Debt servicing consumes 47 and 60 per cent of revenue receipts in India and Pakistan respectively. Similarly, India, Pakistan, and Nepal utilized about two times more export earnings on servicing debt in 1996 than that in 1980.

The situation in Pakistan is particularly worrisome. Since the early 1990s, debt servicing has been the fastest growing item in government expenditure—growing at 21 per cent per annum. All other items have either declined or remained constant in real terms. The unsustainable nature of Pakistan's debt can be realized from the fact that debt servicing has grown four times as fast as GDP during the 1990s. Even in a less indebted country like Maldives, public expenditures on debt servicing have increased by 17 per cent in the last two years alone.

Much of the rise in these interest payments comes from an increasing reliance on costly short-term debt. This is truer of both India and Pakistan, which, unlike other South Asian countries, have increased their reliance on short-term debt between the period 1980-96. In Pakistan, short-term debt has risen by over 100 per cent over the last five years.

Origins of the crisis

What produces these persistently high fiscal deficits that lead to lower growth and a worsening debt profile? Why this perplexing mismatch between resources and expenditures? The answer is reasonably straightforward: political leadership in South Asia has eschewed from fundamental reforms that are often required for mobilizing additional resources and prioritizing existing expenditures.

South Asia's fiscal matrix is an amalgam of sharp inequities and inefficiencies, both in its patterns of resource mobilization and allocation. Any convincing review of South Asia's unjust fiscal policy must first analyse how resources are raised and spent?

Reversal of fortunes: taxing the poor

Governments in South Asia have largely failed to institute a progressive taxation structure that could raise resources from all segments of the society, especially the rich. However, prevailing tax systems reward the rich at the expense of the poor and the middle class.

As discussed below, attempts to raise taxes in South Asia are inadequate, regressive, inefficient, and lack uniformity as well as transparency:

ADEQUACY. South Asia does not collect enough taxes. Tax to GDP ratios, which indicate the ability to tap resources from a growing economy, are low in South Asia. As figure 4.3 shows, compared to international standards, South Asian governments collect a meagre sum by way of taxes. On average, tax revenues in South Asia are only 10.4 per cent of GDP—lower than the developing country average of 15 to 20 per cent and the average of 24 per cent for high-income countries. It is particularly low when compared to several European countries, where tax revenues are between 35-40 per cent of GDP.

But what is even more significant is that these tax ratios are stagnating or declining in many countries. For instance, for the last many years the tax to GDP ratio has remained nearly stagnant in most South Asian countries, particularly India. In Pakistan and Sri Lanka it has recently declined by nearly three percentage points. This is a clear indication of a tax system that remains inelastic and non-responsive to growth in the economy.

South Asia's income tax base remains narrow, since most people refuse to pay taxes and are able to get away with it. Around one per cent of the total population pays income taxes. There are only between 1-1.5 million tax payers in Pakistan and Bangladesh each. Similarly, India has only 8-10 million taxpayers—though it has a sizeable middle class of 0.2 billion people.

EQUITY. Tax effort is not only minimal but also regressive in South Asia. The bulk of this tax burden falls on the poor people, as nearly three-fourths of total revenues in South Asia are obtained by levying indirect taxes. Though many indirect taxes may be progressive and several direct taxes may be regressive, an over-reliance on indirect taxes is generally perceived to be more harmful to the lower income groups than to the rich.

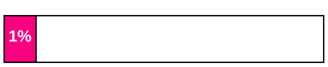
The share of direct taxes in total revenues is abysmally low, and even here the salaried class ends up paying more than the rich. In most South Asian countries the share of indirect taxes in total tax revenues is more than double that of direct taxes (see figure 4.4).

Nearly three-fourths of total revenues in South Asia are obtained by levying indirect taxes

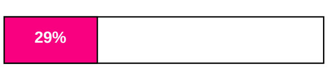
What is more alarming is that revenues from direct taxes in relation to GDP are either declining or stagnating in many countries. Direct tax revenues (as a proportion of GDP) had actually fallen in India by 1 per cent in the thirty years between 1961 and 1991. In Nepal, the relative share of indirect taxes has not changed over a long period of time—and even the growth of income tax revenues is declining.

Even where such revenues have increased, they do not offset the declining share of trade taxes in the wake of liberalization. What is more, such increases remain modest as many of the so-called progressive direct taxes have a *regressive* influence. In Pakistan, for instance, the rise in direct taxes has mainly come from the growth in turn-over and withholding taxes — taxes that finally become regressive as they are ultimately passed on to the final consumers.

Figure 4.4
Too few income tax payers
(income tax payers as a % of total population)



and too little direct taxes
(share of direct taxes in total tax collection)



Source: HDC Governance Tables.

A regressive taxation structure, by taxing the poor relatively more than the rich, tends to compromise equity. It is a looming threat on an already weak social fabric of South Asian society. Though hard evidence is difficult to come by, some South Asian countries like Pakistan have already been witness to such a socially destructive trend, whereby tax burdens are declining for the richer class and increasing for the poorer sections of society. In Pakistan, tax incidence on the richest section of the population has declined by 4.3 per cent against an increase of 10.3 per cent on the poorest strata (Kemal 1994).

EFFICIENCY. One of the prime responsibilities of a tax policy is to ensure the efficiency of resource allocation, a critical condition for investment and growth. South Asian evidence in this regard is not very encouraging. It has been unable to set up economically sensible tax systems that could lead to larger incentives for tax compliance and greater opportunities for production. There are several inefficiencies in the present tax systems:

First, an over-reliance on trade taxes for revenue generation has encouraged smuggling and discouraged domestic production. The abnormally high tariff rates have filled states' coffers (though they have entailed large revenue losses) at the expense of declining national output. The extent of tariff-induced smuggling in Pakistan alone is 5 per cent of GDP. Though the share of trade taxes in total current revenues has actually come down in South Asia (most noticeably in Sri Lanka), it still stood at the high figure of 25 per cent in 1995. In contrast, the share of such taxes has nearly halved at the global level.

Second, multiple tax rates, lack of harmonization between state and federal taxes, and a large number of concessions have created a complex taxation framework, which encourages tax dodg-ing and discourages production. In India, for instance, there are a dozen different customs and excise duty rates. Such complexities normally increase the time taxpayers must spend paying these taxes, providing them the time and incentives to cheat tax authorities.

Third, there is a proliferation of tax anomalies that has too often treated production as an unproductive activity. Tax authorities usually end up taxing production, though it is often not originally intended. In both India and Pakistan, there is a heavy reliance on input taxation, resulting in a system that taxes industrial inputs relatively more than the finished goods. Such anomalies are common in the agricultural sector and the paper-based industry in India.

