terror, or the Afghanistan war.

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But again, it starts because – I've argued in the pieces that I've done for Carnegie as well – that economic growth, whenever it's taken place, has taken place under these conditions of a military government which has not involved civilian actors, which has not – which does not allow decisions to be made which could be challenged by – which could be challenged, which are more consultative, which are more participatory.

So whenever the military government leaves, and that has happened in every single case – in 1969-70, in 1988, and then 2008 – there's always an unraveling, because new actors emerge who have not participated. So one of the reasons for the economic roller coaster in Pakistan has been the absence of any sort of long-term economic policy – whether it's the military, whether it's the civilian government – who have worked with each other, who have been able to work with each other, and have a road map over 40 years, 30 years, or 20 years.

I mean, there have been – whenever a civilian government comes into power, it talks about a 10-year vision program, but then it's never in power for 10 years. No civilian government has been in power for more than three and a half years, not counting the Shaukat Aziz government, which was there for a little longer.

So I think the main thing here, the point that I'm making, is that there is an absence of a long-term contract between the elites in Pakistan – civilian-military – and, say, the economy, or a long-term vision about Pakistan. Again, I say, elites in other countries – I mean, elites are predatory in most countries. But they do have a commitment to give back. They have a commitment to build infrastructure, provide human capital, to build social capital.

I mean, Brazil and India – Brazil prior to Lula, India even now – have very high degrees of inequality, very high poverty rates as well. But I think in such countries there is a commitment – call it under democracy; maybe democracy is, sort of, the veneer which allows some sort of social commitment to take place.

But there is a long-term contract with the people, because there is perhaps an understanding that after a few years, a different government is going to be in power. But you can always be re-elected. So I think there is some commitment that one finds missing in Pakistan. And I think that's a very important missing link in Pakistan.

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The third area is what I call the political economy of aid. As I've already said, Pakistan's economy has been aid-dependent since 1948, and that's a very, very long time. And there is no way that it's going to be weaned off aid. Because it is aid-dependent, it knows – whether it's the 1960s, when aid received from most countries was about 7 percent of GDP, 6 to 7 percent of GDP – very high amounts of aid being used, and actually being used very productively.

Because much of that aid – and the United States has been the largest single donor to Pakistan over the last 60 years, bilateral donor – much of the aid in the 1960s was used very productively. What has happened is that because Pakistan has been a frontline state, since 1979 onwards, it's distorted the nature of the aid relationship. What it's done is that much of the aid in the 1980s, when Zia-ul-Haq was in power, was largely through the mujahedin, for a very different purpose.

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After 2001, it's become counterterrorism, the war on terror. Much of the aid that Pakistan has received has been on that account. It hasn't been what I would call productive aid. It's been, in a sense, military aid supporting Pakistan's military. And that's also had numerous undercurrents which have had an impact on the political economy.

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The first is that because of the American presence in Afghanistan, the drone attacks that take place in Pakistan, and the blowback that has happened within Pakistan as a consequence of the war on terror, all U.S. aid, U.S. aid is seen as bad aid, is seen as supporting the military. So whenever the United States, the USAID has helped schools, had projects, it's always been, sort of, countered by a drone attack that takes place the next day or the next week.

I've written in my report for Carnegie that last year, when the floods took place in Pakistan, it was one of the first sort of moments, in 10 years or so, when the United States was shown very positively in the media in Pakistan – that they had – the United States, I think, was the largest donor last year when the floods took place in Pakistan in 2010. I think they gave about \$450 million, the largest donor.

And the press and the media picked up on that, and they showed all these films of American military men helping, supplying – not arms, but supplying the foodstuffs and medical supplies and water to those affected by the floods. So it's not often that one sees that images in Pakistan's media.

A week later, a drone attack washed out all the images that had. So if you have a war on terror taking place, you have the political economy of aid, which is very closely tied to the military side of the operation – until, at least, this administration took over in 2008. So much of the aid that has been given to Pakistan has been given on account of the war on terror, counterterrorism, dealing with – or not dealing with – the war on terror and its consequences, as we found out in Abbottabad, and then, you know, there are other stories as well.

So much of that aid which has been given to Pakistan has been tied to military operations – not been very effective in the public domain, not had a very good public relations moment at all.

There is another side to this aid – that is that the civilian and the military elite in Pakistan has postponed, I think, almost inevitably, taking very strong, needed, deep structural interventions in the economy. Because it knows that Pakistan will never be allowed to fail. It's like General Motors: Somebody's going to bail it out.

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Pakistan is a nuclear rogue state; it's the most dangerous place in the world; the Taliban is about to take over. With that fantastic scenario on CNN and BBC, Fox News every day, you can't go wrong. There is no need to take economic, structural – deep-rooted structural changes in the economy because Pakistan will always be bailed out.

Whenever Pakistan needs money – whether it's the economy, whether it's the military, whether it's the sports sector – you ask the Americans; they'll come to your aid. They'll give – Admiral Mullen will make a noise one day; the next day things will be back to normal, or somewhat normal. The Pakistan elite can rely on all of you to give your taxpayers' money to the Pakistani elite.

And I think this is important. I need to emphasize this point, that it's not Pakistanis who are getting the money that the Americans – your taxpayer money. It's the Pakistani elite. And why do I say that? Pakistan's tax-to-GDP ratio

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– you know, the amount of money that they collect from taxation as a share of the GDP – has been falling from about 2002 to 2011, 2012. It used to be about 9.5 percent of GDP. Today, it's 8.5 percent of GDP.

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So the economy is growing. Perhaps more money is being collected in taxes, but a much smaller proportion. The reason for that is – as I said, the second argument that I made about Pakistan's elite – civil elite, military elite, any type of elite refuse to tax themselves because they know they are going to be bailed out by the American people. The American government will say that – nukes, Pakistan has nukes; Taliban is going to take over. We can't abandon Pakistan. And they've milked that relationship.

And they continue to do so. Every time Washington turns around, Capitol Hill turns around, the Senate turns around, the Obama administration turns around with a stick and says, OK, you know, you let Osama bin Laden live almost in the Pakistan Military Academy for five years. We're not going to give you any money. They say, well, the Taliban is taking over. They'll take over the nukes. Then more money comes in.

So you know, I think that relationship needs to be rethought. I don't know how, because I think that's for Ashley to decide how. I'll try and deal with the economy side. But you know, how that's going to be worked out? But what it does, in terms of the economy, is that 1.7 million people – you know, that's, I don't know, a small part of Washington, maybe – 1.7 million people pay taxes, income taxes in Pakistan.

