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AGENCY FOR INTERNATIONAL DEVELOPMENT

Washington, D. C. 20523

PROGRAM ASSISTANCE APPROVAL DOCUMENT
(PAAD)

Pakistan (391-0514) Expansion
PAAD Private Investment Program

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AGENCY FOR INTERNATIONAL DEVELOPMENT
DEPARTMENT OF STATE
WASHINGTON, D.C. 20523

PROGRAM ASSISTANCE APPROVAL DOCUMENT (PAAD)

PAKISTAN - PRIVATE INVESTMENT EXPANSION PROGRAM 391-0514

AUGUST 1990

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AID 1120-1 (8-68) PAAD	DEPARTMENT OF STATE AGENCY FOR INTERNATIONAL DEVELOPMENT PROGRAM ASSISTANCE APPROVAL DOCUMENT	1. PAAD NO. 391-0514 2. COUNTRY Pakistan 3. CATEGORY -Commodity Financing - Minimum Procedu - Cash Transfer - Project Assistance 4. DATE

5. TO: The Director, USAID/Pakistan	6. OYB CHANGE NO.
7. FROM: Private Enterprise Office	8. OYB INCREASE TO BE TAKEN FROM:
9. APPROVAL REQUESTED FOR COMMITMENT OF: $ 35,000,000	10. APPROPRIATION - ALLOTMENT: ESF

11. TYPE FUNDING	12. LOCAL CURRENCY ARRANGEMENT	13. ESTIMATED DELIVERY PERIOD	14. TRANSACTION ELIGIBILITY DATE
☐ LOAN ☒ GRANT	☐ INFORMAL ☐ FORMAL ☒ NONE	Sep 1990 - Aug 1997	October 1, 1990

15. COMMODITIES FINANCED

The major items that are to be financed under this Program are: (1) development of services and institutions that promote private investment; (2) assistance to the GOP to reform policy toward private enterprise and promotion of specific demonstration cases; (3) technical assistance and training.

16. PERMITTED SOURCE	17. ESTIMATED SOURCE
U.S. only: $35,000,000	U.S.: $26,720,000
Limited F.W.:	Industrialized Countries:
Free World:	Local: $8,280,000
Cash:	Other:

18. SUMMARY DESCRIPTION

Title: Private Investment Expansion Program (391-0514)

This PAAD authorizes $35.0 million in grant funds, subject to the availability of funds in accordance with the AID OYB/allotment process, as a first tranche leading toward $180 million in policy-based program assistance, private investor support, technical assistance, NGO support, training and conferences.

The Private Investment Expansion (PIE) Program proposed herein will be carried out over a period of seven years and will provide balance of payments support, encourage policy reforms and, develop services and institutions that promote private investment and increase the volume and efficiency of the private sector in Pakistan. There are three major components: (1) Special Projects, Technical Cooperation and Training, (2) Private Investment Promotion (PIP), and (3) Sector Grant Assistance (SGA); (2) and (3) will be approved and carried out subject to the availability of funds and to specific future A.I.D. authorization in accordance with the A.I.D. OYB allotment process.

The STT Component, authorized hereunder as the first phase of the Program, will finance long and short term technical assistance, training, commodities, special project support, including grants, to private institutions and services to complete the design of the PIP and SGA components.

Commodities and services financed hereunder shall be of AID Code 000 source, origin and nationality, except as hereby waived in accordance with Annex G to this PAAD.

19. CLEARANCES	DATE
PEO - Richard Goldman	9/16/90
PRO - Virgil Miedema	9/17/90
EM - Richard McClure	9/18/90
PDM - Gordon West	9/16/90
RLA - Ted Carter	9/17/90
DD - NTumavick	9/17/90

20. ACTION

☒ APPROVED ☐ DISAPPROVED

James A. Norris
AUTHORIZED SIGNATURE

9/19/90
DATE

Director, USAID/Pakistan
TITLE

CLASSIFICATION:

-3-

PRIVATE INVESTMENT EXPANSION PROGRAM

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5.

PRIVATE INVESTMENT EXPANSION PROGRAM
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LIST OF ACRONYMS

ABC	American Business Council
ABLE	American Business Linkage Enterprise, a service of IESC
ADB	Asian Development Bank
ADP	Annual Development Program
AED	Academy for Educational Development
ASSP	Agricultural Sector Support Program
BCCI	Balochistan Chamber of Commerce and Industry, Quetta
BIT	Bilateral Investment Treaty
BOI	Board of Investment
CBR	Central Board of Revenue
CCI	Controller of Capital Issues
CLA	Corporate Law Authority
CMO	Commodity Management Office
COP	Chief of Party
DSTP	Development Support Training Project
EDAS	Education Development Advisory Services
EHS	Environmental, Health and Safety Practices
EI	Entrepreneurs International
EPZ	Export Processing Zone
EXIM	Export Import Bank
FIAS	The World Bank Foreign Investment Advisory Service
FPCCI	Federation of Pakistan Chamber of Commerce and Industry
FSAL	The World Bank Financial Sector Adjustment Loan
FSN	Foreign Service National employee of AID
FSRP	Financial Sector Reform Program
GATT	UN General Agreement on Trade and Tariffs
GDP	Gross Domestic Product
GENESYS	Gender in Economic and Social System Project, a centrally funded AID project
GFCF	Gross Fixed Capital Formation
GNP	Gross National Product
GOP	Government of Pakistan
GSCs	Government Sponsored Corporations
ICP	Investment Corporation of Pakistan
IESC	International Executive Service Corps, a US PVO
IFB	Investment Finance Bank
IFC	International Finance Corporation
IMF	International Monetary Fund
IPB	Investment Promotion Bureau
IQC	Indefinite Quantity Contract
IRS	Internal Revenue Service
KCCI	Karachi Chamber of Commerce and Industry
KSE	Karachi Stock Exchange
LCCI	Lahore Chamber of Commerce and Industry
LPG	Loan Portfolio Guarantee Program
LUMS	Lahore University Management Science
MCB	Muslim Commercial Bank

LIST OF ACRONYMS (Contd)

MOF	Ministry of Finance
NBFI	Non-Bank Financial Institution
NCB	Nationalized Commercial Bank
NDFC	National Development Finance Corporation
NOC	No Objection Certificate
NWFP	Northwest Frontier Province
OECD	Organization for Economic Cooperation and Development
OICCI	Overseas Investors Chamber of Commerce and Industry
OPIC	Overseas Private Investment Corporation
PAAD	Program Assistance Approval Document
PAIP	Program Assistance Initial Proposal
PASA	Participating Agency Service Agreement, USAID
PDM	Project Development and Monitoring Office
PEO	Private Enterprise Office
PIA	Pakistan International Airlines
PICIC	Pakistan Industrial Credit and Investment Corp
PIE	Private Investment Expansion Program
PIFC	Private Investment Finance Companies
PILS	Project Implementation Letters
PPP	Pakistan People's Party
PRE	Private Enterprise Bureau
PRO	Program Office
PSC	Personal Services Contract
PSCIP	Private Sector Commodity Import Program
PSF	Pak-Saudi Fertilizer
PVO	Private Voluntary Organization
SBP	State Bank of Pakistan
SCCI	Sarhad Chamber of Commerce and Industry, Peshawar
SLIC	State Life Insurance Company
SOE	State-Owned Enterprise
STT	Special Projects, Technical Cooperation, and Training
TA	Technical Assistance
TCA	Training Cost Analysis
TDP	Trade and Development Program
UNDP	United Nations Development Program
USAID	United States Agency for International Development
WEC	World Environmental Council, a US PVO

DEFINITION OF FINANCIAL AND ECONOMIC TERMS

Assets	Resources that have the potential for providing future benefits, or other resources of a firm which can be converted into cash and used to pay liabilities.
Bill	A security that represents short-term discount debt, usually issued by the government.
Bond	A security that represents long-term debt.
Book value	The total net worth of a company as estimated in its official accounting records.
Broker/Dealer	A firm or individual that both buys and sells securities as an agent for customers (broker) and also buys and sells securities for its own account and risk (dealer).
Capital	Money or property. Also used to refer to net worth.
Capitalization	The total of a company's long-term debt and net-worth.
Capital Market	The financial markets for long-term securities.
Collateral	Assets that are given as security for a loan.
Debenture	A convertible debt instrument
DFIs	State-owned Pakistani banks which specialize in financing projects and longer-term investment.
Discount	To price a security at less than par value.
Dividend	A payment by a company to its stockholders.
Equity	The capital raised by a company through the sale of stock. Owner's financial stake in an enterprise.
Financial Markets	The combination of the capital market and money market.
Fixed Income Securities	Bonds or other financial instruments which provide periodic interest payments at agreed upon rates.

DEFINITION OF FINANCIAL AND ECONOMIC TERMS
(Continued)

Go public	The act of selling equity, i.e. transferring full or partial ownership to the public for the first time.
Intermediation	Raising money surplus united (e.g. savers), to place it with deficit units (e.g. firms building new projects
Liabilities	Total value of financial claims on a company's assets. Equal to total assets minus net worth.
Liquid	The state of being easily negotiable. A market is liquid when there is a large enough number of traders to make buying and selling easy and relatively inexpensive.
Liquidity	The amount of cash on hand relative to short-term obligations.
Liquidity Ratio	Short-term assets divided by short-term liabilities.
Market Maker	A securities firm that buys and sells securities for its own account and risk at specified prices.
Modaraba	Legal entity in Pakistan in which 90% of annual profit must be distributed to shareholders.
Money Market	The sector of the financial market for short-term securities.
Net Worth	The value of a company's assets minus its liabilities.
OTC Market	Over-the-counter-market. A securities market which lacks a formal decentralized trading arena, such as a stock exchange floor. The trading occurs via telephone, computer, or other types of contacts among brokers and dealers.
Par Value	The value of a security shown on the security certificate itself. Also called the face value.

Primary Market or New Issue Market	The initial distribution of securities by the underwriter. That part of the capital market serving as the market for new long-term capital. Those institutions public and private, needing capital offer shares and securities.
Privatization	The sale of government-owned equity in nationalised industries or other commercial enterprises to private investors, with or without the loss of government control in these organizations.
Secondary Market	Trading in a security after the initial distribution of the securities.
Security	A legal document which provides evidence of ownership or creditorship.
Stock	A security that represents ownership interest in a company.
Underwriting	Buying an issue of securities from a company and reselling it to investors.
Value-added or Net output	The difference between total revenue of a firm and the cost of bought-in raw materials, services and components. It thus measures the value which the firm has "added" to these bought-in components by its processes of production.

I. SUMMARY

A. Recommendations

1. Funding

USAID/Pakistan recommends the FY 1990 authorization of $35.0 million in grant funds to finance the Special Project, Technical Cooperation and Training (STT) Component of the Private Investment Expansion (PIE) Program. These funds constitute the first tranche of a proposed $180 million seven-year PIE Program. It is anticipated that additional funds for Sector Grant and Private Investment Promotion Components will be authorized in the coming fiscal years.

2. Geographic Code

Except as AID may otherwise agree in writing, goods and services financed under the program shall have their source and origin in AID Geographic Code 000. Certain waivers for local procurement are included herein as Annex G.

B. Summary Program Description

Pakistan is in the midst of a shift away from a state controlled economy toward an open market private sector economy. AID has determined that the shortage of private investment capital is, and will be, a major constraint to private sector expansion. In response to this multi-faceted constraint, this Program is designed to achieve the following objectives:

- Improve the policy environment for private investment;
- Strengthen and expand financial markets;
- Provide support to foreign and domestic investors;
- Assist the GOP privatization program; and
- Enhance the voice of private sector representatives.

The initial authorization for the Special Project, Technical Cooperation and Training (STT) component of the Program will provide long-term technical assistance, training, commodities and special project support to achieve these objectives. Funding will also be provided to private institutions to support these initiatives. In addition, project resources will be used to complete the design of the Sector Grant and Private Investment Promotion Components of the Program.

The Sector Grant component, when authorized, will provide cash transfers based on progress in achieving annual benchmarks under a Program Policy Agenda. An initial draft policy agenda is included in this document; this will be refined and negotiated in the coming year.

The Private Investment Promotion component will provide a variety of financial incentive packages to directly assist new private investments, and to develop intermediate financial institutions (IFIs) and organizations which in turn will directly support new investments. Potential incentive packages discussed herein are a private sector commodity import program (PSCIP), a PIE fund to help capitalize private investment finance banks in Pakistan, a privatization grants fund to facilitate specific privatizations, and cooperative investment feasibility and financing programs with the EX-IM Bank and Trade and Development Program (TDP). The feasibility of these options will be further studied in the next year before authorization.

In preparation for the follow-on PAAD Amendment, and so that readers may see the program in context, many of the sections in this paper cover the entire proposed Program. The PAAD Amendment will consist of revisions to certain sections of this original PAAD, including portions of the Program Description--III.B and III.C; all of the Policy Agenda in III.D.; Sections IV.A, B, and C of the Implementation Plan; Sections V. A, B, and C of the Financial Plan; and the Conditions, Covenants, and Negotiating Status as may be necessary. Other sections of this PAAD cover the breadth of all three components.

C. Statutory Criteria and Mission Director's Certification

All statutory requirements have been met for this Program. Statutory checklists and certifications are contained in Annexes C, D, and E to this PAAD.

II. BACKGROUND

A. Role and Importance of Private Investment

1. Private Investment as an Engine of Growth

Economies that invest more generally grow faster**1.
The relationship between investment and growth is especially strong when the investment is private. This is true partly because public sector investments in low income countries are frequently undertaken for purposes of consumption -- public consumption resulting from massive capital projects, private consumption of tax-subsidized wages flowing from employment patronage. Inherently less efficient, such public investments contribute less to future output than private investment.

1** For low and middle income countries for which data was reported in the World Bank's World Development Report, 1989, a simple regression of growth on investment shows that, despite tremendous variations, each extra percentage point of investment corresponded to above one-half of a percentage point higher per capita annual growth rate between 1965 and 1987.

The technical efficiency of the new private investment is frequently generations ahead of the average technical efficiency of the inherited capital stock in low income economies. This higher technical efficiency is due partly to the import of new techniques. This is a particular advantage of foreign private investment. Foreign investment also frequently has the advantage of furnishing fresh financing, improved management techniques, and marketing expertise found in high income economies.

2. Private Investment and Growth in Pakistan

Pakistan registered an annual GDP growth rate of approximately 5.8 percent during 1959/60 to 1987/88, with the agriculture sector growing by 3.6 percent; manufacturing 7.3 percent; mining 6.5 percent; and, construction and services 6.9 percent**2. This growth performance has been founded on a relatively low reported average Gross Fixed Capital Formation (GFCF, or total investment excluding inventories) of about 14.7 percent (See Figure 1). The distribution of GFCF between private and public sectors has been in favor of the latter: the private sector contributed 46 percent of the GFCF compared to 54 percent by the public sector (see Figure 2). The private GFCF has averaged a low 6.5 percent of gross domestic product (GDP). In a recent study (Pfeffermann, Guy P., and Madarassy, Andrea, Trends in Private Investment in Thirty Developing Countries, 1989), Pakistan's private investment as a proportion of national output ranked ahead of only three countries in a sample of thirty**3.

The relative share of private and public sectors in GFCF, however, has fluctuated considerably during the three broad phases of Pakistan's economic history-- early pre-nationalization phase, nationalization era and post-nationalization period.

During the period 1959/60 to 1970/71, GFCF grew annually by 6.1 percent and GDP by 6.6 percent. The share of private GFCF in the total averaged around 51 percent during this period.

These high growth rates, however, were achieved at the cost of a serious neglect of equity issues. The need to address distributive justice coincided in December 1971 with the socialist program of the new Pakistan Peoples Party (PPP) Government. The PPP Government enacted legislation taking over the management and ownership of large as well as small-scale manufacturing (iron and steel, basic metals, heavy engineering, heavy electrical, assembly and manufacture of motor vehicles, assembly and manufacture of tractors, heavy and basic chemicals, petro-chemical, cement, public utilities, vegetable ghee, flour milling, rice milling and cotton ginning); banking; life insurance; petroleum marketing and shipping. The uncertainty

2** Industrial Investment Approval System in Pakistan; (MTech, Islamabad May 1990)

3** Ibid; See Text, Table A and Annex A, Table 1

FIGURE 1: GROSS FIXED CAPITAL FORMATION (% OF GDP)

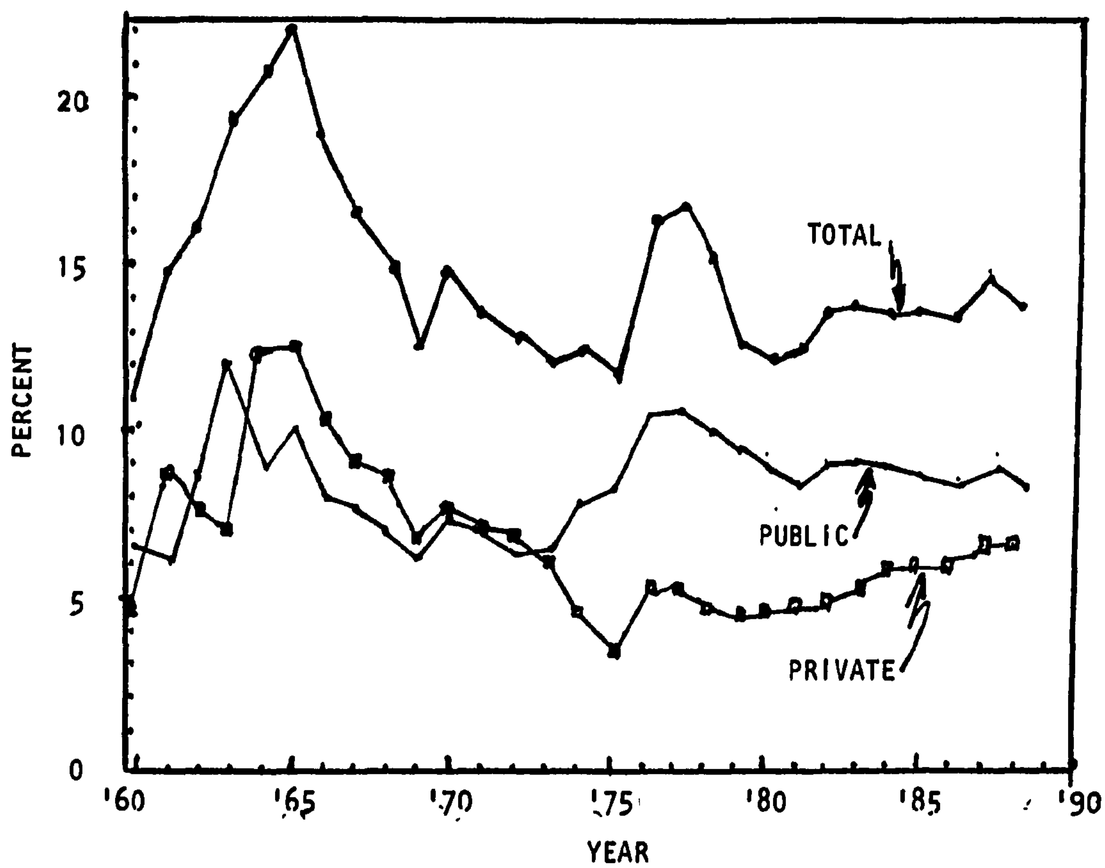
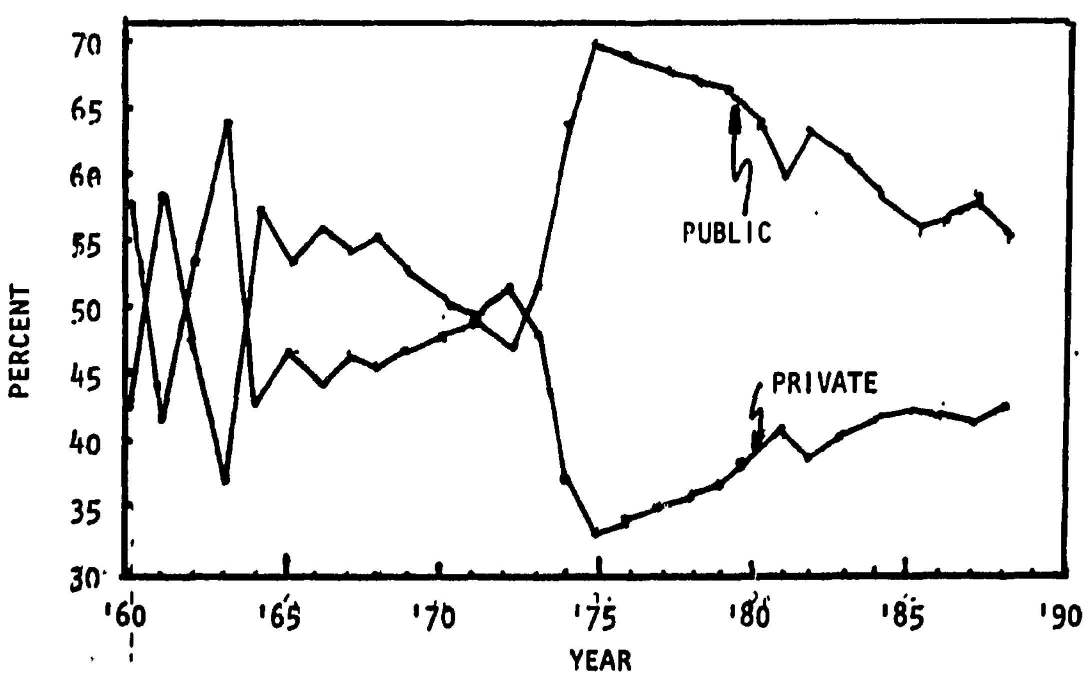


FIGURE 2: PRIVATE AND PUBLIC GROSS FIXED CAPITAL FORMATION



generated by these takeovers resulted in declining private investment which formed only 36 percent of the total during 1971/72 to 1976/77. From 1977/78 onwards, the GOP has attempted to encourage private investment through provision of legal assurances against arbitrary takeovers, selective privatization, and rationalization of monetary, fiscal and trade policies. The private GFCF has responded positively to these measures by recording an annual average growth rate of nearly 9 percent during 1977/78 to 1987/88 and, at the present, the private sector contributes about one-half of total GFCF.

B. Current Constraints to Expanding Private Investment

While the rate of private investment in Pakistan is beginning to accelerate, there remain serious constraints to expanding private sector investment, both domestic and foreign. The continued growth of the economy is largely dependent on the ability of policy makers to overcome these constraints and to create a climate conducive to private investment. This is no small order since many of the problems are deeply embedded in the political and economic fabric of the country. These constraints can be classified into four major headings:

1. Government Involvement in the Economy

One of the principal constraints to increased private investment is the depth and type of Government involvement in the economy. This takes place on a number of different levels.

a. Direct Government investment in the economy

The GOP is one of the largest owners of directly productive assets in the country. There are 173 government sponsored corporations (GSC's) in Pakistan. This list understates the level of government investment in productive enterprises since it only covers companies in which the Federal government has a majority ownership and does not show the companies in which it holds a minority of shares. It also does not show the companies owned in whole or in part by the Provincial governments. They run the gamut of productive enterprises including banking, finance, insurance, export of agricultural commodities, manufacturing, engineering, construction, oil and gas, mining, transport, power, and printing. But as one author put it:

> "Most however have not been able to operate at satisfactory levels of efficiency. An indication of the size of the problem within the public sector is that the combined assets of all the GSC's are Rs. 596 billion and these yielded to the government an after tax return on assets of 1.14% in the 87-88.This is an extremely low return considering that the opportunity cost of capital is 15%. The size of the equity-investment in the GSCs is almost twice the total market capitalization of the companies on the stock exchange. (Zahid Zaheer, Business Recorder, March 12, 1990)."

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The non-financial GSC's produced an after tax loss of Rs. 2.3 billion in 1987. At the same time, these corporations employ some 270,000 people. The size of this workforce is one of the reasons it is difficult for the Government to make changes in its public sector portfolio. For example, rumors about the privatization of Muslim Commercial Bank (MCB) led the employees of the bank to publish bitter advertisements in all of the major Pakistani newspapers decrying the action. This was before any formal discussion of the nature of the privatization with the employees had even taken place.

While the public corporations are not all unprofitable,**4, it is clear that the corporations taken as a whole do not use resources with great efficiency. The usual reasons for this type of performance among public corporations generally hold true in Pakistan: lack of flexibility to adjust to changing markets and input costs; an overstaffed and relatively unproductive labor force; difficulties in firing unproductive workers; and, lack of incentives for managers to improve the bottom line leading to large amounts of GOP assets invested in corporations which are underperforming. The vested interests of civil servants and the apparent inability of the bureaucracy in relinquishing management control of these poorly used assets would appear to be working against the goal of economic efficiency and the general good of the public.

b. Regulatory Framework

Public sector managers and policy makers tend to utilize the regulatory framework to protect public companies and stifle competition from the private sector. This protection can take many forms. For example, the GOP may place import restrictions on commodities competing with those produced by public enterprises. Or, it may refuse to grant an investment sanction because the GOP planned to invest in that area. Sometimes, the GOP has placed outright bans on private sector participation in certain areas in which it wished to retain a monopoly. In general, competition as a means of achieving economic efficiency has not been encouraged in Pakistan.

The financial sector presents an extreme example of this. Five successful privately run banks were nationalized by the GOP in 1974. Today, the nationalized commercial banking system is on the verge of bankruptcy, requiring GOP subsidies each year. The quality of their loan portfolio is highly questionable, with too many loans made on political rather than financial criteria. These banks have not moved to computerize their operation and are inefficient compared to banks in many countries. The system has not been able to encourage sufficiently the much needed mobilization of domestic resources. Foreign banks are tightly controlled and have been regulated out of a number of areas of banking. Only very recently have any private banks been allowed to operate, and then not as commercial banks. Capital markets remain

**4 See, Privatization in Pakistan, MTech, June 1990, particularly Table II, for more information on this subject.

underdeveloped, in large measure due to the lending practices of the nationalized commercial banks (NCBs) and the regulatory framework established by the Government.

Many rules and regulations seem to be designed or implemented in such a way as to discourage both domestic and direct foreign investment. While primary federal sanctioning procedures have been somewhat relaxed recently, the time and delays required in obtaining secondary sanctions for power, water, telephone, no objection certificates (NOCs) from Provincial governments, labor department approvals, etc. are enough to deter all but the most determined or well placed investors**5.

The implementation of the rules is also a constraint because decisions are often made with unnecessarily slow speed or lack of concern for the business persons needs. Many businesses, particularly small and medium ones, report that some officials use their position for financial gain. Regulations, therefore, need to be examined for their reasonableness. However, they also should be designed to ensure that public managers administer the regulations as intended.

c. Poorly Administered Regulations in Certain Areas

While many areas of the economy are overregulated, several areas are underregulated, or regulations are not properly administered. For example, stock markets are not properly regulated, which is one reason for the lack of investor confidence and consequent low growth of market volume. Quality control regulation and administration do not allow many Pakistani products to reach international standards and do not fully protect the Pakistani consumer. Tax administration and compliance is very poor. Accounting standards and regulations leave much to be desired. The legal system is very slow, and in many cases, it may take as long as ten years to get a case through court. Because of this, it is very difficult for banks to collect on defaulted loans, or for business disputes to be settled.

2. Infrastructure and Investment Environment

A second type of constraint to investment in Pakistan is its relatively underdeveloped infrastructure and the often unstable political environment. Frequent power shortages (load shedding), long waits for service hookups, unreliable telecommunications, lack of commercial air freight facilities, and poor road infrastructure are frequently mentioned as major obstacles for foreign investors who are comparing Pakistan to other countries. These problems also slow domestic investment because they delay projects and increase costs. The GOP recognizes these problems, but has had a difficult time allocating enough money for these types of infrastructure investments. The GOP has made an effort to make services available in industrial zones and export processing zones (EPZs). However, a great deal of infrastructure

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**5 See, Small Scale Industry in Pakistan with Special Reference to Their Regulatory Framework, EPRU, June 1990.

investment remains to be done, especially if Pakistan is to compete with other countries in Southeast Asia for foreign investment.

The political environment in Pakistan has been less than ideal for encouraging increased investment. The country has been affected over the past decade by a major war on its western border and the problems created by a huge influx of Afghan refugees. The Kashmir conflict is potentially dangerous and has been damaging to the international perception of Pakistan as a place to invest. The ethnic conflicts in the Sindh, the rise in drug-related violence and the most recent change in government have not helped the country's reputation for stability. As issues such as the Afghan War recede, there is a need for a more clear, long-term statement of GOP policy promoting private investment and for sustained public relations to promote direct foreign investment.

Frost and Sullivan, a company that undertakes risk analysis for businesses, ranked Pakistan's investment climate in about the middle of the 95 countries surveyed, ranking at the same level as countries such as Congo, Costa Rica, Fiji, Ghana, Guinea, Honduras, Israel, Jamaica, Jordan, Turkey, and Uruguay. Pakistan was rated above average for its controls on ownership, dispute settlement, repatriation policy, and investment incentives. It was ranked below average on its approval process, tax rates, domestic and international economic performance, and its exchange controls.

3. Lack of Education and Training

One of the major constraints to changing the economic structure of Pakistan to higher value-added products is the lack of a well-educated labor force. This is particularly true compared to other Southeast Asian countries that have made a large investment in education and training. While there are many well-educated Pakistanis, literacy rates for the population as a whole are estimated to be 25 percent. Pakistani labor costs are low, but so is the productivity of labor.

The provision of basic education is a long-term structural problem for the country as a whole. Improved training is a shorter term need with potentially high returns. Many types of training are needed-- technical and management training; informational seminars; information systems and computers; international marketing management techniques; international quality control; and, communications and public relations. Exposure to modern management practices and the methods of production and quality control used in other countries is also needed.

4. Attitudes toward the Private Sector and Foreign Investment

There tends to be a negative attitude among many government officials towards the private sector, though some improvement seems to have taken place recently. Rather than trying to control entrepreneurs' every move, the Government should try to work with business people to create a more open and productive society. This cooperation will take a real change in attitude by both the private sector and the Government, but that change is necessary if Pakistan is to develop and grow economically.

Part of the problem is lack of a well-informed private sector voice. chambers of Commerce and other business organizations must work together to change the attitudes of the Government and lobby for changes in the economic structure. What's needed is greater democracy and competing self-interest groups. The private sector must support competition as an essential element in its long-run interest. A broadening of the group of investors is also necessary, since the small number that benefited from the first twenty years of Pakistan's private investment was one of the factors that led to popular support for the nationalizations of the 1970's.

The changing GOP attitudes to private investment have also inhibited the flow of direct foreign investment which remained stagnant at low levels until about 1978. Despite recent improvements, foreign investment in Pakistan is a fraction of its level in the Philippines or Malaysia, for example, despite the fact that Pakistan's total gross national product (GNP) is greater than that of either of these two countries.

Limited direct foreign investment appears to be a major constraint in promoting an export oriented growth strategy. (See Annex A). Pakistan has not been able to achieve export diversification either in terms of commodities or destinations and is fast losing ground to other Asian competitors. In a recent article by Gustav Papanek entitled, "Pakistan in Danger of Economic Stagnation**6," Papanek demonstrates how Pakistan's exports of electronics, footwear, and furniture to OECD (Organization of Economic Cooperation and Development) countries have stagnated compared to rapid progress made by Malaysia, Indonesia, the Philippines and India**7. In electronics, for example, Pakistan's exports to OECD countries in 1972 amounted to $2 million compared to $0 for Thailand, $1 million for the Philippines and $2 million for China. In 1987, Thailand, the Philippines and China had attained, respectively, export levels of $559 million, $938 million and $663 million against corresponding Pakistan exports of only $4 million.

C. Program Rationale

1. Overall Program Strategy

While Pakistani efforts to effect long-term changes in attitude, investment in infrastructure, and improved education are important, the Private Investment Expansion (PIE) Program will focus its efforts on objectives that bring the highest return over a short and medium timeframe. These objectives are:

a. Improve the policy environment for private investment

**6 Papaneck, Gustav F., "Pakistan in Danger of Economic Stagnation," Business Recorder, July 22, 1990.

**7 Industrial Investment Approval System in Pakistan; (MTech, Islamabad May 1990)

b. Strengthen and expand financial markets

c. Provide support to foreign and domestic investors

d. Assist the GOP privatization program

e. Enhance the voice of private sector representatives

These objectives and the action plans are described in Section III.

2. Relationship to AID Strategy and Experience

USAID/Pakistan has been a leader in policy dialogue, supporting liberalization and private participation in the sectors of its primary activity: agriculture, energy, health, population, and education. USAID has also recently undertaken private- enterprise oriented activities such as the Private Sector Power Project (391-0494), the Shelter Resource Mobilization Program, and the research activity, Analysis of Corporate Sector Constraints in Agriculture, under the Food Security Management Project (391-0491). USAID has now adopted a strategy for private enterprise assistance with increased emphasis on investment-oriented activities. The PIE Program will be a major element in implementing a coordinated program of private investment expansion.

3. Relationship to GOP Strategy and Programs

In 1988, the GOP reached the conclusion that the pattern of growth pursued since the nationalizations of the early 1970's was not sustainable. Financial imbalances were building, particularly in the GOP's internal and external debts and in the portfolios of Pakistan's financial institutions.