UNIFORMITY. Incomes are not treated uniformly for tax purposes in South Asia, and this has often undermined the objectives of both equity and efficiency. The inability to treat all incomes uniformly is inequitable because different incomes are treated differently, and it is inefficient because it encourages tax evasion in the disguise of tax-exempted income.

The exemption of agricultural incomes from the payment of income tax is a typical case. While the agricultural sector remains completely exempted from income tax in Nepal, a few innocuous attempts have been made to tax agricultural incomes in India, Bangladesh, and Pakistan. Expectedly, such half-hearted attempts have failed to generate substantial revenues from a sector that contributes 25-30 per cent to gross domestic products. Direct taxation of agriculture contributed only 4 per cent to the direct tax revenues of federal and provincial governments in Pakistan in 1990, though value added in the sector accounted for 26 per cent of GDP (Nasim and Akhlaque 1992).

These tax privileges for the agricultural sector have been vehemently safeguarded by landlords who are not only economically powerful but also well-represented in parliaments. It comes as no surprise then that the central governments in India and Pakistan have been hesitant to bring the agricultural sector into the tax net. Tax responsibilities have conveniently been transferred to provincial governments through constitutional provisions—an arrangement that suits the powerful lobby. Abysmally low targets are set and there are major problems meeting even these targets. In Pakistan, for instance, the Punjab Government has collected a meagre sum of less than Rs 1 billion against a target of Rs 2 billion in 1998.

Direct agricultural taxation offers some promise for revenue generation. It has the potential to tap resources not only from agriculture but also from the non-agricultural sectors, since agriculture offers an ideal tax haven for many industrial incomes as well. Many resourceful landlords have set up industries, and the agricultural sector offers them a safe haven for hiding these industrial incomes. Conversely, many industrialists have acquired large tracts of land to hide their industrial incomes. Perhaps, the dividing line between agricultural and industrial incomes is fast blurring in many parts of South Asia.

But the agricultural sector needs a level-playing field, before any serious attempt for agricultural taxation is undertaken. The agricultural sector has historically been exposed to a good deal of concealed taxation—through under pricing of major crops and over-valuation of exchange rates. These distortions provided a disincentive for agricultural production and, thus, came out as a heavy tax. Many of these distortions have already been weeded out by the recent liberalization of domestic and international prices.

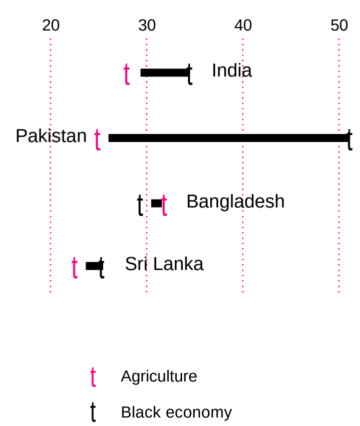
Large black economies pose another challenge to tax authorities. In many South Asian countries black economies (as a percentage of GDP) compare in size with agriculture or industry (see figure 4.5). These parallel economies remain exempted from income tax, undermining government's attempts to raise revenues. They also explain the declining share of economic output by the public sector. In India, one-fifth to one-third of the total economy is dominated by black market. In Pakistan recent research has put the size of black economy to 51 per cent of GDP in 1996 (Iqbal et al. 1998) and in Bangladesh and Sri Lanka it is as large as 25-30 per cent of GDP.

The informal sectors pose a similar dilemma. Cottage industries, owner-operated enterprises, and small farms outside the formal system generate substantial amount of economic activity, yet easily escape direct taxation. They are

The central governments in India and Pakistan have been hesitant to bring the agricultural sector into the tax net

Figure 4.5
Black economies command a sizeable share

As a percentage of GDP



Source: Byres 1998; Iqbal et al 1998; Kumar 1999.

There is a great deal of competitive tax evasion in South Asia today

growing but remain largely untaxed. In fact, Pakistan's informal economy has been shown to be growing faster than the formal economy. This is a worrying sign for the country's public finances and a timely reminder of an inefficient and inequitable taxation structure, which is pushing more and more people into the fringes of the economic system.

There are several other tax-free havens in this poor region. In India, the state governments exempt the services sector from sales tax. In Pakistan, the capital gains tax is virtually absent and the industrial and commercial operations of the defence establishment are exempted from the payment of income tax.

TRANSPARENCY. South Asia's taxation system is nontransparent—characterised by widespread tax evasion, lack of documentation, existence of large untaxed sectors, and a weak administrative capacity to collect taxes. There is a great deal of competitive tax evasion in South Asia today. In Pakistan as much as 50 per cent of the total urban income goes unreported. Total annual tax evasion stands at Rs 152 billion in Pakistan—sufficient to clear off the entire fiscal deficit without any additional tax levies. Similarly, tax evasion in India was estimated to be 18-21 per cent of GDP in 1980. Recently, it was ranked among the top five countries noted for tax evasion in a sample of fifty-three countries (1998 Global Competitiveness Report).

Part of this tax evasion can be attributed to tax dodging in the trade sector. Governments lose substantial revenues when imports are under-invoiced and exports are over-invoiced. This is because importers pay fewer duties by under-invoicing and exporters entitle themselves to more duty drawbacks than they are actually eligible to by over-invoicing their exports. In Pakistan, duty is paid on less than 60 per cent of imports. The value of under-invoiced imports in Pakistan between 1972-94 exceeded $10 billion. In Nepal, a large number of imports are under-invoiced by as much as 50 per cent of the import cost.

How to explain this massive tax evasion in a region that depends so heavily on debts and hand-outs? The answer lies in the unholy alliance between tax officials and tax evaders. The customs and revenue departments are widely perceived as breeding grounds for some of the most corrupt practices that the region has known. Public service in tax departments is characterized by low pay and large discretion—a perfect combination for corruption and tax evasion.

Salaries of tax officials are often a minuscule proportion of their daily bribes. Entrenched corruption in these departments has generated an influential bureaucratic cabal that thrives on the continuation of the present highly inefficient system.

There are several other factors that have aided tax evasion. These include: a high level of taxation, a greater degree of complexity in tax laws, significant arbitrariness in tax assessment, and a weak institutional capacity to administer and collect taxes. However, what is more important is that tax evaders are often precluded from any punishment. Corrupt customs officials and tax evaders are rarely put in jail. Perhaps, it pays more to be a tax evader than to be a taxpayer in South Asia. This culture of default is also promoted at the official level when the politicians and higher civil and military servants legally exempt themselves from the payment of duties on expensive import items.

Another manifestation of a non-transparent tax system, besides tax evasion, is the pervasive use of tax favours. There is an intricate politics of tax amnesties in South Asia today—represented by an elaborate network of concessions, exemptions, tax breaks, and tax holidays for the rich and the powerful. Often, it is not the inability but the unwillingness to tax.