That is less than 1 percent of the population. Less than 1 percent of Pakistan's population pays income tax. And I don't think Mr. Zardari is one of them. I don't think Mr. Gillani, our prime minister, is one of them either because they are landlords, and agriculture in Pakistan is supposed to be – if not exempt, it's not properly taxed in Pakistan.

So as long – whenever there is a fiscal crisis of the state, whenever there is a budget crisis, whenever there is a shortfall in money required for arms or development, there is the United States, or the IMF, or the Asian Development Bank, or the World Bank there to bail Pakistan out. The elite are not going to tax themselves, and unless they start taxing themselves, this whole – the edifice of the economy is going to always be aid-dependent, and it's going to be extremely weak.

[00:35:47]

Now, I mean, this is sort of the broad – as I said, there are lots of other things one can highlight. I just wanted to talk about these (too ?) because I want to move on to two other areas. Has anything changed in Pakistan in the last, say, three years – 2007, 2008 onwards? Has the economy changed? You read any newspaper, Pakistani newspaper; it will tell you that the economy is collapsing. I personally don't agree, I think, because there is a resilience – I mean, I don't like using this word, but I think there's a resilience to the economy.

And if you – I can cite a number of statistics which will show you that the rural economy has actually grown over the last two or three years. One reason for that was that when the Zardari government, when the Gillani government came into power, they raised the procurement prices of food crops. So for urban consumers like me, that may have increased the price of the naan and the chapatti, which it did, but it allowed rural consumers – rural growers – far more money.

And there's been a – there's been a mini-rural boom in Pakistan over the last couple of years, where there's been more money in the pockets of farmers who have bought motorcycles, who have bought television sets, who have

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bought whatever – although there's no electricity, but that's a different thing. But they've bought television sets, mobile phones. Much of the – you know, 67 percent, 66 percent of the population having mobile phones.

The growth sectors are outside of cities. People are buying. So there has been an economic boom of sorts, so I think things have changed a little bit. But in the broader political-economy context, I think two things in particular have changed a great deal.

[00:37:26]

One is the presence of the media. That doesn't really affect the economy, but it – I think, in a sense, it affects how people see the world around them. Ashley and I were just talking about, you know, is it inevitable that the military is going to come back into Pakistan? And I'm afraid the answer is yes, but that inevitability may be a few years from now, rather than immediately. And one major change that has taken place in Pakistan is through the media – that there is far greater consciousness about people's rights.

You know, whenever there's some – an incident of any sort of public awareness, of public – not awareness, what's the right word? Public interest – that's immediately telecast live on television. So the media have been able to, sort of, build a bond. As (you know ?), a lot of people have been talking about the Egyptian Revolution and the Facebook and Twitter. That is very – it's a small niche in Pakistan.

But it's the sort of the normal media, or the electronic media, which has created a bond amongst people about awareness, about prices, about – a medium to voice their discontent, and so on and so forth. So I think that's a major change that has taken place in the overall political economy – maybe not so much directly related to the economy, but overall in the political economy.

Another presence which has emerged in the last three years is that of the judiciary, which has started playing a very – what some people call a judicial activist's role, where they have sort of intervened in the economy, where they've intervened in certain judgments, decisions which have been made by the executive, where the government has been put on hold on a number of times.

For example, the sale of the steel mills – you know, that sounds good, the steel mills – under Musharraf, which were supposed to be privatized – the judiciary challenged that. So there's been some form of judicial activism, which has had an impact not so much on the economy directly but in the overall, sort of, complexion of society in Pakistan. And I think that's – that's been changing a great deal.

[00:39:32]

What has not changed, as I said when I started out, is still this overbearing importance and presence of the military in Pakistan. It is still the, sort of, the keeper of all important decisions – whether Afghanistan, Kashmir, the nuclear issue, India, and much more. But I think there's also been – after Osama bin Laden and Abbottabad, and there have been a few other events – incidents where the military has sort of receded a little bit. It's withdrawn. It's sort of become more circumspect, in a sense.

But I think one would have hoped that the civilian government would have been more proactive, far more – and sort of pushed the gas a bit, and sort of said, OK, we've created this space, or the military has withdrawn. Maybe we can take more space. We can create more space, and give a sense of direction to Pakistan. I think this military-civil – military-civil relationship is one of the areas which I felt has not allowed the economy to, sort of, move along an even keel. That's where the ups and downs come into place.

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So here you have a moment – I think more than a moment – you have a civilian government which is not extremely unpopular, but again, is not – you know, does not have the same level of support it did in 2008. But it's still considered to be a democratically elected government. Some politicians have suggested extra-judicial, extra-constitutional means to end this government, but the public at large has said, no, they want this democratic electoral process to continue. They want change to take place.

But I think one of the unfortunate developments has been that the civilian government has not been able to create the space, and along – and sort of extend its life, and create, sort of, a vision that they're going to be in power, to be able to determine issues about India, for example – something that I'm going to turn to now, and why that matters.

[00:41:26]

It's still the military which controls India. So what is the future if one looks ahead? You know, I mean, I've deviated from just talking about the economy, trying to bring in different things, but I'll come back to the economy. What's going to happen in Pakistan? What should happen? I don't think there is anyone in Pakistan who could have president that Mr. Asif Zardari would be president. So we don't make predictions about Pakistan.

That's one thing we've learned. We never make predictions about Pakistan because we are always wrong. I've been arguing, and I've been writing, and I've been talking, in conversation with Ashley and others, that, you know, I see civilian space being created in Pakistan. I even might predict that the next government is going to be a civilian government which is elected through this parliament. But I'm very cautious about making predictions, because, you know, they're usually wrong. The military is usually waiting in the wings.

So, you know, it's very difficult. But one slight line that I've seen – sort of, slowly, some signals which I've seen growing – which I think is very important to the economy of Pakistan, very important to the political economy of Pakistan, very important to the United States, very important to the region, very important to what happens to Afghanistan after the withdrawal of the U.S. – is the India-Pakistan relationship.

I have argued, and I've said this publicly, that Pakistan's future is New Delhi, not Washington, D.C. And if we could come to some arrangement with that, if we could come to – if the Pakistani elite, the military, civil, technocratic, bureaucratic elite can come to a reconciliation with India, can come to an understanding with India, can come to the – can come to accept the fact that India has won the race between India and Pakistan – the day they come to that conclusion, I think that's where the future of Pakistan lies.