GOP budget deficits in the 1980's were too large to be financed, even by Pakistan's relatively rapid economic growth. Thanks to Pakistan's continuing economic growth, the budget deficit could theoretically be as high as about 5 percent of GNP and the Government's debt and interest payments on that debt would still remain stable as a proportion of GNP and as a proportion of the Government's revenues. However, annual budget deficits, which started in the 1980's at close to 5 percent of GNP, rose to over 8 percent by 1986. The cumulative borrowing to cover the budget deficits, minus loan repayments, raised the Government's outstanding debt from 50 percent to 70 percent of GNP, and from 3.5 times to 4.5 times the size of the Government's revenues.

Budgetary expenditures for interest payments on this mounting debt rose from 2 percent of GNP to over 5 percent. Thus, although the GOP's overall spending rose by over 2 percent of GNP, social and developmental spending fell by 2 percent of GNP.

Pakistan's foreign debt was also growing. Although the GOP's new borrowing in the 1980's drew increasingly on domestic sources, foreign borrowing nonetheless grew faster than earnings from workers' remittances and from exports of goods and services. Consequently, the proportion of these earnings paid out as external debt service (interest plus repayment of principal for medium and long-term debts) grew from roughly 15 percent at the beginning of the decade to an estimated 30 percent after 1985.

Debt was also building in the financial and enterprise sectors. Enterprise investment and operations were financed by borrowing to an inordinate extent. This was encouraged by a number of policies: channeling donor funds through public-sector development finance institutions (DFIs), nationalization of commercial banking in the 1970's, the GOP's directed credit policies for specific sectors, some low fixed interest rates, lax banking regulations and rules concerning non-performing loans and capitalization of financial institutions, and investment capitalization requirements.

As a result of these factors, Pakistan's lending institutions developed heavy burdens of bad loans. While the amount of loans to private enterprise at Rs.110 billion on June 30, 1987 was much more important than loans to parastatals, rough estimates of overall bad loan levels were nonetheless in the 25 percent range for some banks (compared to average bank capitalization equal to about 2.9 percent of liabilities).

GOP leaders concluded that further debt accumulation had to be halted and that mobilization of private investment was needed. This adjustment began in 1988 and is taking a number of forms.

Primarily, the GOP has restrained its own spending, so as to begin to redress its fiscal imbalances, as well as to reduce aggregate demand in such a way as to slow the tendency toward excessive foreign indebtedness. Thus far, relatively little progress has been made in broadening the tax system in order to allow revenues to keep pace with income growth and price inflation. The number of exemptions from import and sales taxes has been reduced, however. Secondly, the GOP has also continued to adjust official exchange rates in line with other prices in order to cap excess demand for foreign exchange. Thirdly, the GOP has started to adjust interest rate and banking policies. Low fixed lending rates were raised (i.e., in agriculture and housing) and artificially high borrowing rates were lowered (e.g., the GOP's national savings schemes), in the first steps of a process that is intended to provide a positive interest-rate spread in the economy and allow private financial institutions to mobilize private financial resources. A process of regulatory change was initiated to permit and encourage the formation of investment companies and housing finance companies in the private sector. Partial privatization of the nationalized commercial banking sector is being studied seriously.

To complement these financial stabilization measures and to ensure continuation of growth on a financially sustainable basis, the GOP has determined that private investment, including foreign direct investment, should assume more importance. As an initial step, the GOP has cut back its regulations that actively discourage private investment by reducing the range of potential investments that must receive GOP permission ("sanctioning"). This requirement now remains only for a small number of sensitive sectors and for capital investments greater than Rs. 1 billion (estimated to be less than 15 percent of total private investment).

Another important tool being used by the GOP to encourage investment has been tax concessions. Like rolling back investment sanctioning requirements, tax concessions are essentially marginal corrections in an underlying factor that basically discourages investment: the commodity taxation system. The GOP's tax system emphasizes heavy taxation of various imports, while many other imports are exempted. Negotiations between the GOP and concerned private enterprises can result in wide, apparently arbitrary changes in rates and exemptions.

In recent years, the GOP has also targeted an increasing portion of credit from NCBs, and public or mixed-sector DFIs to the private sector. While the private sector trend in itself would tend to increase private investment, this policy also causes distortions in the financial sector, in choice of private investments, and in the instruments used to finance investment.

Finally, while privatization is related to private investment, the GOP's privatization program has not yet resulted in increased private investment, except in the sense of portfolio investment. The GOP's privatization efforts to date target only partial divestiture of shares, with no divestiture of management to the private sector.

The GOP is seeking new ideas and assistance in going beyond these limited initiatives to more active and effective methods of promoting private investment. This was the focus of the January 1990 meetings of the US-Pakistan Economic Subcommission, in which USAID participated along with representatives of the US Departments of State and Commerce, and the Office of the Special Trade Representative.

The proposal of a USAID-supported private investment support program was welcomed by the GOP during the Subcommission meetings, which also discussed the possibility of a Bilateral Investment Treaty (BIT), a bilateral tax treaty, investment and trade missions to Pakistan (possibly organized by OPIC), and the idea of putting a number of US investors on a "fast track" for GOP sanctions in order to serve as examples of what can be accomplished and as test cases of what the obstacles are to increased foreign investment.

4. Relationship to USG Agency and Donor Programs

The Private Investment Expansion program, perhaps more than other USAID projects or programs, is designed to interact very closely with other donors and their programs and with other US government agencies. Together, these institutions will work with Pakistani organizations--both public and private.

The GOP asked USAID to consider financing certain studies as a precursor to privatizations. USAID agreed to do this and entered into negotiations with the International Finance Corporation (IFC had already worked with the GOP on earlier aspects of privatization along with the Rothschild investment bankers from London). In addition, the Foreign Investment Advisory Service of IFC and the Multilateral Insurance Guarantee Agency began negotiations for a program on foreign investment with the Government of Pakistan and invited USAID to be one of the co-sponsors. These are excellent opportunities for USAID to leverage a small amount of AID resources and to participate in privatization and investment activities, as well as assuring PIE program staff of the data and analysis that comes from such work. Relations and cooperative programs with the Embassy Economic Section, with Department of Commerce representatives, and with representatives of the United States Department of Agriculture have always been very close and collaborative. This will continue under the PIE Program and probably expand as the US Government Mission to Pakistan participates in the AID/EXIM mixed credit program and as USAID promotes blending EXIM loans or guarantees with the private sector commodity import program to develop a larger and more powerful financial package. As is explained in detail later, USAID has a program for the energy sector with the Trade and Development Program (TDP). Discussions have taken place and a closer and larger cooperation between TDP and the PIE Program is being designed.

Other collaborative activities with the Department of Commerce were begun after meetings in Washington this past April. The Department of Commerce was briefed on the PIE Program and expressed interest in working on areas of mutual interest. At the moment, the Department is working with the US/Pakistan Business Council. The Council is scheduling a meeting in Washington and USAID will finance public sector and private sector Pakistan representatives. They will attend the council meetings, visit US trade fairs, meet with potential investors, and also promote Pakistan as an investment location.

The Program seeks collaborative efforts within the AID organization wherever possible. One targeted area is participation of Pakistan financial institutions, investment banks and leasing companies in the Loan Portfolio Guarantee (LPG) Program of the Private Enterprise (PRE) Bureau. Several visits to Pakistan have been made by PRE staff and the LPG program is being aggressively marketed by AID staff. This is discussed further in Section III.C.2.

In Islamabad, close working level relations have been established between USAID and the UNDP, the Asia Foundation, Asian Development Bank, the World Bank and the IFC. Both the ADB and IFC are actively considering equity investments in IFIs and private industries, which USAID can help leverage and promote. PIE Program will complement the World Bank and IMF and financial adjustment and trade packages, reinforcing the policy dialogue, preparing independent analyses and providing resident TA and support often missing from bank group programs.

The World Bank is currently the leading donor in Pakistan in the field of trade policy reform and export promotion. However, progress has been slow and the GOP remains skeptical about the feasibility of major reforms.

The Export Development Loan (EDL) to Pakistan was approved in May 1986. EDL was a policy-based loan with one tranche of $70 million and a policy program to be implemented in 12 months. Its objectives included:

- An industrial incentives study, focussing on three sectors: textiles, chemicals, and engineering.
- Deregulation, including relaxation of requirements for investment sanctioning.
- Detailed adjustments in export incentives, to streamline the existing system.
- Development of mechanisms for export finance and guarantees.
- Increased awareness of product quality as a factor in export success.
- A computer-based information system for potential exporters.

EDL was meant to form the basis of a subsequent Industry and Trade Adjustment Loan (ITAL). In 1988 the GOP rejected some of the program's basic conclusions and recommendations.

The World Bank has continued to refine technical proposals in the hope of developing an agenda acceptable to the GOP, particularly the Ministry of Finance. Preparation for the ITAL began in 1989 and further detailed technical work is scheduled for October and November 1990. The ITAL is not likely to be approved until mid-1991 at the earliest, however, a limited amount of reform in trade policy was also included in the program of the IMF's Structural Adjustment Facility, signed in December 1989.

In early 1990, USAID was involved in discussions with the World Bank regarding collaboration with their proposed microenterprise development program. As initially envisioned, AID, in conjunction with Dutch assistance, would have provided technical assistance. Subsequently, it was decided to let the Dutch government assume the entire TA component in light of the resources needed for the priorities of the PIE Program. USAID's more modest small and women's business efforts under the PIE Program will take advantage of studies and lessons learned under the World Bank/Dutch program.

The proposed technical assistance advisor for the Ministry of Finance (MOF) will specifically focus on donor policy coordination. USAID's coordinated intraagency and interagency contacts will prevent the Program from duplicating activities undertaken by others and magnify the impact of the PIE program.

III. PROGRAM DESCRIPTION

A. Goal and Purpose

The broad sector goal of the Private Investment Expansion Program is to sustain economic growth in Pakistan through increased private sector contribution to social and economic development.

The purpose of the Program is to increase the volume and efficiency of private investment through three mechanisms: assistance to the GOP to reform policies and regulations concerning the private sector; development of services and institutions that encourage private investment; and direct promotion of specific investment and assistance to entrepreneurs.

B. Program Objectives

There are five program objectives:

- Improve the policy environment for private investment
- Strengthen and expand financial markets
- Provide support to foreign and domestic investors
- Assist the GOP privatization program
- Enhance the voice of private sector representatives

These objectives, and proposed inputs directed toward each objective, are described below. A consolidated description of inputs financed under the two phases of this program can be found in Section III.C., Program Components.

1. Improve the Policy Environment for Private Investment

a. Current Status

The business policy environment in Pakistan is one of the major obstacles to increased investment in the country, both for international and domestic investors. Many years of tight control have led the GOP to institute policies and a regulatory framework that restrain investment and create unfair protection for public-sector companies. Implementation of many regulations has further complicated the investment picture, particularly for small businesses that do not have the resources or political power to work their way through the maze of regulations and overzealous regulators.

There are a number of policy areas which are of interest to the PIE Program. These include:

(1) Industrial Investment Approval System

(2) Foreign Investment
(3) Privatization
(4) Investment Promotion
(5) International Trade
(6) Regulatory Framework
(7) Financial Markets

USAID has had a great deal of experience working in the policy reform area, both in Pakistan and worldwide. The process has been most successful when detailed policy studies have been undertaken and presented to relevant GOP officials. This model will generally be followed under PIE, with support from private sector organizations that have a vested interest in improving business policies.

b. Objective

The objective of this program element is to improve the policy environment of Pakistan in order to encourage domestic and foreign private investment. Specific policy objectives are set forth in Section III.D.2, Policy Agenda, and are detailed in Annex B.

c. Inputs

The major input under this element will be a technical assistance team responsible for most of the policy analysis, working with the GOP on the policy issues, and implementing aspects of the Program's training and promotion efforts.

The technical assistance team will be composed of the following experts: one US Chief of Party, one US financial economist, one U.S. and one Pakistani Promotion Specialist, one U.S. Capital Markets Specialist (Karachi), one Pakistani Commercial Banking Specialist (Karachi) and possibly one Privatization Specialist.

The Chief of Party (COP), based in Islamabad, will be responsible for the overall project, making sure the various team members coordinate their efforts. The COP will have particular responsibility for formulating the policy agenda in conjunction with USAID. A draft policy agenda is included in Section III.D and Annex B. USAID and the GOP will retain ultimate authority for final policy agenda negotiations.

The policy benchmarks will be supported by a substantial reserve of Sector Grant assistance to be disbursed on the basis of policy performance. Sector Grants are described in Section III.C.

2. Strengthen and Expand Financial Markets

a. Current Status

Pakistan's financial system is facing a number of serious problems. The rate of savings as officially reported was a low 10.2% in 1988-89. Domestic resource mobilization is a priority of the Government, but the

GOP's need to finance the budget deficit through the sale of high interest Government bonds has pulled domestic savings mobilization away from the banks. The nationalized banking system is inefficient, at best, and bankrupt by normal definitions, holding many bad loans in its portfolio. Attempts to allocate credit by sectors and political interference in the banking system have worsened matters. The lack of competition for the NCBs has contributed to the lack of innovation and modernization in the banking system. Foreign commercial banks are carefully regulated and excluded from a number of banking areas.

In the existing situation, the links between the Pakistan financial system and the stock market have not proved sufficient to allow more than a token level of investment banking intermediation between investors and savers. However, there is an expectation that the importance of investment banking services in the Pakistan financial system is likely to increase significantly over the next few years. In this context, the recent performance of some DFI's (particularly the National Development Finance Corporation), modaraba companies, and leasing companies in using innovative modes of financing can be considered to be a good start.

Macro financial policies have, in accordance with the requirements of the IMF's Stand-By Arrangement and Structural Adjustment Facility and the World Bank's Financial Sector Adjustment Loan (FSAL), cut back on the plentiful supply of medium- and long-term credit from NCBs and the DFIs (particularly the phasing out of "bridge financing"), thus forcing enterprises to look for alternative financing. In the past few years, there has been liberalization of the policies of "financial repression" (credit ceilings, sectoral allocation of credit, control over lending/deposit rates) pursued since the early 1970's. Above all, there is a perception that the Pakistan corporate sector may have matured to a point where investment banking services are demanded.

These factors have important implications for the prospective development of the stock market. Already in the first half of 1990, there were 22 new listings with another 26 in the listing process (a 30-40 day process) compared to 38 and 26 in 1989. Oversubscribed sales of the stock of Pakistan International Airlines (PIA) suggests that there is a strong demand for shares in good companies.

Despite the growth in the number of company listings on the stock exchange, however, the KSE-- Pakistan's major exchange-- is undercapitalized and too rarely used by companies. Additionally, inefficiencies in the exchange such as lack of depth (number of shares), breadth (number of investors and investment instruments), and informational disclosure, compounded by charges of inadequate accounting practices, have not inspired investor confidence in the stock market.

The long-term bond market is practically non-existent, with legal restriction against long-term bonds and lack of investor confidence in long-term commercial bonds.

b. Objectives

One objective of financial market development is to improve the operation, depth and breadth of the capital market by establishing a responsive regulatory framework.

A second objective is to support increased competition in the financial sector through assistance to the newly formed Investment Finance Banks and reforms which deregulate the national commercial banks (NCBs) and Development Finance Institutions.

c. Inputs

The major input under this element will be technical assistance to the financial sector through the Ministry of Finance, State Bank of Pakistan (SBP), and Corporate Law Authority (CLA). Attached to the Ministry of Finance, the financial economist will be responsible for helping the Ministry determine the regulatory framework needed to encourage competition in the banking sector, rationalization of interest rates, and development of capital markets, and other reforms. The financial economist will help the Ministry develop its own policy analysis capabilities under the new Deputy Secretary for Policy. Two financial operations specialists, both with experience in banking and capital markets, will be based in Karachi so as to be in close contact with the financial community. These advisors will be housed in the State Bank of Pakistan and the Corporate Law Authority, but will work with a wide segment of the financial sector, including the stock market, investment finance banks, the national and foreign commercial banks, and the Pakistan Banking Council.

Assistance to the Investment Finance Banks will also be rendered through a proposed $20 million PIE Fund. This fund will help capitalize the newly established private investment finance banks. This Fund is described more fully in Section III.C.2.

3. Provide Support to Foreign and Domestic Investors

a. Current Status

The PIE Program will work directly with a broad spectrum of business organizations and private enterprises to foster increased foreign and private investment in Pakistan. There are currently numerous constraints to increased investment, these being access to credit, regulatory barriers, lack of information about US products, lack of promotion efforts and the like. One of the major constraints is a lack of credit and the fact that credit is allocated to various selective sectors within the economy. Another constraint is the fact that the foreign banks are discriminated against in favor of the nationalized commercial banks. The nationalized commercial banks also exhibit performance that is basically non-competitive in nature and much of their dealings are predicated upon political and bureaucratic rather than commercial decision making. Opportunities for increased US investment, increased trade between Pakistan and the United States and increased exports of US products, all of which can result in increased income in Pakistan and employment generation, need to be addressed. Most of these topics have been discussed elsewhere in this paper and need not be repeated here. Opportunities do exist for the stimulation of private investment and the AID inputs described below are intended to at least partially address the problems.

There is also the need for some stability in investment sanctioning procedures and promotional activities. For example, under the last government, a Bureau of Investment was organized under the Prime Minister to expedite sanctioning of projects. The Board also proposed policy reforms to the Economic Coordinating Committee regarding investment sanctioning. (It is understood that the interim government has now moved the Board of Investment back under the Ministry of Industries, a possible step backward.) As the situation stabilizes the PIE Program will attempt to assist organizations and government with further de-regulation of the sanctioning process and the development of organizations whose role is promotion and not review, approval, and delay of investment projects.

b. Objective

The objective is to support at least $400 million in new foreign and domestic investment and to develop intermediate financial institutions that will finance new investments.

c. Inputs

The activities planned under the private investment support element are listed below:

i. The Private Sector Commodity Import Program which provides dollar loan funds through banks for the import of American-made commodities. Loan guarantees for large imports may use the U.S. Export-Import Bank and OPIC programs.

ii. A PIE Investment Fund to support privately controlled Investment Finance Banks in their efforts to lend to the private sector. The Fund will support the development of the capital markets.

iii. Technical assistance to the private sector in the form of two promotion specialists working with the ABC to promote US foreign investment in Pakistan and joint ventures between foreign and Pakistani firms.

iv. The business programs of the IESC which will support specific firms through technical assistance and networking on a cost-sharing basis.

v. The training program of Entrepeneurs International (EI) which provides opportunities for on-the-job training with American companies. This program is to be conducted on a cost-sharing basis.

vi. The Loan Portfolio Guarantee Program of PRE which provides guarantees for loans to small companies not currently served by local private financial institutions, leasing companies or banks.

vii. The Trade and Development Program which encourages investment by funding a portion of a feasibility study.

These are described in more detail in Section III.C, Program Components.

4. Assist the GOP Privatization Program

a. Current Status

Many politicians are beginning to accept the need to privatize government owned enterprises. In 1989, the GOP established a high-level Privatization Committee, with representatives from the Ministries of Industries, Finance and Planning, to oversee and supervise privatization efforts. In 1990, the Government offered for sale 10 percent of the shares of the state-owned Pakistan International Airlines. The decision to divest shares of the nationalized Muslim Commercial Bank has been announced and divestiture of Allied Bank and Pak Saudi Fertilizer Company is being investigated. In April 1990, the GOP requested USAID to finance the cost of IFC's consultancy services for privatization of Pak Saudi Fertilizer Company. Additionally, an ADB sponsored expatriate is currently working with the Privatization Wing in the Ministry of Finance to develop a strategy for privatization of 14 industrial establishments.

The GOP's emerging privatization strategy, however, is ambiguous on two major counts: first, the willingness of the GOP to transfer ownership and management control to the private sector as opposed to minority disinvestment; and second, its political and administrative strength to implement majority divestitures. Lack of a well-defined privatization policy, resistance from the bureaucracy and labor unions, absence of a clear legal framework, and inadequate technical information are some of the factors inhibiting privatization. Privatization plans are particularly sensitive to the negative reaction of the public enterprise work force.

b. Objectives

The primary objective of this element of the Program is to broaden private asset ownership and increase private management of public sector enterprises. A secondary objective is to develop Pakistan's primary and secondary equity markets through divestitures.

c. Inputs

Inputs will focus on two broad areas: first, analytic support for a privatization policy and for development of technical information required for implementing privatization decisions; and, second, establishment of a fund to partially finance the cost of selected privatizations.

i. Analytic Support

Initial analytic support will be provided through the Ministry of Finance to assist in the development of an appropriate policy and operational environment for privatization. Working with the Deputy Secretary for Policy and the Privatization Wing, this effort will provide both research and documentation needed for enabling legislation and rules. Given the highly political nature of this subject, the MOF will dictate the pace and direction of all such policy-related input.

The second set of analytical support will focus on the development of technical information on enterprises to be privatized. The technical analyses on corporate and organizational structure (laws governing ownership, management profiles, employee policies); production technology (type, utilization, maintenance standards); marketing (demand, sales, distribution network); investments (securities, equipment, buildings); financial structure (assets, liabilities, operating costs) will be done.

Technical assistance will be provided. The long-term technical assistance, if required however, will commence in the second or third year of the Program after sufficient time has elapsed for the GOP's privatization plan to become clear. The form in which the GOP decides to implement privatization of such institutions as MCB, Allied Bank and Pak Saudi Fertilizer Company will provide unambiguous evidence of the extent of its commitment to privatization.

The long-term advisor will identify short-term technical assistance needs, oversee assistance on privatization research and documentation, assure development of technical analyses, assist the GOP in implementation of specific privatizations, and, more generally, serve as a privatization facilitator. The incumbent will work primarily with the Privatization Wing in the Ministry of Finance coordinating activities with state-owned enterprises, the Corporate Law Authority, and the Karachi Stock Exchange.

ii. Privatization Funds

A total of $8,000,000 will be reserved under the Private Investment Promotion component of the Program for partially financing privatization costs of selected financial or manufacturing firms.

These costs may include technical fees, "golden handshakes" or other critical financial inputs. It is anticipated that the availability of these funds will help the GOP surmount a major privatization constraint and encourage transfer of majority ownership or management control. (See also Section III.C, Program Components).

5. Enhance the Voice of Private Sector Representatives

a. Current Status

Pakistan's businesses are currently organized into regional chambers of commerce and industries, foreign investment related groups, business-specific associations, locality-based traders bodies, and women's entrepreneur groups. From this large universe, 23 regional chambers of commerce and industry, 2 foreign investment groups, and 103 business associations are affiliated with the Federation of Pakistan Chambers of Commerce and Industry (FPCCI) which, as an apex body, serves as the national business voice.

The Karachi Chamber of Commerce and Industry (KCCI), Karachi; the Lahore Chamber of Commerce and Industry, Lahore (LCCI); the Sarhad Chamber of Commerce and Industry (SCCI), Peshawar; and, the Balochistan Chamber of Commerce and Industry (BCCI), Quetta are the principal fora for articulating provincial business concerns. The Overseas Investors Chamber of Commerce and Industry (OICCI) and the American Business Council of Pakistan represent the foreign investment voice.

These national, provincial and foreign investment business fora currently undertake promotional activities such as seminars, press releases, trade fairs, discussions and formal presentations to the GOP, particularly at the time of annual budget and trade policy preparation.

Their impact on changes in policies on trade and investment is small. One reason is the landlord dominated power structure of Pakistan and the traditional insensitivity of the bureaucracy to private business. The second reason concerns weaknesses in the business interest promotion system. Most business groups (with exception to some degree of APTMA, FPCCI, KCCI, and LCCI) are not adequately organized to develop rigorous business policy reform analyses, further overseas trade relations, and promote investment. The current composition of business groups overwhelmingly favors medium and large businesses (mainly traders) and has a very limited role for women-owned and small enterprises.

b. Objectives

Specific objectives for this PIE Program element are: (i) upgrade the capabilities of selected business groups to advocate effectively national, provincial and foreign investment business interests; (ii) promote linkages between foreign and local investors; and, (iii) demonstrate the practical utility of business group networks. These objectives support the overarching PIE Program goals of democratizing the decision-making process and of encouraging a more open society.

c. Inputs

Program activities will focus on five major areas: (i) institution building of selected business groups to voice more effectively private business interests; (ii) trade and investment services designed to encourage joint ventures between US and Pakistani investors; (iii) private investment policy analyses; (iv) integration of small and women-owned businesses in the overall business institutional framework; and, (v) improvement of environmental, health and safety (EHS) practices. These activities will be complemented by policy initiatives aimed at enhancing private sector voice through effective representation of private sector concerns to GOP's policy-related agencies.

i. Institution Building

Institution building will focus on supporting a variety of trade and manufacturing associations, producer groups and chambers of commerce who express a keen interest, perhaps through a competitive proposal process, to address the above objectives. We expect such grantees will include ABC, KCCI, LCCI, SCCI, and BCCI. Specific activities will include installation of systems to improve networking with members; development of industry specific computerized data bases; dissemination of market information; periodic publication of investment guides; and, preparation of analytical papers outlining business positions on reforming the trade and investment policy environment. These activities will help develop strong business policy analysis cells in cooperating groups. This institution building effort will be undertaken through provision of grants, short-term technical assistance, and training.

ii. Trade and Investment Services

PIE Program activities will be based on a combination of "facilitator" and "promoter" approaches and focus on US trade and investment. Specific trade and investment services will include seminars; trade fairs; reciprocal trade missions; identification of industries for investment promotion; and, joint venture promotion. The ABC will be strengthened to serve as "one-window" facility for investment related information for US investors. Also, closer links between ABC and various local chambers will be established to facilitate contacts between U.S. and Pakistani investors. Primary inputs in the development of trade and investment services will be long-term technical assistance, grants, and training.

iii. Private Investment Policy Studies

The Board of Investment (BOI) and the Advisory Committee on Investment Promotion, or their successors, will be supported through grants to private consulting firms for investment policy studies covering such areas as new investment approval systems, taxation, trade policy, credit, indigenization, and capital repatriation. These studies will be supervised by the Advisory Committee, a body comprised of public and private sector representatives, and responsible for guiding the GOP's private investment promotion activities. The results of these studies will be widely disseminated and discussed at seminars.

iv. Enhancing Voice of Small and Women Owned Business

Small and women-owned businesses are not represented adequately in the chambers of commerce and industry or in trade associations. Although information on women-owned enterprises in Pakistan is very limited, it is possible nonetheless to make a few general observations: these enterprises are small scale, are widely dispersed across the country, and are mainly agriculture based. The PIE Program will provide resources to develop small and women owned enterprises. This might include the development of base line information and subsequent interventions. Services of programs such as AID/W's GENESYS Project may be commissioned to assist local organizations such as the Network of Enterprising Women and the Entrepreneur and Career Institute which are already involved in supporting women in business. PIE funds will partially finance women's training programs coordinated by AED, USAID's Mission ' e contractor for training programs.

v. Environment, Health and Safety (EHS) Control Services

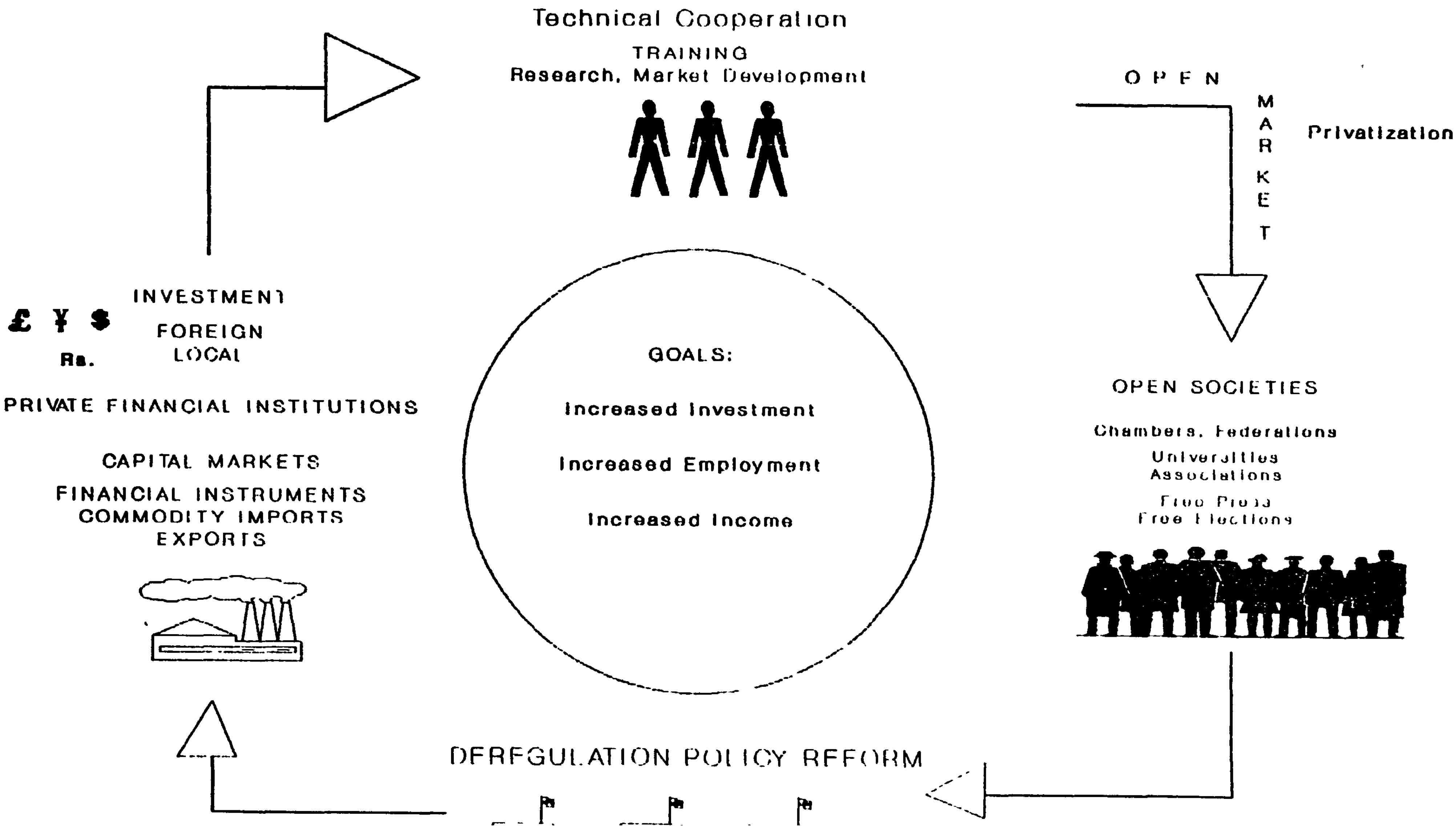
The World Environment Council (WEC), is a New York based non-advocacy, non-profit organization with core funds provided by ANE. PIE will finance a WEC program to increase awareness and improve EHS practices in Pakistan. Near-term activities will include a visit of US experts and TA at selected Pakistani private industrial establishments, on-the-job training in the US, development of technical material, and EHS surveys. Medium-term activities will include public education and training of business owners and managers. The long-term effort will target institutional restructuring and regulation development by the Government and industry.

C. Program Components

The PIE Program's three major components will be mutually reinforcing to achieve program objectives, goals and purposes of the Program. These are: sector grant assistance (SGA); private investment promotion (PIP); and special projects, technical cooperation and training (STT), the latter consisting of technical assistance, training, institutional grants and special projects (See Chart 1). The first two components are non-project program assistance and USAID intends to authorize up to $145 million for them in the latter part of FY91. The third component,

Private Investment Expansion Program

A Wheel of Reinforcing Ideas & Activities



STT, is authorized at $35 million by this PAAD. This phased authorization allows USAID to develop further the policy agenda and private investment support mechanisms during the initial project year. This will allow time for training plans to be initiated and for grants to be negotiated and started. The descriptions below of components one and two and the policy agenda are subject to change and refinement when the FY91 Amendment is issued. For component three, what you see is what you get (see Chart 2).

1. <u>Sector Grant Assistance</u>

Sector grants provide the opportunity to set an agenda with Government for policy reform and deregulation after consultations with the private sector and after an analysis of issues and the presentation of options which lay out clearly costs and benefits. Under the PIE Program, and starting in USAID fiscal year 1991, a framework for short and medium-term policy reform and deregulation will be established.

The policy dialogue aims to replace the role of central planning and regulated pricing with a system that is much more reliant on market signals, entrepreneurship, risk assumption, comparative advantage, and the participation of democratic institutions. Illustrative policy areas and benchmarks that will be negotiated and further clarified within the Program next year are discussed in Section III.D, supplemented by recommendations in Annex B.