In Pakistan such a preferential tax treatment is meted out to powerful business groups through hundreds of Statutory Regulatory Orders (SROs, colloquially known as Swift Route to Opulence), which are used by rulers for granting discretionary tax favours to their cronies. The fiscal cost of these arbitrary concessions is huge. The price tag of such exemptions and concessions was over 2 per cent of GDP in 1991. In Sri Lanka it is at least 3 per cent of GDP. All over South Asia, annual budgets refrain from providing estimates of revenue loss from tax concessions—an exercise that is regarded essential all over the world.

Public expenditures: misplaced priorities

The real concern for human development is not the level of public expenditures but their composition; not the size of public spending but its effectiveness. At the present average of 29.4 per cent of GDP, public expenditures in South Asia cannot be considered as outrageously high.

The more formidable challenge is the use such resources are normally put to. Thus the real question to ask is where do those resources actually go? Who benefits from them? Do they complement private spending or simply crowd it out? These questions have genuine implications for human development. The answer is not too reassuring: the bulk of public spending in South Asia today is directed towards non-priority and low-return investments. South Asian countries spend an extremely large proportion of their expenditures on secondary activities, where opportunities for rent-seeking and power strengthening may be greater than the core activities that governments should be involved in.

Expenditures for social services and development remain inadequate. They are normally crowded out of government priorities by higher spending on defence and debt servicing, investment in prestige projects, inefficient subsidies, support for loss-making enterprises, and the maintenance of large executive structures. For every dollar of public expenditures that is spent on social sectors, Pakistan spends more than four dollars on defence and debt servicing. India spends 70 per cent more on defence and debt-servicing than on social sectors (table 4.5). Such priorities are even more skewed at the central government level: for every dollar on social sectors, defence and debt servicing receive $8.65 in Pakistan and $3.12 in India.

Governments have often borrowed and printed money to finance consumption, not development. And even here, governments have often met the conspicuous consumption of the rich by squeezing the subsistence consumption of the poor. This is even while millions of people lack the most basic requirements of a decent life.

Governments have often met the conspicuous consumption of the rich by squeezing the subsistence consumption of the poor

A good deal of public expenditures in South Asia promote neither economic growth nor human development. Here are a few anomalies:

First, an expanding force of civil servants devours a huge chunk of resources without delivering any matching output. In India, out of every rupee of revenues that the State governments receive, nearly 60 paisas are consumed on wages and salaries of State employees. There has been a growth in such expenditures as well: in Nepal, public outlays on general administration (as a percentage of GDP) have increased by 0.7 percentage points since 1993.

Table 4.5
Claims on public expenditures, 1997

Country	Defence and debt servicing	Subsidies
	For every dollar spent on social sectors	
India	1.70	0.26
Pakistan	4.32	0.16
Sri Lanka	1.50	0.63
Nepal	0.23	0.10
Maldives	0.11	0.02
Bhutan[a]	0.30	0.23

a. year 1996; public expenditures refer to consolidated expenditres.

Source: GOM 1998; HMG 1998b; IMF 1998d; and World Bank 1998k, 1998m, and 1996b; HDC staff calculations.

Public corporations in South Asia are large in size but low in efficiency

Despite such huge expenses, public employment seems to be rising in many countries. In Sri Lanka, for instance, employment in government departments and ministries has risen by more than 15 per cent since 1993. There is a catch here: public servants are not paid properly and yet expenditures on public employment are rising. This is because governments have preferred a large and low-paid bureaucracy to a lean and well-paid administration.

Second, public expenditures on defence and debt-servicing constitute nearly three-fourths of central government budgets. Debt-servicing alone consumes as much as 66 per cent of total government revenue. Lack of financial discipline has increasingly pushed governments into costly domestic borrowing, raising the servicing costs of total public debt. The average interest bill of Indian States, for instance, has increased by 0.5 per cent of GDP since 1990. Similarly, despite a decline in real defence expenditures, South Asia still spends 71 per cent of its combined expenditures on education and health on defence, compared to the developing country average of 60 per cent. The most striking example is that of Sri Lanka, where military expenditures (as a percentage of total government expenditures) have increased by 450 per cent between the period 1981-97.

Third, generous subsidies entail huge fiscal cost in many South Asian countries. Devoted mainly to the agricultural sector, subsidies account for 1.5 per cent of GDP in India and 0.5 per cent of GDP in Pakistan. For every 100 paisas of the Indian budget, 7 paisas go towards subsidies. Besides inflicting a considerable fiscal cost, subsidies are also known for creating micro-economic distortions by encouraging over-exploitation of natural resources, and benefiting the relatively affluent sections of society. In India subsidies to the agricultural sector have shown to be benefiting the rich farmers and have promoted capital-intensive farming (Joshi and Little 1995). Recent research for Pakistan also exhibits that the reduction of subsidies would harm rich more than the poor (Iqbal and Siddiqi 1999).

In many South Asian countries there has been a modest decline in central government subsidies, particularly those targeted to the export sector. But increasing outlays on subsidies by provincial governments have often negated such reductions. Thus, despite a decline in the relative size of subsidies, the aggregate size of subsidies has actually increased. The total explicit subsidies by the central government of India, for instance, have annually grown at the rate of 19 per cent since the 1970s. What is more, the total size of subsidies grows even more, if hidden and implicit subsidies in the provision of electricity, water, credit, and transport facilities are properly accounted for. If hidden subsidies are included, total subsidies in India amount to 15 per cent of GDP. These concealed subsidies add to the fiscal deficits as well: indirect subsidies have contributed between 3.64 and 7.67 per cent of the overall fiscal deficit in Pakistan alone.

Fourth, huge losses of public enterprises act as a significant claim on budgetary resources. Between 1972 and 1990, South Asian governments have extended nearly fourteen times more credit to the public sector (as a percentage of GDP) than the governments in East Asia. The combined deficit of just seven large public sector corporations in Pakistan equals 1.7 per cent of GDP. Such losses were 2 per cent of GDP in Bangladesh in 1993.

Public corporations in South Asia are large in size but low in efficiency. Decades of protectionist policies have made these organizations non-competitive, reliant on subsidies, corrupt, and significantly over-staffed (box 4.2). Most of these corporations do not have the financial capacity to discharge their key liabilities relating to taxes, debt servicing, and transfer of dividends. They provide key economic services, such as electricity, transport, and telecommunications, at a cost phenomenally higher than that in private sector.

Public money that is regularly pumped into such enterprises yields low or negative returns. In Nepal, gross return on public investments in state-owned enterprises was only 0.55 per cent in 1996, whereas such returns were negative for 39 corporations in Bangladesh in 1993. Obviously, such investments would have yielded much more if they were made in the private sector. In India, between 1976-87 the real rates of return on public sector manufacturing were five times less than those in private manufacturing.