And Musharraf almost did that. I remember he gave – (it was ?) one of the most extraordinary press conferences that Musharraf gave, when it was in front of editors of newspapers from the media. And he said, let's not talk about India any more. Let's talk about Pakistan. Somebody said, you know, what about India? He said, look, India is doing something else. We are not concerned. Let's just – and I think he publicly confessed that India is now a better country, a bigger country – economic growth, democracy, and so on and so forth.

[00:43:56]

And I think if that recognition falls through in larger sections of society, we have the solution to Talibanization, the military in Pakistan, democracy, and the economy. And I'll just spend maybe five minutes on explaining what I mean by this.

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If Pakistan and India start trading – they do trade. Trade is about \$2 billion, very small. Much larger for Pakistan, very insignificant for India. If India and Pakistan have better economic relations – yesterday somebody in New York told me – I think he’s well-known here – Shuja Nawaz, who works for the Atlantic Council – and he came up with what I think are extraordinary figures.

He said that a study was undertaken – I think he said either Shahid Javed Burki or Mohsin Khan did it – and they said that trade between India and Pakistan should be 100 billion (dollars). I don’t think so, but you know, even if you divide that by 10, 10 billion (dollars) is a good number. So if India and Pakistan’s trade can be 10 billion, that changes the economy of Pakistan, for many reasons.

[00:45:04]

The region which India and Pakistan – you know, the boundaries of India and Pakistan, West Punjab and East Punjab – Sindh, not so much, but Sindh and Rajasthan, but mainly Punjab and Khyber Pakhtunkhwa – if India and Pakistan start trading, have normal economic relations, not these selective – I’ll allow you to trade chilies only, and you will buy your onions, but nothing else than that.

If it moves beyond just what’s called a positive list and becomes a more real – they became more real trading partners, I think that the political economy, the social economy of Pakistani Punjab, Khyber Pakhtunkhwa, will change enormously. There used to be a fear in Pakistan that the Pakistani market will be swamped by Indian goods. But then they found out that it’s been swamped by Chinese goods, so it doesn’t matter.

So then, you know, they said, OK, if Chinese goods are everywhere, why can’t there be Indian goods? And then I was – we were talking to – I was talking to Ashley as well – that there is now a growing constituency in Pakistan – businessmen, traders, consumers – who say, let’s trade with India. And you know, the whole relationship of India being the enemy – you know, things have changed.

[00:46:21]

And the first thing that Mr. Zardari did – he was not president then – when his party was elected in 2008 – they took over power on March 19, March 18, 2008 – the first budget was announced in June 2008, and the trade policy was announced a month later. And this is when Nawaz Sharif and the People’s Party were almost together. I’m not sure if they were completely together, but almost together, so that means Nawaz Sharif also has a buy-in into this.

The trade policy that was announced by the first – in the first year of the People’s Party government – opened up the stores to India. They said we’re going to trade much more. After that, Mumbai happened, and I think Mumbai spoiled the entire relationship between India and Pakistan. And I think we know why that happened. And I think it’s fairly clear who was behind Mumbai – the same political economy of defense actors who intervene, at times, when they see India and Pakistan making – moving ahead.

Because a friendship with India, for Pakistan, means the military in Pakistan becomes less relevant to itself, to the country, to its defense, and to the political economy of defense. So I think one of the things that seems to be moving, and has moved – and this has happened in the last three or four months as well – is Pakistan’s foreign minister going to India, being well-received, and saying that, well, you know, the visa regime needs to change. More trade needs to take place.

Two weeks ago, the commerce minister went to India, and he said that they are going to give Pakistan the most favored nation – Pakistan is going to give India the most-favored-nation status, which doesn’t mean very much, but

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it sounds good. You know, it sounds that some progress has been made. And if you translate that into Urdu, then it shows that a lot of progress has been made, because it means that – our best friend, or something – that country which is our closest friend, or something like that.

So I think there's been some sort of recognition by members of the elite, and the main question here is, is the military on board or not? Is the military elite allowing this to happen? Because, you know, a lot of people feel that any decision that Pakistan's civilian government makes with India has to be approved first – maybe, a lot of discussion taking place – by the military. And if that's the case, then we see a very major positive development taking place.

[00:48:40]

I actually think that if India and Pakistan can move ahead, in terms of economic – sort of, not integration, but at least, to start with economic – better relations, more trade, joint projects, joint ventures. And Nawaz Sharif – I know in Washington, people don't like to hear his name, and they think he's a conservative, and he's extremely – he's an Islamist and all that – he's a businessman, first of all. That's the most important thing.

It was under his regime, one of his earlier – one of the earlier too – where he was talking to Ambari (ph), their alliance people, and saying, OK, let's have a committee plan it. Because he wanted to be a partner in it, like Mr. Zardari. So business is good for both countries, and as long as both politicians, of all parties, think that they're businessmen – whether it's Mr. Zardari, Mr. Gillani, or Nawaz Sharif – I think there's, you know, a possibility of India-Pakistan trade and economic relations improving.

And I actually see that as a – solution is not the right word, but at least, a major door opening to addressing numerous problems in Pakistan. You know, whether it's the Talibanization, whether it's the role of the military, whether it's the Afghanistan, post-U.S. withdrawals, system. So I'll end here with – you know, there have been lots of fragments here and there – but I'll end here by saying that one could have a wish list of what needs to be done:

The taxation – Mr. Zardari should start paying taxes; that's my first item on my wish list – I don't think that's going to happen; that, you know, there should be a more – that USAID should more carefully tied to Pakistani – the Pakistani government doing something in equal measure. I don't think that's going to happen either because the United States needs to spend a lot of money for different purposes.

[00:50:26]

But if this India-Pakistan relationship – if this could evolve into a relationship, maybe even like China-Taiwan, maybe even China-Japan – certainly China-Japan – I think we can see the beginnings of a change – one can maybe predict the future.

I'll stop there. Thank you very much. (Applause.)

MR. TELLIS: Thank you. Thank you, Akbar; that presentation covered an enormous amount of terrain, both on the economics and of course the political economy. I want to open the floor to people's questions and if you can just start by identifying yourself so that Akbar knows who you are, and then I'll just recognize you as we go along.

Yes, ma'am?

Q: (Off mic.)

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MR. TELLIS: Just – microphone.

