

Policies vs packages

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Published March 28, 2022 - Updated about 8 hours ago

Cost-benefit studies at the Pakistan Institute of Development Economics (PIDE) concerning subsidy and relief packages reforms tend to show that these reforms rarely have a rational economic justification, either in terms of economic efficiency or in terms of equity. But rationality all too often does not determine policy.

There exist two extremes of the management of self-interest within any society. The first is the idealised competitive market model of Adam Smith in which self-interest produces a globally efficient outcome. The second is war, where individuals and groups compete violently for their share of the resource base of the economy.

Whereas the competitive market is productive, war is totally unproductive since it destroys wealth and creates none. In between these extremes lies various mixtures of productive and unproductive activity.

As noted above, unproductive activity emerges from “rent-seeking”, that is, the process of using time, effort and resources to secure a bigger share of the resource base for the rent-seeking individual or group.

Think of policy as a framework similar to that of a cricket match — it never changes during play or even every few games but only after much data and evidence

Subsidies are effectively rents and thus attract rent-seekers who create a “special interest state”. To tackle subsidies effectively, it is argued, one has to tackle rent-seeking behaviour. But according to some, one can never destroy rent-seeking since it is rooted in human self-interest, a motivation that is genetically powerful and unlikely to be changed dramatically.

The response to this gloomy view is that rent-seeking is indeed highly unlikely to go away. But rent-seekers have to have rents to capture, and if the rents are not there they will be thwarted in their aims. The classic means, in view of PIDE, is dissipating rents is to liberalise markets so that they become competitive, thus reducing rents. Further, research by PIDE argues that the social packages often result in continuous dependency in long term and thus an economy remains uncompetitive and needs relief for survival.

Against this, if the rents accrue to those in power, as is all too often the case, then government itself has no incentive to dissipate rents. Rents and rent-seeking become perpetual, and this, no doubt, explains why so many corrupt societies survive.

The answer then appears to lie in much grander realms, namely the whole process of generating participatory democracy such that (a) governments substitute some criterion of social welfare maximisation as their goal, and (b) those previously excluded from rent capture secure a “voice”

to counterbalance those who remain dedicated to capturing rent: rent dissipation through countervailing power.

Ultimately, then, whatever the specific policies for subsidy reform, they are unlikely to work unless the much broader conditions of participatory democracy are in place.

The policy is all about choices and trade-offs. For instance, a choice can be made between announcing subsidies/packages and providing a better business environment. Subsidies and relief packages have certain short term advantages but on the other hand, a better business environment can create employment opportunities.

Thus a trade-off involved is short term consumption smoothing/benefits versus the opportunity to make society capable of surviving on its own. From every aspect, a competitive society is highly desirable as compared to a society relying heavily on special treatments. Another aspect of a policy, according to Dr Nadeem Ul Haque, is that a policy must be clear, learning all the time and slow to change. It should be learning and evolutionary.

PIDE emphasises that policymakers, must not keep on changing policies and rules over and over again. Dr Haque in his tweet depicted policy as a framework that sets up a cricket match. It never changes during play or even every few games policy changes are slow to come after much data and evidence.

To shed light on the role of the government in an economy, PIDE has conducted research and many webinars. In the view of PIDE, the role of a government is to provide the policy to consumers, investors and producers to operate in. It sets the rules, the legal framework, the basis for government monitoring, providing maximum room for economic actors to act and shape the economy as they will.

A study by PIDE showed a concerning level of government involvement of around 67 per cent in the economy. The ever-increasing involvement of the government in the market suffocates the business environment, space for private investment and productive activities.

The need of the time is to bring rationality and economic justification to every policy and reform. The choices must be clear and priorities should be set straight. The subsidies and reliefs given to any segment of the economy must be abolished.

However, the government may choose to gradually eliminate special treatments or involvement within the economy. The gradual route has several advantages: the beneficiaries have time to adjust and “death by a thousand cuts” is usually preferred to sudden shocks. In such a way a competitive environment can be achieved that is based on self-reliance, sustainability and maximum participation of private economic agents in productive activities.

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Published in Dawn, The Business and Finance Weekly, March 28th, 2022