Loss-making public enterprises are not only enlarging the fiscal gap, but are also holding down investment activity as the cost of their inefficiency is often passed on to industrial producers in the form of higher taxes and overpricing of power for industrial and commercial consumption. A 1993 survey in Bangladesh discovered that around a half billion taka worth of production was

Box 4.2 The steal mills of South Asia

From steel mills and power authorities to transport and airline corporations, public enterprises in South Asia are often viewed as a microcosm of the wider financial mismanagement in the region. They have served political constituencies, filled the pockets of bureaucrats, absorbed the kith and kin of their employees, and pampered to the demands of powerful lobbies in the industrial and agricultural sector.

State enterprises have been a victim of many populist policies. Most public enterprises remain significantly overstaffed, since they have often been used as employment exchange for political workers. In Bangladesh most public corporations are overstaffed by 20-50 per cent. In Bangladesh's public transport sector, the number of people operating these vehicles were ten times more than the number of vehicles. Similarly, the state electricity boards in India also remain considerably overstaffed with around a million employees.

Undisciplined unionization has made matters worse. While unions have sometimes protected worker interests, their influence has generally been perverse in other cases. In Pakistan's Water and Power Development Authority (WAPDA), even a lineman could not be hired without the consent of union leaders. As a result, a certain labour aristocracy has emerged in many corporations, which wields considerable influence in key decisions—from hiring new employees to contracting out procurement orders.

Most public enterprises in South Asia are insulated from market competition and lack any commercial orientation. Thus, key economic services, such as electricity and water, are usually provided either below the cost of production or on a very nominal profit margin. Much of these prices are deliberately depressed through liberal subsidies to urban consumers and farmers.

Rampant corruption has eroded their financial viability even further. Governments have often filled key administrative positions with political sycophants. The long-drawn investigation of corruption charges against the former chairman of Pakistan Steel provides a relevant example. Be it water, electricity, or gas, there are widespread instances of theft. In Pakistan, for instance, power theft is so common that even some sitting federal and provincial ministers were found involved in this pilferage. Those found guilty were so influential that WAPDA had to seek assistance from the armed forces for recovering outstanding dues.

Add to this the low investments for the maintenance of technical equipment. Wastage is common between the generation and distribution of electric power and gas. Such theft and technical leakages are so high that in Bangladesh 'for every 100 kWh produced only 59.6 kWh is actually paid for'.

Systems losses in public power utilities, 1998

Country	Systems Losses (%)
Bangladesh	33
India	23
Pakistan	23
Sri Lanka[a]	18
Nepal[a]	26
World	8-10

a. Figure for year 1995.

As the table shows, systems losses in South Asia's power utilities are two times as high as those in the rest of the world. Such losses are also common in the provision of gas and water. In Bangladesh, systems losses in water and gas authorities are 50 per cent and 26 per cent respectively.

Such gross mismanagement has taken many of these public enterprises to the brink of financial insolvency. Commercial losses of state power boards in India were about 24 per cent of GDP at the end of October 1998. The states often need to dole out public money to keep these boards afloat. Thus, in 1995, power subsidies by the Indian state governments equalled 1.5 per cent of GDP.

Even public transport services, like buses and railways, run at a loss. In 1997, eighty-nine out of ninety-three Peoplised Bus Companies in Sri Lanka ran at a loss. Many of these buses are idly parked in company garages due to lack of repair and theft of key spare parts. Fewer buses are able to ply on roads. Thus, only 30 per cent of the vehicles of the Bangladesh Rural Transport Corporation were worthy of road travel in 1995. Similarly, the rail transport in Pakistan incurs financial losses, though trains are full and tickets are sold in the black market.

Quality of services diminishes, consumer welfare declines, and power breakdowns become imminent—when public enterprises run in losses. South Asia needs to make its public enterprises operationally efficient, if it wishes to meet the demands of a growing private sector. The Indian states of Haryana and Orissa have already shown the way to reform by giving a corporate orientation to their electricity boards.

Source: IMF 1998a, 1998d, 1999b; and World Bank 1996a, 1997b, 1998k and 1999b.

Larger allocations alone cannot guarantee better social outcomes

being lost due to power shortages. Huge losses in such organizations have a particularly harmful impact on the lives of ordinary people, as political regimes are more comfortable with regressive additions in utility surcharges than the recovery of unpaid utility dues, reduction of technical losses, and the elimination of corruption.

Fifth, increasing democratization in South Asia has claimed a good deal of public resources. Federal and provincial cabinets have been expanding, demand for both public services and public employment has been rising, development resources have increasingly been sought after by politicians for personal use, and public money has more often been spent on politically motivated projects. Politically divided coalitions often need to spend a lot on maintaining large cabinets. In the Pakistani province of Balochistan, half of the members of Provincial Assembly are provincial ministers as well, costing Balochistan's battered treasury a hefty Rs 55,000 for each minister every month. This is while the Balochistan government is already well-known for surviving on over-drafts from the State Bank of Pakistan.

These are some of the more glaring examples of how South Asia mismanages its limited resources. Clearly, South Asia can easily rectify under-investment in the social sectors, if it manages its resources well. But enhanced investments in social sectors are simply not enough. They need to be complemented by the effective use of resources, as demonstrated by the following section.

The development wasteland

South Asia devotes insufficient resources for human development. Yet a bigger social irony is that these limited resources are put to low-priority use and are often susceptible to wide-spread waste and corruption.

What matters for human development is not just the level of social spending, but its quality and effectiveness. Larger allocations alone cannot guarantee better social outcomes. There are numerous examples of how social expenditures have often been unable to result in commensurate improvements in social indicators. For instance, between the period 1984-95 Bangladesh's Annual Development Programme increased its spending on anti-poverty programmes from 30 per cent to 50 per cent. Whereas poverty, as measured by Head Count Index (HCI), decreased by a mere five percentage points in the corresponding period. Similarly, per capita education expenditure in South India is only 23 per cent higher than that in Uttar Pradesh, but there is a phenomenal difference in the social indicators of both regions (Gazdar and Dreze 1997).

Increased resources for social services become meaningless in the face of wrong priorities, improper implementation, financial leakages, and ineffective provision. As Mahbub ul Haq correctly observed a few years ago: 'there are far too many examples of inefficient and inequitable priorities: urban hospitals for a privileged few rather than primary health care for all; enormous subsidies for the universities while basic education goals await their turn in the budgetary queue; piped water supply to posh localities rather than stand pipes for the masses'.