[00:51:13]

Q: Thank you very much for that presentation. I would like to know how – you know, for – Prime Minister Manmohan Singh has made statements which sort of confirm sort of your – (chuckles) – own assertions. I would like to know how you think the elites – the intellectual elites and the business – you know, how they work this in private rather than in public because, you know, it is a delicate – you know, so – because there are Pakistanis, I hate to say this, that have wanted to see this unification of India and Pakistan and, you know – you know, the – you know, taking away these borders and so forth.

And, you know, this is in contrast with the ones that don't want that. You know, this is the inner – one of the major inner tensions in Pakistani society, obviously, which took me a long time to figure out, like, in the last five years. And I just wondered, how do you think this has worked? I mean, what literature has pointed to – I mean, where do you think it's going? You – I mean, you're saying it's positive but I'm interested how it works with – how they work it with the military and so forth.

MR. ZAIDI: Shall I –

MR. TELLIS: Sure, please.

MR. ZAIDI: I think it works in the sense that it just makes a public presence more often than it used to, which means that, you know, whenever people used to talk about India-Pakistan trade, that discussion used to be halted very quickly. And now, we don't – again, something that I was – I think, you know, a lot of people don't realize that a number of subtle things have changed in Pakistan on account of developments over the last year or so. One is that previously when we used to write for newspapers or the media, we never mentioned this institution called the ISI. We used to say “the agencies” or the “secret arm of the army.” Now we talk about the ISI very openly.

[00:53:29]

The – I was setting – actually, this is – I've never seen so much criticism against the army as I have since the Osama bin Laden episode. And in fact, the army has been a whipping boy now for the last three or four – and continues to be. And you know it's created its own sort of PR sort of responses by having television programs, by having ads, by having plants on – you know, people planted on television for discussions to defend the army. But it never needed to do that. So I think it's in the retreat. So that's the first sign.

The second is, you know, there is – people have now sort of – a different generation. Mr. Zardari has no reason to fight against – to India – against India. You know, there's no – in fact, as I said, I think his personal and public persona is one where he just sort of fits in very easily. He's not a Punjabi, you know. And, you know, it just sort of fits him comfortably. Even Nawaz Sharif, I mean, he was the one who opened the door to Vajpayee's visit and – which was then sabotaged by Musharraf.

So I think that, you know, there's more space and there's less resistance. There is, of course, a very strong hawkish lobby which says, you know, we will take the Pakistani flag and plant it on the Red Fort. But I think there are five people left to say that, you know, compared to 500 10 years ago. So the world has moved on. And I think 9/11 and fighting Pakistan's war on another border – and you may have – things may have changed. And I'm not sure

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whether it's changing the military. That's something that is a big black box; maybe other people know – may know that.

But at least there is more conversation about the – and the fact that they've been talking about the most-favored nation status for a year. The commerce minister went last month and he said: We're going to give it in February. February is 500 years away, but maybe it'll happen. You know, maybe if another Mumbai does not happen it may happen. So the Indian government has also said we're going to facilitate visas and – small things. And just so it's – these are signals which are – no one's stopping you from saying this.

[00:55:38]

I think that's amazing. It's not – it's sort of a – it's sort of a negative in the sense that it's not that lots of things have suddenly started happening; it's that a few things have started happening and nobody's stopping you. So I think that's the indication.

MR. TELLIS: Yes?

Q: Thank you very much. Raghuraj Goyal, India Globe, Asia Today. I have heard many, many experts, think tanks and including the finance minister of Pakistan and others at the Atlantic Council. This is the first time that I've heard from you talking about most-favored nations and also reduced tension and Pakistan should recognize that India – there is nothing in the fight between these two countries. My questions is that I think both countries are spending more on military because of ego or personal (ventures ?) and other things than any country on the earth. And both are underdeveloped because of the expenditure on military – for nothing.

One, Pakistan has always – are talking about Kashmir issue only. I don't understand what – where Kashmir comes each and everywhere on the talks. Second, what role do you think China is playing as far as U.S. – I mean, Pakistan and India relations are concerned? And finally, Pakistani finance minister and others were saying that as far as U.S. aid to Pakistan, which was – withheld about \$900 million or something, this is nothing. But why India and Pakistan are not coming closer when they share everything and everything common like two Germanys became one and so forth? You think whether this can happen between two countries and that's the only solution?

MR. ZAIDI: No, I don't think it's going to happen. I think that India and Pakistan will always be independent countries. And I think that's fine for everybody. I don't think that anybody wants to go back in pre-1947. It's how they can live as two independent countries. But, no, I think, the point that you raise about Kashmir also is something that I should have mentioned.

[00:57:46]

Nobody mentions Kashmir anymore in Pakistan. It's as if it's, you know, off the map. And in the 2008 elections not even Nawaz Sharif spoke about Kashmir. So you know, what's happened to that – to the militancy of the right wing? And, you know, Kashmir Day and the – you have people on the streets, a few hundred. But even Kashmir has – so you – these are – these are – maybe these are just temporary changes.

I acknowledge the fact these could be very temporary. But that's why I argue that there is a temporary space – I see the space which has been created – (inaudible). I am not sure about what – the China, the India-China, India-Pakistan-China relation. I won't talk about that because I'm not very – you know, that's not my area.

Q: (Off mic.)

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MR. ZAIDI: China, you know, it's funny that on the one hand China is supposed to be Pakistan's best friend, but I don't think it gave \$5 for the floods. America gave \$450 million last year. And I – you know, I'm not completely sure of what nature of friendship Pakistan has and who has a friendship with China. It has a military relationship. Mr. Zardari seems to like China a lot and has tried to bring in economic interests from it. But China doesn't seem to be interested. China's got, I think, other interests.

And I'm not sure – there was a time in the 1990s where China was a very active economic investor in Pakistan – the Gwadar Port, the highways, the telecommunications. But after a number of Chinese engineers were killed and kidnapped and, I think, maybe because some diplomatic relations changes there as well, China is no longer an – not – doesn't seem to be a very major economic investor. I don't know who is because, you know, not many people are at the moment because there is some – a sense of instability, certainly. But – so China had a presence. At the moment I'm not sure where it is.

[00:59:36]

MR. TELLIS: Yes?

Q: Bill Milam from the Wilson Center. Thank you. Akbar, I have two historical caveats and then a question. On the history I would have said – you went very swiftly over the Zulfikar Ali Bhutto period. It strikes me that one of the holes that this dug, if you will, for the Pakistani economy to climb out of were the holes he dug with his very wide nationalization program. You don't have to answer this, by the way; these are my caveats which you may or may not want to comment on.