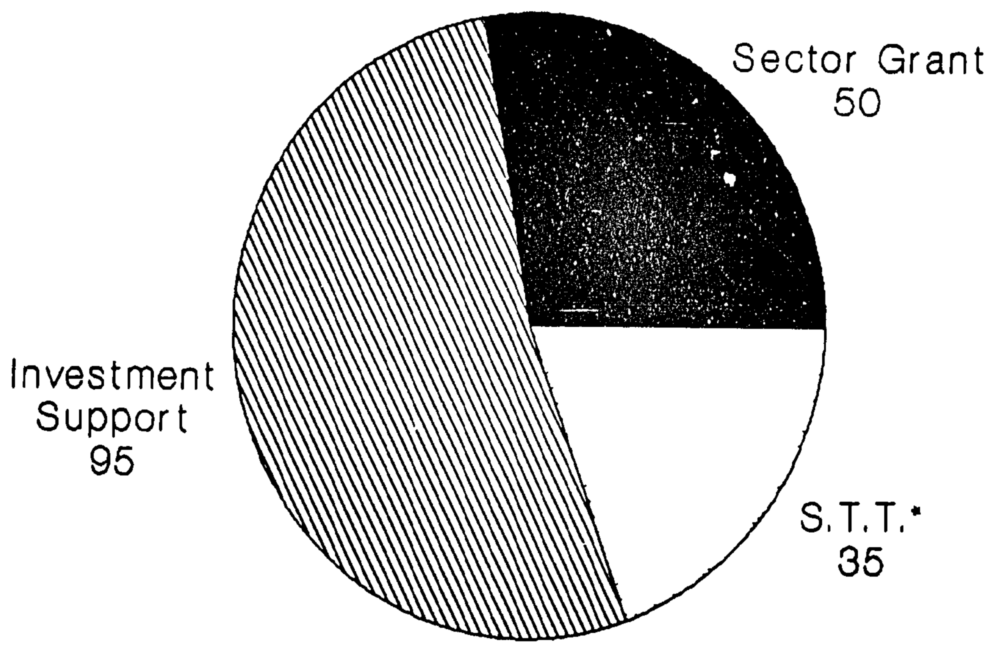
In accordance with AID Handbook 1, Part 7, sector grants will provide a cash transfer subsequent to agreement on a negotiated yearly set of benchmarks for policy reform and deregulation. The sector grants program will not generate local currency and local currency is not required for the implementation of the agreed upon benchmarks. USAID will concur with the Government of Pakistan on the uses of the foreign exchange provided by sector grants prior to obligation of sector assistance funds, and will follow all procedures required such as setting up a separate account and not co-mingling these funds with other GOP foreign exchange resources.

Such a program has been used in the Agriculture Sector Support Program and the same general formula will be followed under PIE. This formula calls for agreeing on a policy agenda in year one which fits within a long term set of targets. Once there is agreement and a commitment to implement, USAID will make the cash transfer. In subsequent years, a new set of benchmarks will be negotiated and agreed upon, and an analysis and review will be held on the status and implementation of the agreed upon reforms and deregulation activities.

If it is determined that both satisfactory progress has been made in the attainment of the benchmarks and that a substantive package of new benchmarks has been agreed upon, then sector grants will be made in the following years. When satisfactory performance is not attained, the grant either will be eliminated or substantially reduced. It is certainly conceivable that in some years there will be no sector grant.

Private Investment Expansion Program

The Components (Figures in Million Dollars)



* Special Projects, Technical Cooperation & Training

2. Private Investment Promotion

The private investment promotion (PIP) component of the PIE Program will consist of a number of non-project, financial incentives to promote private investment. We envisage the following incentive packages will be provided.

1. Private Sector Commodity Import Program

USAID's ongoing PSCIP aids entrepreneurs in Pakistan by providing dollar funds for the import of US equipment. These funds are outside of the credit ceilings allowed banks by the State Bank of Pakistan and are therefore net additions to the pool of available foreign exchange. The PSCIP is often a catalytic input or component of new projects and a vehicle for technology transfer. The program also benefits the United States in increasing US exports.

The PIE program's funding for the PSCIP will not only stimulate new investment and encourage the transfer of technology from the United States to Pakistan, but also stimulate further trade and investment links. Currently, many of Pakistan's industrialists and entrepreneurs look toward Europe or the Far East, primarily Japan but also Australia, Taiwan and Hong Kong, as traditional suppliers of machinery, equipment, joint venture partners and technology. America has much to offer at competitive prices and the existence of the PSCIP can stimulate an interaction between the two countries and further enhance the position of the United States as one of Pakistan's major trading partners.

What is required is financing, exposure to exporters, market research, and competitive prices. Exposure has been developed by the USAID-supported commodity import programs in agriculture and energy. USAID has found that the US banks participating in the PSCIPs make good middlemen and, in addition to providing financing, also match industrialists with suppliers and sources of technology. Exchange rate adjustments over the past five years have made the US increasingly competitive as have improvements in productivity and cost reduction.

The PSCIP will work in conjunction with other programs of EXIM bank and OPIC to make available loan guarantees for projects of a large size. EXIM in particular has agreed to cooperate with AID in Pakistan to support new capital investments in such areas as telecommunications, power, construction and transportation. The PSCIP might supply a $5-10 million loan combined with loan guarantees from the EXIM bank to a bank that would lend the borrower additional funds for such capital projects. The EXIM bank will guarantee up to 100% of the repayment of fixed or floating rate export loans from US lenders to Pakistani buyers of US exports. PSCIP could also cooperate with an institution such as the IFC to form a financing package for larger projects.

Other PIE Program activities provide additional support for the PSCIP and vice versa. For example, the research service of IESC's ABLE program provides Pakistani businesses with trade leads as do AID and

Department of Commerce trade opportunity announcements. Publications, exposure to trade shows, training opportunities and commercial visits to the US will facilitate an increase in trade and investment by US firms in Pakistan.

An important ancillary benefit of the Private Sector Commodity Import activity is that it provides balance of payments support to the Government of Pakistan by making available scarce foreign exchange for procurement. It further provides rupees for use by the GOP for the implementation of its Annual Development Program (ADP). Rupee availability is often the major bottleneck to the implementation of ADP projects. Thus, rupee availability results in a shrinking of the development assistance pipeline.

ii. PIE Investment Fund

The PIE Investment Fund is proposed as a means of supporting newly formed private investment banks and directly encouraging reform and growth in capital markets. At the same time, such a Fund would encourage the IFBs to undertake projects with small and medium-sized businesses (including women-owned business or projects from disadvantaged areas) that they might not otherwise have undertaken.

The basic mechanism is as follows. A corporation would be founded in Pakistan. USAID would then make a reimburseable grant or loan through the GOP for the Corporation of up to $20 million in several disbursements. A US Fund manager under USAID contract would head the corporation and manage it according to agreed upon, sound investment banking principles. Monthly activity reports and quarterly financial reports would be submitted to USAID for its scrutiny.

The purpose of the Fund would be to make medium to long-term (5- 10 year) loan funds available to authorized Investment Finance Banks to onlend to companies in which the IFBs are making an equity investment. A suggested ceiling on lending would be two rupees of Fund lent to one rupee of equity participation. The terms of the loan for each investment project would be negotiated by the manager of the Fund. A proposed guideline for lending terms would be 5 to 10 years with an initial grace period of 1 to 2 years.

The interest rate should not be below market rates. However, it would be possible to use a convertible debenture to keep servicing requirements as low as possible in the early years of the project. This would work as follows: the loan would carry an interest rate of around half of the maximum lending rate set by the State Bank in the form of a convertible debt instrument (debenture). This instrument, upon conversion and with the sale of shares to existing shareholders at a previously agreed upon price, would yield the Fund an effective return of the maximum lending rate.

The Fund also would provide other areas of support (and fee generation) to the investment community. This could take the form of guarantees to be used in underwriting new share issues on the Stock Exchange which would encourage the deepening of the equity market. It could also undertake risk sharing on the endorsement or issuance of money market instruments including term-finance certificates, participation term certificates, and other types of commercial paper. This activity would encourage the formation of secondary markets for commercial paper.

All of these activities would be undertaken on a fee basis with the understanding that the Fund should become entirely self- supporting by the end of the five year period. USAID would provide the original $20 million loan to get the Fund started, as well as subsidize the first five years of the Fund manager's costs. Profits from the operation would be reinvested in the Fund. This would help to ensure that the Fund continued to grow and that the Fund manager was sufficiently motivated to maximize the amount of lucrative deals made.

At the end of four years, USAID would decide if it should continue to finance the Fund. If the Fund is making money, funding should be decreased and a greater share of salaries should be paid out of profits. The goal of the Fund should be to increase its capital base by going public in year six or seven of its operation. After year ten of the operation, a schedule would be worked out to return in rupees the equivalent amount of dollars, plus interest, originally contributed by USAID to the Government of Pakistan. This would normally take place by Year 15 of the Fund.

The Fund would only lend to companies which meet the USAID development criteria. At the same time, USAID would strongly encourage project lending to small and medium-sized businesses, women-owned businesses, or projects in disadvantaged areas of Pakistan. USAID would monitor the performance of the Fund but should refrain from becoming involved in the approval process on every loan.

Brought in as a PSC or as a company employee, the Fund manager would be based in Karachi and travel to other areas of the country on a regular basis. The manager would also work with other USAID programs such as the agribusiness project to encourage the IFBs to invest in projects identified by these programs. Prior to proceeding with implementation of the Investment Fund further technical and administrative feasibility needs to be done. The Fund may not be implemented.

iii. Privatization Fund

Funds may be used to provide financing for the implementation of privatization activities. For example, if a privatization requires a major restructuring of a company prior to its sale, this restructuring and modernization might be financed by the Private Investment Support component of the PIE Program, especially in instances where there is agreement for a 100 percent divestiture of assets and independent private sector management of a previously government owned and operated enterprise.

Another example of the potential need for privatization financing is where a large industrial enterprise is being privatized and negotiations with labor produce a requirement of severance payments for redundant workers. This payment might be something on the order of several years' salary and an allowance for retraining. Here is an instance where AID financing might be critical in breaking a bottleneck and allowing a major privatization to take place.

iv. Loan Portfolio Guarantee Program

The Loan Portfolio Guarantee (LPG) Program of the Bureau for Private Enterprise provides loan guarantees to participating banks on behalf of small business. The LPGs can be used for both new and existing businesses. For new, small business loans, the US Government provides a credit guarantee of up to 50 percent of the principal amount.

Guarantees for small business loans are made to finance any productive or commercial activity, subject to certain restrictions. The maximum loan size to a qualifying small business is $150,000. The amount of LPG funds to be allocated to Pakistan has not been decided yet, but the Mission expects a five-year allocation in the range of $9-12 million, which would support loan programs with three or four private banks.

The overall LPG program is managed out of Washington. The USAID serves as a liaison between Washington and Pakistani banks. The actual guaranteed loan portfolios are managed by the banks without USAID interference. Loan portfolio reports are required twice each year.

v. Trade and Development Program

The Trade and Development Program of the US Government provides US investors with interest-free financing for feasibility-type studies for projects in developing countries. There are five types of studies or activities funded under TDP: (1) Definitional studies; (2) Pre-feasibility studies; (3) Feasibility studies; (4) Technical symposia; and (5) Technology orientation missions. The program in Pakistan would tend to undertake the first three types of activity.

If a proposal passes the initial screening by USAID (the criteria to be agreed upon by Mission and TDP officials) it would be referred to the private sector office of TDP. The project would then be analyzed with respect to TDP's normal criteria (e.g. sound financing for the project, relevant experience, US export potential, etc.) If the proposal passes this review, the project would be grant-funded 1/3 by TDP, 1/3 by the Mission and 1/3 by the investors. The PIE Program will earmark up to $2 million dollars under this program.

The TDP program would be administered by the Training and Grants specialist under the PEO, working in conjunction with the Promotion specialists and IESC.

3. Special Technical Cooperation, Training, and Institutional Grants

This component ties together and provides both the technical skills and the practical commercial feedback required for effective policy/sector grant and investment support components of the PIE Program. Working level assistance, dialogue and support to business enterprises, chambers of commerce and industry, trade and industry associations, and small business provide a feedback mechanism on what works well in Pakistan and where there is a need for policy reform, deregulation, credit facilities or other changes from the status quo. Such feedback and working level relationships are absolutely necessary if the program is to have an impact on business, trade and investment as it is performed in Pakistan, and if these commercial activities are to expand and become more efficient.

Specific activities to be financed under this element of the PIE component are described in more detail below.

(i) Technical Cooperation

The intellectual heart of the PIE Program is the core technical cooperation team recruited through open competition from the best firms and individuals in investment banking, finance and macroeconomics. Both Pakistani and American experts dealing with capital market development, financial instruments, financial institutions, investment expansion, and entrepreneurship (deal making) will be sought. The long-term team will be comprised of one US Chief of Party, one Financial Economist, one U.S. and one Pakistani Promotion Specialist, one U.S. Capital Markets Specialist and one Pakistani Commercial Banking Specialist. Professional staff will be augmented by short-term consultants, and possibly a privatization specialist. The team will arrange in-country seminars and workshops to discuss research findings and policy options. The contractor will arrange visits both by public sector and private sector representatives to the US and other countries to undertake business promotion activities, to witness practices of regulators, and to see market operations. Visits to the Chicago Board of Trade, New York Stock Exchange, the Federal Reserve, and Securities Exchange Commission, in addition to trade fairs and other activities which will be coordinated with the Department of Commerce, will be arranged. The technical cooperation team will work with the representatives of local bodies and with government officials in the State Bank, the Ministry of Finance, the Ministry of Industry, the Board of Investment and or the Investment Promotion Bureau (IPB), and the Privatization Wing.

Under the direction of the Chief of Party, the team will collect and analyze the data and prepare it for consideration by policy makers and private sector organizations. The COP will work from the Ministry of Industry, in close cooperation with private sector organizations and others. Seminars and workshops will be held to discuss the issues, and, depending on the topic, government counterpart agencies or legislative bodies will bring recommendations to the cabinet level Economic

Coordinating Committee chaired by the Prime Minister for approval. The technical cooperation team will work closely with the USAID Director, the Chief of the Private Enterprise Office and other Mission offices as they establish and negotiate the package of policy benchmarks to be agreed upon and implemented prior to sector grants being made on an annual basis.

In addition to the Chief of Party and team-wide policy responsibilities, the following long-term assignments are proposed for the contract team:

Financial Economist-- Based in the MOF, work to develop the Ministry's policy research and implementation capability through the new Deputy Secretary for Policy. Initially advise the Privatization Wing until the MOF believes a long-term privatization specialist is required. Assist the Ministry in implementing specific policy reforms.

Capital Markets Specialist-- Based in the Corporate Law Authority, assist in the broad array of reforms needed to energize and properly regulate the stock market and related long-term capital accumulation instruments and institutions.

Commercial Banking Specialist-- This Pakistani advisor will work with the SBP and commercial banking sector to help coordinate and expose the interest rate structure to market forces, to promote sound commercial banking practices and regulations, to increase competition among state-owned banks, and to promote private commercial and investment banking institutions.

Promotion Specialists-- Two promotion specialists will work with the American Business Council to promote direct foreign investment in Pakistan, with an emphasis on American investors. The promotion specialists will work with a US promotion company to seek out potential investors in targeted sectors such as electronics, and machinery parts. These two person, based in Karachi, will coordinate with the policy team in Islamabad as well as work with IESC, the ExImBank capital projects/warchest fund, and the TDP program to package investments.

Administrative Officer-- One Pakistani administrative expert will be required to facilitate contract administration.

The team will be supplemented by up to 120 person-months of short-term experts on subjects such as privatization, legal reform, trade development, capital markets, and financial deregulation. Also associated with this team will be three sub-contractors. One will be a Pakistani marketing firm which will undertake all public promotion campaigns, and seminar and workshop organization. The second will be a US-based investment advisor who will actively pursue and follow up on potential US-Pakistan investment leads. The third will be with a participant training backstop firm in the US to help identify and manage short-term US training opprtunities to be financed under the training component. The detailed scopes of work for the institutional TA team is included as Annex L.

In support of overall program management, four personal services contract positions will be financed under the PIE Program. One will be an assistant project officer to help on overall management; the second will be a training and grants program administrator; the third will be a training and grants assistant; and the fourth a financial policy analyst to work on policy negotiations and benchmark tracking. The first two positions will be local-hire contracts of US dependent spouses or FSN. The latter two will be program-funded FSN positions.

(ii) Training

The PIE Program will include three categories of training: long and short-term overseas training; in-country training; and, Entrepreneurs International (EI). The overseas participant training program, inclusive of EI, will involve training for 200 private and public sector participants over a five year period at an estimated cost of $3,200,000. Such training will be focused on critical policy implementation, increasing private sector voice, and investment promotion. Participant training backstop support will be funded under the Development Support Training Project. The in-country training program will target about 500 participants at a cost of about $1,800,000. The in-country program will respond to the needs of the institutional contract team in implementing the program and promoting policy and investment initiatives. In addition, program-funded training will be conducted under grants to IESC, WEC, and the Chambers.

Entrepreneurs International is a USAID training program which provides training in the United States in the areas of management, marketing, production, and technology. Potential activities include working directly with US companies for a period of 1-4 weeks, attending short-term technical workshops or seminars, and/or participating in industrial and trade conferences. It is expected that participants develop long-term linkages with the firms they visit in the United States, either as a joint venture or trade partners.

The EI program would be managed by the Academy for Educational Development (AED) under an already existing USAID program. AED would coordinate their work with the Training and Grants Advisor. Cooperation with the Promotion Specialist and IESC country director in Karachi is planned and at least 20 participants will be sent each year.

Overall training program outputs are: (i) at least three institutions able to voice private business interests more effectively; (ii) minimum of 600 public and private representatives trained; (iii) base line data established on women-owned businesses; (iv) improved EHS awareness and practices; and (v) improved private investment policy information. A more detailed description of these training activities follows in Section IV.D.

(iii) Institutional Grants

STT also provides grants to private sector non-profit organizations for institutional development under the open societies/private sector voice initiative of PIE.

One key grant will support a greatly expanded International Executive Service Corps operation in Pakistan. IESC activities have been extremely successful to date and demand for services has outstripped the organization's funding capacities. This has been partially remedied by increasing the IESC grant with PIE bridge financing and additional funds from ASSP. IESC activities will be further transformed under the PIE Program.

Already established in Pakistan, the IESC would expand its business programs and establish offices in both Karachi and Lahore. The major thrust of the program would be to provide technical assistance to as many as thirty Pakistani enterprises each year on a cost-sharing basis.

The in-country director would be responsible for identifying specific technical assistance needs with businesses in Pakistan. The country office would then work with the US IESC office to find retired business executives in the United States who have the skills to work with the businesses in Pakistan on a volunteer basis. The Pakistani firms are required to pay a significant portion of the costs since they would be uniquely benefiting from the technical assistance. Because IESC volunteers have been senior executives involved in all aspects of running a business, many companies using IESC's services receive practical advice in a number of areas including production management, personnel, marketing, and finance. IESC has submitted a proposal and budget for a five year period and would plan to work directly with 1500 Pakistani businesses over that period.

IESC also will provide technical assistance and training to Pakistani business associations and Chambers of Commerce. These associations help channel firms toward possible partners, alternative technologies, and other educational resources. IESC will provide assistance to selected groups to build management capacities in planning, controlling, organizing, and outreach. Coordinating with the Promotion Specialist on the TA team, IESC will provide technical assistance and training directly to the associations and chambers.

Another funded IESC service program is the American Business Linkage Enterprise Program. ABLE is a business information service which links foreign companies with US markets, companies, and technologies. A Pakistani business identifies the information that it desires about US business or the US market. The information generally concerns exporting, joint venture partners, or sourcing. Follow-up services, such as a presentation service, equipment and material quoting service, export management assistance, and US business trip scheduling can be provided. Businesses using the services are asked to pay $1,500 for 40 hours of research.

The program of industrial health, safety and environmental management will be implemented by a grant to the World Environment Council. This program was suggested by AID/Washington and complements PIE's objectives in that improved environmental, health and safety practices enhance firms' efficiency and productivity. The Council is a non-advocacy, non-profit group whose members consist of multinational organizations which provide their staff on a pro bono basis. The WEC will work with volunteer organizations in Pakistan to provide assistance to Pakistani firms for pollution control, health, and safety programs.

To support the investment promotion specialist activities and develop US-Pakistan trade and investment ties, a grant will be provided to the American Business Council in Karachi. This grant will fund specific promotion activities and selected ABC expenses deemed appropriate to expand its membership and increase its effectiveness on behalf of US business and expanded investment. Similar grants will be provided to trade associations, manufacturing and producer groups and local Chambers, on a competitive basis, to support investment and private sector voice objectives.

Grants are also contemplated to promote investment-related research through key local institutions. One possibility is to grant funds to the Investment Board Advisory Committee. Other possible candidates include LUMS or the EDAS.

Through a series of studies and interventions conducted under grants to programs such as the centrally-funded GENESYS project, the special needs of women and small businesses will also be identified and addressed under PIE.

(iv) Special Projects

A fund of approximately $3 million will be reserved to finance critical studies and activities outside the scope of the large TA team. These funds are essential to help the new Private Enterprise Office respond to a variety of needs associated with the start-up of a new private sector program, to respond promptly to windows of opportunity for promoting private sector initiatives, and to develop future program directions.

(v) Commodities

A modest amount of commodities, such as vehicles, computers and office equipment, will be required to support the technical assistance team. In addition, we anticipate a need for a variety of small commodity procurements to support various institutional development activities such as capital markets. A total amount of $1 million is reserved for such requirements, in addition to commodities procured under the CIP portion.

D. Program Process and Objectives

1. Policy Dialogue and Negotiation

In recent years, the AID Mission in Pakistan has had considerable experience in the process of policy dialogue. The Agricultural Sector Support Program, a $330 million sector grant and commodity import program, has included an annual policy benchmark negotiation that is the core of policy dialogue and reform.

Experience under ASSP demonstrates that policy dialogue is substantially strengthened and accelerated by the availability of detailed analyses of complex policy issues, particularly when the analysis generates reliable data to replace speculation and offers specific information on the costs and benefits of particular policy reforms. ASSP experience suggests that analysis performed outside the government, such as may be done by private sector voice organizations, is a valuable resource for government officials to consider. At the same time, it is important to work with government and private sector counterparts to build knowledge and experience with policy analysis. The PIE Program's long-term and short-term technical assistance, as well as the grants and training components, strengthen the ability of both government officials and private sector representatives to undertake meaningful and substantive policy dialogue.

The ASSP experience also shows the need for flexibility in the administration of a program designed to promote policy change. Many of the policy reforms contemplated are complicated and politically sensitive. Their implementation must be carefully timed, often within a narrow window. The Mission must be able to work rapidly and directly with the GOP and private business leaders to assist in the implementation of policy reforms, tailoring its assistance to the specific needs of the reform involved and circumstances of the moment.

Because of the need for flexibility, a set of benchmarks will be determined and negotiated each year. Sector grants will generally be made on the basis of progress made on the agreed upon benchmarks. Progress achieved outside of benchmarks will also be assessed. Experience demonstrates that flexibility must be balanced against rigor in negotiating reforms and assessing progress. Parties to the dialogue must retain the ability to determine objectively whether real progress has been made toward an improved investment climate, market liberalization, and privatization to prevent the program from simply becoming a resource transfer. The balance between flexibility and rigor will be maintained in the PIE Program through the preparation of an annual assessment based on a thorough analysis of progress to date and serving in turn as the basis for the next year's assessment.

2. Policy Agenda

The following chart delineates the major proposed areas for policy reform under the PIE Program. This agenda will be refined further during the initial program year, prior to final approval and authorization of sector grant funding. Other modifications will be identified on an annual basis during the life of the program. The overall objective of the agenda is to redefine the role of the public sector to one of monitoring and enforcing quality standards in consumer products and the role of the open market to make pricing decisions (reduce the oligopolistic forces in the private and public sector) and to take the public sector out of production and price setting.

Policy Reform Objectives and First Year Benchmarks

Industrial Investment Approval

Objective

Establish a system where businesses face a minimum number of steps and agencies involved with the approval process; liberalize approval criteria of each of the agencies within the considerations of national security, citizens health and safety, and religious sensitivity.

Benchmark

To be determined.

Foreign Investment

Objective

Widen the coverage of foreign private investment to cover all sectors of the economy and achieve maximum uniformity in application of rules to foreign and domestic investment.

Benchmark

Issue a notification clarifying that the sanctioning criteria specified by the Federal Government in Notification No. BOI-Misc.(5)/89 dated April 8, 1990, applies to new investment as well as investment in expansion of existing facilities of foreign companies.

Revise and enforce appropriate legislation to protect intellectual property rights.

Privatization

Objective

Broaden asset distribution through divestiture by limiting state acquisition of new assets and increasing the amount of privately owned assets as a proportion of GNP.

Benchmark

Announce a policy to restrict Federal Government sponsored enterprises to undertake new investment except for modernization and rehabilitation of existing facilities; for activities in which private sector is not forthcoming; and for considerations of national security, infrastructure development, and public education, health and safety. Institute majority privatization of one NCB and at least one industrial unit.

Investment Promotion

Objective

Increase private sector participation in investment promotion programs.

Benchmark

Provide equal representation to the public and private sectors on the Advisory Committee on Investment Promotion Bureau.

Trade Policy

Objectives

Establish a macroeconomic policy program which makes exporting more profitable and at least as profitable as manufacturing for the domestic economy.

Reduce the regulations governing exporting to an absolute minimum.

Benchmark

Announce a policy that abolishes all absolute bans on the export of agricultural and other commodities. The Government should also publish a set of criteria to determine when an export restriction can be placed on a product. Export restrictions, if absolutely necessary, should generally only be in the form of an export tariff levied at a rate that does not undermine the ability of exporters to compete in international markets.

Design and begin implementation of a more flexible duty drawback system which can more rapidly change the level of drawback according to changing economic conditions, and which is administered with less delay. USAID can provide technical assistance if needed.

Further reduce the dispersion and average level of tariffs in the economy, according to the program established with the assistance of the World Bank and IMF.

Regulatory Framework

Objectives

Reduce and rationalize the rules and regulations that govern the start-up and operation of business, particularly for small enterprises.

Develop an administrative system which results in eliminating or substantially reducing the discretionary powers accorded to regulatory officials.

Benchmark

The GOP, in consultation with provincial and municipal authorities, will develop and begin implementation of a streamlined "negative list" approach to the issuance of the No Objection Certificates, i.e. only those sectors on the list should be required to obtain an NOC. The NOC should be granted according to a clear set of requirements and guidelines in a streamlined fashion.

Financial Sector

Objectives

Establish a more efficient and diversified capital market, including a secondary market for debt instruments, and increase the amount of capital raised through equity markets.

Increase competition in the financial sector while providing the regulatory framework needed to ensure soundness of the financial system and to protect consumers.

Benchmarks

Amend the regulatory framework to allow the newly formed investment finance banks to compete with nationalized commercial banks in all aspects of banking, except in taking short-term (30 days or less) deposits. This includes authorization for the IFB's to function as foreign exchange dealers, allowance for companies to issue Term Finance Certificates in favor of the IFB's, removal of the stamp duty on IFB commercial paper products, and IFB eligibility for use of the banking tribunal. In addition, the approval process for new IFB's should be accelerated and made much more transparent.

Amend the Companies Ordinance to permit company issuance of short term commercial paper and long-term debt instruments that are consistent with Islamic banking principles.

Revise personnel policies for all national commercial banks and development finance institutions to permit these institutions to establish their own personnel system, including hiring and releasing staff and establishing pay scales.

Reduce the access of NCB's and DFI's to subsidized government liquidity financing, and reduce the total flow of directed credits through these banks.

Establish a new policy disallowing stock brokers from accepting corporate positions involving potential conflicts of interest.

Enforce regulations on new stock issue pricing to ensure market prices are established.

IV. IMPLEMENTATION PLAN

A. Administrative and Monitoring Arrangements

1. USAID Responsibilities

The Private Investment Expansion Program will be administered by the Private Enterprise Office, USAID/Pakistan. Implementation of this large program requires that many Mission offices assume responsibilities and authority for implementing various components.

For example, the day-to-day operations of the Private Sector Commodity Import Program will be handled by the Commodity Management Office as will reporting and monitoring requirements. The programming and tracking of foreign exchange and local currency generated by the CIP Program will be handled by the Program Office (PRO) along with PRO's responsibilities for programming other local currency generating programs in USAID's portfolio, such as the PL-480 program. Negotiations for the sector grant policy package will be the responsibility of PEO though much of the analysis and actual benchmarks will come from the technical cooperation team, the GOP, and local chambers and industrial associations. The program is designed to maximize efficiency of the AID staff, and to delegate as much responsibility as possible both within PEO and to contractors and grantees. AID resources are leveraged by jointly undertaking activities with US and local private companies, institutions, NGOs and multilateral agencies. USAID staff will expedite the execution of grants and contracts and monitor their execution by having two full-time Training and Grants Administrators on a PSC basis--one US local hire and two FSN. Additionally, there is a full-time US local hire PSC assistant project officer.

USAID staff will be active full time in promoting policy reform, policy dialogue and deregulation at every level within Government, and with the private sector, academic community, and chambers of commerce and industry. The people of Pakistan will be familiar with the PIE program through frequent contacts with PEO staff. This will ensure that the PIE Program is reflective of commercial and political reality.

In the past, USAID has been pleased with the work of NGOs such as the Industry Council for Development and the International Executive Service Corps. These groups have a history of independently and successfully implementing the tasks for which they were granted assistance. USAID also has been pleased with the support Land O'Lakes has given to agribusiness clients in Pakistan, even when USAID was not directly involved (centrally funded program). Contracts to organizations such as Land O'Lakes have been very effective in implementing USAID's developmental objectives with a minimum of Mission staff time.

Under the PIE Program, we will clearly define what is expected of staff, grantees and contractors and delegate a maximum amount of responsibility and authority. With the proposed staffing pattern, no problems of monitoring, guidance or leadership are envisioned.

The PIE Program has taken a slightly unusual approach in its design. With the exception of some base resource studies, only minor local support was contracted for and only one major team recruited from the US to look at the capital markets area. Once the main constraints were determined and the design theme known, potential grantees and cooperators were asked to make their own analysis of the situation and design an activity in their area of expertise. Thus, those who implement the program are designing and working closely with their counterparts in the private and public sectors. (This approach embodies the USAID/Jordan model as recommended at the ANE Private Sector Workshop in Amman in May, 1990.) Many of these organizations are local, such as the Lahore University of Management Science which is looking into a public policy and training program.

PIE will be implemented in a business like mode with maximum transparency and efficiency, and this approach will be clearly established through the ProAg, amendments and PILs. Contractors and grantees are expected to adhere to a job, as outlined in their scopes of work, with consultations but without day-to-day Mission intervention.

2. Contractor/Grantee Responsibilities

Contractors and grantees will be responsible for the execution of their respective sections of the Program as delineated in their contracts and grants. The various responsibilities, by contract/grant, are described further below:

- The long-term technical assistance team scopes of work are included as Annex L to this PAAD. This team will bear primary responsibility for the implementation of the program, including program coordination, policy analysis, investment promotion, conceiving scoping and hiring for short term consultancies, managing subcontractors for public promotion, investment promotion and training, procuring its own commodities, and arranging its own logistics support. Because AID cannot delegate policy negotiation authority, the contract team will not officially represent AID in policy negotiations with the GOP. The team will prepare annual training plans, nominate overseas trainees, and manage in-country training programs. Primary responsibility for overseas training will reside with AED and the USAID training and grants PSC. PIE's "private sector voice" responsibilities will be shared with institutional grantees.

- The PSC positions reporting to USAID will constitute the focal point for managing grants and training. Thus the private sector voice objective of the PIE Program will effectively be administered by USAID with contract staff assistance. This administration will involve coordination and promoting "networking" among grantees. As noted earlier, implementation of grants will be fully delegated to the grantees. Grantees will also be responsible for establishing systems of financial accountability. These financial systems however, will be approved by the USAID or have been approved as part of the AID PVO registration process. Grantees will be financed incrementally and subject to evaluation to ensure responsibilities are indeed undertaken and results forthcoming.

3. GOP Administrative Arrangements

Key counterparts for the PIE Program include the Ministries of Finance, and Industries; and the American Business Council. Below are the proposed counterpart authorities and working relationships for the three program components. These may be altered with changes in governmental and GOP organizations. (However, the Economic Affairs Division will continue to perform a valuable role as facilitator.)

a. Sector Grants

The policy agenda for sector grants will cover a broad spectrum of topics not easily covered by any one ministry. Since the Ministry of Finance coordinates most economic policy, we will recommend that the Additional Secretary for Development, MOF, be the authorized signatory for this component. (Additional Secretary, Budget, MOF, is the signatory for the World Bank FSAL). Under the Additional Secretary we will work closely with the Joint Secretaries for Internal Finance, Investment and Policy. Other MOF agencies which will receive assistance are the Corporate Law Authority, Privatization Wing, and Central Board of Revenue. Other important actors on policy deliberations will be the Ministry of Industries; the Ministry of Commerce; the Ministry of Production; and the Ministry of Law. Private sector inputs into policy dialogue will be promoted through PIE's third component--STT.

b. Private Investment Support

Primary counterparts for this component will be private sector businesses. However, initial approval of the various financial packages to be offered should logically rest with the Ministry of Finance. We would again recommend the Additional Secretary for Development, MOF, as the authorized signatory. This would include inputs such as the PSCIP, the PIE Fund, TDP grants and privatization funds. For actual implementation responsibilities USAID will be looking toward intermediate financial institutions (IFIs) to actually administer such inputs. The actual selection of these IFIs will be determined over the next year for inclusion in the PAAD Amendment.

c. Special Projects, Technical Cooperation and Training

The technical assistance team will work with organizations throughout the public and private sector. Since this will be a direct AID contract, principle supervisory responsibility will reside with the Chief, PEO. For signing authority on behalf of the GOP, we recommend an Additional Secretary, MOF, to provide program continuity. This would also apply for the proposed PSC positions recommended under technical assistance, and for the approval of institutional grant PIO/T's.

Training programs will be broken down into two components. For normal public sector overseas training, the Economic Affairs Division (EAD) will have primary responsibility. For all private sector training, including EI and private sector overseas participant training, we anticipate EAD providing a blanket No Objection Certificate for a specified number of participants prior to selection, so that these participants can be processed without referral to government committees.