Scarce resources are often spent on promoting wrong social objectives. For instance, the overwhelming weight of international evidence shows greater social returns on public investments in basic education and primary healthcare. Yet these are the very areas that face the neglect of national budgets. For instance, South Asia devotes, on average, 47 per cent of its education budget to basic education, compared to 70 per cent in many East Asian countries.

Another anomaly includes a disproportionately higher emphasis on curative health and a relative neglect of preventive health services. This is despite the fact that preventive health services, such as maternal health, childcare, health education, and immunization have a more favourable impact on the poor. Moreover, the private sector often takes care of curative health services. Despite some recent improvements, many South Asian countries still attach a higher priority to secondary and tertiary health facilities. In 1996-7, the government of Pakistan spent fifteen times more on general hospitals and clinics than on preventive health care. Nearly 80 per cent of the current expenditure on health in Sri Lanka and about 40 per cent of the total health budget in Nepal is devoted to non-primary health facilities. This mis-prioritization does not come cheap: it costs between $100-600 to save each additional life through preventive health care, whereas the corresponding range for curative care is $500-5000.

Urban health facilities receive a similarly large preference in health budgets. In the North West Frontier Province of Pakistan about 27 per cent of the total provincial budget in 1991-2 was devoted to two teaching hospitals. Though the exact situation varies from state to state, most Indian states devote a larger share of their health budgets to urban health facilities, as opposed to primary health care and rural dispensaries. For instance, for every one rupee spent on rural secondary hospitals in Indian West Bengal nine rupees are spent on urban secondary hospitals. Similarly, Bhutan's capital expenditure programme for health has allocated 47 per cent of its total expenditures on expanding hospital facilities. Clearly, there is a significant urban bias in social expenditures.

Another key feature of social spending, besides meagre allocations and unprioritized spending, is the higher salary component of recurrent expenditures. It is ironic that despite abysmally low levels of remuneration, salaries and wages in most rural and urban hospitals account for about two-thirds of total expenditures. Consequently, maintenance expenditures are squeezed and essential supplies become non-existent, compromising the quality of social services. The result: ineffective provision of social services.

Table 4.6 Pakistan: misgovernance in Social Action Programme
(Cases with unmet criteria as a % of total)

	Recruitment	Procurement	Absenteeism
Health	52	30	59
Education	33	52	39
Population	80	100	39

Source: AGP and MDSU 1998.

While low salaries encourage absenteeism and irregular attendance of teachers and doctors, inadequate expenditures lead to the absence of critical facilities, such as clean toilets, water, leakage-proof roofs, text books, and essential drugs. Teachers lack motivation to teach and are often found engaged in other economic activities during work hours. Similarly, medical doctors are found busy in private practice during official time, visiting rural dispensaries only once or twice a week. A recent report by the Auditor General of Pakistan identifies gross irregularities in staff recruitment and procurement of essential items under the Social Action Programme (SAP) in Pakistan. The Report shows that in nearly 50 per cent of the cases, a proper system for monitoring staff absenteeism was missing. Table 4.6 shows the percentage cases where appropriate criteria for recruitment, procurement, and monitoring of absenteeism was lacking in the health, education, and population sectors under SAP.

There is a significant urban bias in social expenditures

Widespread abuse of social services by the politicians makes these services non-existent for the poor. Locally elected politicians use the social infra-structure to further their own vested interests. School buildings are sometimes used by politically influential landlords for keeping their household cattle. And teachers often need to be in the good books of politicians, if they are to prevent frequent transfers. Recent surveys in India and Pakistan have found that local politicians often use public works programmes for patronizing their favourites—by handing out contracts to cronies and by providing

There is a wide gulf between the promise and practice of welfare programmes

employment to faithful voters (Dreze and Sen 1997; Gazdar 1999).

The cumulative impact of these unprioritized expenditures, rampant corruption, low maintenance expenditures, and political interference is that social services get ineffectively provided. The result, as chapter six shows, is that even the poor use such services with much hesitation. There is no single solution to this dilemma. A suitable and more pro-poor cost recovery policy may be one option. Greater cost recovery can generate the much needed resources for non-salary components of social expenditures that often get starved of resources. Cost recovery through user charges is extremely low in South Asia. For instance, an average 2-3 per cent of public expenditure on education is recovered. Similarly, the average cost recovery from healthcare programmes is 3.8 per cent in India and only 2 per cent in Pakistan. Compare this to the experience of several developing countries that normally recover 15-20 per cent of the revenue.

Beyond the promise of welfare programmes

There is a wide gulf today between the promise and practice of welfare programmes in South Asia. Programmes that are initiated with the honest intentions of assisting the poor often lead to perverse outcomes. Institutional weaknesses abound and implementation failures are common. Some of the disquieting features include: centralized administration; higher per-unit cost; lack of proper targeting; limited participation of women; financial leakages; political interference; and the existence of multiple objectives.

Several projects fall short of implementation. A recent study in Bangladesh has shown financial progress in only 35 per cent of the total projects initiated in 1995-6 (Sen, B. 1998). In many cases, governments have tried to do too much with limited resources. For instance, in Pakistan in 1996 projects worth Rs 700 billion were under implementation, whereas only Rs 85-90 billion were available annually (Hasan 1998).

Many projects do not even see the light of the day. In Pakistan, for instance, it has been estimated that one in every nine public schools is a *ghost* school—schools that are recorded by government but are missing in reality. In the Punjab Province of Pakistan, army has helped government unearth more than 50,000 teachers who were either 'dummies or untraceable'. Perhaps, as social spending increases, leakages are multiplied.

Development programmes are open to widespread abuse and corruption in South Asia. Political abuse remains widespread in Pakistan, as the bulk of development resources are channelled through politicians. Leakages in the Integrated Rural Development Programme in India range from 20 to 50 per cent, and are as high as 70 per cent in Bangladesh's Rural Rationing (Rice) Programme. In most South Asian countries today, the same size of development effort can be delivered at a 20 per cent less cost, if various kickbacks and corruption are eliminated.

Resources for social development are limited, and even worse, these limited budgets don't get translated into the lives of the poor. Increases in social sector allocations have not substantially altered the face of poverty. Some of the key failures of poverty alleviation programmes are discussed in box 4.3. In India such programmes had the capacity to move only 4.5 per cent of the total number of absolute poor out of poverty. Similarly, there was an insignificant decline in several poverty indices due to subsidies (table 4.7).

This failure of social expenditures to reach the poor is a collective failure of the entire economy, polity, and society. Economic policies had limited success in ensuring adequate financial allocations for the *right* kind of social services. Politicians have mismanaged social services even further—by laying illegitimate claim to public resources and by using development programmes to advance their own

Table 4.7
India: do subsidies lessen poverty?