The second one is that the Musharraf period – the growth rates – my understanding is that the growth rates were a little bit phony in the last few years because of these bubbles that developed in the investment sector because, again, bubbles are created quite often by central banks being a little loose on the money supply. And that's exactly what happened, I think, on – basically on credit limitation. But you may have a different view on that.

[01:00:50]

Now, the question – and that is about India-Pakistan trade. Now, if you read the BBC website this morning or the Financial Times, it appears that the MFN is a done deal and that it only has to be worked out in the next few weeks when whoever it is of – the commerce minister, I think – visits Delhi. And by the way – a digression – Musharraf once said that he couldn't do MFN because it translated into Urdu as “my favorite country” or something like that, which I thought was rather amusing.

But anyway, so if it's a done deal, does that – does that mean, one – or should I say, A – that the military has now reversed its course and is now on board with a full and open trade partnership with India? Two, that they have to – that when they go to Delhi they will circumscribe the MFN so that it won't be much more than now – it's about 5 billion (dollars ?) now if you count, I think, all of the illegal or informal trade. And – or – and three, that the civilian government has actually had a hand in pushing it this way or is – and if so – or will it be a real MFN that really promotes free and flow – free flows of trade? What do you think?

MR. ZAIDI: OK. The MFN stands for exactly what it did when Musharraf was in power as it does today if you translate it. So it's nothing like that – that's a – Musharraf was right; it does mean my best friend or my – most friendly nation. And the fact that it means the same when a civilian government is in power and they can get this through means – as I was saying, these are small indications. As I said, tomorrow we could read the newspaper

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with a different Kayani in charge. You know, that possibility is not off the map. Maybe not – it may not happen, but can happen. So I'm just –

Q: I wouldn't bet against it.

[01:03:04]

MR. ZAIDI: OK. Now, will it be real? What it actually does is that it treats – at the moment, India and Pakistan have a positive list. They can trade these 101,873 items this way and this way. An MFN status means that they can trade everything – they have a negative list, which is obviously more than a positive list. So what – that's the main difference. And I think it's also a diplomatic, psychological sort of a signal to say that, OK, you know, we can treat each other somewhat better than we did in the past. We can treat each other differently. So I think – will it be real in terms of trade? I think so.

One of the problems that the Pakistani business community has is not with Pakistan's military; it's with Indian bureaucracy – and especially Indian bureaucracy on the trading side. They say that, you know, they just can't get through there. I mean, the British did a very good job. They say that we can't – they just can't get through this – you know, this entanglement of how the bureaucracy works. So that is a problem there.

So, you know, the Pakistani – and the trade – it's very interesting. Pakistan imports from India – exports nothing. It exports about \$200 (million) or \$300 million, imports about 1.4 billion (dollars), 1.5 billion (dollars). And the reason for that is not India. India is not the problem. Pakistan has nothing to export, that's the problem. Whether it's China, whether it's Saudi Arabia, you know, we cannot export anything.

So this trade imbalance is going to – this may cause a political problem at some point. But I hope it will be pointed out that Pakistan has a trade imbalance with most countries. So the – but I think what might happen is, say, if all goes well, that's a big if – capital I-F – if all goes well, if trade does take place, what it allows the Pakistani industrialists to do is to lower his costs; raw materials are cheaper, faster, more quickly available; a larger market, once it overcomes the Indian bureaucracy – I don't know how – but once it comes – overcomes that, it has a larger market there.

[01:05:01]

So this will have sort of second, third-round effects on the economy, on employment, and say – that's why a lot of people say it's not just trade. It's not oranges and apples going from one place to another. It's much more than that. And I think that's where it has a political economy impact.

Q: That was my question about the military. Has the military changed – converted to free trade?

MR. ZAIDI: I think they were always in favor of free trade, but not with India. (Laughter.) Now, the fact – the fact – they want trade in everything. They want to trade everything. But I am not sure – again, about the India – about the India factor, maybe there's been U.S. sort of influence. Maybe they've felt that, OK, you know, this India situation is not going anywhere, respective of trade. But, you know, I think we have to keep reminding ourselves this, that it can take 20 minutes for the relationship to collapse – not just break down, but be destroyed. I think Mumbai was a very good example.

I never liked Musharraf, but I give him a lot of credit for improving conditions with India, whether it was on account of 9/11 or his own interests or whatever. I think he did a great deal forward. It was 2008 when the

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Mumbai events took place. That can happen again, you know, at a moment – at a – it's a phone call away. So that's the – that's the fear.

MR. TELLIS: I think the short answer to the question you asked, Bill, is that we don't know.

MR. ZAIDI: Yeah.

[01:06:23]

MR. TELLIS: We don't know the answer to what –

Q: (Off-mic) – I was only asking for speculation.

MR. TELLIS: No, it's an important question –

Q: Yeah.

MR. TELLIS: – because it plays on the longevity, you know, of the – of the initiative. But I think something that Akbar said is very important, that because of the opportunities after Abbottabad there has been a space created for the civilian regime. And if the civilian regime can push the envelope – and it's all a matter of negotiations in an implicit sense – if they can push the envelope and do it competently, and if India can reciprocate in a way that actually yields returns, then it becomes a virtuous circle. And so we have to see now how the MFN idea gets implemented in practice because I believe if there are payoffs in the near term then there's nothing like – you know, nothing succeeds like success. And that will give them greater leverage in dealing with the military.

But you put your finger exactly at the heart of the question. And it's really open at this point. Yeah. But the trend line is right and, you know, if this is sustained then we all come out ahead. Josh (ph), do you have your hand –

Q: Thanks for a really enlightening discussion. I wanted to tease out a little bit what you said about the cyclical nature of GDP growth over time. If I understood your argument, you were saying on the one hand that there's a correlation between periods of relatively high GDP growth and military regimes. And then you tease that out a little bit further to say that there's – those are times in which there's a lot of – a lot of foreign aid. But you also said that that foreign aid tended to be very narrowly targeted, that it went to certain accounts, that it was effectively non-productive aid.

[01:08:05]

Given that GDP is a very broad measure of an economy's success, I was wondering if you could square that circle a little bit and try to explain what's happening causatively – if you think there is a causation between aid and GDP growth – and then talk about whether there are any other underlying factors in terms of productivity growth or other dynamics which would give us a sense of whether that aid is effecting the economy more broadly.