B. Program Implementation Schedule

The following schedule represents major events and benchmarks for the STT Component of the Program and PAAD Amendment through December 1991.

Date	Event	Responsible Party
Sep 90	Original PAAD Authorized	USAID
Sep 90	Program Agreement Signed	USAID, EAD
Sep 90	Training and Grants Manager on board	USAID
Oct 90	CPs met, including legal opinion and authorized signatories	EAD, MOF
Nov 90	RFP for institutional TA contract advertized	USAID, MOF
Nov 90	PIO/T for Training and Grants PSC approved	USAID, MOF
Nov 90	PIO/T for Monitoring and Evaluation Baseline Studies Approved	USAID, MOF
Nov 90	Final procedures for private sector training approved via PIL	USAID, EAD

Nov 90	PIO/T for buy-in to AED Contract for US participants and Entrepreneurs International approved	USAID, EAD
Dec 90	Private Sector Office in Blue Area opened	USAID
Dec 90	Final negotiation of IESC and WEC Grants; initial negotiation of ABC Grant	USAID, IESC, WEC, ABC
Dec 90	GENYSYS or other small and women's business team contracted to do initial study	USAID, MOI, MOF, AID/W
Jan 91	IESC and WEC grants signed	IESC, WEC, USAID
Dec Jan 91	PIO/T for Special Projects funding of policy agenda and promotion studies approved	MOF, USAID
Feb 91	Review proposals for institutional TA contract	USAID, MOF, MOI
Mar 91/92	Contracts awarded for policy agenda and promotion studies	USAID
Apr 91	Entrepreneurs International training begins	AID/W, AED, USAID
Apr 91	ABC Grant signed	ABC, USAID
Apr 91	Review of Components 1 and 2 for PAAD Amendment begins	Contractor
May 91	Institutional TA Contract awarded	USAID
May 91	GENYSYS study completed; negotiations on long-term grant(s) for small and women's business advocacy groups initiated	AID/W, USAID, Local PVOs
May 91	Major implementation seminar for Program kick-off	MOF, USAID

Jun 91	Grants signed for small and women's businesses	USAID
Jun 91	All studies completed on policy agenda and promotion; PAAD Amendment draft completed	USAID
Jun 91	Final negotiations between USAID/GOP on policy agenda and benchmarks	USAID, MOF
Jun 91	Baseline evaluation data and purpose level monitoring indicators complete	TA Contractor, USAID
Jun 91	First annual training plan submitted and approved	EAD, USAID AED
Jul 91	AID/W approval of PAAD Amendment or delegation	AID/W
Aug 91	PAAD Amendment authorized, Program Agreement amendment signed	USAID, EAD
Aug 91	Long-term advisors arrive	MOF, MOI, ABC
Sep to Dec 91	Initial steps to implement PSCIP, PIE Fund, TDP Grants and/or other Amendment components as may be approved	USAID, MOF, and various private sector organizations

Beyond 1991 major annual events will involve reporting on Purpose Level Monitoring, approval of annual training plans, annual grant evaluations, review of policy benchmarks and sector grant approvals, and perhaps an annual investment promotion month. The TA team will continue through April, 1996. There will be an option to extend the contract based on performance and need.

C. Procurement Plan

1. Technical Assistance and Grants Procurement Plan

The primary technical assistance contract will be an umbrella institutional contract committed and awarded in accordance with AID direct contracting regulations. The draft scopes of work for this contract are contained in Annex L. The USAID Office of Contracts (OCC) will negotiate the contract based on technical recommendations from a committee chaired by PEO. As set forth in the Implementation Schedule, this contract will be advertized in November, 1990, with contract award anticipated in May, 1991. The contract will provide for an option to extend in the event the PACD is extended or Program amended.

In addition, there will be two initial US local hire PSC's. These procurements will involve informal competition for PSC's. One position, the assistant project manager, is already filled. The second US position will be filled by November, 1991.

Institutional grants will be awarded in accordance with AID Handbook 13. Circumstances for individual grants will vary. For instance, the proposed IESC and WEC grants are unsolicited proposals of a unique and proprietary nature, and can be awarded on that basis. Proposed grants to the local chambers and the American Business Council (ABC) will be awarded on the basis of exclusive capability based on their existing relationship with the cooperating country and beneficiaries, or on a competitive basis as appropriate. Other proposed grants will either be competed or awarded on exceptions allowed under Handbook 13. These grants will be negotiated by O/CC, with liaison assistance from the Training and Grants Manager in PEO. All grants will be subject to annual reviews of performance and financial accountability. Local PVOs which do not have adequate administrative systems will be assisted by the PIE Program and USAID to develop the necessary systems to receive support.

2. Commodity Procurement Plan

No major commodity procurements are planned under the STT Component. Minor procurements of vehicles, computer hardware and software, and office equipment will be contracted using AID direct procurement regulations. PEO will help manage these procurements except for commodities procured under the institutional TA contract.

3. Gray Amendment Organization Contracting

Opportunities for contracting with Gray Amendment organizations including the identification of 8(a) set-asides, and prime contracting and sub-contracting possibilities to meet technical assistance and grant requirements, have been reviewed during preparation of the PAAD. Implementation of the PIE Program will entail contracting for technical assistance services through a competitively awarded contract. Mission policy requires that the use of minority firms receive special consideration in all contracting procedures, and this special consideration will be incorporated into the procedure for advertisement and award of this contract. The evaluation system for the contract award will give priority to firms which include 8(a) firms in consortia, as prime contractors and/or as subcontractors.

The Mission has consistently endeavored to increase the involvement of 8(a) and other disadvantaged firms in technical assistance and other activities. The Mission will continue to review each contracting activity on a case by case basis to identify as many opportunities as possible to promote the involvement of disadvantaged firms in the implementation of AID's assistance program. At a minimum, all contractors are encouraged to use "Gray Amendment" subcontractors. (A Gray Amendment compliance certification is found in Annex D).

D. Training Plan

The PIE Program will include overseas and in-country training. The overseas participant training program will train 195 private and public sector participants over a five year period, including 55 participants to be trained through Entrepreneurs International and 20 academic long-term participants. The Entrepreneurs International program will work directly with US companies for a period of one to six weeks, attending short-term technical workshops or seminars, and/or participating in industrial and trade conferences. The total estimated cost of overseas training is $3,200,000. The in-country training program will target approximately 2500 participants at a cost of roughly $1,800,000.

The overall manager of the local and overseas training activities will be a PSC Training and Grants Manager in USAID's Private Enterprise Office. This person's function will be supplemented by a foreign service national Training and Grants Assistant. The overseas components of the training program will be administered through a buy-in to the Development Support Training Project (391-0474) and its contractor, the Academy for Educational Development. The in-country training program will be administered by the PSC Training and Grants Manager in coordination with the long-term Technical Assistance Team and supported by a local training sub-contractor.

1. Participant Training

The overseas training program will focus on three broad areas: (i) financial deregulation, including capital markets, investment banking, loan-deposit transactions under commercial banking, tax administration, and privatization; (ii) trade development, including export promotion, marketing, GATT, and property rights; and, (iii) organizational management, including management information systems, and application of micro computer based models in business analysis. While the first two categories of training will expose managers in the public and private sector to developments in trade and finance, the purpose of the training grouped in the final category is to enable private business organizations to manage better their operations. Public sector nominations for participant training will be solicited, as per the current practice, through the GOP's Economic Affairs Division. Application for private sector candidates will be invited through all the regional Chambers of Commerce and Industry, OICCI, and ABC.

Selection will be made through a Committee comprising USAID, GOP and private sector representatives, on the basis of criteria developed during Program implementation.

Overseas training will be provided for approximately 195 participants. The programs will vary in length, but are budgeted for one to three months for short-term technical participants, and a one month (average) program for Entrepreneurs Internationals participants. Twenty participants have been included for two year masters programs beginning in 1991. This small effort will be the bridge between the ending of DSTP and the beginning of a new training project to be designed during FY91. Since DSTP's PACD is January, 1993, no long-term participants can be placed after 1990.

Participant training will be conducted in compliance with Handbook 10, including processing, monitoring/reporting and follow-up. Annex N presents the Training Cost Analysis (TCA) Budget Worksheets for the PIE program. These worksheets are representative of the costs for one participant for each major type of training.

2. In-country Training

In-country training will focus largely on business regulation and management, and investment promotion. The specific agenda for in-country training will be developed by the long-term Technical Assistance team in the fist six months of Program implementation and updated annually. Each year, at least four courses will be organized in collaboration with regional chambers, or other business associations. These courses will be coordinated and supplemented by the in-country training component of the Development Support Training Project. DSTP has had an in-country private sector management training program for men and women since 1986 and annually offers 6-10 courses.

PIE will provide in-country training for 2500 trainees. This number is based on the following plan: 1500 through IESC (30 firms/year x 10 employees for 5 years); 375 through WEC (75/year); 125 through the Chambers of Commerce; and 500 through short-term programs designed to meet specific needs (100/year) and delivered by technical assistance for periods ranging between one and three weeks.

In addition to soliciting attendees for in-country training through business associations, the media and direct contact, the in-country contractor will use (as appropriate) the returned participant list from the Mission. The Mission has previously offered training to over 1200 private sector and private sector related participants for overseas training. These returned participants will be invited to attend PIE Program courses and will be a part of the Mission's follow-up procedure.

3. Expected Outputs

Expected training outputs are: (i) at least three private sector institutions able to advocate and represent private business interests more effectively; (ii) minimum of 600 public and private representatives trained in the aforementioned areas; (iii) relevant courses and workshops which address Pakistan private management needs being conducted in host country institutions; (iv) creation of base-line data on women-owned businesses; (v) improved environmental, health and safety awareness and practices; and (vi) improved collection and analysis of private investment policy information.

SUMMARY OF TRAINING OUTPUTS
FY91-95 (October 1990 - September 1995)

a. Participant Training -- Overseas

Training Period	Number of Participants					
	FY 91	FY 92	FY 93	FY 94	FY 95	Total
One Month (General)	15	15	15	15	15	75
Entrepreneurs International (1-6 weeks)	10	15	10	10	10	55
Three Month (General)	9	9	9	9	9	45
WEC Program	5	5	5	5	5	25
Masters Degree	0	20	0	0	0	20
Total	39	64	39	39	39	245

b. In-Country Training

Training Period	Number of Trainees					
	FY91	FY92	FY93	FY94	FY95	Total
One week or less	75	75	75	75	75	375
Two-Three Weeks	25	25	25	25	25	125
IESC	300	300	300	300	300	1500
WEC	75	75	75	75	75	375
Chambers	25	25	25	25	25	125
Total	500	500	500	500	500	2500

The major priorities of training are:

1. Financial deregulation; including capital markets, commercial banking reform, state bank, tax administration and privatization.

2. Trade; including international property rights, GATT, export promotion and marketing.

3. Private sector voice/organizations; including chambers of commerce, trade associations, PVOs, etc.

4. Entrepreneurs International will arrange placements in fields of training based on individual applicant needs. Program will be coordinated with DSTP and the private sector.

E. Monitoring and Evaluation Plan

Monitoring of the Program is to be a continuous full-time process, especially given the broad nature of the Program. Because this is a new operational area for USAID, data is limited. A draft monitoring (PLM) plan has been prepared, but an additional nine months is required to refine the monitoring criteria and collect data. A Pakistani consultant will be hired full-time for the duration of the Program for monitoring and evaluation, with the first task being completion of the PLM framework. This consultant will be assisted by a US IQC consultant for three person-months during the first year. Once the PLM is agreed upon it will be formally included in the FY 1991 PAAD Amendment. This will include quantification of specific end of program objectives and targets.

As noted above, the monitoring and evaluation process will be continuous. In addition to annual PLM reviews, there will be annual policy benchmark negotiations between USAID and the GOP. Formal interim evaluations will be conducted in December of 1993 and 1995. IQC assistance will be provided along with the local consultant. The Project Development and Monitoring (PDM) and Program Offices of USAID will manage the monitoring and evaluation process.

F. Environmental Considerations

The proposed program supports a series of activities which have been independently reviewed with regard to the provisions of 22 CFR 216 "AID Environmental Procedures." The following text outlines the procedures that will be adopted during implementation to assure the environmental soundness of program funded activities.

1. Policy Based Sector Grant Assistance

The central element of this line item will be a five-year policy agenda. The initial policy agenda will focus on investment sanctioning, financial sector reforms, and privatization.

Most of the work in this area will not involve activity in production or construction which would warrant environmental examination, therefore a categorical exclusion has been issued by the Mission's environmental officer.

2. Private Investor Support

This will include financial incentives for increasing US and Pakistani investments. The primary funding element will be a private sector commodity import program to encourage the development of US/Pakistan trade and direct US investments and technology transfers to Pakistan.

Commodities procured under this element of the program will conform to AID Regulation 1 to assure that no materials that are potentially environmentally harmful will be considered for funding. It should be noted that no pesticides, herbicides, fungicides, rodenticides, or other types of toxic/hazardous chemicals may be procured under this program element without formal clearance from the ANE Bureau Environmental Coordinator and the S&T Bureau Pesticides Management Advisor.

3. Special Projects, Technical Assistance and Training

This program element is exempt from further environmental review under the "Categorical Exclusion" provisions of 22 CFR 216 "AID Environmental Procedures".

The signed Initial Environmental Evaluation, as amended, is in Annex F.

G. Social Soundness Analysis

1. Introduction

This project has five objectives which, when achieved, will result in a stronger private sector and its concomitant, greater, more productive employment.

The objectives are: (1) improve the policy environment for private investment; (2) strengthen and expand financial markets; (3) provide support to foreign and domestic investors; (4) assist the GOP privatization program; and, (5) enhance the voice of private sector representatives.

Objective four, privatization, implies more efficient industries and may result in displacement of workers in inefficient industries--though it is hoped that they will be absorbed by the new industries developed as a result of the other four objectives.

The project will result in a broad gamut of beneficiaries, including those who invest in, work for or are served by the private sector organizations USAID will assist.

2. Background

Pakistan's private sector has endured numerous variations and reverses in the policy environment. During the years after its independence the country favored a manufacturing focussed import substitution growth strategy. In 1959 there was a switch to a more liberal monetary and fiscal policy and a protectionist trade regime. The latter promoted growth through private investment, especially in the manufacturing sector.

This high growth was not, however, reflected in correspondingly better living conditions for the working class. As a result, the PPP entered the scene with a socialist program which resulted in a sharp growth of the public sector and policies which served this sector at the expense of the private sector. Many industries were nationalized and, by the 1971-77 period, private sector investment represented only 36 percent of the total. The new policies resulted in large groups of workers being employed inefficiently in unproductive industries. Popular political policy was going to result in the stagnation of Pakistan's economy and the need for major corrective measures.

In 1977 the policy environment turned somewhat more favorable toward the private sector, providing legal assurances against arbitrary takeovers, selective privatization and nationalization of monetary, fiscal, and trade policies. The private sector responded well and today contributes about half of the GFCF.

While these changes were beneficial much remains to be done. Parastatals in 1987 produced a tax loss of Rs. 2.3 billion in 1987. Privatizing and streamlining them is imperative, but must be done carefully as these inefficient organizations employ 270,000 individuals, many of whom would lose their jobs in any meaningful reorganization. At the time same time, overall unemployment rates for Pakistan, currently estimated at a rather low 3.13 percent of the labor force, can be predicted to rise sharply as a result of current low public investment rates associated with tight budgets unless private sector investments grow substantially to take up the slack.

3. Beneficiaries

a. Provision of Education and Training

One of the major constraints to strengthening Pakistan's private sector is the lack of a well educated and well trained labor force. Illiteracy is over 75 percent and productivity is low.

While AID's Primary Education Development program addresses itself to the question of educational quality and literacy, the PIE program has a major training segment focussing on business oriented skills which will benefit the participants directly. Specifically, the program proposes to train 250 participants overseas ranging from one month courses to full masters degree programs. The overseas training will focus on three broad areas: (1) financial deregulation; including capital markets, investment banking, loan deposit transaction, tax administration and privatization; (2) trade development; including export promotion, marketing, GATT, and property rights and (3) organizational management; including MIS, and application of micro-computer model in business analysis.

The first two categories will expose both public and private sector managers to developments in trade and finance. The third category is aimed at greater efficiency in the private sector.

Some 2,500 individuals from the public and private sector will be selected for in-country training. This will focus largely on business regulation, management, and investment promotion.

While the direct beneficiaries will be the 2,750 training participants, indirect beneficiaries will be investors and recipients of private sector services who benefit from the increased efficiency provided by these better trained individuals. The public sector will benefit from more efficient management.

b. Credit Facilitation Activities

(i) Private Sector Commodity Import Program (PSCIP)

This activity will provide dollar funds for Pakistan entrepreneurs for the import of US equipment. The direct beneficiaries will be approximately 500 entrepreneurs who will be able to finance US purchases. US industry will benefit by increased sales to Pakistan and the potential of developing a long-term market here. Pakistan will directly benefit from new employment and income generated through these investments. Using the least generous employment generation estimates per fixed asset investment, we would expect a minimum of 6,500 new jobs to be created via the PSCIP.

c. PIE Investment Fund

This fund will provide up to a $20 million grant to IFB's for onlending to small and medium sized businesses.

It is estimated that, during the life of project, some 400 loans will be made benefitting small and medium-scale businesses, many of them women owned (see WID section). The direct beneficiaries will be those companies that participate in this program. Based on a much higher employment generation factor per fixed asset investment in the small scale industries sector, these investments could easily generate 20,000 or more new jobs. Indirect beneficiaries will be consumers benefitting from increased competition.

d. Privatization Fund

An $8 million fund will be formed to help facilitate privatizations. As noted earlier, one of the principal concerns about privatization is that it may result in loss of jobs for superfluous personnel in parastatals. This fund could help finance severance benefits and job placement activities for workers displaced in the privatization process.

4. Impact on Women

In Pakistan, as in many developing countries, small and medium-scale enterprises suffer from a lack of access to credit. This is even more acute for women. This program will facilitate the economic advancement of women through several activities.

Services such as the AID/W GENESYS Project may be commissioned to assist local organizations such as the Network for Enterprising Women and the Entrepreneur and Career Institute which are already involved in supporting women in business. An estimated $1 million will be provided to enhance the advocacy and participatory role of women-owned businesses.

Concrete steps will also be taken to assure that women benefit from training and education activities and have access to loan and guaranty funds. Women-owned enterprises will also be targetted for assistance by IESC.

5. Future Research

In order to more accurately determine the impact of the PIE program, research will be carried out to develop a spectrum of baseline data prior to approval of the PAAD Amendment. This will include sex disaggregated information on employment, industry ownership, and education.

V. FINANCIAL PLAN AND ECONOMIC ANALYSIS

A. PIE Budget

As earlier noted this original PAAD will result in the authorization of only the Special Projects, Technical Cooperation and Training (STT) Component of the PIE Program. Thus the official financial tables presented herein will represent only the $35 million planned LOP authorization for the STT Component.

Subject to further review and revision, Components 1 and 2 of the Program--Sector Grants and Private Investment Promotion--will be authorized via a PAAD Amendment. The planned AID budget for all components is as follows:

Sector Grants	$ 50,000,000
Private Sector CIP	$ 65,000,000
PIE Fund	$ 20,000,000
Privatization Grants	$ 8,000,000
TDP Matching Grants	$ 2,000,000
Total - Above Components	$145,000,000
Total - STT Component	$ 35,000,000
LOP Grant Total	$180,000,000

Specifics on the financial plan for components 1 and 2 will be set forth in the PAAD Amendment.

For the STT Component, Table 1 provides the line item breakdown for all funding. Please note there has been no host country contributions included, since this is not a requirement under ESF funding. There will, nevertheless, be substantial in-kind GOP contributions, as well as substantial inputs from the private sector, which will be difficult to project at the outset. Also note that in response to recent AID/W guidance on local cost procurement, the proposed local currency expenditures noted in Table 1 are supported by appropriate waivers contained in Annex G.

Table 1 provides annual estimates of both obligations and expenditures of AID funds by U.S. fiscal year. Again, FY91 obligations and expenditures will change when the FY91 authorization is added. Table 3 provides a summary of the methods of implementation and financing for the STT Component. Section V.B includes detailed descriptions of the cost factors and details supporting the Summary Financial Plan estimates.

B. Cost Factors

The basis for the summary cost estimates by line item for the STT Component is set forth below.

1. Technical Assistance

The cost estimate for US long-term institutional experts has been set at $250,000 per year. This is a fully loaded figure, including overheads, indirect costs and profit. While some experts may in fact be over or under this budget, we believe this represents a good average cost, representing the somewhat more expensive services of experts in the private sector financial and investment community. The estimate for Pakistani long-term institutional experts has been set at $50,000 per year. This again is a fully loaded cost.

TABLE 1: SUMMARY COST ESTIMATE AND FINANCIAL PLAN

Source:	A.I.D.		Host Country		Total
Line Items	FX	LC	FX	LC	
1. Technical Assistance	11,350	1,550	-	-	12,900
2. Training	3,200	1,800	-	-	5,000
3. Institutional Grants	6,500	3,500	-	-	10,000
4. Special Projects	2,000	1,000	-	-	3,000
5. Commodities	750	250	-	-	1,000
6. Evaluation/Audit	220	180	-	-	400
7. Contingency/Inflation	2,700	-	-	-	2,700
	26,720	8,280	0	0	35,000

TABLE 2: PROJECTED A.I.D. OBLIGATIONS AND EXPENDITURES BY FISCAL YEAR ($000)

Line Item	FY90		FY91		FY92		FY93		FY94		FY95		FY96		FY97		Totals
	OBL	EXP	OBL	EXP	OBL	EXP	OBL	EXP	OBL	EXP	OBL	EXP	OBL	EXP	OBL	EXP	
1. Technical Assistance	1,000	-	4,150	750	2,800	2,000	1,400	2,500	2,150	2,300	1,400	3,150	-	1,500	-	700	12,90
2. Training	900	-	750	250	1,250	1,000	500	1,000	600	1,000	1,000	1,000	-	500	-	250	5,00
3. Institutional Grants	1,500	-	3,500	500	1,000	2,000	2,000	2,000	1,000	2,000	1,000	2,000	-	1,250	-	250	10,00
4. Special Projects	500	-	500	200	500	400	500	500	500	500	500	500	-	500	-	400	3,00
5. Commodities	1,000	-	-	150	-	250	-	250	-	350	-	-	-	-	-	-	1,00
6. Evaluation/Audit	100	-	100	100	-	50	100	-	50	100	-	50	-	50	-	50	40
7. Cont/Inflation	-	-	-	-	450	200	500	500	500	750	1,000	600	-	600	-	200	2,70
Totals	5,000	0	9,000	1,950	6,000	5,900	5,000	6,750	5,050	6,850	4,900	7,300	0	4,400	0	1,850	35,000

Table 3: Methods of Implementation and Financing

Method of Implementation	Method of Financing	Estimated Amount ($000)
AID Direct TA Contract	Direct Payment	11,400
Personal Services Contracts (AID Direct)	Direct Payment	1,500
Participant Training - U.S. including Entrepreneurs Int'l through DSTP Contractor - AED	FRLC	3,200
In-country training under Institutional TA Contract	Direct Payment	1,800
Grants to U.S. PVOs, including IESC, WEC	Handbook 13 Grant	7,000
Grants to local PVOs, including ABC	Handbook 13 Grant	2,000
GENESYS small and women's business program	AID/W Buy-in	1,000
Special Projects--Direct AID Purchase Orders, PSCs and Direct Contracts	Direct Payment	3,000
Commodities AID Procurement	Direct Payment	1,000
Evaluation and Audit IQCs and Direct Contracts	Direct Payment	400
Inflation/Contingency	(Per above)	2,700
Total		$ 35,000

Short-term expatriate technical assistance is costed at $20,000 per month, and includes the possible two to three year assignment of a privatization expert. Experience in other USAID private sector programs shows that there are often times when a very short consultancy from a top expert in the finance/investment field is warranted. We anticipate some of these cases, which will require AID salary waivers. In such cases the cost for one or two weeks may well equal the $20,000 one month estimate, but the results will more than offset the cost. The 120 person-months is a rough estimate of time required, and the available budget will require proper management of tasks and personnel accordingly.

Personal services contracts for US citizens hired locally have been estimated at $100,000 per year. This amount should cover possible contingencies of the contract and possible salary requirements based on prior salary history. FSN PSCs are budgeted at $25,000 per year.

Three subcontractors to the umbrella TA contract are proposed. First, there will be a Pakistani marketing firm which will handle PR, local training, seminars and workshops. Part of this subcontract will be reserved for TV, radio, and newspaper promotionals. It is estimated this subcontract will cost $250,000 per year, including two full time professionals plus promotion expenses. A separate local training budget will be provided under the umbrella contract. The second will be a US subcontractor for investment promotion. This firm will probably operate on a retainer basis, to be used at the discretion of the long-term investment promotion specialists. We estimate this will require two high level experts on a part-time basis, with a cost of approximately $300,000 per year. The third subcontractor will be a US training assistant to help arrange specialized short-term training for participants. This assistance is estimated to cost $100,000 per year.

An inflation factor of five percent per annum on all technical assistance is included in the inflation and contingency line item. The total technical assistance line item budget, using the above cost estimates (in $000) is as follows:

Long-term institutional contract experts

Chief of Party	(US)	5 py x $250	= $1,250	
Financial Econ	(US)	5 py x $250	= $1,250	
Capt Mkts Spec	(US)	5 py x $250	= $1,250	
Comm Bkg Spec	(Pak)	5 py x $ 50	= $ 250	
Investment Spec	(US)	5 py x $250	= $1,250	
Investment Spec	(Pak)	5 py x $ 50	= $ 250	
Admin Officer	(Pak)	5 py x $ 50	= $ 250	$ 5,750

Short-term institutional contract experts

120 p-m x $20	$ 2,400

Institutional Subcontractors

Public Relations (Pak)	5 years x $250 = $1,250	
U.S. Inv Promotions	5 years x $300 = $1,500	
U.S. Training	5 years x $100 = $ 500	$ 3,250

Personal Services Contractors

Asst Proj Mgr (US)	6 years x $100 = $600	
Trng/Grants Mgr (US)	6 years x $100 = $600	
FSN Professionals (Pak)	12 yrs x $ 25 = $300	$ 1,500
Total		$12,900

2. Institutional Grants

From the $10 million reserved for institutional grants, $9 million is for pre-selected grantees, from which we have $6 million in draft grant proposals already in hand. The International Executive Service Corps (IESC) has submitted a draft grant proposal totalling almost $6 million. However, several components relating to its proposed Trade and Investment Service (TIS) may be eliminated if they duplicate investment promotion provided through other Program elements. A less optimistic implementation schedule will be proposed. We estimate an eventual IESC grant of $4 million. The World Environment Council has submitted a grant proposal for $2 million, which in great part appears to be acceptable.

Based on detailed prior discussion with the American Business Council (ABC) and the local chambers, we have estimated a budget of $2 million for a grant (or grants) to these organizations. No draft grant agreement has yet been prepared. We also estimate a $1 million grant for organizations working specifically to promote small and women's businesses. This may be done through a buy-in to the AID/W centrally-funded GENYSYS Project, or to US or local PVOs. We have also provided a $1 million reserve for other local grants to private sector voice organizations such as trade associations, industrial groups or unions. These funds will be awarded on a competitive basis. These grants are totalled as follows:

IESC	$ 4,000
WEC	$ 2,000
ABC/trade assoc/chambers	$ 2,000
Small/Women Business	$ 1,000
Private Sector Voice	$ 1,000
Total	$10,000

3. Training

Details of training are fully covered under Section IV. D, Training Plan. Standard AED cost estimates for all long term and short term US training, including Entrepreneurs International, have been used. The breakdown of US training is:

US long term 20 participants x $43,650	$ 873,000
US short term 120 participants x $13,341 (Avg)	$1,600,000
EI participants 55 participants x $13,200	$ 727,000
Sub-total	$3,200,000
In-country training 500 participants x $3,600	$1,800,000
Total	$5,000,000

A seven percent inflation factor has been included in the contingency and inflation line item. More detailed training costs are included in Annex N.

4. Special Projects

The $3 million reserved for special projects is estimated on the basis of the experience of other USAID private sector programs. Experience has shown that the start up phase of a private sector program benefits greatly from the availability of quick response funding mechanisms to assist in relieving key constraints which cannot be anticipated under a normal project framework. The $3 million amount, representing $500,000 per year for six years, is consistent with other USAID program demands as confirmed at the recent ANE Bureau Private Sector Workshop. First year TDP funding will come from the Special Projects account.

5. Commodities

From the $1 million commodities line item, approximately $200,000 will be required for vehicles, office equipment and computer support for the technical assistance team. The balance of $800,000 is basically a commodities contingency reserved to eventually support a $180 million project. USAID/Pakistan's experience clearly supports the need for such a reserve, in particular to meet computerization needs which arise during program implementation. (Note the contingency item is very small.)

6. Evaluation and Audit

Evaluation expenses are estimated on the basis of 6 person-months of US short-term assistance costing $20,000 per month; plus 6 person-years of Pakistani long-term contract assistance costing

$30,000 per year. This totals $120,000 plus $180,000 or $300,000. An additional $100,000 is reserved for potential audit costs, for a total line item budget of $400,000.

7. Contingency and Inflation

Inflation has been anticipated for technical assistance at five percent, and for overseas training at seven percent. Institutional grants, special projects, commodities, in-country training, and evaluation and audit are considered fixed costs not subject to inflation.

For technical assistance, the $12.9 million budget represents an annual expenditure rate of $2.580 million over five years. Using this as the first year base, the five year costs adjusted for inflation are:

Year 1		$ 2,580
Year 2		$ 2,709
Year 3		$ 2,844
Year 4		$ 2,987
Year 5		$ 3,136
Total		$14,256
Less Budget	(-)	$12,900
Inflation		$ 1,356

The overseas training budget of $3.8 million represents $640,000 per year. This results in the following indexed costs:

Year 1		$ 640
Year 2		$ 685
Year 3		$ 733
Year 4		$ 784
Year 5		$ 839
Total		$3,681
Less Budget	(-)	$3,200
Inflation		$ 481

Total estimated inflation costs are $1,356,000 plus $481,000 equals $1,837,000. In addition, a contingency fund of $863,000 has been allotted, for a total contingency and inflation line item of $2,700,000. Although this is a modest contingency amount, we believe the variable line item costs, particularly TA and commodities, are sufficiently budgeted to cover most contingencies.

C. Flow of Funds

All funding mechanisms for the STT Component follow traditional project flows as set forth in Table 3 of this chapter, Methods of

Implementation and Financing. These flows include direct AID TA and commodity contracts with direct payment features; Handbook 13 grants to US and local PVO's with probable advances for operating cash; training through the DSTP-funded AED Contract, and possible buy-ins to AID centrally funded projects. Components 1 and 2 will require considerably more detailed analysis since there will be several non-traditional modes employed. These will be described in the FY91 PAAD Amendment.

D. Expected Impact of Program on Pakistan's Economy

1. Investment and Growth

a. The Problems

Pakistan has one of the lowest rates of investment in the Third World, and within total investment, Pakistan has one of the lowest private shares. In a recent IFC study ("Trends in Private Investment in Thirty Developing Countries", 1989, by Guy P. Pfeffermann and Andrea Madarassy), Pakistan's private investment as a proportion of national output ranked ahead of only three other countries in the sample (one of them Hungary). Total investment was 7th from the bottom (although it has been argued that Pakistan's statistics underestimate total investment).

Foreign investment in Pakistan is a only fraction of its level in the Philippines or Malaysia, for example, despite the fact that Pakistan's total GNP is actually greater than that of either of those two countries. Correspondingly, Pakistan's economy is relatively closed, with a smaller share of output being exported (13 percent in 1987) than in all but a handful of (mostly very low-income) economies.

Enterprise investment and operations were financed to an inordinate extent by borrowing rather than by equity. This was encouraged by a number of policies: channeling donor funds through public-sector DFIs, nationalization of commercial banking in the 1970's, the GOP's directed credit policies for specific sectors, some low fixed interest rates, lax banking regulations rules concerning non-performing loans and capitalization of financial institutions, and investment capitalization requirements.

Public-sector financial intermediaries' lending policies effectively permitted new investments to be made with as little as 10 percent equity. Large outstanding overdraft lines of credit, particularly to public-sector firms, were uncritically extended and increased. Financial institutions' management gave little emphasis to loan recovery, partly due to the high legal and judicial cost of enforcing lenders claims. Banks were not systematic, however, in reviewing the repayment performance of applicants before granting new loans.

As a result, Pakistan's lending institutions are heavily burdened by bad loans. An indication of the scope of the problem is that in late

1989, the GOP issued special bonds to the banks to pay off Rs.4.4 billion worth of bad loans to parastatals outstanding as of June 30, 1987. This represented 24 percent of the Rs.18.3 billion in bank loans outstanding to parastatals at that time. While the amount of loans to private enterprise at Rs.110.4 billion on June 30, 1987 was much more important than loans to parastatals, rough estimates of overall bad loan levels were nonetheless in the 25 percent range for some banks (compared to average bank capitalization equal to about 2.9 percent of liabilities).