Index	Decline due to subsidies[a] (%)
Head Count	1.71
Poverty Gap	0.90
FGT[b]	0.47

a. Data base for 1986-7.
b. Foster Greer Thorbeck Index.
Source: Radhakrishna et al. 1997.

political objectives. And finally, it is a civic failure as local communities have rarely bothered to ensure accountability for slippage in implementation, teacher absenteeism, and irregular attendance of medical staff.

South Asia needs to ensure that poverty alleviation programmes reach their target beneficiaries. But it requires to move well beyond these poverty programmes to attack poverty in all its possible dimensions. This is because poverty cannot be targeted properly without targeting the basic economic and political structure that breeds and sustains poverty.

The burden of adjustment

In the late 1980s nearly all South Asian states have undergone a series of economic reforms as a part of the structural adjustment and stablization programmes implemented under the umbrella of World Bank and the International Monetary Fund (Table 4.8). The catalogue of recent economic reforms broadly include: liberalization of external trade; exchange rate convertibility on current and capital account; deregulation of interest rates; privatization of loss-making public enterprises; and price, tax, and expenditure reforms.

These economic reforms have evolved South Asia into a more open and a less distortionary region. Some of the results have been positive. Budget deficits have declined (figure 4.6). The share of trade taxes in total tax revenues has come down substantially. Average tariff rates are two to three times less today than in 1980s, and annual inflows of foreign direct investment have increased by as much as seven times.

But the record of economic reforms has been far from favourable—despite these positive trends. While economic adjustments have been made, the quality of such adjustments remains low as the choices made by political regimes have been hard for the poor and soft for the rich. Several governance and institutional failures have diluted the efficiency of structural adjustment programmes.

First, economic reforms remain incomplete and their implementation remains slow and reluctant. Many of the fundamental agendas remain untouched. Reforms have sufficed on a window dressing rather than a deep surgery of these battered economies. Some selected issues:

- Average tariff rates still remain high by global standards, though considerable liberalization has taken place. Liberaliz-

Table 4.8
A calendar of economic liberalisation

Country	Year
Pakistan	1988
Sri Lanka[1]	1989
Bangladesh	1989
India	1991
Nepal	1991

1. Third round of liberalisation.

Box 4.3 Poverty programmes: bypassing the poor

Poverty alleviation remains a 'missed target' despite a plethora of poverty initiatives in South Asia. Selected evidence from several micro studies confirm the non-progressive nature of public spending in South Asia.

The Public Distribution System (PDS) in India, which provides essential food supplies at below market prices to Indian consumers, has problems reaching the poorest Indians. 50-60 per cent of the beneficiaries of PDS have been estimated to be non-poor. PDS network remains limited in poorer states. Poor states like Bihar, Madhya Pradesh, and Uttar Pradesh have received far less food supplies than less poorer states, such as Kerala and Andhra Pradesh.

Only about 40 per cent of the total wheat supply reaches the poorest 40 per cent of the Indian people. The lowest monthly purchases from PDS came from the very poor in India. Thus, the actual income benefits of these subsidies remain limited for the poor: less than 22 paisa for every rupee.

In rural areas, PDS serves to raise individual incomes only modestly, amounting to 2.7 per cent of their per capita expenditure. In North and Central India, where poverty is massive, PDS provides subsidies equal to an income of only Rs 2.5 per person per month. Thus, with a few exceptions, the coverage of PDS remains uneven—with a large number of poor being left out.

Evidence from other parts of South Asia is equally instructive. The percentage of non-poor benefiting from the Food Stamp Programme (FSP) in Sri Lanka was as high as 60 per cent in 1991. In 1987, 30 per cent of the people in the poorest half of the population were not receiving food stamps. Food distribution in Nepal has also tended to benefit the non-deserving—government officials and the urban middle class.

The administrative cost of procuring, marketing, and delivering food and non-food subsidies often entails a financial burden that is several times the actual benefits received by the poor. Though exact estimates vary, it costs between four to six rupees to provide every rupee worth of benefit to the poor through PDS. In Bangladesh the Rural Rationing Programme (Rice) costs nearly six and half taka for transferring one taka of income. In Sri Lanka's FSP the government's cost of providing a given amount of food calories was 250 per cent of the cost incurred by households in getting the same amount of calories.

Even ostensible success stories like the Food for Education Programme (FFEP) in Bangladesh fall short of delivering the poor. FFEP, which links food distribution with school attendance, has recently faced some problems: the leakage to children from non-poor households is estimated to be 26 per cent. And the coverage remains low: it caters to only 13-15 per cent of all students enrolled.

There is an urgent need to improve the targeting and efficiency of such programmes—if they are to benefit the poor at all.

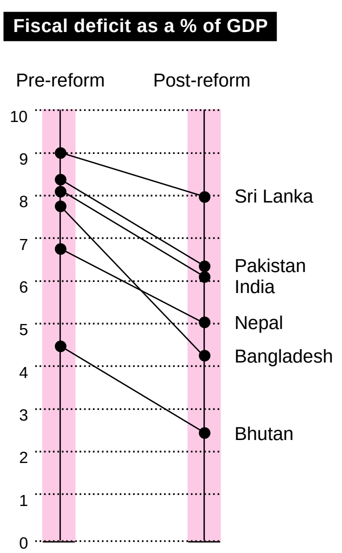
Source: Dev 1998; Parikh 1994 and 1998; Radhakrishna et al. 1997; and CPD 1998.

The institutions needed to assist the economic transition are either missing or remain weak

ation remains incomplete, as South Asian states continue to exert dominant control over major economic activities. What is more, external liberalization has not been accompanied by internal and regional liberalization of trade. Domestic trade is subject to taxes, though controls on external trade have largely been abolished. In India, for instance, the inter-state sale of goods is subject to significant taxation. Similarly, while trade with the outside world has soared, many South Asian countries refuse to trade with each other. A striking example is that of bilateral trade between India and Pakistan, which has consistently been very low (see box 4.4.).