MR. ZAIDI: OK. To – very good question. Under Zia-ul-Haq, the aid which came into Pakistan was very different compared to the 2001, post-9/11 situation. I think that two or three things happened – I mean, there's more than aid as well. I mean, there's remittances, also, which are very interesting. And under Zia-ul-Haq, remittances from the Middle East grew a great deal, as they have in the last two, three – the last two years as well.

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But, you know, I – the aid that – after 9/11 has been largely military-oriented aid – military aid, CSF funds, counterterrorism funds – which – not all of it is spent on what it was meant for. A large amount of that – I don't know how much – but a large amount of that is spent by those who receive it as individuals, as groups of people within the country. So what it does is it becomes a multiplier of some kind or the other within the economy as well. A lot of it is sent out to the Swiss accounts, but some of it stays back and is used productively as well. So that – there is a productive nature of – the unintended consequence – productive consequences of military aid.

Under Zia-ul-Haq, I think there was more of, OK, take this money and, you know, whether it came from the Saudis or from Reagan or the CIA – just take this money. And that was handed – it seems to be more transparent now, the channels of aid – more, but not completely – than when it was under – in the first Iran War. And you know, a lot of current politicians, a lot of generals have publicly acknowledged that they were given 140 million rupees or dollars in this bank account on account of the ISI military relationship from the CIA.

[01:10:24]

I mean, it's – because it's history, you can confess to that. You can't confess to the – you know, what – the aid you received last year. You can't confess to the aid that you received – which you embezzled 20 years ago. So that's the difference. So some of the – a lot of that money, as I said, is parked outside. But a lot of it is also spent domestically. So I think it does act as a motor. That's the unintended consequence. The aid which has come for development projects is directly related to building roads, dams or schools, or whatever – you know, so that's been a different impact.

Now, you said, you know, are they under, as you said, a sort of a productivity – I mean, this is just obviously all very superficial. Is there also sort of a motor of productive growth in Pakistan? In the last two years, the main motor – there've been two things which have happened which, again, we sort of – you know, which sort of belittle this crisis concern. Pakistan's exports were the highest ever. I mean, they're very small, but they were the highest ever last year at \$25 billion. And as a countermeasure, India's software exports are about twice Pakistan's total exports. That'll just give you a size of how small and how poor Pakistan's export economy is.

But nevertheless, they were the highest ever last year for two reasons. One is that the price of cotton had risen internationally so you – textiles and garments were exported; it brought in more money. The second is that they – one of the – one of the factors which – you know, a lot of people write about the crisis economy. If you look at the – what are – what are called the fundamentals, they're all wrong. If you look at all the fundamentals, they're actually showing a sense of crisis. But Pakistan's economy does not work on fundamentals. I think that – if you understand that, then you'll understand that why it's not – why it's not collapsing.

The remittances that come in, for example, they don't go into Zardari's pocket. They don't go into Kayani's pocket. They go into small villages – Gohert (ph) and Benuan (ph), Mittlehas (ph) and, you know, Jelum (ph). They go into small hamlets. They go into small towns and cities. They go into individuals' houses. And this becomes – 1 billion (dollars) a month is what Pakistan has been receiving for the last one year.

[01:12:36]

Which is, you know – so this, I think, has allowed – so – you know, Ashley was asking me later that it doesn't look like there's going to be a revolution in Pakistan. And I think one reason is not U.S. money, not U.S. aid, but these private remittances which have been coming in. So in a sense this becomes a driver. It's a – it's a very consumption-oriented – and Ambassador Milam is right. Musharraf's boom was speculative. It was a bubble.

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There's no – you know, it was real estate prices which went through the roof – maybe like here – stock market – the stock market which went – but very little productive investment taking place.

This money which comes in is – goes more into productivity. This is a weak economic market, you know, because it's – suppose the remittances dry up, then what happens? The fundamentals are weak. But as long as the un-fundamentals or the non-fundamentals are prolonged, there's an informal sector, people, when they don't pay taxes, means they have money to spend. So, you know, that allows sort of the discontent or the pressure to be eased a great deal. But it's a very good question.

[01:13:35]

MR. TELLIS: I mean, it's interesting to actually see that study has been done on this because in practice what aid has done is that it's spiked up effective demand. And remittances have exactly the same effect except that they are a bottom-up process. But it's a spiking effect with demand. Now, if you want to see productivity increases, it would be interesting to see – I mean, in general, productivity increases are linked to investments, either in technology or in some enabling conditions.

And I'm less certain about productivity increases because I don't see the state having done that. But effective demand can be sustained the moment you get injections of capital from the outside – assuming they're not parked in Swiss banks. So, even if you have some fraction spent in the domestic economy you can – you can sustain growth, you know, quite decently for some period of time.

MR. ZAIDI: Yeah, the remittances allow you to do that. They can be parked outside, but they're very small amounts. So they do this and do – it has become more of a remittance-based economy which has sort of helped move the economies at a lower level – lower, lower level. It's not really building dams, for example. All the money that is remitted is tax-free. That's another thing. It's not taxed. So – and there have been arguments that a lot of rich Pakistanis are sending their illegal money abroad which comes in as remittances which – you know, declared as quite legal, untaxed money. So that's another thing.

MR. TELLIS: Yes, ma'am?

Q: Hi, Margaret Matchers (ph). I've worked as a consultant on USAID projects in Iraq and Afghanistan.

Toward the end of your talk, you said, with regard to U.S. aid, you don't think it will happen, but you said, it should be more carefully tied to – I'd like you to elaborate on that, and then I'd just like to toss in Afghanistan and the Taliban. You sort of – I mean, they are issues, but do they – can you just connect the Taliban and why it's not such a problem? And also, does Afghanistan play in this?

MR. ZAIDI: OK, do you want to take another one as well? So – (inaudible) –

MR. TELLIS: Yes, why don't we do that actually because one has to leave at 3:30, so.

[01:15:37]

Q: Thank you, Akbar, for the very candid and wide-ranging assessment. I think you might be the most intelligible economist I've ever heard speak.

MR. ZAIDI: But I didn't – I didn't speak a word of economics, that's why. (Laughter.)

MR. : (I agree ?).

MR. ZAIDI: Sorry, go ahead.