Yet Pakistan's real GNP growth rate of about 6 percent annually since the 1960's is relatively high. The growth of Pakistani manufacturing output, currently the 'modern' sector in low-income countries (though not necessarily in high-income countries any longer), has been quite high at about 9 percent annually in the 1980's, which compares favorably with some very successful economies such as Malaysia. And, although net foreign direct investment in Pakistan started from a low base and is still quite low compared to successful developing economies, it has grown about 17 percent annually in U.S. dollar terms since 1975. Furthermore, export revenues (converted to constant U.S. dollars), after stabilizing from their long slide up to 1961, rose by a 7.2 percent annual rate from 1962 to 1988, a trend marked by three major spurts at the end of the 1960's, 1970's, and 1980's.

b. PIE's Impact on Investment and Growth

As a rule of thumb, the growth rate of output (relative to GDP) will be about one-third the investment rate, providing the investment is of average efficiency. Pakistan's long-term goal should be to raise the private investment rate from its current level of under 10 percent to 25-30 percent, resulting in a growth rate near 10 percent. Other successful developing economies' experience indicates that this process can take 20 to 30 years.

The private savings rate may lag behind the investment rate, as an important part of the initial growth in investment will be financed by external capital. Pakistan's current annual rate of direct foreign (equity) investment, which is less than $200 million per year (3 percent of total investment, or about 15 percent of investment in large-scale manufacturing, electricity, and gas), could easily be doubled or more within a short period of time.

The GOP therefore needs to avoid repetition of past mistakes in steering the economy toward low-productivity public-sector investments and in preventing the financial sector from mobilizing private financial resources. It also needs to do more to attract direct foreign investment.

PIE will assist in putting new policies and programs in place to reach these goals. The quantitative impact of PIE's contribution cannot be projected in advance. However, specific activities can be monitored

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during implementation to quantitatively evaluate their impact. For example:

-- Promotion of direct foreign investment can record the volume of investment for which it was partly responsible.

-- Export policy reforms and promotion programs can record the volume of new exports for which they were partly responsible.

-- Privatization assistance can record the volume of capital whose management was shifted from the public sector to the private sector with its support.

-- Financial sector reform and development assistance can record the volume of private resource mobilization and private investment finance achieved partly as a result of its support.

2. Public Finances

a. The Problems

An inadequate and stagnant tax system forced the GOP to reduce spending on the development budget in the 1980's from 8 to 6 percent of GNP, and to freeze current budget spending on education and public health at 2-2.5 percent of GNP. Nonetheless, the annual budgetary deficit still rose during the decade from 5 percent to over 8 percent of GNP. Borrowing to cover each year's deficit added to the Government's debt, whose annual servicing requirements (including both interest and amortization) have risen from 4 to 7 percent of GNP, or from 20 percent to 30 percent of all federal and provincial government spending. The budget deficit also contributes to high foreign borrowing requirements and balance of payments difficulties.

The GOP uses the tax system to direct private investment and production according to its closed-economy strategy. As a result, the tax base in Pakistan is unusually narrowly concentrated on foreign trade transactions. This holds back international trade, especially exports.

In addition, private initiative is diverted into the political arena to compete for all-important tax exemptions or reductions in tax rates, neglecting market research and technical development. As a result, Pakistan has lost much of its technical ability to compete in world markets.

Basic data on government sector revenues, spending, and borrowing are shown in the tables in Annex A entitled, "Consolidated Federal & Provincial Government Expenditure" and "Consolidated Federal & Provincial Government Revenues".

b. Economic Impact of PIE on Public Finances

A major shift of tax policy is required to move away from the stagnant closed economy strategy to a more balanced and buoyant revenue base. The range of issues involved in such a major shift goes far beyond PIE's mandate. PIE's impact on the fundamental problems of public finance will thus be relatively small.

PIE will, however, assist the ongoing efforts to improve public finances. PIE will negotiate agreements that reduce excessive trade taxation. PIE will assist in privatization, which if properly handled, should reduce unproductive budgetary subsidies, increase self-financing by private enterprises, and thus reduce the GOP's budgetary expenditures.

Finally, PIE will directly supplement the development budget through the sales proceeds from PIE's dollars bought by private importers under the Private Sector CIP. (Under current procedures, these purchases are made on credit terms. The repayments of these loans to private importers are then available to the GOP's development budget.)

E. Balance of Payments Analysis

1. Balance of Payments Assessment

Pakistan's economy is relatively closed. Only 13 percent of Pakistan's GDP is exported, compared to a 20 percent weighted average in other low-income economies and 22 percent in middle-income economies (World Bank data for 1987).

This closed economy has resulted from an early and explicit policy choice on the part of the GOP to encourage industrialization on the basis of production for the internal market. Pakistan prefers that production be based, at least initially, on the internal market and that only the surplus of internal production over internal consumption be exported.

To ensure that private investment would target production of internal markets, GOP planners took steps after independence to ensure that profits would be higher for sales in internal markets than for exports. For this purpose, the GOP introduced a number of artificial distortions into the price structure. High barriers against imports were erected to prevent competition and thus to ensure sufficient profits for private industry in internal markets. These barriers included both high import taxes and administrative restrictions on imports. In addition, production for external markets was actively discouraged by administratively setting an artificially low value for foreign currencies earned by exporters (overvaluation of the Pakistani rupee) and through export bans for specific products.

Thus, Pakistan closed itself off from the path followed by the most successful economies in the last 20 years -- growth led by non-traditional exports. (See the following table on "Non-Traditional Industrial Exports - Pakistan's Lagging Position".)

NONTRADITIONAL INDUSTRIAL EXPORTS - PAKISTAN'S LAGGING POSITION

A. Exports to all OECD countries ($ millions)

Electronics	1972	1982	1987
Pakistan	2	2	4
India	5	45	53
Thailand	0	135	559
Philippines	1	789	938
Malaysia	5	441	2,736
China	2	29	663
Footwear			
Pakistan	5	8	15
India	10	35	111
Thailand	0	24	115
Philippines	1	60	59
Malaysia	3	23	26
China	8	135	417
Furniture			
Pakistan	0	0	1
India	1	4	5
Thailand	0	36	139
Philippines	1	92	172
Malaysia	0	9	16
China	3	142	184

B. Garment and "Other" Exports ($ millions)

	United States		World			
	Garments		Garments		New Manufactures*	
	1981	1986	1983	1988	1983	1988
Pakistan	29	96	160	340	520	620
Indonesia	69	291	160	800	410	1,600
Bangladesh	6	172				
India	175	384				
Sri Lanka	110	279				
Thailand	100	216				
Philippines	227	423				

* Includes manufactures except textiles, garments and wood products.
Pakistan for 1983/4 and 1988/9, so lower in 1983 & 1988.

Source: G. Papanek, "The Risk of Economic Stagnation, The Potential for Rapid Growth with Social Justice", April 6, 1990.

Paradoxically, despite the GOP's efforts to close Pakistan's industrial economy, the GOP's policy toward Pakistan's most important agricultural product, wheat, holds back production and results in unnecessary dependence on imports.

Pakistan's external debt burden doubled in the 1980's. In 1980, Pakistan paid 15 percent of its foreign-exchange income (exports of goods, non-factor services, and factor services, including workers' remittances) to service its external debt. This "debt service ratio" rose by 1990 to over 30 percent (see the following table on the "External Debt Service Burden"). This increasing burden resulted both from low export growth and from the fact that national investment was not financed sufficiently by national saving or by direct foreign equity investment.

Pakistan's 1989 debt-service burden of 30 percent was in the same range as in the countries termed "severely indebted low-income countries" by the World Bank's World Debt Tables. By contrast, countries characterized by the World Bank as being "without debt servicing difficulties" have debt-service burdens in the 15 to 20 percent range, which was Pakistan's position in 1980.

Basic data on Pakistan's trade, workers' remittances, aid inflows, and external borrowing are shown in the next table, "Balance of Payments Summary". Detail on commodity trade is also shown below in the tables, "Structure and Growth Trends of Export Revenues" and "Structure of Spending on Imports".

Table: External Debt Service Burden

(Millions of U.S. Dollars)

	78-79	79-80	80-81	81-82	82-83	83-84	84-85	85-86	86-87	87-88	88-89
Debt Service											
Interest	279	333	356	456	540	638	661	752	787	933	1,016
Repayment of Principal											
LT Official	181	279	271	273	395	499	449	515	722	714	740
LT - Banks	0	0	0	0	0	0	0	0	16	20	21
LT - Others	37	37	36	31	36	35	107	182	48	53	53
ST - Official	0	0	0	7	55	0	195	231	151	262	715
ST - Others	0	0	0	0	0	0	0	0	0	0	0
IMF	85	79	0	0	0	46	172	311	358	322	41
TOTAL	582	728	663	767	1,026	1,218	1,584	1,991	2,082	2,304	2,586
Current receipts											
Gds,Srvcs,&Intrst	2,156	3,007	3,557	3,215	3,549	3,644	3,398	3,905	4,511	5,332	5,584
Remittances	1,497	1,895	2,243	2,436	3,087	3,046	2,688	2,828	2,572	2,264	2,091
TOTAL	3,653	4,903	5,799	5,651	6,636	6,691	6,086	6,733	7,083	7,596	7,675
Debt Service Ratio	15.9%	14.8%	11.4%	13.6%	15.5%	18.2%	26.0%	29.6%	29.4%	30.3%	33.7%

Data: State Bank of Pakistan Annual Reports. Worksheet: eabase interntl exdbtsrv.wk1.

able: BALANCE OF PAYMENTS SUMMARY

(percent of GDP)

Items	1978-79	1983-84	1987-88	1988-89	July-Mar 1988-89	July-Mar 1989-90
1 Merchandise Exports	8.4%	8.6%	11.4%	11.5%	8.3%	8.9%
2 Merchandise Imports	-19.4%	-19.2%	-18.0%	-17.9%	-13.7%	-13.3%
Trade Balance	-11.0%	-10.7%	-6.7%	-6.4%	-5.4%	-4.4%
3 Non-Factor Services (Net)	-1.0%	-0.9%	-1.4%	-1.5%	-1.0%	-1.0%
4 Investment Income (Net)	-1.2%	-1.4%	-2.2%	-2.2%	-1.6%	-1.7%
Income	0.2%	0.6%	0.3%	0.3%	0.2%	0.2%
Payments	-1.4%	-2.0%	-2.4%	-2.5%	-1.9%	-1.9%
5 Private Transfers (Net)	7.6%	9.8%	5.9%	5.2%	3.9%	4.0%
(Workers Remittances)	7.1%	8.8%	5.2%	4.7%	3.6%	3.7%
Current Account Balance	-5.7%	-3.2%	-4.4%	-4.8%	-4.2%	-3.1%
6 Private Capital (Net)	0.8%	0.9%	0.9%	0.8%	0.5%	0.6%
6.1 Direct Investment (a)	0.2%	0.1%	0.4%	0.4%	0.4%	0.2%
6.2 Other Long-term	0.5%	0.4%	0.4%	0.5%	0.4%	0.2%
6.3 Short-term	0.2%	0.3%	0.0%	-0.1%	-0.2%	0.1%
7 Public Capital (Net)	3.8%	2.1%	3.2%	4.1%	3.9%	2.8%
7.1 Disbursements, Long-term (b)	4.3%	3.4%	4.4%	6.1%	5.1%	3.9%
7.2 Less: Repayments, Long-term	-0.9%	-1.6%	-1.9%	-1.8%	-1.5%	-1.4%
7.3 Others (Sht-term & Lg-term)(c)	0.4%	0.3%	0.7%	-0.3%	0.3%	0.3%
8 Allocation of SDRs (Net)	0.2%	0.0%	0.0%	0.0%	0.0%	0.0%
9 Changes in Reserves (-=increase)	0.9%	0.3%	0.4%	-0.0%	-0.3%	-0.4%
0 Errors & Omissions (Net)	-0.1%	-0.0%	-0.1%	-0.1%	0.2%	0.1%
Memo: GDP (dollars million)	$19,688	$31,134	$38,376	$40,229	$40,229	$40,773

Data: State Bank of Pakistan Annual Reports. Worksheet: eabase interntl bopnet.wk1.

a) Includes Portfolio Investment except Foreign Exchange Bearer Certificates.
b) Includes Net Official Transfers.
c) Includes Foreign Exchange Bearer Certificates (introduced August, 1985).

able: BALANCE OF PAYMENTS SUMMARY

Table: STRUCTURE AND GROWTH TRENDS OF EXPORT REVENUES

COMMODITY GROUP	Trend Growth Rate 1969-89	1969 Share	1989 Share
Fish & Fish Preparations	8.0%	5.2%	2.3%
Guar & Products	5.2%	1.6%	0.8%
Oil & Cakes	NA	0.7%	NA
Tobacco Raw & Manuftrd.	-1.6%	1.1%	0.0%
Rice	7.4%	5.8%	6.6%
Animal Casings	4.9%	0.9%	0.2%
Hides and Skins	-21.7%	1.1%	0.0%
Leather	8.0%	6.8%	NA
Raw Wool	4.6%	1.7%	0.4%
Raw Cotton	9.9%	13.1%	20.0%
Cotton Waste	3.5%	0.9%	0.3%
Cotton Yarn	6.2%	15.8%	12.9%
Cotton Thread	-2.2%	NA	0.1%
Cotton Cloth	6.8%	16.0%	9.9%
Synthetic Textiles	21.2%	1.1%	2.5%
Garments and Hosiery	21.7%	1.2%	10.7%
Foot Wear	2.6%	1.4%	0.4%
Petroleum & Products	4.2%	3.0%	0.4%
Cement and Products	NA	1.2%	NA
Paints & Varnishes	-3.5%	0.4%	0.0%
Drugs and Chemicals	2.2%	0.7%	0.3%
Surgical Instruments	12.2%	0.9%	1.4%
Carpets and Rugs	11.4%	3.4%	4.9%
Sports Goods	8.0%	1.9%	1.5%
Other Exports	12.0%	14.1%	19.0%
Total	8.9%	100.0%	100.0%

Table:

STRUCTURE OF SPENDING ON IMPORTS

COMMODITY GROUP	Share in Total Imports 1988/89	1987/88
Tea & Coffee	3.0%	2.7%
Edible Oil	8.0%	7.1%
Sugar	0.1%	1.0%
POL Products	14.5%	7.5%
Chemicals	8.1%	8.4%
Fertilizer	3.1%	4.7%
Dyes, Paints etc.	1.3%	1.5%
Plastic, Resins etc.	4.3%	3.6%
Rubber Products	1.4%	1.5%
Paper, paper board, wood pulp	2.2%	3.0%
Yarn & Fabrics etc.	4.2%	6.0%
Iron and Steel	7.3%	6.8%
Metal other than gold	1.9%	2.6%
Machinery	21.1%	23.3%
Vehicles	6.5%	7.4%
Other Categories of Goods	12.9%	13.0%
Grand Total	100.0%	100.0%

2. Economic Impact of PIE on Pakistan's External Sector

PIE's principal impact on Pakistan's external sector problems will be to promote greater policy and administrative openness to exports and direct foreign investment. More rapid growth in export revenues will allow Pakistan to meet its external debt service obligations without cutting imports and crippling internal production. Increased direct foreign investment is the method of meeting Pakistan's external financing requirements with the most favorable long-term implications for the balance of payments.

Pakistan's economic policy bias against exports and direct foreign investment has been considerably reduced in the 1980's by moving to a market-based exchange rate in 1982, and by removing some non-tariff barriers to trade (such as bans and quotas). This trend is currently being supported by assistance from the IMF. The World Bank has also assisted the GOP to streamline its programs to partially compensate some exporters for the cost of the policy bias against exports. This assistance started with an Export Promotion Assistance Loan in 1986 and has continued from that time through the present in prolonged policy negotiations over a possible Industry and Trade Adjustment Loan. An agreement on a trade policy reform package may be reached in 1991.

Implementation of this policy direction needs to continue. The average rate of trade taxation is still quite heavy on non-exempt commodities (an unweighted average of about 100 percent, including all import charges, according to World Bank sources) and has fallen relatively little. Major elements of Pakistan's industrial structure remain highly protected and thus continue to attract economically inefficient investment, diverting capital away from potential export opportunities. Pakistan's international image in the eyes of potential investors is quite poor.

The GOP is far from agreement with technical proposals from the World Bank and other sources for reform of its external sector policies. It comes under frequent political pressure to overvalue the Pakistani rupee. The GOP therefore needs to increase its commitment to an open-economy development policy.

PIE will support increased international trade and direct foreign equity investment in Pakistan not only through policy initiatives, but also financially and through private sector managerial training. PIE's sector grants and CIP funds will compose about 0.03 percent (0.0003) of Pakistan's foreign exchange receipts over the life of the PIE program. More importantly, the Private Sector CIP will support US direct investments in Pakistan. Training and investment promotion activities will build contacts between US and Pakistani private businesses, which should pay off in technical cooperation and increases in productivity, trade and investment.

VI. CONDITIONS, COVENANTS, AND NEGOTIATING STATUS

A. Conditions Precedent to PAAD

There are no conditions precedent to this Program other than the standard proforma conditions relating to Government signatures and the like.

B. Covenants

The Government of Pakistan has progressively and effectively implemented a program of policy reform and regulation in consultation with the population and with bilateral and multilateral support. The PIE program is designed to encourage the Government to proceed at a faster pace with policy reform and deregulation. There are no specific covenants relating to the program. However, in the future, conditionalities will be placed on the availability of funds for sector grants. The private sector commodity import program also has many conditions concerning local currency generation, reporting requirements, and commodity eligibility.

C. Negotiating Status

The GOP has moved quickly in approving the Private Investment Expansion Program concept and in requesting our assistance. Their request for assistance is available in Annex H. USAID has kept the design and development of this program at a level of high transparency. Copies of the Program Assistance Initial Proposal (PAIP) were formally transmitted to the Government and have been shared with bilateral and multilateral agencies, with chambers of commerce, trade associations, legislators and others who expressed interest in the Program. Universities have also been provided copies of the Program. The design team requested comments and suggestions from potential grantees and collaborators (IESC, FIAS, LUMS, etc.). The response to the Program has been overwhelmingly positive, from both public and private sector individuals and organizations. The Mission intends to present a draft Project Agreement during the first week of September and sign the Agreement with the GOP before September 30, 1990. No negotiating problems are expected.

VII.

PRIVATE INVESTMENT EXPANSION PROGRAM

(391-0514)

ANNEXES

TABLE I : RATIOS OF PRIVATE AND PUBLIC GROSS FIXED CAPITAL FORMATION (GFCF) TO GDP

Year	GDP	GFCF			GFCF/GDP RATIO (Percent)		
	(------- Rupees in Millions -------)						
		Private	Public	Total	Private	Public	Total
1960/61	17,649	1,484	1,079	2,563	8.4	6.1	14.5
1961/62	18,710	1,385	1,580	2,965	7.4	8.4	15.8
1962/63	20,056	1,377	2,420	3,797	6.9	12.1	18.9
1963/64	21,357	2,448	1,863	4,311	11.5	8.7	20.2
1964/65	23,360	2,721	2,387	5,108	11.6	10.2	21.9
1965/66	25,126	2,541	2,097	4,638	10.1	8.3	18.5
1966/67	25,901	2,294	1,986	4,280	8.9	7.7	16.5
1967/68	27,659	2,235	1,873	4,108	8.1	6.8	14.9
1968/69	29,454	1,965	1,758	3,723	6.7	6.0	12.6
1969/70	32,337	2,392	2,289	4,681	7.4	7.1	14.5
1970/71	32,736	2,249	2,237	4,486	6.9	6.8	13.7
1971/72	33,495	2,201	2,028	4,229	6.6	6.1	12.6
1972/73	35,773	2,085	2,193	4,278	5.8	6.1	12.0
1973/74	38,439	1,693	2,987	4,680	4.4	7.8	12.2
1974/75	39,930	1,511	3,193	4,704	3.8	8.0	11.8
1975/76	41,229	2,104	4,408	6,512	5.1	10.7	15.8
1976/77	42,401	2,301	4,656	6,957	5.4	11.0	16.4
1977/78	45,679	2,330	4,602	6,932	5.1	10.1	15.2
1978/79	48,204	2,296	4,452	6,748	4.8	9.2	14.0
1979/80	51,736	2,493	4,413	6,906	4.8	8.5	13.3
1980/81	55,048	2,642	4,087	6,729	4.8	7.4	12.2
1981/82	59,012	2,805	4,893	7,698	4.8	8.3	13.0
1982/83	62,975	3,359	5,408	8,767	5.3	8.6	13.9
1983/84	65,968	3,719	5,480	9,199	5.6	8.3	13.9
1984/85	72,014	4,070	5,765	9,835	5.7	8.0	13.7
1985/86	77,023	4,310	6,150	10,460	5.6	8.0	13.6
1986/87	81,427	4,834	7,043	11,877	5.9	8.6	14.6
1987/88	84,166	4,920	6,767	11,687	5.7	7.9	13.6

Source: Government of Pakistan, "Economic Survey, 1989/90", 1990.

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Average Investment Shares (1970-1988)

	Total I/GDP	Private I/GDP	Public I/GDP	Private I/GDI	Public I/GDI
Korea	27.8	21.2	6.6	76	24
Philippines	21.5	15.7	5.8	73.5	26.5
Guatemala	14.6	10.2	4.4	70.5	29.5
Thailand	23.9	16.8	7.1	70.3	29.7
Singapore	38 2	26.7	11.5	69.5	30.1
Portugal	29.8	19.7	10.1	69.3	30.7
Costa Rica	21.6	14.2	7.4	66	34
Uruguay	12.1	7.7	4.4	64.3	35.7
Brazil	22.6	14.4	8.2	63.3	36.7
Mexico	20.5	12.6	7.9	62	38
Colombia	19	11.7	7.3	61.4	38.6
Ecuador	20.5	12.2	8.3	59.3	40.7
Kenya	20.9	12.3	8.6	58.8	41.2
Zimbabwe	18.2	10.4	7.8	57.2	42.8
Peru	16.3	8.9	7.4	55	45
India	18.4	9.9	8.5	54.4	45 6
Bangladesh	13.2	7.2	6	54.2	45.8
Venezuela	25	13.8	11.2	54	46
Argentina	19 9	10.9	9	53.9	46.1
Indonesia	22.5	11.8	10.7	52.5	47.5
Chile	15.3	8.2	7.1	50.7	49.3
Malaysia	31.2	15.8	15.4	50.1	49.9
Turkey	21.5	10.8	10 8	49.9	50.1
Sri Lanka	24.7	12.8	11.9	48.5	51.5
Bolivia	13.6	6.2	7.4	45.1	54.9
Tunisia	26.1	11.4	14.7	44	56
Pakistan	15.2	6	9.2	40	60
Nigeria	12.2	3.6	8.6	29.2	70.8
Zambia	14.5	2.4	12.1	16.3	83.7
Hungary	24.9	3.6	21.3	14.8	85.2

Note: Countries are ranked by share of private in total investment.

Source: Pferffermann, Guy P. and Madarassy, Andrea, Trends in Private Investment in Thirty Developing Countries, 1989

TABLE 3(1): FEDERAL PUBLIC SECTOR OPERATING ENTERPRISES		
Enterprise	Year of GOP control	Remarks
Banking, Finance and Insurance		
Agricultural Development Bank of Pakistan	1961	
Bankers Equity Limited	1979	
Equity Participation Fund*	1970	
Federal Bank for Cooperatives	1976	
House Building Finance Coporation	1952	
Investment Corporation of Pakistan	1966	
Industrial Development Bank of Pakistan	1961	
National Development Finance Corporation	1973	
National Developmnet Finance Corporation		
Regional Development Finance Corporation		
Asian Leasing Corporation		
BRR Invetment Limited		
National Investment Trust	1962	The NIT is managed by National Investment Trust Limited, a public sector joint stock company.
PICIC	1957	
Pak-Kuwait Investment Company	1976	
Pak-Libya Holding Company	1978	
Pak-Saudi Investment Company	1981	
Small Business Finance Coporation	1972	
Allied Bank Limited	1974	Created through merger of nationalized private Banks: Australasia Bank, Sarhad Bank, Commerce Bank and Pak Bank.
Habib Bank Limited	1974	Nationalized private bank established in 1941.
First Women Bank	1989	
Muslim Commercial Bank Limited	1974	Established as a private bank in 1947 and merged with Premier Bank after nationalization.
National Bank of Pakistan	1949	
United Bank Limited	1974	Established as a private bank in 1959.
Pakistan Insurance Corporation	1952	
National Insurance Corporation	1976	
State Life Insurance Corporation	1972	Integrated form of taken over private insurers.
Commerce		
Cotton Export Coporation of Pakistan	1973	
Rice Export Corporation of Pakistan	1974	
Trading Corporation of Pakistan	1967	
Manufacturing		
Carrier Telephone Industries	1969	
Federal Chemical and Ceramics Corporation	1973	
Antibiotics (Pvt) Limited		
Ittehad Chemicals		
Kurram Chemicals		
Nowshera DDT		
Nowshera PVD Pipes		
National Fibres Limited		
Pak Dyes Chemicals		
Pakistan PVC Limited		
Ravi Rayon Limited		

Enterprise	Year of GOP control	Remarks
Ravi Engineering Limited		
Sind Alkalis Limited		
Swat Ceramics Company		
Swat Elutriation Plant		
Ghee Corporation of Pakistan	1976	The list excludes 2 closed units (Punjab Vegetable Ghee and General Mills and Khyber Vegetable Ghee Mills); 1 unit under Baluchistan Development Authority (Chilton Ghee Mills); and, 3 units under Sarhad Development Authority (Bara Ghee Mills, Dargai Vegetable Processing Industries, and Haripur Vegntable Oil Processing Industries).
A & B Industries		
A & B Oils		
Asaf Industries		
Associated Industries		
Bengal Vegetable Industries		
Burma Oils		
Cement Factories and Vegetable Ghee Mills		
E.M. Oil Industries		
Fazal Vegetable Ghee Mills		
Hydari Industries		
Kakakhel Industries		
Kohinoor Oil Mills		
Maqbool Company		
Marfco Industries		
Sargodha Vegetable Ghee and General Mills		
Sheikh Fazal ur Rehman and Sons		
Suraj Ghee Industries		
United Industries		
Universal Oil and Vegetable Ghee Mills		
Wazir Ali Industries		
Karachi Shipyard and Engineering Works	1952	
National Fertilizer Corporation	1974	
Hazara Urea Fertilizers		
Lyallpur Chemical and Fertilizers		
Pak-Arab Fertilizer		
Pak-American Fertilizer		
Pakistan Fertilizer Company		
Pak-Saudi Fertilizer		
National Fertilizer Marketing Limited		
Pakistan Automobile Corporation	1973	
Baluchistan Wheels Limited		
Bela Engineers		
Bolan Casting Limited		
Domestic Appliances Limited		
Mack Trucks		
National Motors		
Naya Daur Motors		
Pakistan Motor Car Company		
Pak-Suzuki Motor Car Company		
Republic Motors Limited		
Sind Engineering		
Millat Tractors		
Trailer Devlepment Corporation		
Al-Ghazi Tractors		
Hino-Pak Motors		

Enterprise	Year of GOP control	Remarks
Pakistan Industrial Development Coporation	1952	Corporation's 2 units (Losbella Textile and Bolan Textile) are closed since 1983; operation of 3 units (Haranai Woollen Mills, Zulfikar Ali Bhutto Textile Mills, and Dir Forest Industries) is under suspension; and, Cotton Ginning Factory has been leased out to private sector.
Cotton Ginning and Processing Factory		
Harnai Woollen Mills Limited		
Indus Steel Pipes Limited		
Shahnawaz Bhutto Sugar Mills		
Quadabad Woolen Mills		
Zulfiker Ali Bhutto Textile Mills		
Pakistan Steel Mills	1966	
State Cement Corporation of Pakistan	1973	
Associated Cement Company		
Dandot Cement Company		
D.G. Khan Cement		
General Refractories		
Gharibwal Cement		
Javedan Cement		
Kohat Cement Company		
Maple Leaf Cement		
Mustehkam Cement		
National Cement		
Pak Cement Company		
Thatta Cement Company		
White Cement Industries		
Zeal Pak Cement Factory		
Roti Corporation of Pakistan	1976	4 of the 6 closed units were leased to the private sector of which 2 have been surrendered.
State Engineering Corporation	1973	
Heavy Foundry and Forege		
Heavy Mechanical Complex		
Karachi Pipe Mills Limited		
Metropolitan Steel Corporation		
Pakistan Machine Tool Factory		
Pakistan Engineering Company		
Pakistan Switchgear		
Peineer Steel Mills		
Quality Steel Works		
Spinning Machinery Company of Pakistan		
Textile Winding Machinery Complex		
Telephone Industries of Pakistan	1952	Established in collaboration of Seimens.
<u>Construction</u>		
National Construction Limited	1977	
National Power Construction Corporation	1974	
National Tubewell Construction Corporation	1974	
Railway Construction of Pakistan	1980	
<u>Oil and Gas</u>		
Southern Gas Company	1985	Merged form of Karachi and Indus Gas companies.
Oil and Gas Development Corporation,	1961	
Pakistan Oilfields	1950	
Pakistan Petroleum	1950	
Pak-Arab Refinery	1974	
Pakistan State Oil Company	1974	
Petroleum Refining and Petrochemical	1974	
Sui Gas Transmission Company	1952	

Enterprise	Year of GOP control	Remarks
Sui Norther Gas Pipelines	1963	
<u>Mining</u>		
Pakistan Mineral Development Corporation	1974	
Resource Development Corporation	1974	
<u>Transport</u>		
Pakistan International Airlines	1952	Railways are a part of the Government. Also, Civil Aviation Authroity, National Logistic Cell, Port Qasim Authority, and Karachi Post Trust are Government controlled.
National Shipping Corporation	1979	
<u>Power</u>		
Karachi Electric Supply Corporation	1952	Established in 1913.
Water and Power Development Authority	1959	
<u>Printing and Publication</u>		
National Book Foundation	1972	
Pakistan Security Prinitng Corporation	1971	
Security Papers Limited	1965	
<u>Consultancy</u>		
Investment Advisory Center of Pakistan	1963	
National Engineering Services of Pakistan	1973	
<u>Others</u>		
Pakistan Agricultural Services and Storage	1973	
Overseas Employment Corporation	1976	
Shalimar Recording Company	1974	
Utility Stores Corporation	1971	
Agricultural Marketing Storage	1981	

Source : (a) Government of Pakistan, <u>Government Sponsored Corporations, 1987-88</u>, 1989.
(b) Government of Pakistan, <u>Annual Report 1987-88 : Public Sector Industries</u>, 1989.

Table: Consolidated Federal & Provincial Government Expenditure

(Percent of GNP)

	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89
Total Expenditure	21.6%	21.2%	20.5%	21.6%	21.7%	22.4%	22.8%	23.6%	25.1%	25.1%
Federal		16.5%	15.8%	16.8%	16.5%	17.3%	17.0%	17.4%	18.6%	19.4%
Provincial		4.7%	4.6%	4.8%	5.2%	5.1%	5.8%	6.3%	6.5%	5.7%
Current Expenditure	13.0%	12.6%	12.8%	14.3%	15.6%	16.1%	16.1%	18.0%	18.1%	19.2%
Federal		9.6%	9.9%	11.2%	11.9%	12.4%	12.3%	13.7%	13.7%	15.1%
Provincial		3.0%	3.0%	3.2%	3.7%	3.7%	3.8%	4.3%	4.4%	4.1%
Defense	5.0%	5.1%	5.4%	5.8%	5.8%	6.1%	6.1%	6.4%	6.5%	5.8%
Interest	2.0%	2.0%	2.2%	2.8%	3.1%	3.2%	3.4%	3.7%	4.2%	4.9%
Federal	1.9%	1.8%	2.1%	2.6%	2.9%	3.1%	3.2%	3.6%	4.1%	4.7%
Provincial	0.1%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.2%	0.2%	0.2%
Current Subsidies	1.5%	0.8%	0.7%	0.7%	1.0%	1.0%	1.0%	0.9%	1.0%	1.7%
Federal		0.5%	0.4%	0.4%	0.7%	0.7%	0.6%	0.5%	0.6%	1.3%
Provincial		0.3%	0.3%	0.3%	0.3%	0.3%	0.3%	0.4%	0.4%	0.4%
General Administration	1.2%	1.0%	1.0%	1.0%	1.3%	1.3%	1.3%	1.6%	1.3%	1.7%
Federal		0.6%	0.6%	0.6%	0.9%	0.8%	0.8%	1.1%	0.7%	1.1%
Provincial		0.4%	0.4%	0.4%	0.4%	0.5%	0.5%	0.5%	0.5%	0.6%
Social Services	1.6%	1.7%	1.5%	1.8%	2.1%	2.0%	2.1%	2.4%	2.5%	2.5%
Federal	0.4%	0.4%	0.4%	0.5%	0.5%	0.5%	0.5%	0.6%	0.6%	0.7%
(Education)				0.2%	0.2%	0.2%	0.2%			
(Health)				0.0%	0.1%	0.1%	0.1%			
Provincial	1.1%	1.2%	1.1%	1.4%	1.6%	1.5%	1.6%	1.8%	1.9%	1.8%
(Education)				1.0%	1.1%	1.0%	1.3%			
(Health)				0.3%	0.3%	0.3%	0.3%			
All Others	1.7%	2.1%	2.0%	2.2%	2.3%	2.5%	2.4%	3.0%	2.5%	2.6%
Federal		1.1%	1.0%	1.2%	1.1%	1.3%	1.1%	1.5%	1.2%	1.4%
Provincial		1.0%	1.0%	1.0%	1.2%	1.2%	1.3%	1.5%	1.4%	1.2%
Development Expenditure	8.6%	8.6%	7.6%	7.3%	6.1%	6.4%	6.8%	5.6%	7.0%	5.8%
Federal		7.0%	6.0%	5.6%	4.5%	4.9%	4.7%	3.6%	5.0%	4.3%
Provincial		1.6%	1.7%	1.7%	1.6%	1.5%	2.1%	2.0%	2.1%	1.6%
GNP (Millions of rupees)	252,463	300,086	347,143	403,279	460,840	520,419	588,485	644,638	716,963	800,283

Data from Economic Survey. Worksheet: eabase fisc expend.wk1.