- Financial sector reforms are incomplete. Public banks are still burdened with a large stock of non-performing loans (box 4.1).
- Deficit reduction is slow and lacks continuity.
- There has been a relatively higher emphasis on reducing expenditures than on mobilizing additional resources. Even efforts towards expenditure reduction have been marred by uneven progress. For instance, the progress made by the Indian Central Government is often diluted by setbacks in the performance of states. On the taxation side, additional resources have largely been mobilized through increase in tax rates and introduction of new taxes rather than a major effort to expand the existing tax base.
- While official incentives for foreign investment abound, political and administrative instability have diminished the positive impact of these incentives. The Enron case in India and the controversy with Independent Power Producers (IPPs) in Pakistan are apt reminders of how arbitrary state actions can hamper private investment. But perhaps, Sri Lanka offers the best example, where historical variations in economic performance have shown to be attributed to inconsistent policies of different regimes (Snodgrass 1996).
- The revenues generated from the privatization of public enterprises have failed to match the potential. Between the period 1990-6 the proceeds from privatization were equal to a mere 2 per cent of the combined GDP of South Asia. Besides, the process of privatization has been perceived by some quarters as being non-transparent. In many countries privatization is carried out for bridging budgetary gaps rather than retiring public debt. In Pakistan, for instance, by 1996 only 5.5 per cent of the total privatization proceeds had been used to retire national debt.
- Frequent devaluation of the exchange rates has reduced the anti-export bias. But the region has fallen short of achieving optimal export performance—largely because the non-price bias still needs to be weeded out. An under-developed infrastructure, bureaucratic delays, and poor administration of export promotion schemes still remain the key hurdles in the way of export promotion. The costs of bureaucratic delays and corruption for a garments exporter in Bangladesh are 340 per cent of the costs of establishing the business. Governments have relied more on creating new incentives for exports—rather than ensuring quick availability and better access to existing schemes. In India exporters have to typically wait for six to eight weeks for receiving their duty drawbacks. In many cases, small exporters have been bypassed by such official schemes.

Figure 4.6
Fiscal discipline: improving



Source: GOB 1998b; GOI 1998b; GOM 1998; GOP 1998c; IMF 1998d; HMG 1998b; World Bank 1996b.

Second, the institutions needed to assist the economic transition are either missing or remain weak. In Sri Lanka, for instance, trade reforms were initiated before the establishment of export institutions. Similarly, market regulations to protect the poor and the vulnerable from the private greed of the affluent are either weak or non-operative. Central banks lack the level of independence needed to impose the necessary fiscal and monetary discipline. In many South Asian countries, monetary policy is still conducted by the Ministry of Finance.

There have been limited, if any, legal reforms to aid the economic transition. Archaic laws and court delays have

Box 4.4 Some dangerous myths about Pakistan-India trade

Political expediency triumphs over economic rationality when it comes to bilateral trade between India and Pakistan. Trade is guided by dangerous myths, which as evidence indicates, are a much ado about nothing.

Bilateral trade should not take place without resolving the dispute over Kashmir—But such a denial of trade does no good to either of the countries if the lack of trade only weakens them. Countries don't grow strong when cheap and quality products are denied to millions of consumers, when profitable opportunities are refused to thousands of producers, and when the scope for revenue generation are left unavailed.

India and Pakistan have a great deal to learn from the global experience, where trade is increasingly being used as a prelude to political reconciliation. The Sino-American trade relations offer a convincing example of how trade can be skilfully used to enhance mutual confidence between two politically hostile nations.

Domestic markets in both countries would be swamped by foreign goods—Evidence demonstrates that such an apprehension has no intellectual basis. First, mutual trade would not exceed beyond a few percentage points even after the relaxation of trade restrictions. For instance, even if Pakistan awards a Most Favoured Nation (MFN) status to India, its trade with India would still remain less than 2.5 per cent of its total trade. Second, trade would emerge from different strengths. Indian commodities are generally noted for their cheap prices whereas Pakistani goods are regarded as qualitatively better.

Varying cost structures in India and Pakistan are a concern for many. But even here, the strengths of both countries are different. While labour costs are estimated to be lower in India, labour productivity is higher in Pakistan. For instance, though wages in India are 12 per cent lower than those in Karachi's knitwear industry, labour productivity is at least 25 per cent higher in Karachi.

Third, there is no point restricting goods from neighbouring countries, when domestic markets are already flooded with all kinds of foreign goods through smuggling along a long porous border. While governments have opted for economic isolation, people have always traded. There is a small legal and sizeable illegal trade. Estimates on smuggling vary a lot—from $100 million to $1 billion annually.

Fourth, India and Pakistan should buy from the cheapest source to reduce their trade deficit, even if it turns out to be a hostile neighbour. It makes perfect economic sense if Pakistan buys wheat from the Indian states of Punjab and Rajasthan instead of buying it from Canada and America. As importing wheat from India would entail a financial saving of $25 in freight charges alone on every ton of imported wheat.

Fifth, the combined producer and consumer losses in Pakistan alone are estimated to be Rs 800 million. These losses can be turned into profitable opportunities, if bilateral trade is increased. Producers in both countries can look for price efficiencies, if India benefits from Pakistan's lower count yarn and Pakistan utilizes India's cheap yarn of higher counts. India can also provide cheap textile machinery, dyes, and chemicals—inputs that can make Pakistani products inexpensive. Though qualitatively inferior, Indian machinery can be imported at half the cost of world prices.

But a more promising area for Pakistan is the availability of steel on lower prices from India. This would support both public revenues and basic industries. Only one-third of steel is domestically produced in Pakistan and that too of uneven quality. Reject rates on domestic steel range from 10 to 20 per cent. In comparison Indian steel is both cheap and qualitatively better.

Pakistan: revenue gains from trade with India (Rs mn)

Smuggling estimates ($mn)	Effective tariff rates		
	10%	20%	30%
750	3450	6900	10350
600	2760	5520	8280
500	2300	4600	6900

Note: The dollar-rupee conversion rate is treated as Rs 46 per dollar. The assumptions for smuggling estimates are adopted from Naqvi and Suri 1996.
Source: HDC staff calculations.

And the freight costs from India are only 5 per cent of total costs, whereas such costs are 8-10 per cent otherwise.

Enhanced trade cooperation can also mean lower prices for millions of consumers. The poor are likely to benefit more—through cheap textile clothing, lower bicycle prices, stable prices of essential food items, etc. Recent estimations show that Pakistani consumers can decrease their food bill by 20-30 per cent through increased trade with India. For every agricultural product that is sold for Rs 100 in Pakistan can be made available at less than Rs 40. Obviously, the poor can get the much needed support that has so far been denied to them by badly managed policies.

Domestic producers need some more time before bilateral trade is increased—This is a misleading argument as the infant industries in India and Pakistan should have been adults by now. Do India and Pakistan have to wait for another fifty years before they trade with each other? Agreed that many domestic products may be displaced by foreign competition, but then this calls for making essential adjustments at home, not a boycott of bilateral trade.

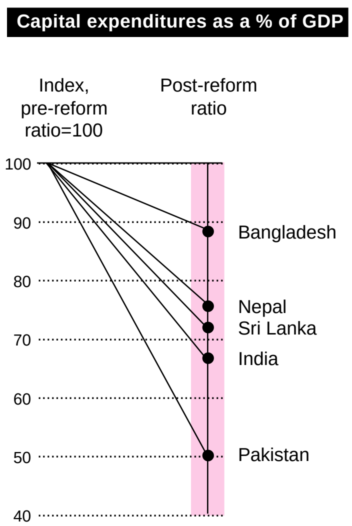
If the stumbling blocks are distorted production incentives, rising costs of energy and industrial finance, and lower productivity of workers, then governments should try to remove them. What is more, India and Pakistan can continue to trade while maintaining a negative import list of key items that they wish to protect from each other for a defined period.