Q: (Inaudible.) My name is Ahmed Chun (ph), and I've just moved over from Dubai, and the reason I mention that is that, while I was there, I got to know, over a period of several years, some Gulf-based Indian business families, a number of whom, by virtue of being domiciled in Dubai, are able to invest in Pakistan without any of the stigma and problems that they would if they were coming from India.

[01:16:10]

And what they told me was quite interesting – is that their experiences of setting up businesses and getting things off the ground in Pakistan was significantly easier than it had been going into India, whether it was ease of hiring skilled workers; whether it was the tax regime; whether it was corruption which, in relative terms, was, they say, a greater problem in India. And I was wondering – obviously setting aside the insecurity question, which is paramount, but who do you credit for creating that environment – that business environment in Pakistan? And how would you suggest it can be encouraged, strengthened and bolstered in order to take advantage of, you know, the hopefully soon-to-arrive period of greater stability and less insecurity?

MR. ZAIDI: OK, I'll – a very good – again, a very good question. I almost thought you were going to say that the Gulf-based Indian businessmen were not able to enter the Pakistani market. Because I'll tell you what happened when – I think this was even Ahmed Sharif (ph) or Musharraf – I'm not – I can't remember – there was a law – there was a sort of wide privatization process which took place. So they found out that a lot of Indians based in Dubai wanted to buy Pakistani companies. And when they found that out, they said, OK, we're not selling to this conglomerate, this group of people. So I think – I thought that you were going to say that. So I'm surprised that you say that.

Who do I sort of credit for this? It's – you know, Pakistan – other than Benazir Bhutto, all Pakistani politicians, leaders, have been businessmen, whether it's Zardari – well, maybe not Musharraf – but Zardari, Shaukat Aziz to some extent, and certainly Nawaz Sharif. Much of the – sort of – you know, this sort of – Dubai – I think one of the studies which I've always wanted to do, and I think which is one of the most interesting studies to do is – and I believe that Dubai is the first South Asian city. You know, it's not Bombay, it's not Delhi, it's not – certainly not Calcutta, not Karachi, but it's Dubai. So how – whether it's Dawood Ibrahim (ph) or whether it's, you know, the cricket matches or, you know, the – or Bollywood – how does – how this – the Dubai network has worked in India and Pakistan, some of the – one study which I've always wanted to do, but have not been able to.

[01:18:22]

But – I'm not – I don't think there's sort of anyone who deserves particular credit for creating a business environment. I think there's – it's been around since the '80s and '90s. Pakistan is – if you look at the sort of business investor policies, it has far more – far friendlier policies than India does in terms of remittances, in terms of taking your entire investment out and, you know, even if you're bankrupt, you can take the entire investment out.

Pakistan isn't – is an investor-friendly country. It's just everything else which doesn't work: you know, Talibanization, you don't get alcohol, you know, whatever else you want, or everything – I mean, the social – those conditions. In terms of business, the power sector is supposed to be bad, but at times better than India; people who go to India say that sort of the IT setup/system seems to be much easier in Pakistan. Maybe India is

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improving now, and it is. The – so infrastructure is not as bad as India, so, you know, even outside of Karachi, Lahore and Islamabad, you know, but it's better in some cases.

[01:19:29]

So I think that Pakistan has been an investor-friendly country, has been a business-friendly country. It's just, you know, this – the whole mess other than – around it which has created the problem. So it's difficult to sort of credit one individual or one group of people because Nawaz Sharif has been very pro-business; Zardari's already very pro-business whenever Benazir was in power as well. So, you know – so, anyway. I'm sorry, your question, yes.

(Unintelligible) – I – when I said that it's the American taxpayer who bails out the Pakistani elite, and unless the aid-givers decided to – either to impose conditions on the Pakistani government or the elite in terms of saying that, OK, if we give you a hundred million or 500 or 1 billion, whatever, you have to raise taxes by so much, you have to reform taxes – and then the Pakistani elite or the ruling group can say, OK, we don't want your money, you know – (laughter) – which is also fine, which I think is a good – you know, I've even suggested perhaps try this experiment: Don't give Pakistan aid. You know, it's not going to become more Talibanized than it is. Just try that experiment; you know, turn around and say, the Obama administration to say, we are not going to give you aid, full stop.

And you're not fighting our war anyway; look at – you housed Osama bin Laden in your backyard, so obviously something is – the Haqqani Network, so on and so forth. So some – you know, I think that the U.S. administration should take a very, very tough line. I think it's good for Pakistan, so – but I don't think anybody else would agree with me. But that's my thing.

About the Taliban and Afghanistan, I think Osama bin Laden's killing has ended the Taliban moment in Pakistan. There's a different type of insurgency which is taking place. It's complicated because the ISI has been involved. It's complicated because Pakistan has become more conservative, on account of, you know, the conditions around us and on account of the war on terror. It's complicated because somebody like Mumtaz Qadri, who assassinated the governor of the Punjab, is seen as a hero. It's complicated because of Saudi influence in Pakistan, but I think – I actually believe that the killing of Osama bin Laden was a major – sort of changed the game. And I – and you know, the Taliban movement in Pakistan or the al-Qaida movement was – he may have been the poster boy, but once you remove that poster boy, then you know, there's – there is serious vacuum. So I think that it did change a great deal.

[01:21:58]

I was telling Ashley also that this threat – you know, in 2011, there've been far fewer suicide bombings than there have over the last three years, and there's still a lot of suicide bombings taking place, but there're far fewer. Fewer people are being killed on account of Taliban attacks. So is that – I think that's a good sign. I think maybe the – maybe the drones are helping. Maybe the operation in Malakand in Swat in 2009 – maybe that helped. Maybe the Pakistani military has said that, you know, it's time to put a stop to the monsters that they've created.

So maybe all those factors and maybe, you know, so they – you know, maybe the movement is broken because of the killing of Osama. So I think there's been a change, but that is not to say that there is just trouble still brewing. There are problems; there are different types of groups who are very active in Pakistan, who have official support and patronage as well, and we know that. So, you know, it's – they do exist, but things have shifted after 2<sup>nd</sup> of May.

MR. TELLIS: We'll take one last question because Akbar has to go back to New York and so – yes, ma'am.

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MR. ZAIDI: Or I could take –

MR. TELLIS: If you would just wait for the microphone for me. Thank you.