Table: Consolidated Federal & Provincial Government Revenues

(Percent of GNP)

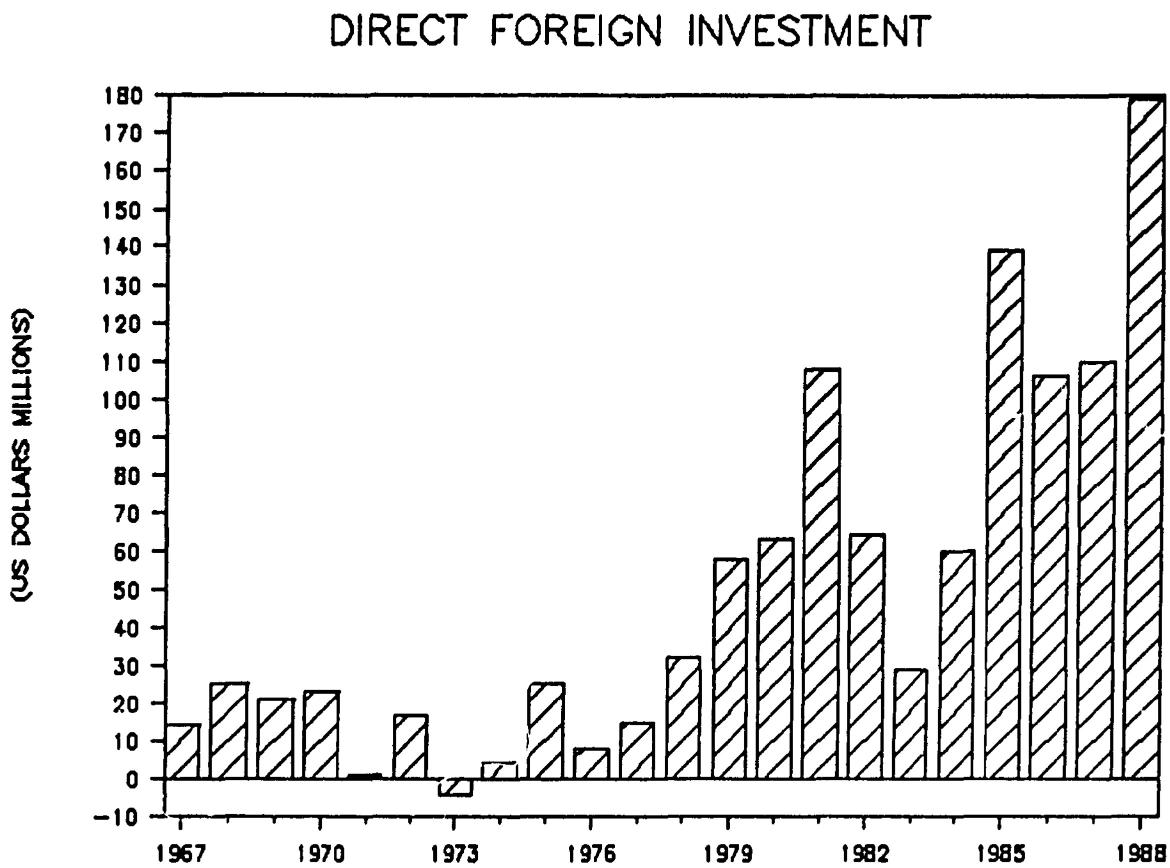
	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89
Total Revenues	15.3%	15.7%	15.0%	14.7%	15.7%	14.9%	15.3%	16.1%	16.5%	18.6%
Federal	14.3%	14.7%	14.0%	13.9%	14.9%	14.0%	14.4%	15.2%	15.6%	17.9%
Provincial	0.9%	1.0%	1.0%	0.8%	0.8%	0.8%	0.8%	0.9%	0.8%	0.7%
I. Tax Revenues	12.9%	12.9%	12.4%	12.2%	11.6%	10.8%	10.7%	12.9%	13.0%	15.1%
Federal	12.2%	12.2%	11.6%	11.5%	11.0%	10.1%	10.1%	12.2%	12.4%	14.6%
Provincial	0.7%	0.8%	0.8%	0.6%	0.7%	0.6%	0.6%	0.6%	0.6%	0.5%
A. Direct Taxes	2.2%	2.5%	2.6%	2.3%	2.0%	1.9%	1.7%	1.7%	1.8%	2.0%
1. Income & Corporation Tax	2.1%	2.3%	2.4%	2.2%	1.9%	1.7%	1.6%	1.6%	1.6%	1.9%
2. Taxes on Property	0.1%	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.2%	0.2%
B. Indirect Taxes	.NA	10.4%	9.8%	9.9%	9.6%	8.9%	9.0%	11.1%	11.2%	12.5%
3. Excise Duty	.NA	4.1%	3.9%	3.9%	3.4%	3.0%	2.7%	2.4%	2.4%	2.6%
(Federal)	.NA	4.1%	3.9%	3.9%	3.4%	2.9%	2.6%	2.4%	2.4%	2.6%
4. Sales Tax	1.0%	1.0%	0.9%	0.9%	1.0%	0.9%	0.8%	1.0%	1.1%	1.8%
4.1 On Imports	0.8%	0.8%	0.8%	0.7%	0.8%	0.7%	0.6%	0.8%	0.9%	1.4%
4.2 On Domestic Products	0.2%	0.1%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.4%
5. Taxes On International Trade	5.0%	4.8%	4.3%	4.5%	4.7%	4.5%	5.0%	5.2%	5.3%	5.7%
5.1 Import Duties	4.8%	4.5%	4.2%	4.5%	4.6%	4.4%	4.1%	4.4%	4.2%	4.6%
5.2 Iqra Surcharges	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.7%	0.7%	0.6%	0.6%
5.3 Export Duties	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%	0.2%	0.0%	0.5%	0.5%
6. Surcharges	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	2.1%	1.8%	1.9%
6.1 Gas	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.3%	0.5%	0.4%
6.2 Petroleum	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.7%	1.4%	1.4%
7. Other Taxes	0.6%	0.6%	0.6%	0.5%	0.6%	0.5%	0.5%	0.5%	0.4%	0.4%
7.1 Stamp Duties	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
7.2 Motor Vehicle Taxes	0.1%	0.1%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
7.3 Others	0.3%	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%	0.2%	0.1%	0.1%
II. Non-Tax Revenues	.NA	2.7%	2.4%	2.5%	3.6%	4.0%	4.7%	3.2%	3.5%	3.5%
(Federal)	.NA	2.5%	2.2%	2.3%	3.4%	3.8%	4.4%	3.0%	3.2%	3.3%
8. Interest & Dividend	.NA	1.0%	0.9%	1.0%	0.9%	1.0%	0.9%	1.2%	1.2%	1.2%
(Federal)	.NA	1.0%	0.9%	0.9%	0.9%	0.9%	0.9%	1.1%	1.1%	1.2%
9. Trading Profits	0.2%	0.4%	0.2%	0.1%	0.1%	0.1%	0.0%	0.0%	0.0%	0.1%
10. Post Office & T&T	0.3%	0.3%	0.3%	0.4%	0.4%	0.5%	0.5%	0.6%	0.6%	0.6%
11. Receipts from Civil Admn.	.NA	0.3%	0.3%	0.4%	0.4%	0.8%	0.8%	0.7%	0.6%	0.6%
12. Others	0.5%	0.6%	0.6%	0.7%	1.7%	1.8%	2.5%	0.8%	1.1%	1.0%
(Federal)	.NA	0.4%	0.4%	0.5%	1.6%	1.6%	2.3%	0.6%	0.9%	0.9%
GNP (Millions of rupees)	252,463	300,086	347,143	403,279	460,840	520,419	588,485	644,638	716,963	800,283

Data: Economic Survey. Worksheet: eabase fisc revenue.wk1.

Table: Consolidated Federal & Provincial Government Deficit Financing

	Proportion of GNP									
	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89
Total Expenditure	21.6%	21.2%	20.5%	21.6%	21.7%	22.4%	22.8%	23.6%	25.1%	25.1%
Total Revenues	15.3%	15.7%	15.0%	14.7%	15.7%	14.9%	15.3%	16.1%	16.5%	18.6%
Surplus of SOEs	0.6%	NA	0.5%	0.6%	0.6%	0.5%	0.5%	0.3%	0.8%	0.5%
DEFICIT	5.8%	NA	4.9%	6.4%	5.5%	7.1%	7.1%	7.2%	8.0%	7.0%
External Borrowing	2.8%	NA	1.5%	1.3%	1.1%	1.0%	1.5%	1.3%	1.8%	2.2%
Non-bank internal borrowing	0.6%	NA	1.8%	3.6%	2.7%	2.5%	4.6%	4.2%	4.3%	4.7%
Internal bank borrowing	2.5%	NA	1.6%	1.5%	1.7%	3.6%	1.0%	1.7%	1.9%	0.1%
GNP (Millions of rupees)	252,463	300,086	347,143	403,279	460,840	520,419	588,485	644,638	716,963	800,283

Data: Economic Survey. Worksheet: eabase fisc ¢ ffin.wkl.


DIRECT FOREIGN INVESTMENT
(US DOLLARS MILLIONS)
180
170
160
150
140
130
120
110
100
90
80
70
60
50
40
30
20
10
0
-10
1967
1970
1973
1976
1979
1982
1985
1988

Annex B

Detailed Policy Agenda

1. Industrial Investment Approval System

a. Problem Statement

Pakistan has in place a complex approval system whereby the Federal and Provincial Governments regulate the entry of new industrial investment in an attempt to avoid excess capacity, limit market concentration, increase indigenization, direct resources to priority areas, and ration scarce foreign exchange, infrastructure and utilities. This industrial investment approval system requires the private sponsors to satisfy the criteria of each of the several concerned public agencies. For instance, agencies involved with investment sanctioning, location clearance, import licensing, tax and custom duty exemptions, and provision of utilities must be satisfied before actual initiation of the industrial production process *1.

In recent years, the GOP has taken several steps to streamline the industrial investment approval system through liberalization of investment sanctioning criteria and reform of institutional arrangements to expedite sanction and post-sanction formalities. Federal Government sanction is now required only for investment (domestic or foreign) (a) costing Rs 1 billion and above and (b) covered by the Federal Specified List of 7 industries (arms and ammunition, security printing, currency and mint, high explosives, radio-active substances, alcohol and beverage industry based on imported concentrates, manufacture of automobiles and tractors, and, petroleum blending plants). Government of Punjab sanction is needed for flour mills and cotton ginning units located in the Punjab province. The institutional reforms include establishment of a Board of Investment chaired by the Prime Minister to evaluate expeditiously investment proposals, formation of a Committee on Investment to expedite post-sanction formalities for the BOI-sanctioned investment, and initiation of a "one window" approval facility at the industrial estate level. These measures, though steps in the right direction, are not commensurate with the size of the problem and significant reforms are needed to overhaul the industrial approval regime.

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*1 Recent studies such as the World Bank's Pakistan Industrial Regulatory Policy, (draft) 1988 and MTech's Industrial Approval System in Pakistan, 1990, indicate that the approval system, on the one hand, has not been successful in realizing the GOP's stated objectives and, on the other, has led to costly delays which have sometimes resulted in aborting of proposed new investment.

Annex B

b. End of Program Objectives

Establish a system where businesses face a minimum number of steps and agencies involved with the approval process; liberalize approval criteria of each of the agencies within the considerations of national security, citizens health and safety, and religious sensitivity.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmarks

o Benchmark : Amend "alcohol and beverage industry based on imported concentrates" in the Federal Specified List to read "alcohol and beverages based on alcoholic concentrates."

Rationale : The phrase "alcoholic and beverage industry based on imported concentrates" is restrictive and imposes sanction requirement for non-alcoholic beverages based on imported concentrates which are not offensive to known religious and social norms.

ii. Directions in Subsequent Years

(a) Liberalize Sanctioning Criteria : Shorten Federal and Punjab Provincial Specified Lists.

(b) Liberalize Location Policy : Shorten "negative list" of areas for industrial location and increase reliance on economic incentives to direct location.

(c) One-window Sanctioning : Evaluate the "one window" approval experience at the industrial estate level and the feasibility of its extension to the national level.

(d) Minimize Discretionary Behavior : Minimize discretionary elements in taxation and import policies so that the need to seek firm-specific exemptions is minimal.

d. Suggested Study Areas

Management audit of post-sanction procedures and industrial location policy will receive priority attention. The first study will suggest simplification of procedures based upon a detailed evaluation of existing systems for registration of firms, issuance of capital, project appraisal in financial institutions, location clearance, issuance of National Tax Numbers, clearance of imported goods, and provision of utilities. The second study will focus on the development of economic criteria for regulating industrial location and rationing scarce utilities.

Annex B

2. Foreign Investment

a. Problem Statement

GOP foreign investment policies have largely been geared to promote foreign investment in capital intensive manufacturing and natural resource exploitation. Foreign private investment is prohibited in agriculture land, forestry, irrigation, real estate, radioactive minerals, insurance, and health; and, is generally not treated as priority in banking, commerce and services (with the possible exception of tourism). While an elaborate legal framework exists for industrial undertakings, less clear are the rules on non-industrial activities. Investment in industrial undertakings is regulated by the Foreign Private Investment (Promotion and Control) Act, 1976. The Act guarantees foreign capital against arbitrary nationalization; promises equal treatment of foreign and domestic capital in matters relating to international trade and taxation; and, provides for remittances of profit and capital. It also provides for relief from double taxation in cases of those countries with which Pakistan has bilateral tax agreements.

In recent years, the GOP has taken at least three significant steps to encourage foreign investment. First, export for the Karachi Export Processing Zone to the tariff area has been allowed; second, the "positive list" restricting foreign investment to 21 specified industries has been withdrawn; third, foreign equity has been removed from the list of sanctioning criteria and new foreign and domestic investment are subject to uniform sanctioning procedures. However, these reforms may not create sufficient conditions to attract foreign investment which, despite some recent gains, amounted to a low $179 million in 1988. Foreign private investment is constrained by several factors such as complicated approval procedures, administered prices, disincentives in the tax structure, restrictive trade policy, inadequate protection of intellectual property rights, and, civil disturbances in Sindh.

b. End of Program Objectives

Widen the coverage of foreign private investment to cover all sectors of the economy and achieve maximum uniformity in application of rules to foreign and domestic investment.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmark

o Benchmark : Issue a notification clarifying that the sanctioning criteria specified by the Federal Government in Notification No. BOI-Misc.(5)/89 dated April 8, 1990, applies to new investment as well as investment in expansion of existing facilities of foreign companies.

Rationale : The clarification will bring the existing foreign investors at par with new entrants. Further, the existing foreign companies are in a position to make the additional investment much faster than the new investors.

- Benchmark : Revise and enforce appropriate legislation to protect intellectual property rights.

  Rationale : Protection of intellectual property rights is an area of increasing concern to foreign investors and should receive GOP's priority attention.

ii. Directions in Subsequent Years

(a) Eliminate the Prohibited List : Foreign investment should be permitted for all sectors of the economy including agriculture land; forestry; irrigation; real estate including land, housing and commercial office buildings; insurance; and health.

(b) Liberalize Loan Procedures : Loans to foreign investors from development finance institutions should be permitted according to the same procedures applicable to local companies.

(c) Rationalize Application of Tax Rules to Non-Resident Companies : Non-resident companies having a permanent establishment in Pakistan should be treated at par with resident companies for deduction of tax at source.

(d) Eliminate Restrictions on Foreign Banks: Foreign commercial banks should be permitted to lend to public sector entities and undertake their letter of credit business; limitation of a maximum of three branches should be removed; and, wholly-owned foreign investments banks should be allowed.

(e) Establish More Export Processing Zones : An Export Processing Zone in Punjab should be established as recommended by the 1988 National Industrial Commission. This Export Processing Zone should be privately run rather than administered by the GOP.

d. Suggested Study Areas

There is a need for priority research on the impact of retail price controls on foreign investment. This study will target those industries where foreign investment is pronounced and assess the distortions generated by price controls.

3. Privatization

a. Problem Statement

Current issues in privatization have already been outlined in Section III.B.4. Briefly, Pakistan has a large and inefficient corporate sector sponsored by the Federal and Provincial Governments which participate directly in the production, processing and marketing of goods and services. There is emerging recognition within the GOP of the need to privatize state-owned enterprises. However, implementation has been constrained principally by lack of an appropriate privatization policy framework, resistance from bureaucracy and labor, absence of a clear legal framework, and inadequate technical information.

b. End of Program Objectives

Broaden asset distribution through divestiture by limiting state acquisition of new assets, and increasing the amount of privately owned assets as a proportion of GNP.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmark

o Benchmark : Announce a policy to restrict Federal Government sponsored enterprises to undertake new investment except for modernization and rehabilitation of existing facilities; for activities in which private sector is not forthcoming; and, for consideration of national security, infrastructure development, and public education, health and safety.

Rationale : Limitation on new public investment for direct participation in economic activities will encourage private sector growth and also provide the needed credibility to the privatization programs.

o Benchmark : Institute majority privatization of one NCB and at least one major industrial unit.

Rationale : Initiation of privatization in the financial and manufacturing sectors during the first year of the Program will provide the needed credibility to the GOP's stated privatization plans.

ii. Directions in Subsequent Years

(a) Legislation for Privatization : Enact legislation to remove legal constraints to privatization.

Annex B

(b) Legal Framework for Privatization : Initiate a study on legal constraints to privatization and, based on the recommendations of the study, develop a schedule of amendments in the relevant legislation.

(d) Privatize Loss-Making Enterprises : Investigate the feasibility of auctioning loss-making units at discounted prices. If auctioning is not feasible, develop and implement a program for management and financial restructuring as a pre-privatization activity.

(e) Divest Profit Making Enterprises : Design and implement a long-term plan for majority divestiture of profit making entities.

d. Priority Research Areas

Studies on legal constraints to privatization and on the feasibility of auctioning loss-making units should be undertaken on a priority basis. The first study will cover all Federal Government sponsored holding and subsidiary companies in banking and finance, insurance, trade and commerce, manufacturing, construction, oil and gas, transport, power, printing and publication, and consultancy. For each company, the study will identify legal constraints, if any, and recommend appropriate legal changes. The second study will focus on the financial aspects of loss-making enterprises and develop auction criteria satisfactory to the GOP and attractive to the private sector.

4. Investment Promotion

a. Problem Statement

Pakistan's foreign investment promotion system is comprised of three institutional mechanisms: the Investment Promotion Bureau, trade and commercial sections in Missions abroad, and Chambers of Commerce and Industries. The IPB has thus far served more as an investment sanctioning agency rather than an investment promotion organization; overseas trade and commercial sections are largely inactive; and, the promotion efforts of the Chambers of Commerce and Industry, though positive, have suffered from lack of strong monetary support.

The GOP is currently in the process of reorganizing and reorienting the role of IPB towards investment promotion. The reorganization plan envisages creation of a separate wing, headed by a Director General, to focus exclusively on planning, publicity and promotion. This new unit will be responsible for identifying new areas for potential investment, preparing project profiles, developing investment related literature, organizing seminars, counselling prospective investors, and opening investment centers both at home and abroad. The GOP has also established an Advisory Committee, consisting of private and public sector representatives, to guide IPB, among others, in developing and implementing promotional programs. Although an assessment of the adequacy of this promotional plan will have to wait until the proposed re-organization is fully implemented, it can nonetheless, be stated that the planned participation of the private sector appears to be peripheral.

b. End of Program Objective

Increase private sector participation in investment promotion programs.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmark

o Benchmark : Provide equal representation to the public and private sectors the Advisory Committee to the Investment Promotion Bureau.
Rationale : The Advisory Committee as presently constituted is comprised of 6 private sector representatives, 18 public sector officials and 4 industrialists/professionals to be nominated by the Federal Government. Greater private sector representation will result in a more appropriate balance between the private and public sectors.

ii. Directions in Subsequent Years

(a) Contract Selected Activities to the Private Sector : The GOP should contract promotional activities, to the maximum possible extent, to private firms. This could include preparation of project profiles, development of investment related literature, and organization of seminars.

(b) Finance Overseas Visits of Private Delegations : Funds should be made available to the FPCCI to finance overseas visits of trade and investment delegations in accordance with a well developed long-term plan.

d. Suggested Study Areas

A study should be commissioned to explore the feasibility of undertaking local and overseas investment promotion activities through the Federation of Pakistan Chamber of Commerce and Industry and other private business groups.

5. Trade Policy

a. Problem Statement

Pakistan is rapidly falling behind in its attempts to compete on the international market. While traditional exports (cotton, rice and textiles) have grown at reasonably high rates in recent years, there is limited scope for further expansion. Export diversification into different products, especially those which have a higher value-added, is essential for continued economic growth.

There are a number of reasons for lack of diversification in the mix of export products. The rate of exchange has often been overvalued over the past thirty years, encouraging imports rather than exports. The tariff regime has made production for the domestic market more profitable than for the export market. The effective protection of the tariff regime has made Pakistani enterprises less competitive and less able to compete on international markets. Complicated government regulations for investment and export have made export-oriented investment, especially in manufacturing, so risky and difficult that many investors prefer to invest in real estate and trade activities.

Of course, a number of structural constraints to diversified exporting remain. For example, better infrastructure for export-oriented projects is needed in certain areas, and may require priority consideration in Government investment planning. Another problem is the lack of knowledge of overseas markets and modern production processes. However, the private sector, given the proper set of incentives, should be able to overcome these problems.

b. End of Program Objectives

(a) Establish a macroeconomic policy program which makes exporting more profitable and at least as profitable as manufacturing for the domestic economy.

(b) Reduce the regulations governing exporting to an absolute minimum.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmarks

o Benchmark: Announce a policy that abolishes all absolute bans on the export of agricultural and other commodities. The Government should also publish a set of criteria to determine when an export restriction can be placed on a product. Export restrictions, if absolutely necessary, should generally only be in the form of an export tariff levied at a rate that does not undermine the ability of exporters to compete in international markets.

Rationale: Export markets, especially for certain fruits and vegetables, have been lost or seriously undermined because of absolute bans on certain products. Pakistan must gain a reputation as a serious and reliable exporters if it is to gain market share in non-traditional exports.

Annex B

o Benchmark: Design and begin implementation of a more flexible duty drawback system which can more rapidly change the level of drawback according to changing economic conditions, and which is administered with less delay. USAID can provide technical assistance if needed.

Rationale: Exporters complain that the present duty drawback system is slow and not responsive to changing economic conditions. The CBR presently does a detailed investigation of the proper level of duty drawback and then rebates exporters accordingly. However, if inputs into the process change, the entire investigation process must begin afresh. There could be a need for more staff working on the program or a need to simplify and/or computerize the present investigative procedure.

o Benchmark : Further reduce the dispersion and average level of tariffs in the economy, according to the program established by the World Bank and IMF.

Rationale : This benchmark will expedite the needed liberalization of the trade regime.

ii. Directions in Subsequent Years

(a) Minimize Export Licenses and Permits : To compete with dynamic exporters from Thailand and Hong Kong, Pakistan needs to simplify and minimize the list of licenses, regulations, and prohibitions which control trade and investment.

(b) Minimize Import Licenses and Permits : Minimize the need for import licenses and permits, especially for import of capital machinery and industrial raw material.

(c) Develop Infrastructure for Export Industry Some priority needs to be given to the development of the appropriate infrastructure to facilitate export, including equipment for quality control, communications, and air transport, including the development of a private cargo service.

(d) Reduce Tariff Regime There is the need to further reduce the dispersion and average level of tariffs in the economy, according to the program established by the World Bank and IMF.

(e) Implement Macroeconomic Program to Equalize Investment Incentives in the Import and Export Sectors Through a series of exchange rate adjustments (possibly using the "compensated devaluation approach" suggested by Gustav Papanek) and other types of policy changes such as taxation measures, the GOP should work to make investment for export as attractive and profitable as investment for the domestic market. Taking the steps necessary to make the Rupee a convertible currency would obviate the need for many of the current regulations.

d. Suggested Study Areas

The first area is an in-depth study with the Ministry of Commerce on the permit and licensing system used for exports and imports. This should be conducted with expatriates who have a practical knowledge of and long experience with customs procedures in other countries. Macroeconomic studies needed include an investigation of the applicability of the compensated devaluation scheme and a study of the measures needed to make the Rupee a convertible currency. There is also a need for both study and implementation of measures to equalize the profitability of investment for export and domestic markets. The taxation policy issues are the subject of continuing discussion and study in Pakistan. USAID should provide technical assistance to study these issues as required, although the GOP may not feel that it is necessary. However, the appropriate macroeconomic policies are critical to the success of the PIE program and should therefore be the subject of considerable study by USAID.

6. Regulatory Framework

a. Problem Statement

The regulatory framework controlling both the set-up and operation of business can be daunting, particularly for small businesses. To begin a business, one must not only put together sources of funding, but also go through a costly and time consuming process for registration, particularly the No Objection Certificate. To stay in business, one must deal with a multitude of Government agencies responsible for things such as electricity, food safety, sanitation, social security, education, and labor. These agents and inspectors have broad discretionary powers. Many business people complain about the unjust way in which these powers are used to extract illegal payments. While the intent of many of the regulations may be reasonable, the implementation of them is not.

Implementation of the regulatory framework has a number of economic distortions which are undesirable.

- First, it discourages some people from investing in or staying in business, so investment is lower than it might otherwise be.

- Second, it may discourage people from registering in the system at all; these businesses become a part of the "informal sector." This represents a considerable loss to the Government in tax revenues that should have been collected and is unfair competition for those businesses that are trying to abide by the rules.

Annex B

- Third, the regulations may lead to distortions in the way business is structured. For example, there is a law exempting firms with ten employees and under from many of the labor laws which apply to larger firms. Because many small businesses view those laws and their enforcement by Labor Department officials as onerous, some firms either sub- contract much of their labor or form a number of horizontally linked firms/units, each one with 10 employees. This practice is a large waste of economic resources when multiplied throughout the economy. Many of the labor regulations are considered so burdensome that employers spend considerable time and effort avoiding them The end result is damaging for employers and employees alike.. the employers' resources are wasted avoiding regulations, and the workers end up with little or no protection.

Small business is at a disadvantage in the regulatory framework. Many of these people are illiterate and have a difficult time countering the assertions of the regulators. They often do not have sufficient resources to hire legal assistance and the legal system is slow and inefficient. Although there is a system of appeal for administrative decisions made by an agent, its efficiency, especially for small business people, is questionable.

b. End of Program Objectives

(a) Reduce and rationalize the rules and regulations that govern the start-up and operation of business, particularly for small enterprises.

(b) Develop an administrative system which results in eliminating or substantially reducing the discretionary powers accorded to regulatory officials.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmarks

o Benchmark: The GOP, in consultation with Provincial and Municipal authorities, will develop and begin implementation of a streamlined "negative list" approach to the issuance of the No Objection Certificates, i.e. only those sectors on the list should be required to obtain an NOC. The NOC should be granted according to a clear set of requirements and guidelines in a streamlined fashion.

Rationale: The NOC process is cumbersome and costly. It discourages investment and in many cases represents lost time and money for both the private and public sectors. A negative list approach would minimize the number of sectors that are subjected to this procedure and require the government to make clear its criteria for granting the NOC. A simplified business license approach could be used to help keep track of businesses for taxation purposes.

ii. Directions in Subsequent Years

(a) Re-evaluate Definition of Small Business : The present definition of small business -- 10 employees or less -- may be too limited to accommodate the needs of growing businesses in a modernizing economy. The Labor Department, with technical assistance if required, should undertake a study and review of this issue and consider changing the definition of small business to something like 50 employees.

(b) Review Labor Laws : The present set of laws protecting labor is so complicated and rigid that it invites evasion by employers and therefore provides little protection for workers. At the same time, employers complain about the difficulty of firing workers. Labor laws should be reviewed and revised to increase the efficiency of the system. For example, in return for improved protection on the job, labor may need to accept a more flexible system of hiring and firing. An unemployment scheme also should be explored for workers in large businesses.

(c) Reduce Discretionary Powers : Ways to eliminate or substantially reduce the discretionary powers of regulatory officials should be studied, approved, and implemented by the top officials of the concerned agencies including the Ministries of Commerce and Industries, as well as the concerned administrators at Provincial and Municipal levels.

(d) Strengthen Small Business Voice : Particular attention should be paid within the Chambers of Commerce and Industries to assisting the small business sector in formulating its policy concerns and transmitting them to the proper authorities. In addition, there is a need to provide small business people with regulatory and legal advice, which should be organized at the Chamber level. Training sessions on certain topics would be one method of addressing this concern.

d. Suggested Study Areas

There is a need for studies in two major areas. First, there is a need for work done in organizational management to determine how to reduce the discretionary power of individual agents while conforming to the desirable rules and regulations. To this we would also add a study on how to reduce the rules and regulations that pertain to business start-up and operation. This is an enormous task, and may best be tackled on an industry by industry basis. Second, there is a need for an overall review of labor rules and regulations, again an enormous (and contentious) task. While USAID has traditionally not ventured too close to labor regulations, it may prove useful to provide some low-key interventions (such as through the AFL-CIO's Asian-American Institute of Labor, based in Karachi) to help in these areas. Understanding the relationship between labor and business is essential to moving forward on many of the policy areas targeted under this program, particularly privatization.

7. Financial Sector Reform

a. Problem Statement

The financial sector is dominated by five state-owned commercial banks, which control 80 to 90 percent of the nation's financial resources, leaving little room for the private sector's involvement in financial sector activities. Before discussing the problems of the NCBs, it is important to note that during the past decade, the GOP has adopted numerous corrective measures for encouraging private sector participation in the financial sector. These measures include (1) Islamization of the financial system (i.e. shifting banking transactions from an interest-bearing basis to a profit and loss sharing basis) which has culminated in the creation of numerous types of financial institutions and instruments in the private sector, (2) provision for establishment of IFBs, and (3) provision for establishment of an off-shore fund, which would attract global attention to Pakistan's securities market. Despite some liberalization in the past few years, and the Government's stated intention to do more, the financial sector remains dominated by the Government through broad ownership and control of financial institutions. This contributes to: rigidity or lack of innovation and flexibility in the system; poor performance reflecting entrenched bureaucratic personnel; and, economic waste due to inefficiency, corruption, redundant personnel, high costs, and excessive interest rates.

Over the past few years, the financial institutions have been confronted with numerous difficulties. The most important problem is the status of their loan portfolios: presently the banking system faces a big problem of arrears which appears to be endemic throughout the system. There have been a large number of willful defaults in the absence of efficient recovery mechanisms; banking tribunals are ineffective and the litigation process is lengthy and tedious. There is inadequate competition among the banks, as they are all owned by the Government, and are managed under a set of uniform rules and regulations which are established by the bureaucrats and embodies all aspects of the banking operations. Unavailability of credit information has caused concentration of credits in relatively few established enterprises and individuals, making it quite difficult for new entries to the credit market. Although there are

19 foreign private commercial banks in the system, they do not provide competition due to the limited size of their financial resources and the statutory limitations on their activities. The newly licensed IFBs are in no hurry to begin operation due to the lack of equitable conditions in the financial market.

A recent review of the financial sector by the World Bank makes it clear that creating a more efficient and competitive financial sector with particular emphasis on capital markets (equities and fixed income securities), as well as increased participation of private sector institutions (domestic and foreign banks, venture capital companies, etc.) in the banking sector is critical to continued growth of Pakistan's economy. However, this is a complicated and far-reaching issue in Pakistan. The nationalized banking system has stifled competition in the financial sector. Companies have grown used to receiving up to 90% or more of their financing needs for new projects from the banking system until recently, at concessional interest rates under SBP lines of credit, and see little need to go to the trouble and cost of raising capital in equity markets. Likewise, companies do not issue fixed income securities in a bond market because: (a) it is cheaper to borrow from state-owned banks; (b) the issuance of risk-free debt instruments by the Government with high yields make it excessively expensive to issue commercial paper attractive to investors; and (c) the Companies Ordinance makes it difficult for companies to issue long-term debt.

Many reform measures are needed. For an efficient capital market, there is need to liberalize interest rates, reduce abuse by insiders; modify the regulatory and supervisory framework; strengthen enforcement; establish a credit rating process or organization; create private mutual funds to compete with Government owned mutual funds such as the National Investment Trust; introduce a market-based mechanism for floating Government securities and for pricing of new private share issues; promote evolution of institutions and instruments needed for the functioning of a secondary market; increase supply of shares of public enterprises and multinationals; encourage investment by pension funds, insurance companies, and other large institutional investors; and, improve accounting and auditing standards. For an efficient and competitive banking system, there is need to increase autonomy and improve efficiency and profitability of the nationalized commercial banking system; improve borrower discipline; establish more transparent accounting policies, particularly for non-performing loans; strengthen regulation and supervision; reduce the share of government financial institutions through disinvestment/privatization of NCBs and freer entry of private sector banks; and establish an effective legal system for debt recovery.

b. End of Program Objectives

Establish a more efficient and diversified capital market, including a secondary market for debt instruments, and increase the amount of capital raised through equity markets.