Trade liberalization between India and Pakistan would weaken their domestic economies—This is a classic misunderstanding of free trade that benefits all sides. Europe and America are the largest trading partners of India and Pakistan, and if trade with them doesn't weaken them how can bilateral trade be a harm. Interestingly, Pakistani products that are likely to face intense competition from India are the same that face maximum competition in global markets.

Bilateral trade also means more public revenues, since governments can earn more through custom revenues when smuggled items switch to formal trade. The table shows that public revenues in Pakistan can increase by more than Rs 2 billion even with an unusually low tariff rate of 10 per cent.

Note: The arguments are based on the speeches and statements of Dr Mahbub ul Haq.
Data Source: Khan and Mahmood 1996; Nabi 1997; Naqvi and Suri 1996.

Figure 4.7
Capital expenditures have shrunk since adjustment



Source: IMF 1998d and 1999b; World Bank 1998k, 1998m; World Bank and ADB 1998e.

hindered business activities. In India, the government restricts private firms from liquidating—the avowed objective being the protection of workers. But it normally takes as much as ten years to wind up a company. The judicial system also offers little help when it comes to protecting private property rights and enforcing business contracts. While the rich have access to private thugs, the poor, particularly women, are left at the mercy of petty officials and business Mafia.

Third, economic reforms have not been particularly friendly to the poor. Structural adjustment programmes are often perceived to be socially blind—producing unwanted repercussions for the poor, women, and the environment. In many parts of South Asia the burden of adjustment has fallen on the poor through falling social and development expenditures. Figure 4.7 shows how capital expenditures have declined in relation to GDP since the start of adjustment programmes in the late 1980s. Social expenditures are the first victims, whenever the government tries to balance its budget. And within social expenditures, rural hospitals, primary health care, and primary education are the worst hit. Since 1991 real education expenditures have actually fallen in India (Dreze and Sen 1995). Worse still, even the absolute number of teachers has fallen. During the first two years of adjustment in India, real health expenditures have fallen by 4 per cent. The reduction has been more pronounced at the rural level: public expenditures on rural health care have been reduced by nearly half since 1989 in the Indian states of Karnatak, West Bengal, Punjab, and Andhra Pradesh. Pakistan presents a similar picture, where health expenditures (as a percentage of GDP) have declined from 0.95 per cent in 1988 to 0.77 per cent in 1995, with the largest impact of these expenditure cuts on the poorest households in the rural and urban areas (Khan, S. R. 1998).

The negative social influence of structural adjustment programmes is far from conclusive: only circumstantial evidence is available to establish a connection between economic reforms and poverty. But increase in poverty could be anticipated on account of key reforms that are neutral or sometimes even harmful to the poor. These include: withdrawal of subsidies, expenditure cuts, wage restraint in the public sector, layoffs through privatization, interest rate liberalization, devaluation, and a vigorous tax effort.

The impact of these reforms in different countries of South Asia has been anti- or pro-poor in varying degrees either due to differences in prevailing conditions or due to differences in emphasis on reforms. In India, the head count ratio of poverty has slightly increased in the post-reform period. Some studies have also shown a rise in rural poverty in the aftermath of recent reforms (Pant and Patra 1998). Initially, urban poverty rose modestly before it subsequently declined to previous levels, as reforms slackened in 1993 (Tendulkar 1998).

National poverty seems to be unaffected by the recent series of reforms in Sri Lanka, though urban poverty has registered a slight increase. But this is no sign for complacency: aggregate data hides the widening regional disparities in the wake of liberalization. The ensuing civil war has prevented rural areas from taking advantage of liberal economic policies. Thus, agricultural exports from the Jaffna peninsula have actually declined (Dunham and Jayasuriya 1999).

The most conclusive evidence comes from Pakistan, where nearly all recent studies point towards worsening poverty and income inequality in the wake of structural adjustment programmes. Adjustment programmes have hurt the poor in Pakistan, since real incomes of the lowest income group have declined by nearly 56 per cent since the start of adjustment. Similarly, the Gini coefficient of inequality has risen from 0.35 in 1987-8 to 0.42 in 1993-4.

Economic reforms in Bangladesh have been relatively harmless to the poor. Though poverty has increased since 1985 (mainly due to devastation caused by floods), the incidence of poverty has not changed much since the start of recent economic reforms. The Bangladesh experience demonstrates that adjustment programmes can be made socially relevant, if social expenditures are skilfully protected. The slow pace of reforms and the virtual absence of tough economic reforms may be one reason for this favourable performance. But the credit also deservedly goes to the successful execution of micro-credit programmes, growth of off-farm activities, and the protection of social expenditures, especially those earmarked for safety-net programmes for the poor.

Fourth, economic reforms have only touched the price structures, not the structures of economic and political power. Markets may discriminate against the poor, if productive assets like land and capital are badly distributed, and if a powerful rentier class has access to all economic opportunities. If economic adjustment has to be meaningful, it must be accompanied by social adjustment. Countries must spend as much time correcting social fundamentals as on correcting economic fundamentals.

Unfortunately, governments have conveniently used adjustment programmes as a political instrument—by avoiding painful adjustments and by directing popular wrath towards international institutions for an economic crisis that is largely of their own making. Perhaps, the fundamental reality before and after the reforms has remained unchanged in South Asia. Economic policies have tended to benefit a select group of exporters, industrialists, and farmers. In the presence of weak institutions and intense distributional conflicts, a mere dismantling of economic controls may not be the best hope for South Asia.

Finally, the Bretton Woods Institutions should also accept their part of the blame for the socially harmful ways in which adjustment programmes get implemented. International institutions must make sure that economic reforms are combined with growth and social equity. As late Mahbub ul Haq had correctly suggested:

> 'They (the Bretton Woods Institutions) must…stand firm on slashing subsidies to the rich, elitist groups in a society before subsidies to the poor are touched. They must spend as much time discussing politically sensitive issues such as land reform and corruption as they do now on the distorted prices in the economic system. These are not easy issues; some will be politically distasteful. However, unless the Bretton Woods Institutions are willing to take some political heat on these issues, the cause of the poor—always weakly defended in their own systems—will go by default in implementing adjustment programmes.' (Haq, M. 1998b).

Economic reforms have only touched price structures, not the structures of economic and political power

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If economic reforms are to deliver their promise, they must combat corruption that is rapidly eroding the vitals of South Asian societies. The next chapter addresses the key linkages between corruption and human development and presents a concrete agenda for combating entrenched corruption.