Q: Akbar, Paula Newberg from Georgetown. Akbar, I'm going to ask you one of those questions that probably should have come at the beginning rather than the end. But could you just talk a little bit about the micro economy? You mentioned the urbanization without mentioning whether this was internal migration or population change. You didn't talk at all about what's happening to the class structure and whether this – the growth, whether high or low, reflects a very different kind of economy that is being created or the absence of an economy? And this – the answer to any one of those questions has a tremendous effect on what might count as future governance for the country –

MR. ZAIDI: Right.

Q: – you know, aid notwithstanding.

[01:23:48]

MR. TELLIS: We'll take one more. Arshad (ph) has a question.

MR. ZAIDI: Yeah, sure.

Q: (Off mic) – you indicated, you know, that the Pakistani military is going to go out of business if they become friends with India. I'm wondering if there are any signs – because Pakistani military is also a big business conglomerate – are there any signs that they're now hedging their bets towards peace with India? Are they shifting their investments in any way? I mean, how do you make them partners in this by giving them economic incentives?

MR. ZAIDI: That's, again, as – I think I actually answered that question a little while ago, saying we don't know – (inaudible) question – and I think this is the same thing. I just think it's too early to tell.

This – the signs are good; I think that's important. You know, for once we can say, certain things are happening, which are surprising – the MFN status – which doesn't mean much, but it's a good sign – signal – the fact that the military is not interfering or they're giving the – giving their approval to go ahead. So these signs are good.

[01:24:47]

Now, what else they're doing behind the scenes, whether they're waiting, they think OK, or maybe there's going to be another Kargil-type of adventure, we don't know. Because, you know, when Vajpayee came in '99 February, Kargil took place just two months later. So one doesn't know. So, you know, with the military, at least I have no idea how they think or if they think at all. But, you know, it's – so that's something. But so far, they are good signals. I – and we can leave it there.

Paula, your question is very interesting. I think what's happened over the last 10 years, the data that we have is that income inequality has grown in Pakistan. There's been an overall shift of per capita income rising, but the distribution has shifted towards those who are already better off. You know, they've benefited most by the bubble economy of Musharraf, but it was aid-oriented or remittances-oriented, or they're the sort of the deals that were taking place in Pakistan. So I think that's one clear indication.

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The poverty levels – I think they may have also increased in the last two or three years. After 2008, you know, the growth rate has been lower in the last three years. Two reasons – two or three reasons: One is the global economic slowdown, the rise in oil prices, rise in food prices; the floods did affect the food production last year and this year. So there's been some sort of negative income effect on that. But, as I said earlier, the rural economy seems to have grown; they're about 40 percent of the population. They seem to have grown in terms of higher incomes, more consumer goods being sold in the rural economy because the price at which the produce was bought was increased – doubled by the People's Party government.

[01:26:32]

The migration – that's been largely internal. I think it's been different types of migrants, from, you know, this is all sort of anecdotal evidence. I haven't seen any study, but so different types, both from – all from – also from the lower and also from the sort of the educated sector who are looking for jobs. And I always wonder where the jobs are? Where are these people finding (remittances?)? One doesn't see a sort of mass open unemployment. The figures are not right. The government says 5.6 percent, but, you know, I don't know what that means. But 5.6 are – percent unemployment – it's obviously much higher than that.

But I was teaching at Karachi University, and I had – I had about 40 students in my class from all over Pakistan, and they all said that they'll get a job somewhere or the other. So, you know, maybe there is a – an absorptive capacity of the economy to – for – because one doesn't see sort of unemployment, which one would expect if the economy was in a crisis. One doesn't see that – one sees agitation in terms of an absence of power – electricity and power, but not – but not so much in terms of the price rise.

Inflation has been – this government has been in office for 36 – 42 months. We've had double-digit inflation for 41 months, so – but there hasn't been sort of massive street protests as there were in, you know, Egypt or other countries in the world. So there's some sort of some sense of – some safety net whether it's through, you know, they are through kinship or whether it's through remittances or the illegal informal economy – so that keeps people going a little bit.

I don't know if that answered the class structure – yeah – yeah –

Q: (Off mic) – just – (off mic) – follow up with, if a percentage of (the value added?) to the economy – (off mic) – and yet there's not a reduction on the other side, that it's either absorbed internally or it is available for trade, it definitely leads you to wonder what the actual political economy is – (off mic) –

[01:28:46]

MR. ZAIDI: One thing that a lot of Pakistani economists have talked about is – which they've suddenly discovered is something called the middle class. It's suddenly – I think it's been around for 20 years, but Shahid Javed Burki and others have been saying that, OK, now it's become a significant player. I think it's become a major political entity as well.

You know, the lawyers' movement was indicative of that; they said that – I mean, and the middle class is not necessarily a very, you know, a revolutionary or progressive class. It's extremely reactionary as well. It's the same people who support the Brotherhood in Egypt; they're the middle class as well. It's not just, you know, the – (inaudible) – element. One needs to be careful of, you know, how – what they can achieve.

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But I think that one sees sort of a middle class as one does in most developing countries who – which is struggling with high inflation, with jobs, with admissions to schools, with hospitals, but it's sort of – it's getting a middle-class consciousness, where perhaps it's more interested in its own rights. It's more interested in certain types of freedoms, which one associates with the middle-class freedoms – you know, access to information, entertainment, things like that.

[01:29:53]

So I think the middle classes has (sic) emerged and, to you, it hasn't – it is playing different types of roles. It's conservative as well as, you know, lean forward, forward-looking in that sense as well. So it's – so I think in the last 10 years that may be sort of a – sort of a group of people who have emerged on the political map, perhaps, earlier but certainly – (inaudible).

MR. TELLIS: Well, this – there's so much work to be done on these issues –

MR. ZAIDI: (Off mic) – certainly – oh, yeah.

MR. TELLIS: – I mean, just trying to understand the class relationships in Pakistan and how they are changing, I think, is something we have not paid attention to and need some more work. But that'll have to wait for another round of conversations. I just want to take the opportunity to thank Akbar; we will certainly get him back. We can't allow him to leave the United States having visited his – the institution where he has a fellowship just once. He will be teaching at Columbia for all of the next calendar year, so we will have opportunities to have him back here and continue this conversation.

[01:30:56]

And you know, just keep paying attention to the website. We will announce whenever we have Pakistan events. We plan to have a series over the next – looking at some foundational questions like interprovincial equity, questions of technical change in Pakistan, and so anyway we will work with Akbar and others to have this conversation in the months to come.

Thank you very much for coming this afternoon.

MR. ZAIDI: Thank you very much too. (Applause.)

(END)

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