Increase competition in the financial sector while providing the regulatory framework needed to ensure soundness of the financial system and to protect consumers.

c. Steps to Achieve End of Program Objectives

i. First Year Benchmarks

- Benchmark: Amend the regulatory framework to allow the newly formed Investment Finance Banks to compete with nationalized commercial banks in all aspects of banking, except in taking short-term (30 days or less) deposits. This would include authorization for the IFBs to function as foreign exchange dealers, allowance for companies to issue Term Finance Certificates in favor of the IFBs, removal of the stamp duty on IFB commercial paper products, and IFB eligibility for use of the banking tribunal. In addition, the approval process for new IFBs should be accelerated and made much more transparent.

  Rationale: The success of the new Investment Finance Banks is critical to increasing competition in the financial sector and providing an additional source of funds to the business community. Therefore, banking regulators must allow the IFBs access to a substantial segment of the banking universe.

- Benchmark: Amend the Companies Ordinance to permit company issuance of short-term commercial paper and long-term debt instruments that are consistent with Islamic banking principles.

  Rationale: This is a necessary for the development of new capital market instruments for long-term financing and the evolution of the secondary market.

- Benchmark: Revise personnel policies for all National Commercial Banks and Development Finance Institutions to permit these institutions to establish their own personnel system, including hiring and releasing staff and establishing pay scales.

  Rationale: In order for state-owned banks to increase their efficiency they must be delegated more autonomy to manage their resources. This is particularly important for staff.

Benchmark: Reduce the access of NCBs and DFIs to subsidized government liquidity financing, and reduce the total flow of directed credits through these banks.

Rationale: There can be no true competition between public and private banks when the Government subsidizes the source of funds for public banks. The GOP should phase out major subsidies, such as State Bank liquidity credits and directed credits, to increase efficiency and competition. Various Government time deposits should also be restricted in the future.

ii. Directions in Subsequent Years

(a) Bond Pricing : Price government bonds according to market criteria in order to allow fair competition for corporate bonds.

(b) Debt Recovery : Improve the system for the recovery of debt to increase the effectiveness of the banking system.

(c) Lower Debt Financing : Lower the percentage of a project that is financed by banks to encourage the use of capital markets by corporations that wish to raise long-term capital.

(d) Increase Competition in Financial Sector : Allow private commercial banks, Development Finance Institutions, and other financial institutions (including grameen-style banks) to undertake banking functions, including accepting deposits, to encourage the mobilization of savings particularly in rural areas and to provide increased competition for the nationalized commercial banking system.

(e) Brokerage Eligibility : Broaden the eligibility criteria for licensing traders in the primary and secondary financial and capital brokerage markets.

(f) Capital Market Supervision : Strengthen the supervision and regulation of the stock market to increase investor confidence and reduce abuse by market insiders. Make the Corporate Law Authority an independent regulatory agency supervising capital markets and separate it from the Civil Service to ensure top quality professionals.

(g) Financial Disclosure : Improve financial disclosure provisions and accounting and auditing standards applicable to stock and bond issues to increase the quality of financial information available to investors. To this end, the financial operations and capital markets specialists should work with Pakistan's Institute of Chartered Accountants to establish an effective, self-regulatory body of accountants. Accountants should be required to apply the same accounting standards to all financial statements for both public and private companies.

(h) Create Private Mutual Funds : Private mutual funds should be created to compete with the NIT. The benefits provided to NIT, as well as the restrictions imposed, should be gradually removed so that other mutual funds can compete.

c. Suggested Study Areas

Studies are needed in all of the above areas. They will be performed largely by the long-term technical assistance team in Islamabad and Karachi.

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TAGS:
SUBJECT: PAKISTAN - ANPAC PRIVATE INVESTMENT EXPANSION PROGRAM (391-0514)

SUMMARY:

THE ANPAC, CHAIRED BY BRUCE ODELL AND ATTENDED BY AA ADELMAN AND DAA BLACKTON MET ON APRIL 23, 1990 TO REVIEW THE PRIVATE INVESTMENT EXPANSION PROGRAM (PIE) PAIP. ANPAC HEREBY APPROVES THE CONCEPT OF THE DOLS 180 MILLION PROGRAM, DELEGATES AUTHORITY TO THE MISSION TO DEVELOP AND AUTHORIZE A DOLS 35 MILLION FY90 PAAD FOR THE PROJECT ELEMENTS OF THE PROGRAM. PAAD FOR THE SECTOR PERFORMANCE-BASED GRANT, THE PRIVATE SECTOR CIP AND OTHER FUTURE PROGRAM ELEMENTS WILL BE SUBMITTED TO AID/W FOR REVIEW PRIOR TO AUTHORIZATION IN FY91.

END SUMMARY

1. ANPAC VIEWED EXPANSION OF PRIVATE SECTOR INVESTMENTS AS PRESENTED IN THE PAIP AS CRUCIAL TO THE ECONOMIC GROWTH OF PAKISTAN. ALTHOUGH IT LACKS MANY DETAILS, IT DOES WARRANT ANPAC APPROVAL OF THE CONCEPT AND

DELEGATION TO AUTHORIZE THE DOLS 35 MILLION PAAD FOR THE PROJECT ASPECTS OF THE PROGRAM. ANPAC RECOGNIZED THAT THE MISSION WILL NOT HAVE A DETAILED POLICY AGENDA READY, HENCE AUTHORIZATION FOR THE FIRST YEAR IS LIMITED TO PROJECT ELEMENTS OF THE PROGRAM. PRESENTATION OF ANPAC ISSUE DISCUSSIONS AND RECOMMENDATIONS FOLLOWS:

1.A. THE MECHANISM FOR ASSISTANCE

DISCUSSION: PIE DOESN'T MEET THE USUAL DEFINITION OF NON-PROJECT PERFORMANCE-BASED SECTOR ASSISTANCE. INSTEAD IT INCLUDES A NUMBER OF PROJECT ELEMENTS, WITH MANY QUESTIONS TO BE CLARIFIED. SUSTAINABILITY QUESTIONS ALSO NEED SPECIFIC ATTENTION. THE PAIP CONTAINS MANY SENSIBLE, YET PRELIMINARY, PROPOSALS. THERE IS A CONSENSUS BETWEEN MISSION REPS AND BUREAU THAT A FULLY COHERENT, AUTHORIZABLE PACKAGE AT THE 180 MILLION LEVEL DOES NOT EXIST AT THIS TIME. ANPAC

CONCURS THAT THE MISSION NEEDS TO BE AN ACTIVE PARTICIPANT AND NOT AN OBSERVER IN ASSISTING THE GOP TO MOVE QUICKLY WITH ITS POLICY FOR MUCH GREATER PRIVATE SECTOR PARTICIPATION IN THE ECONOMY.

RECOMMENDATION: ANPAC AUTHORIZES THE MISSION TO PREPARE A PAAD AND DELEGATES AUTHORITY TO THE MISSION DIRECTOR TO AUTHORIZE THE DOLS 35 MILLION INITIAL PAAD, WHICH WILL BE INCREMENTALLY FUNDED WITH A MINIMUM FY90 OBLIGATION OF DOLS 5 MILLION. THE MISSION MUST ENSURE THAT THE FY90 PAAD COVERS A WELL-DEFINED AND INTEGRATED SET OF PROJECT ELEMENTS. THE BUREAU ENCOURAGES THE MISSION TO THINK FLEXIBLY ABOUT DEFINING THE NATURE OF FUTURE INTERVENTIONS (POSSIBLE OPTIONS: A SINGLE PROGRAM, TWO OR MORE PROGRAMS, OR A COMBINATION OF PROGRAMS AND PROJECTS).

1.B. POLICY AGENDA

DISCUSSION: THE CENTRAL ELEMENT OF PROGRAM ASSISTANCE IS A POLICY AGENDA, WHICH IS TO BE DEVELOPED DURING THE FIRST YEAR. THE PROGRAM WILL WORK THROUGH THE GOP TO REACH THE ULTIMATE BENEFICIARY, THE PRIVATE SECTOR, THROUGH A SERIES OF POLICY REFORMS.

RECOMMENDATIONS: THE MISSION'S ILLUSTRATIVE LIST OF POLICY OBJECTIVES IS A GOOD POINT OF DEPARTURE; HOWEVER, THE BUREAU EXPECTS CHANGES OVER TIME. THE POLICY AGENDA SHOULD ESTABLISH FIRM AND REALISTIC BENCHMARKS FOR THE FIRST YEAR. END-OF-PROGRAM INDICATORS SHOULD BE

ESTABLISHED ALONG WITH INTERMEDIATE BENCHMARKS. BENCHMARKS FOR INTERMEDIATE YEARS MAY BE LESS FIRM, BUT JUST AS IMPORTANT. THE BUREAU RECOGNIZED THE MISSION'S NEED FOR FLEXIBILITY IN NEGOTIATIONS WITH THE GOP AND THE INHERENT FACT THAT BENCHMARKS ARE EVER EVOLVING. HOWEVER, THE MISSION SHOULD SPELL OUT ITS GAME PLAN FULLY. THE BENCHMARKS SHOULD PROGRESS THROUGH PROGRAM IMPLEMENTATION OF KEY POLICY REFORMS ULTIMATELY TO ACTUAL SECTOR PERFORMANCE, WHERE MEASURABLE AND ATTRIBUTABLE TO THE PIE PROGRAM

1.C. OPEN SOCIETIES VIA THE PRIVATE SECTOR

DISCUSSION: THE PAIP TARGETS PAKISTAN'S PRIVATE SECTOR AS THE ULTIMATE BENEFICIARY OF PIE, BUT MANY OF THE ACTORS AND THE KEY RECIPIENTS OF AID'S TA ARE PUBLIC INSTITUTIONS. THE PAIP HAS HEAVY EMPHASIS ON THE GOP'S NEED FOR POLICY REFORM, BUT DOES NOT DISCUSS THE PRIVATE SECTOR'S ROLE IN MOLDING AND IMPLEMENTING THESE REFORMS.

RECOMMENDATIONS: MISSION REPS CONCURRED WITH THE NEED

TO ARTICULATE A STRONGER ROLE FOR PRIVATE SECTOR ORGANIZATIONS (SUCH AS CHAMBERS OF COMMERCE, TRADE ASSOCIATIONS, AND EXPORT GROUPS) IN THE POLICY REFORM PROCESS. PROVIDING TA DIRECTLY TO THE PRIVATE SECTOR GROUPS IS CONSIDERED ESSENTIAL.

1.D. CAPITAL MARKET DEVELOPMENT

DISCUSSION: THE PAIP IS NOT CLEAR WHETHER ONE OF ITS STATED AIMS , TO ASSIST THE DEVELOPMENT OF PRIVATE SECTOR CAPITAL MARKET INSTITUTIONS - MEANS TO ASSIST ESTABLISHMENT OF INVESTMENT FINANCE CORPORATIONS (IFCS) OR TO HELP TO DEVELOP STRUCTURAL REFORMS IN THE PAKISTAN POLICY ENVIRONMENT WHICH WILL ASSIST IFCS.

RECOMMENDATIONS: THE MISSION SHOULD PREPARE AN ANALYSIS OF THE CAPITAL MARKET DEVELOPMENT CONSTRAINTS AND AN ASSESSMENT OF THE NEED FOR IFCS VIS-A-VIS OTHER CAPITAL DEVELOPMENT MECHANISMS (I.E. COMMERCIAL BANKS, LOCAL AND INTERNATIONAL BONDS, ETC). THE MISSION SHOULD ALSO EXPLORE THE LEVEL OF DEMAND AMONG PAKISTANI INVESTORS FOR IFC CAPITAL AND POTENTIAL TYPES OF REGULATORY AND OPERATIONAL RULES GOVERNING IFC ACTIVITY. THE PAAD SHOULD DEMONSTRATE HOW THIS COMPONENT RELATES TO THE REST OF THE PROJECT.

1.E. STAFFING

DISCUSSION: PRIVATE SECTOR INITIATIVES ARE PERSONNEL INTENSIVE. THIS SECTOR IS ALSO TOO IMPORTANT TO RELY ON PSCS AND TA CONTRACTORS FOR LONG-TERM MANAGEMENT.

RECOMMENDATIONS: THE PAAD SHOULD CONTAIN AN ANALYSIS AND STAFFING PLAN FOR THE FULL TERM OF THE PROGRAM.

1.F. WOMEN'S AND SMALL ENTERPRISES

DISCUSSION: THERE WAS CONCERN ABOUT WOMEN'S AND SMALL ENTERPRISE EFFORTS BECOMING LOST OR OVERSHADOWED BY THE BROAD GENERAL CHARACTER OF PIE.

RECOMMENDATIONS: THE MISSION SHOULD CONSIDER THE USE OF A SEPARATE INTERVENTION FOR THIS VERY IMPORTANT SECTOR. IF IT MAKES SENSE TO CONTINUE THIS AS A PART OF PIE, THE PAAD SHOULD ARTICULATE HOW THE INTERVENTIONS WILL EXPAND INVESTMENT IN THIS SECTOR. IF NOT, MISSION SHOULD PURSUE OTHER OPTIONS.

1.G. LOCAL CURRENCY

DISCUSSION: BUREAU STAFF AND MISSION REPS AGREED THAT THE MISSION DOES NOT HAVE SUFFICIENT INFORMATION AT THIS TIME TO MAKE DECISIONS RELATED TO THIS ISSUE.

RECOMMENDATIONS: LOCAL CURRENCY ISSUES MUST BE HANDLED IN ACCORDANCE WITH APPLICABLE POLICY PAPER GUIDANCE IN HANDBOOK 1, PART VII. THE MISSION MUST EVALUATE THE NATURE OF THE PLANNED INTERVENTIONS AND PROVIDE THE

RATIONALE FOR THE DECISIONS RELATED TO LOCAL CURRENCY ISSUES. THE PAAD SHOULD DOCUMENT THE PROPOSED COURSE OF ACTION. LOCAL CURRENCY GENERATION/USE OR ABSENCE THEREOF WILL RECEIVE SUBSEQUENT REVIEW BY AID/W, WHEN THE MISSION SUBMITS THE FY91 PAAD FOR AID/W REVIEW PRIOR TO AUTHORIZATION OF THE REMAINING DOLS 145 MILLION.

2. ADDITIONAL PAAD DESIGN GUIDANCE

ANPAC CONCURRED WITH THE DESIGN GUIDANCE RECOMMENDATIONS DISCUSSED BY THE PRC. THE FOLLOWING CONCERNS ARE TO BE ADDRESSED IN THE PAAD:

2.A. PROGRAM COORDINATION WITH OTHER DONORS: AS THE PROGRAM PLANS TO LEVERAGE PROGRAM FUNDING FOR INCREASED PRIVATE INVESTMENT FUNDS (THROUGH EX-IM, IBRD, ETC), WHAT LEVEL OF INTER-AGENCY COORDINATION HAS BEEN ACCOMPLISHED TO DATE? WHAT'S PLANNED? WHAT SPECIFIC ROLES ARE ENVISIONED FOR EX-IM BANK, ADP, AND THE PRE REVOLVING FUND? WHAT MECHANISMS WILL BE USED FOR IMPLEMENTATION?

2.B. COORDINATION WITH IMPLEMENTATION ENTITIES: A LARGE NUMBER OF PLAYERS ARE INVOLVED IN THIS PROGRAM (I.E., GOP, PRIVATE INVESTMENT FINANCE COMPANIES, CHAMBERS OF COMMERCE, AND PRIVATE INVESTOR GROUPS). HOW DOES THE MISSION PLAN TO COORDINATE WITH ALL OF THEM?

2.C. TECHNICAL ASSISTANCE - EACH OF THE THREE LONG-TERM ADVISORS HAVE THEIR PRIMARY CONTACT IN THE PUBLIC SECTOR. HOW CAN THE TA TEAM ESTABLISH DIRECT RELATIONSHIPS WITH THE PRIVATE SECTOR (SUCH AS MAJOR BUSINESS ORGANIZATIONS OR CHAMBERS OF COMMERCE).

2.D. ENVIRONMENTAL CONCERNS - THE IEE FOR THE PROGRAM HAS BEEN REVISED BY THE BUREAU ENVIRONMENTAL COORDINATOR IN CONSULTATION WITH THE MISSION'S PRIVATE SECTOR

OFFICER. THE CHANGES RELATE TO ENVIRONMENTAL ACTIVITIES INCLUDING TA, TRAINING AND POLICY DEVELOPMENT. THESE CHANGES HAVE BEEN SENT TO THE MISSION. WORLD ENVIRONMENTAL CENTER STAFF WILL PLAN A VISIT TO PAKISTAN IN LATE MAY OR EARLY JUNE TO HELP MISSION STAFF PREPARE A DETAILED WORKPLAN IN CONSULTATION WITH THE CHAMBERS OF COMMERCE, INDUSTRIAL TRADE ASSOCIATIONS AND SPECIFIC TARGETED INDUSTRIES.

2.E. FINANCIAL SECTOR REFORM - THE MISSION HAS PREVIOUSLY TRIED AND FAILED TO ENCOURAGE FINANCIAL SECTOR REFORM. WHAT ARE THE CONSTRAINTS (E.G. LEGAL, INSTITUTIONAL, ETC.) TO SUCH REFORM? WHAT ARE OTHER DONORS DOING IN THIS AREA AND WHAT ROLE CAN A.I.D. PLAY?

2.F. EXPEDITING THE INVESTMENT APPROVAL PROCESS - HOW WILL COMPANIES/INVESTORS BE SELECTED FOR THE FAST TRACK ASSISTANCE OR FOR FINANCING OF FEASIBILITY STUDIES?

2.G. WOMEN'S AND SMALL ENTERPRISE ASSISTANCE - WHAT LOCAL ORGANIZATIONS ARE WORKING IN SMALL BUSINESS AND MICROENTERPRISE DEVELOPMENT? DO ANY FORMAL FINANCIAL INSTITUTIONS LEND TO SMALL BUSINESSES? DO WOMEN FACE GENDER-BASED CONSTRAINTS IN ENTERPRISE GROWTH? SINCE THE RELATED DESIGN RESOURCE PAPER IS NOT FINISHED, THE SITUATION IS NOT WELL KNOWN. IF THIS SECTOR REMAINS A PART OF THE PIE PROGRAM, THE MISSION IS ADVISED TO PROVIDE ITS PRELIMINARY POLICY DIALOGUE TARGETS (FOR THIS SECTOR) TO ANE/TR/HR AND PPC/WID DURING THE PAAD DEVELOPMENT. IF NECESSARY, MISSION CAN SEEK MATCHING FUNDS AND TA FROM PPC/WID GENESYS PROJECT IN THIS PROCESS.

2.H. TRAINING - MANAGEMENT OF TRAINING ACTIVITIES IS A MAJOR TASK FOR PROJECT IMPLEMENTATION. HOW WILL THE MISSION HANDLE THIS TASK: COORDINATED WITH DSTP OR AS A STAND ALONE EFFORT?

2.I. CONTRACTING PLANS - THE MISSION SHOULD PLAN FULL AND OPEN COMPETITION FOR THE MAJOR TA CONTRACT. RECENT BUREAU EXPERIENCES USING SHORT-CUT CONTRACTING METHODS FOR SERVICES FROM FIRMS HAVING TRADITIONAL AID TA EXPERIENCE HAVE BEEN DISAPPOINTING. MISSION SHOULD EXPLORE WAYS TO BRING FRESH IDEAS AND APPROACHES TO THIS PROGRAM. HOWEVER, THIS DOES NOT PRECLUDE INTERMITTENT USE OF OTHER PROCUREMENT APPROACHES (I.E. PSCS, PASA, IQCS, BUY-INS, ETC).

THE MISSION HAS INDICATED THE POSSIBILITY OF A CONTRACT OR AGREEMENT WITH INTERNATIONAL FINANCE CORPORATION. AS THE MISSION'S PLANS MATURE IN THIS REGARD, THE MISSION MAY WISH TO CONTACT EITHER GC/ANE AND MS/PPE WITH RESPECT TO ANY FURTHER OR MORE CURRENT PROBLEMS IN CONNECTION WITH TAKING THIS APPROACH.

3. REPORTING REQUIREMENTS

?ECIFIC REPORTS ARE REQUESTED, BOTH DURING FY90 PAAD
ESIGN AND PROGRAM IMPLEMENTATION.

.A. REPORTING CABLES DURING PAAD DESIGN ON:
1. THE SCOPE AND RESULTS OF RESOURCE STUDIES;
2. THE POLICY AGENDA CHANGES THAT ARE IDENTIFIED
JRING PAAD DESIGN;
3. MISSION STAFFING PLANS AND RELATED ANALYSIS
;EF PARA 1.E); AND
4. PLANS FOR WOMEN'S AND SMALL ENTERPRISE ASSISTANCE
:SPECIALLY IF NOT CONTAINED IN THE INITIAL PAAD).

.B. A POLICY AGENDA REPORT (WITH DETAILED BENCHMARKS)
; REQUIRED DURING THE FIRST YEAR OF IMPLEMENTATION AND
:IOR TO NEGOTIATIONS OF ANY PROGRAM SECTOR ASSISTANCE
REEMENT.

. THIS CONCLUDES ANPAC GUIDANCE. EAGLEBURGER

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Annex D

Certification for Compliance with Gray Amendment

I, James A. Norris, the principal officer of the Agency for International Development in the Islamic Republic of Pakistan, do hereby certify that the acquisition plan in the Private Investment Expansion Program Assistance Approval Document was developed with full consideration of maximally involving Minority- and Women-Owned Firms, or Gray Amendment Organizations, in the provision of required goods and services. To the extent possible at this stage, opportunities for such organizations to participate in the Program have been identified and are described in the acquisition plan. During the course of implementation, further opportunities for such organizations to participate will be fully considered.

James A. Norris
James A. Norris
Director
USAID/Pakistan

Sept. 19 1990
Date

ANNEX E: STATUTORY CHECKLIST

Attached is the latest statutory checklist for FY90 for non-project assistance. It consists of the Standard Item Checklist and the Non-Project Assistance Checklist. Please note that the first page only of this Annex E has been numbered as page 106. Page 107 is the beginning of Annex F.

5C(3) - STANDARD ITEM CHECKLIST

Listed below are the statutory items which normally will be covered routinely in those provisions of an assistance agreement dealing with its implementation, or covered in the agreement by imposing limits on certain uses of funds.

These items are arranged under the general headings of (A) Procurement, (B) Construction, and (C) Other Restrictions.

A. PROCUREMENT

1. FAA Sec. 602(a). Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed? — Yes.

2. FAA Sec. 604(a). Will all procurement be from the U.S. except as otherwise determined by the President or determined under delegation from him? — Yes.

3. FAA Sec. 604(d). If the cooperating country discriminates against marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company? — N.A. Cooperating country does not discriminate against U.S. marine insurance companies.

4. FAA Sec. 604(e). If non-U.S. procurement of agricultural commodity or product thereof is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.) — Yes

5. FAA Sec. 604(g). Will construction or engineering services be procured from firms of advanced developing countries which are otherwise eligible under Code 941 and which have attained a competitive capability in international markets in one of these areas? (Exception for those countries which receive direct economic assistance under the FAA and permit United States firms to compete for construction or engineering services financed from assistance programs of these countries.) — No.

6. FAA Sec. 603. Is the shipping excluded from compliance with the requirement in section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 percent of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on privately owned U.S. flag commercial vessels to the extent such vessels are available at fair and reasonable rates? — No

7. FAA Sec. 621(a). If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? Will the facilities and resources of other Federal agencies be utilized, when they are particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs? — Yes

8. International Air Transportation Fair Competitive Practices Act, 1974. If air transportation of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available? — Yes.

9. FY 1990 Appropriations Act Sec. 504. If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States? — Yes.

10. FY 1990 Appropriations Act Sec. 524. If assistance is for consulting service through procurement contract pursuant to 5 U.S.C. 3109, are contract expenditures a matter of public record and available for public inspection (unless otherwise provided by law or Executive order)?

Yes.

11. Trade Act Sec. 5164 (as interpreted by conference report), amending Metric Conversion Act of 1975 Sec. 2 (and as implemented through A.I.D. policy). Does the assistance program use the metric system of measurement in its procurements, grants, and other business-related activities, except to the extent that such use is impractical or is likely to cause significant inefficiencies or loss of markets to United States firms? Are bulk purchases usually to be made in metric, and are components, subassemblies, and semi-fabricated materials to be specified in metric units when economically available and technically adequate? Will A.I.D. specifications use metric units of measure from the earliest programmatic stages, and from the earliest documentation of the assistance processes (for example, project papers) involving quantifiable measurements (length, area, volume, capacity, mass and weight), through the implementation stage?

Yes.

12. FAA Secs. 612(b), 636(h); FY 1990 Appropriations Act Secs. 507, 509. Describe steps taken to assure that, to the maximum extent possible, foreign currencies owned by the U.S. are utilized in lieu of dollars to meet the cost of contractual and other services.

Yes, to the maximum extent possible, but Pakistan is no longer an excess currency country.

13. FAA Sec. 612(d). Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?

Pakistan was removed from the "Near-Excess Currency" list at the end of FY 1988.

14. FAA Sec. 601(e). Will the assistance utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?

Yes.

B. CONSTRUCTION

1. FAA Sec. 601(d). If capital (e.g., construction) project, will U.S. engineering and professional services be used? — N.A.

2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable? — N.A.

3. FAA Sec. 620(k). If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed $100 million (except for productive enterprises in Egypt that were described in the CP), or does assistance have the express approval of Congress? — N.A.

C. OTHER RESTRICTIONS

1. FAA Sec. 122(b). If development loan repayable in dollars, is interest rate at least 2 percent per annum during a grace period which is not to exceed ten years, and at least 3 percent per annum thereafter? — N.A.

2. FAA Sec. 301(d). If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights? — N.A.

3. FAA Sec. 620(h). Do arrangements exist to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of the Communist-bloc countries? — Yes.

4. Will arrangements preclude use of financing:

a. FAA Sec. 104(f); FY 1990 Appropriations Act under heading "Population, DA," and Secs. 525, 535. (1) To pay for performance of abortions as a method of family planning or to motivate or coerce persons to practice abortions; (2) to pay for performance of involuntary sterilization as method of family planning, or to coerce or provide financial incentive to any person to undergo sterilization; (3) to pay for any biomedical research which relates, in whole or part, to methods or the performance of abortions or involuntary sterilizations as a means of family planning; or (4) to lobby for abortion? — Yes (1) / Yes (2) / Yes (3) / Yes (4)

b. FAA Sec. 483. To make reimbursements, in the form of cash payments, to persons whose illicit drug crops are eradicated? — Yes

c. FAA Sec. 487. To or through individuals or entities which we know or have reason to believe have either: (1) been convicted of a violation of any law or regulation of the United States or a foreign country relating to narcotics (or other controlled substances); or (2) been an illicit trafficker in, or otherwise involved in the illicit trafficking of, any such controlled substance? (Section 487 requires the taking of "reasonable steps to ensure that assistance" (under the FAA and the Arms Export Control Act) is not provided in the foregoing cases.) — Yes

d. FAA Sec. 620(g). To compensate owners for expropriated or nationalized property, except to compensate foreign nationals in accordance with a land reform program certified by the President? — Yes

e. FAA Sec. 660. To provide training, advice, or any financial support for police, prisons, or other law enforcement forces, except for narcotics programs? — Yes

f. FAA Sec. 662. For CIA activities? Yes

g. FAA Sec. 636(i). For purchase, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained? Yes

h. FY 1990 Appropriations Act Sec. 503. To pay pensions, annuities, retirement pay, or adjusted service compensation for prior or current military personnel? Yes

i. FY 1990 Appropriations Act Sec. 505. To pay U.N. assessments, arrearages or dues? Yes

j. FY 1990 Appropriations Act Sec. 506. To carry out provisions of FAA section 209(d) (transfer of FAA funds to multilateral organizations for lending)? Yes

k. FY 1990 Appropriations Act Sec. 510. To finance the export of nuclear equipment, fuel, or technology? Yes

l. FY 1990 Appropriations Act Sec. 511. For the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights? Yes

m. FY 1990 Appropriations Act Sec. 516; State Authorization Sec. 109. To be used for publicity or propaganda purposes designed to support or defeat legislation pending before Congress, to influence in any way the outcome of a political election in the United States, or for any publicity or propaganda purposes not authorized by Congress? Yes

5. FY 1990 Appropriations Act Sec. 574. Will any A.I.D. contract and solicitation, and subcontract entered into under such contract, include a clause requiring that U.S. marine insurance companies have a fair opportunity to bid for marine insurance when such insurance is necessary or appropriate? Yes

6. <u>FY 1990 Appropriations Act Sec. 582.</u> Will any assistance be provided to any foreign government (including any instrumentality or agency thereof), foreign person, or United States person in exchange for that foreign government or person undertaking any action which is, if carried out by the United States Government, a United States official or employee, expressly prohibited by a provision of United States law?

3(A)2 - NONPROJECT ASSISTANCE CHECKLIST

The criteria listed in Part A are applicable generally to FAA funds, and should be used irrespective of the program's funding source. In Part B a distinction is made between the criteria applicable to Economic Support Fund assistance and the criteria applicable to Development Assistance. Selection of the criteria will depend on the funding source for the program.

CROSS REFERENCES: IS COUNTRY CHECKLIST UP TO DATE? HAS STANDARD ITEM CHECKLIST BEEN REVIEWED?

A. GENERAL CRITERIA FOR NONPROJECT ASSISTANCE

1. FY 1990 Appropriations Act Sec. 523; FAA Sec. 634A. Describe how authorization and appropriations committees of Senate and House have been or will be notified concerning the project.

   Through Congressional Presentation and through Congressional Notification.

2. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

   No legislative action necessary.

3. FAA Sec. 209. Is assistance more efficiently and effectively provided through regional or multilateral organizations? If so, why is assistance not so provided? Information and conclusions on whether assistance will encourage developing countries to cooperate in regional development programs.

   No. This Program is not designed to encourage regional development programs.

4. FAA Sec. 601(a). Information and conclusions on whether assistance will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.

   This Program is designed to directly encourage: (a), (b). and (d) and as a consequence of this, encourage indirectl (c) and (e).

5. FAA Sec. 601(b). Information and conclusions on how assistance will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

   This Program will promote increase in U.S. trade with this country as one of its outputs.

6. FAA Sec. 121(d). If assistance is being furnished under the Sahel Development Program, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of A.I.D. funds?

   N.A.

B. FUNDING CRITERIA FOR NONPROJECT ASSISTANCE

1. Nonproject Criteria for Economic Support Fund

   a. FAA Sec. 531(a). Will this assistance promote economic and political stability? To the maximum extent feasible, is this assistance consistent with the policy directions, purposes, and programs of Part I of the FAA?

   Yes

   Yes.

   b. FAA Sec. 531(e). Will assistance under this chapter be used for military or paramilitary activities?

   No.

c. FAA Sec. 531(d). Will ESF funds made available for commodity import programs or other program assistance be used to generate local currencies? If so, will at least 50 percent of such local currencies be available to support activities consistent with the objectives of FAA sections 103 through 106?

Yes.

d. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

No commodities are to be granted which will result in sale proceeds accruing to the recipient country.

e. FY 1990 Appropriations Act, Title II, under heading "Economic Support Fund," and Sec. 592. If assistance is in the form of a cash transfer: (a) Are all such cash payments to be maintained by the country in a separate account and not to be commingled with any other funds? (b) Will all local currencies that may be generated with funds provided as a cash transfer to such a country also be deposited in a special account, and has A.I.D. entered into an agreement with that government setting forth the amount of the local currencies to be generated, the terms and conditions under which they are to be used, and the responsibilities of A.I.D. and that government to monitor and account for deposits and disbursements? (c) Will all such local currencies also be used in accordance with FAA Section 609, which requires such local currencies to be made available to the U.S. government as the U.S. determines necessary for the requirements of the U.S. Government, and which requires the remainder to be used for programs agreed to by the U.S. Government to carry out the purposes for which new funds authorized by the FAA would themselves be available? (d) Has Congress received prior notification providing in detail how the funds will be used, including the U.S. interests that will be served by the assistance, and, as appropriate, the economic policy reforms that will be promoted by the cash transfer assistance?

Not a cash transfer.

2. Nonproject Criteria for Development Assistance

a. FAA Secs. 102(a), 111, 113, 281(a). Extent to which activity will: (1) effectively involve the poor in development, by expanding access to economy at local level, increasing labor-intensive production and the use of appropriate technology, spreading investment out from cities to small towns and rural areas, and insuring wide participation of the poor in the benefits of development on a sustained basis, using the appropriate U.S. institutions; (2) help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward better life, and otherwise encourage democratic private and local governmental institutions; (3) support the self-help efforts of developing countries; (4) promote the participation of women in the national economies of developing countries and the improvement of women's status; and (5) utilize and encourage regional cooperation by developing countries?

(1) By promoting the policy of privatization and special emphasis on small and women-owned businesses PIEP will expand poor's access to the economy.

(2) Not in particular.

(3) Yes.

(4) Yes, the main theme of PIEP includes helping promote women-owned businesses.

(5) N.A.

b. FAA Secs. 103, 103A, 104, 105, 106, 120-21. Is assistance being made available (include only applicable paragraph which corresponds to source of funds used; if more than one fund source is used for assistance, include relevant paragraph for each fund source):

(1) [103] for agriculture, rural development or nutrition; if so (a) extent to which activity is specifically designed to increase productivity and income of rural poor; [103A] if for agricultural research, account shall be taken of the needs of small farmers, and extensive use of field testing to adapt basic research to local conditions shall be made; (b) extent to which assistance is used in coordination with efforts carried out

N.A.

under Sec. 104 to help improve nutrition of the people of developing countries through encouragement of increased production of crops with greater nutritional value; improvement of planning, research, and education with respect to nutrition, particularly with reference to improvement and expanded use of indigenously produced foodstuffs; and the undertaking of pilot or demonstration programs explicitly addressing the problem of malnutrition of poor and vulnerable people; and (c) extent to which activity increases national food security by improving food policies and management and by strengthening national food reserves, with particular concern for the needs of the poor, through measures encouraging domestic production, building national food reserves, expanding available storage facilities, reducing post harvest food losses, and improving food distribution.

(2) [104] for population planning under Sec. 104(b) or health under Sec. 104(c); if so, extent to which activity emph[illegible]zes low-cost, integrated del[illegible] systems for health, nutrition [illegible]ly planning for the poorest [illegible], with particular attention to needs of mothers and young children, using paramedical and auxiliary medical personnel, clinics and health posts, commercial distribution systems, and other modes of community outreach. — N.A.

(3) [105] for education, public administration, or human resources development; if so, (a) extent to which activity strengthens nonformal education, makes formal education more relevant, especially for rural families and urban poor, and strengthens management capability of institutions enabling the poor to participate in development; and (b) extent to which assistance provides advanced education — N.A.

and training of people of developing countries in such disciplines as are required for planning and implementation of public and private development activities.

(4) [106] for energy, private voluntary organizations, and selected development problems; if so, extent activity is: N.A.

(i)(a) concerned with data collection and analysis, the training of skilled personnel, research on and development of suitable energy sources, and pilot projects to test new methods of energy production; and (b) facilitative of research on and development and use of small-scale, decentralized, renewable energy sources for rural areas, emphasizing development of energy resources which are environmentally acceptable and require minimum capital investment;

(ii) concerned with technical cooperation and development, especially with U.S. private and voluntary, or regional and international development, organizations;

(iii) research into, and evaluation of, economic development processes and techniques;

(iv) reconstruction after natural or manmade disaster and programs of disaster preparedness;

(v) for special development problems, and to enable proper utilization of infrastructure and related projects funded with earlier U.S. assistance;

(vi) for urban development, especially small, labor-intensive enterprises, marketing systems for small producers, and financial or other institutions to help urban poor participate in economic and social development.

(5) [120-21] for the Sahelian region; if so, (a) extent to which there is international coordination in planning and implementation; participation and support by African countries and organizations in determining development priorities; and a long-term, multidonor development plan which calls for equitable burden-sharing with other donors; (b) has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of projects funds (dollars or local currency generated therefrom)?

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IEE ADDENDUM FOR PIE PROGRAM

The Bureau Environmental Coordinator agrees that the program meets criteria for a Category Exclusion. However, programs aimed at industrial demonstrations and technical assistance on selecting industrial manufacturing processes and production equipment have the potential to cause negative environmental and human health impacts. Therefore, as a matter of policy, USAID/Islamabad should, wherever possible, design program activities to contribute to environmental soundness, comply with Pakistan's environmental regulations and build host country capability for industrial pollution assessment and control. Also, the program should, within the context of PIE components, address industrial pollution prevention, process modification and in-plant controls that often improve production efficiency and profitability while reducing industrial pollution.

Environmental activities that the PIE program plans to undertake include technical assistance, training and policy development. The technical specialists will provide short term assistance to private sector firms and the GOP Board of Investment, Chambers of Commerce and industrial trade associations on pollution prevention, clean industrial processes, and Best Management Practices. Potential investors will be informed about the availability of these services in informational/promotional materials, including notices on the CIP. Technical assistance to the Chambers of Commerce will include seminars, training, exchange tours with USA industry experts and follow-up TA. The PIE program dialogue with the GOP will pursue timely and appropriate environmental issues and concerns. Technical assistance on environmental policy should include analysis and dialogue with the GOP on appropriate industrial pollution regulations and program policys in concert with Chambers of Commerce and trade associations.

The PAAD will provide details of the environmental activities including technical assistance, training and policy development. ANE/PD/ENV is prepared to provide assistance on the industrial pollution assessment and control component of the program.

Signature R H Gol
Date 4/20/90

Dick Goldman, Chief
Private Enterprise Office
USAID/Islamabad

Signature M. Kux
Date 4-20-90

Molly Kux, ANE/PD/ENV
Bureau Env Coor

Annex G

Buy-America Provisions and Local Cost Financing Waivers

The Private Investment Expansion Program has been designed to optimize the provisions of AID's new Buy-America "policy" and to thereby minimize procurement in third countries. The program is being authorized for Geographic Code 000 only and includes substantial planned funding for commodity imports from the United States and sector grants which will probably be used for US debt servicing. Seventy-six percent of the initial $35 million authorization is for foreign exchange expenditures for procurement of goods and services whose source-origin or nationality is from the United States (Geographic Code 000). This percentage will increase to about 85 percent in later years as funding is added for commodity imports and sector grants. Despite efforts to utilize Geographic Code 000 source-origin and nationality, project designers found that 100 percent Code 000 procurement was not possible. In order for the program to be well designed, some local currency and in-country "off-the-shelf" procurement is critical to the success of the Program. Criticality is one of the justifications for waiver authority. In addition, the recent cable traffic on Buy-America (STATE 265071 and STATE 276461) admonished Mission Directors to use common sense in their application of the Buy-America procurement emphasis.

Accordingly, with specific regard to each of the transactional categories set forth below, USAID has determined for the reasons set forth that services and commodities of Pakistan source/origin and nationalities are critical to the success of the Program objectives in keeping with the criterion of AID HB 1B, Ch 5, B 4.

The PIE Program invokes the Mission Director's Delegation of Authority No. 652 to waive procurement from Geographic Code 000 in amounts up to $5 million per waiver category. The PIE authorization will waive $8.280 million worth of local cost procurement from Host Country and the free world (Geographic Code 941). These procurements are in five categories, with each falling under the waiver authority of $5 million per category.

Category 1: Technical Assistance, local cost financing $2.550 million. The execution of a technical assistance contract requires incidental services procured in the Host Country and a local sub-contract for logistic support. In all but the very poorest of the developing countries, technical assistance requires a team of expatriate Americans and local professionals and support personnel for cost-effective and technically effective implementation. USAID has therefore agreed with the Government of Pakistan to perform certain functions such as local public relations through sub-contracts to local consultants. In addition, it is anticipated that approximately $1.0 million of the $3.0 million Special Projects funds will be awarded to local consultants who are best suited to study the local context of some private sector initiatives. The remaining $2.0 million Special Projects funding will be

Annex G

Buy-America Provisions
and Local Cost Financing Waivers
(Continued)

reserved for U.S. consultancies. Therefore, out of the $15.9 million budget for technical assistance and special projects, $2.550 million is set aside for local cost financing.

Category 2: Training: Some training is best accomplished in-country, and as such it requires private sector collaborators and institutions as the focus of our program is on non-governmental entities. $1.8 million out of a $5 million training budget is set aside for local cost training procurement.

Category 3: Institutional Grants: The PIE Program places much emphasis on institutional grants as a means of accomplishing project goals and purpose with the least administrative burden on USAID, the greatest private sector collaboration and a minimum of public sector support. The Institutional Grants component is designed to further Agency and ANE Bureau goals of fostering democratic pluralism and enhancing local private sector voice. These activities, by definition, are often best done with and by local organizations. Based on estimated needs for local PVO participation, including the American Business Council, $3.5 million out of the $10 million institutional grants component is reserved for local cost financing.

Category 4: Commodities: Only $1 million in commodity procurement is envisioned for the $35 million Special Project Technical Cooperation, and Training component. Only incidental procurement will take place within the Host Country or from free world sources. Therefore, $250,000 is reserved for local costs. The majority of this procurement falls under the headings of shelf-item like procurement as defined in Handboook 1-B, Chapter 5, B-2, which defines eligible procurement of commodities whose individual or unit value is under $5,000.

Category 5: Evaluation and Audit: $180,000 out of $400,000 in this category is reserved for local cost financing. Evaluations and audits take place within the Host Country and in this case will require local logistic support and local professionals. Two progress evaluations are scheduled and a final evaluation is planned at the end of the project.

In summary the facesheet authorization for the Special Projects, Technical Cooperation, and Training component of the Private Investment Expansion Program will approve local cost financing of up to $8.28 million.

ACTION AID INFO AMB DCM/3

VZCZCILC770 13-SEP-90 TOR: 02:43
CO RUEHIL CN: 39265
DE RUEHC #9267 2550242 CHRG: AID
ZNR UUUUU ZZH DIST: AIDA
C 130239Z SEP 90 ADD:
FM SECSTATE WASHDC
TO RUEHIL/AMEMBASSY ISLAMABAD IMMEDIATE 5061
INFO RUEHNE/AMEMBASSY NEW DELHI IMMEDIATE 7424
BT
UNCLAS STATE 309267

AIDAC

E.O. 12356: N/A
TAGS:
SUBJECT: BUY AMERICA POLICY

REFS: (A) ISLAMABAD 17436
(B) STATE 276461
(C) STATE 265071

OFFICE	ACTION	INFO
LT		✓
OD		✓
PRJ		✓
PIO		✓
RLA	✓	
CC/CMO		✓
POM		✓
ENR		
ENG		✓
HPN		✓
HRD		
ARD		✓
FM		✓
EXO		✓
GSO		
PER/TRV		
PROC		
EMS		
ADP		
C/RP		✓
AID/REP		

1. GENERAL PROGRAMMATIC AND IMPLEMENTATION ISSUES RAISED REF (A) WILL BE ADDRESSED, ALONG WITH ISSUES RAISED BY OTHER MISSIONS, IN FURTHER WORLDWIDE GUIDANCE CABLE.

2. SPECIFIC ISSUES RAISED PARAS 7 AND 9 REF (A) CAN BE RESOLVED UNDER PRESENT GUIDANCE REF (B) WHICH PERMITS BROAD CATEGORICAL AUTHORIZATIONS OR WAIVERS FOR LOCAL COST FINANCING PROVIDED THEY CAN BE DESCRIBED WITH SOME SPECIFICITY AND THEY MEET WAIVER CRITERIA. FROM PARA 7(A) IT APPEARS THAT MISSION COULD STATE ESTIMATED AMOUNTS AND TYPES OF ANTICIPATED LOCAL PROCUREMENT IN THE AUTHORIZATION DOCUMENT FOR THE PIE PROJECT. PROBLEM RAISED IN PARA 9 REGARDING THE TADP PROJECT COULD BE HANDLED SIMILARLY.

RECEIVED
SEP 13 1990

3. RE PARA 8 REF (A) QUESTION CONCERNING SMALL VALUE IMPORTS NOTE THAT HB 1B CH. 5B4C(2) (PG. 5-11) EXEMPTS TRANSACTIONS UNDER DOLLARS 5000 FROM INDIVIDUAL WAIVER REQUIREMENT. MISSION REPORTING SHOULD NONETHELESS COVER THESE TRANSACTIONS. AID/W REVIEWING HB 1B, CH. 18, IN LIGHT OF MISSION COMMENTS.

4. DELEGATIONS OF AUTHORITY WILL BE REVIEWED TO BE SURE THAT MISSIONS HAVE AUTHORITY TO EXERCISE RESPONSIBILITIES UNDER NEW BA INITIATIVE. EAGLEBURGER
BT
#9267

NNNN

بسم اللہ الرحمٰن الرحیم

Annex H

No 1(3)US-I/90
Government of Pakistan
MINISTRY OF FINANCE AND
ECONOMIC AFFAIRS
(ECONOMIC AFFAIRS DIVISION)

Islamabad, the 11th June, 1990.

Telegram ECONOMIC
Telex ECDIV No 05 611

ACTION
Due Date 4/25
Action Taken
Date
Initial

FROM: JOINT SECRETARY,
TELE: 821682.

Dear Mr. Norris,

REG H 2298

As part of the economic assistance program between our two Governments, the Government of Pakistan formally requests United States assistance in the amount of one hundred eighty million dollars($ 180,000,000) grant, subject to the availability of funds, to finance the Private Investment Expansion Program.

Following submission of the policy paper relating to Private Investment Expansion Program to the Government of Pakistan through its letter dated April 11, 1990 addressed to the Deputy Chairman, Planning Commission, and inclusion of this activity in the joint US-Pakistan Economic Subcommission communique, the Government of Pakistan endorses implementation of a bilateral private investment support program covering sector grant assistance, foreign exchange for commodity imports(CIP), special projects, technical assistance, and training. The $ 180 million program proposed would meet current and future needs of these activities.

It is requested that funding for this program may be processed on priority basis.

RECEIVED
JUN 14 1990

With kind regards,

Yours sincerely,

(Saad Ashraf)

Mr. James A. Norris,
Director,
USAID Mission in Pakistan,
Islamabad.

Reserved for PAAD Amendment

Reserved for PAAD Amendment

Reserved for PAAD Amendment

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

The contract "Team" shall be comprised of seven long-term advisors for a period of five years (35 person years) plus short-term advisors to be provided at the discretion of the Team COP and USAID for up to 120 person-months. In addition, up to three person-years of long-term assistance in privatization may be added as an option. An additional option is for a possible three year extension of the Team comprised of 21 person-years of long-term assistance and 30 person-months of short-term assistance. Both options will be exercisable at USAID's option.

The long-term Team shall be comprised of a Chief of Party (US), a Financial Economist (US), a Commercial Bank Specialist (US), a Capital Markets Specialist (FSN), two Investment Specialists (one US, one FSN), and one Administrative Officer (FSN). The general scope of work for the team is to develop, manage, and monitor all aspects of a broad policy agenda to promote private investment under the direct guidance of the Chief, PEO, USAID; to independently manage a large, multi-faceted investment promotion and packaging program, including substantial financial incentive packages from PIE Program finances, focussed primarily on US and domestic investments in Pakistan; and to help develop key public and private institutions in Pakistan which can help expand private investment, including but not limited to the MOF Policy Group, the stock exchange, IFBs, local Chambers and business groups, and the Investment Promotion Board and Bureau.

The Team is expected to broadly share all responsibilities. However, specific responsibilities should be assigned to individuals. Below are Scopes of Work for the long-term positions.

CHIEF OF PARTY

A. Qualifications

The COP will have a graduate degree with emphasis on macroeconomics and will have at least 15 years experience in trade and investment policies and in development of investment and industrial programs, particularly in developing countries.

B. Statement of Work

1. Objective

The COP will perform advisory functions for developing and implementing policy reforms for private investment promotion in Pakistan.

2. Major Responsibilities

The COP will be responsible primarily for the following functions:

CHIEF OF PARTY (Continued)

a. Advise the GOP on reform of monetary, fiscal, trade, and règulatory parameters affecting increased private participation in the economy;

b. Provide analytical support to USAID/Pakistan in maintaining policy dialogue with the GOP on major issues of financial sector/capital market and regulatory policies;

c. Assist USAID/Pakistan in formulating the policy agenda for the Program;

d. Assess the need, in conjunction with PEO, for short-term technical assistance for policy studies in support of the policy agenda and design the terms of reference;

e. Coordinate the work of the long-term and short-term advisory team members in order to ensure that it supports the policy agenda and is consistent with the direction of the Program;

f. Serve as a special advisor to the Ministry of Industry, especially assisting in the design and implementation of small business development programs and analytical studies relating to industrial policy.

g. Monitor privatization progress and recommend to USAID/Pakistan the appropriate time for arrival of the long-term Privatization Specialist, whose work is expected to commence sometime in the first two years of the Program;

h. Undertake assessment of short-term technical assistance and training needs, plan and implement technical assistance, and arrange management and implementation of local training;

i. Maintain liaison with other donors (particularly the IMF, World Bank Group, and the ADB) for supporting policy reform in the area of financial sector/capital market;

j. Supervise and manage administration of the Program, including the timely preparation and submission of reports to the GOP and USAID/Pakistan.

C. Local Counterparts

The local counterpart agency for the COP will be the Secretary in the Ministry of Industries in Islamabad. The COP, however, will maintain close working relationships with other GOP entities such as the Board of Investment, Ministry of Commerce, Ministry of Finance, State Bank of Pakistan, and the Central Board of Revenue. The COP will also maintain contacts with other donors, particularly the IMF, the World Bank and the ADB.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

FINANCIAL ECONOMIST

A. Qualifications

The Financial Economist will have a graduate degree with emphasis on financial economics and will have at least ten years experience in the financial sector and capital markets area, i.e., experience in the merchant banking (investment banking) division of a money center bank or in an investment and discount brokerage firm, or in a supervisory and regulatory agency with jurisdiction over the securities market. The Financial Economist should be familiar with the institutions, mechanisms and instruments of money and capital markets, as well as with the legal and regulatory aspects of financial sector and capital market operations. Some experience in less developed money and capital markets is desirable.

B. Statement of Work

1. Objectives

The Financial Economist, located in Islamabad at the Ministry of Finance, will serve as a senior advisor to the GOP for developing and analyzing the regulatory framework needed to encourage the development of the capital markets, and to help the Ministry of Industries develop policy analysis and implementation capabilities.

2. Major Responsibilities

Major responsibilities will include but not be limited to the following:

a. Analyze the implementation of ongoing Financial Sector Reform Programs (FSRP), particularly those having a direct or indirect bearing on capital formation and investment activity in the private sector, in order to suggest appropriate mid-course corrections and policy adjustments;

b. Evaluate the impact of recent changes in regulatory policies (particularly since 1987) on capital formation and the functioning of capital markets;

c. Examine existing financial sector and regulatory policies with a view to identifying constraints on expansion of private medium- and long-term investment and highlight the costs of these constraints in terms of commercial and industrial growth;

d. Advise the MOF Deputy Secretary of Policy on how to develop staff resources; actively involve his staff in analytical projects and studies; help strengthen this institution and recommend appropriate training of this staff for Program funding.

FINANCIAL ECONOMIST (Continued)

e. Propose, on the basis of the above analysis, other financial sector reforms and changes in regulatory framework, in order to stimulate capital market development;

f. Collect and analyze data, undertake policy analysis, prepare studies, and recommend and help to coordinate seminars and workshops to be conducted by contracted training teams;

g. Work in collaboration with the Commercial Banking and Capital Markets Specialists, based in Karachi to ensure that the proposed policy and regulatory reforms are feasible and practical;

h. Maintain close interaction with counterparts in the Ministry of Finance (External Finance, Internal Finance, Investment, Policy Coordination, Privatization Wings/Cells, CLA, CCI) and in the Board of Investments;

i. Assess the technical assistance and training needs of CLA/CCI for regulatory reform and effective implementation and enforcement;

j. Assess the technical assistance and training needs of capital market institutions (selected DFIs, leasing companies, modaraba companies, IFCs) for learning innovative and sophisticated capital market techniques and instruments.

C. Local Counterparts

The primary counterpart entity for the Financial Economist will be the Ministry of Finance. However, the incumbent will interact closely with the CLA, CCI, the State Bank of Pakistan, and the banking and finance community at large.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

PROMOTION SPECIALISTS

A. Qualifications

Two promotion specialists, one US and one Pakistani, will work together on all investment promotion programs. Each Promotion Specialist will have a advanced degrees in business administration with at least 10 years experience in finance or marketing in the private sector. Experience in promotion of joint ventures between private sectors in the US and developing countries is desirable.

B. Statement of Work

1. Objective

The Promotion Specialists will be responsible for promoting direct foreign private investment, particularly US, in Pakistan.

2. Major Responsibilities

The Promotion Specialists will be responsible primarily for the following:

a. Identify potential sectors for foreign investment, plan and manage short-term studies to refine an information base, and develop sector-specific promotion literature;

b. Develop a detailed promotion campaign for sectors potentially attractive to foreign private investment, and implement the plan in the US, Pakistan and possibly Europe and the Far East; manage the US subcontractor responsible for US investment research and follow-up.

c. Advise USAID on the design and implementation of all investment promotion financing and packages. Liaise with all IFIs selected to implement investment promotion components of the PIE Program, such as PSCIP banks, to both promote and coordinate the overall program of investment promotion.

d. Guide and assist overseas and local companies in joint venture opportunities;

e. Undertake enterprise specific deal-making between US and local investors;

f. Promote the Trade and Development Program of the PIE Program and the Export/Import Bank program;

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

PROMOTION SPECIALISTS (Continued)

g. Monitor the GOP's promotion activities, especially through the Investment Promotion Bureau, advise the Mission on possible interventions and undertake specific activities to enhance institutional performances as may be agreed on by USAID.

h. Actively encourage private business groups operating in Pakistan and the US to play an expanded role in trade and investment development. Advise USAID on how the PIE Program could foster increased private sector involvement. Identify and manage promotion-related overseas and local training.

C. Local Counterparts

The Promotion Specialists, located at the American Business Council in Karachi, will coordinate all activities with the US Commercial Attache. The incumbents will work closely with the Federation of Pakistan Chambers of Commerce and Industry, Overseas Investors Chambers of Commerce and Industry, and IESC and maintain effective liaison with public sector organizations such as the Export Promotion Bureau and the Investment Promotion Bureau.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

CAPITAL MARKETS SPECIALIST

A. Qualifications

The Capital Markets Specialist (CMS) will have an MBA with emphasis on finance and capital markets and will have at least ten years experience in merchant banking (investment banking securities trading, including first-hand, on-line experience with the mechanisms and instruments of money and capital markets.

B. Statement of Work

1. Objectives

The CMS, located in the Corporate Law Authority in Karachi will assist the CLA and other banking and financial institutions to design and implement reforms that will encourage the use of capital markets.

2. Major Responsibilities

Major responsibilities will include but not be limited to the following:

a. Assess the impact of ongoing financial sector and regulatory reforms on the functioning of money and capital market institutions in Karachi, identifying problems of implementation and proposing solutions;

b. Assess, in collaboration with the Financial Economist based in Islamabad, the realism and feasibility of proposed financial sector and regulatory reforms, taking into account the reactions of the financial community in Karachi;

c. Provide technical assistance (and/or design terms of reference for short-term technical assistance, where appropriate) to CLA for implementation of the recommendation of the long-term IMF Advisor to MOF for the issue of marketable T/bills and other government securities, and for the development of primary and secondary markets for government securities, for example;

Establish a debt management organization in the State Bank (if technical assistance is not already being provided by the IMF);

Develop a primary dealer group, including NCBs, DFIs (particularly NDFC) and SLIC, dealing directly or through designated brokers in Karachi;

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

CAPITAL MARKETS SPECIALIST (Continued)

Develop a secondary market, including the aforementioned agents as secondary dealers (particularly NCBs, with large numbers of outlets and more brokers in Karachi and outside) and establish an Inter-dealer Broker System;

d. Actively assist the CLA, CCI, the KSE and independent brokers to develop a properly regulated, expanding stock exchange in Karachi and secondary cities;

e. Maintain liaison with the Karachi financial community, including PBC, NCBs, foreign banks, DFIs, and other NBFIs (such as NDLC, modaraba companies), SLIC, Karachi Stock Exchange, etc;

f. Assess the need of NCBs/DFIs, stock exchanges, and brokerage houses for technical assistance and training to achieve regulatory and operational reforms;

g. Collaborate with CLA/CCI and private companies in facilitating the issue of private equity fixed income securities, especially as may relate to potential privatizations of State-owned enterprises;

h. Assess the technical assistance and training needs of State Bank of Pakistan, NCBs, DFIs and other interested institutions for establishment of securities departments, training of securities lawyers, and making concerned staff familiar with financial instruments and with the use of modern money and capital markets;

i. Design terms of reference for short-term technical assistance and related training to assist State Bank in establishing a new department/subsidiary for supervision and regulation of NBFIs, starting first with leasing companies and PIFCs (if technical assistance not already provided by another development agency);

j. Assess needs of KSE for technical assistance, training and equipment for modernization of its operations, and for new building with auditorium, research center, and library.

C. Local Counterparts

The primary counterpart entity for the Capital Markets Specialist will be the Corporate Law Authority. He/she will also work with the private broker community, State Bank of Pakistan, CCI, institutional investors, MOF and potential privatization candidate firms.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

PRIVATIZATION SPECIALIST

A. Qualifications

The Privatization Specialist will have an advanced degree in economics, business management, or accounting with at least 10 years experience in banking, finance or industrial management in the private sector, five years of which should be related specifically to privatization activities. Candidates with joint business management and law degrees will be given preference.

B. Statement of Work

1. Objectives

The Privatization Specialist, located in Islamabad, will serve as a senior advisor to the GOP for developing and implementing a long-term privatization program.

2. Major Responsibilities

Major responsibilities will include but not be limited to the following:

a. Assist the GOP in (a) developing a comprehensive privatization policy defining privatization goals, strategies and schedules; (b) undertaking management and financial restructuring of loss-making enterprises; (c) developing technical analyses on partial privatization candidates; and (d) expediting implementation actions for privatization;

b. Identify, plan and manage studies in such illustrative areas as legal constraints to privatization, auctioning of loss-making enterprises, and privatization of management through leasing;

c. Advise the Mission on potential opportunities for utilizing a Privatization Fund established for partially financing GOP's privatization costs;

d. Monitor the progress of privatized enterprises, and advise the GOP on regulatory constraints which may impede performance;

e. Actively participate as a consultant on specific privatization actions, and recruit PIE Program resources as may be appropriate to assist in such privatizations;

f. Assist the Mission in the development of annual privatization related benchmarks for negotiation with the GOP under the Sector Grant Component of the Program;

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

PRIVATIZATION SPECIALIST (Continued)

g. Identify short-term technical assistance and training needs.

C. Local Counterparts

The primary counterpart entity for the Privatization Specialist will be the Privatization Wing in the Ministry of Finance. The incumbent, however, will maintain close working relations with other public and private organizations such as the Corporate Law Authority, the Expert Advisory Cell and the Karachi Stock Exchange.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

Commercial Banking Specialist

A. Qualifications: The Commercial Banking Specialist will have a Masters Degree in Business Management, Economics, or related field and at least ten years' experience in commercial banking in the private sector. The candidate should have a minimum of five years' experience in a senior management position or consultancy in financial management.

B. Statement of Work:

1. Objective. The Commercial Banking Specialist located in Karachi will work broadly with the whole commercial and investment banking sectors to both promote increased competition within public banks and among private and public banks, to help rationalize the commercial banking interest rate structures, to help improve the regulatory environment between the government, particularly the State Bank of Pakistan, and the commercial banking sector, and to help promote private investment through commercial banking in Pakistan.

2. Major Responsibilities. Major responsibility will include but not be limited to the following:

(a) Work with the Financial Economist in Islamabad to identify the key constraints to increasing competition in and market forces in both the public and private banking sectors.

(b) Analyze the GOP and other donor community action plan for deregulation of the financial sector and select targets of opportunity to help increase competition among state-owned banks from the private banking sector.

(c) Advise the GOP and banking sector in ways to integrate the various financial markets in ways that will rationalize the overall interest rate structure in Pakistan consistent with Islamic banking principles.

(d) Assist specific public banks in restructuring their personnel and operational systems to increase competitive forces among State Banks.

(e) If and when specific state banks are nominated as privatization candidates, work with those specific NCBs to prepare and implement privatization plans.

(f) Advise the IFBs in means to increase market share and better promote their investment banking objectives.

Scopes of Work- Long-Term Technical Cooperation Team

Commercial Banking Specialist (Continued)

(g) Advise the State Bank of Pakistan on means to revise regulatory and supervisory frameworks in monetary policies which will promote private investment in commercial banking.

(h) Advise the Pakistan Banking Council on how to better promote a private sector oriented banking agenda to the government and general public in Pakistan.

(i) Recommend to the GOP, Banking Council and the private and public banking communities, means to better utilize the present banking tribunal system to resolve legal issues in the banking community.

(j) Identify short term technical assistance and training needs which broadly help promote all of the objectives above and also help with specific development requirement of the State Bank of Pakistan.

C. Local Counterparts: The primary counterparts for the Commercial Banking Specialist will be the State Bank of Pakistan, the Pakistan Banking Council, and the commercial banking community.

Annex L

Scopes of Work- Long-Term Technical Cooperation Team

Administrative Officer

A. Qualifications: The Administrative Officer will have a University degree and will have a minimum of ten years' experience in operationally managing a large corporation or office. Such experience will specifically include logistic and personnel support experience.

B. Statement of Work:

1. Objectives: The Administrative Officer, located in Islamabad, will directly assist the Chief of Party in managing all aspects of team personnel, financial and logistics support.

2. Major Responsibilities: Major responsibilities, will include, but not be limited to the following:

(a) Establish a personnel system consistent with AID regulations, for the recruitment assignment, orientation and well-being of both long and short-term advisors under the contract team.

(b) Liaise with the USAID EXO office on all aspects of logistics support for the entire team. Assume full responsibility for the management all logistic support.

(c) Establish a financial management procedure to assure accountability of all funding under the contract. Prepare all necessary reports for both team corporate reporting and for reporting to USAID for financial management.

(d) Liaise with the Government of Pakistan concerning provision of all office space and support as may be required from the Government of Pakistan.

(e) Arrange for all necessary commodity procurements including customs import and shipping arrangements, as may be necessary to support the team under this contract.

(f) Act as timekeeper for all corporate activities and ensure that personnel policies including leave, as required under AID regulations for direct contracts, be properly followed.

(g) At the end of the contract, arrange for the orderly close out and transfer of all properties, personnel, and procedures.

(h) Ensure that all required reports for both the government and AID are prepared in a timely manner and published up to professional standards.

C. Local Counterparts: The primary counterparts for the Administrative Officer will be the Chief, PEO, USAID and the Chief, EXO, USAID, as well as the various Ministry and private sector offices where the team members will be sitting.

Annex L

PIE Fund Manager (PSC)
(Not part of TA Team)

A. Qualifications

The PIE Fund Manager will have an advanced degree (Master's Degree or higher) in business administration, economics, or industrial organization with at least 10 years of experience in investment banking or similar project investment work. At least two years of experience working in a developing country is highly desirable.

B. Statement of Work

1. Objectives

The PIE Fund Manager's major goal is to make the PIE Fund a profitable and self-sustaining organization that supports the banking activities of the Investment Finance Banks. The Manager will be responsible to USAID in assuring that the PIE Fund meets the requirements set forth by USAID for the Fund's operation.

2. Major Responsibilities

Major responsibilities will include but not be limited to the following:

a. Assist the USAID's PEO in the specific design and specification of the legal form of the corporate entity established by USAID to become the PIE Fund;

b. Submit monthly activity reports and quarterly performance statements on the performance and activities of the PIE Fund;

c. Establish guidelines for assessing and lending to projects brought to the PIE Fund by Investment Finance Banks;

d. Encourage, where feasible, new project activities that would be attractive to the IFBs;

e. Become acquainted with a broad cross-section of Pakistani business people with the goal of developing projects in a wide range of sectors;

f. Develop other fee-generating activities of the PIE Fund such as guarantees, underwriting new share issues on the Stock Exchanges, and endorsement or issuance of other money market instruments;

g. Assure that the activities of the PIE Fund are in agreement with the guidelines set up by USAID for the Fund;

PIE Fund Manager (PSC) (Continued)
(Not part of TA Team)

C. Local Counterparts

At the beginning of the project, there will be a need for assistance from the Ministry of Finance and the State Bank of Pakistan. Once the PIE Fund has been established, it will be a private organization without formal need of a counterpart. One goal of the Fund is that it become self-sustaining and turned over to Pakistani management after the first five years of the project.

Annex M

SUMMARY PROGRAM TECHNICAL ANALYSES

A. Background

The technical soundness of PIE activities is founded on the results of several analytical studies undertaken by the private sector, international donor community, and the GOP. During the PIE design process, the USAID commissioned, through local private contractors, six short term studies related to investment approval, investment promotion, privatization, informal sector, small business, and the financial sector. Additionally, a team from Price Waterhouse intensively examined Pakistan's financial sector with particular attention to capital markets. This Annex summarizes the findings of these studies.

B. Findings of Selected Studies

1. Small Scale Industry in Pakistan with Special Reference to their Regulatory Framework, (Economic Policy Research Unit, Lahore)

a. Scope of Work

This study analyses the impact of regulatory framework on small scale industry (SSI) in Pakistan. The assessment is based on a survey of 18 manufacturing units in five industries (surgical instruments, hand-knotted carpets, electric fans, furniture and packaging), interviews with public sector officials and private sector representatives.

b. Principal Findings

The small scale industries contributes about 5 percent to GDP, employs about 2 million workers in over 100,000 establishments, and has a share of about 30 percent of manufactured exports. The average investment cost per worker in SSI is estimated at around $1,800 whereas the average capital output ratio is about 0.8. The GOP's industrial policy has traditionally been biased towards large scale manufacturing. However, a number of developments such as accelerating population growth, nationalization of large scale manufacturing and workers migration to the Middle East have contributed to a dynamic growth of SSI in recent years.

The study analyses the impact of regulatory framework (principally taxation, labor, and credit regulations) and concludes the following:

i. Regulatory Framework Causes Limited Distortions at the Tails of the Size Distribution: The regulatory framework causes little distortions to the functioning of enterprises at the extreme ends of the size distribution. Enterprises employing less than 10 workers are exempt from a wide variety of legislative measures. At the other end of of the size spectrum, very large enterprises are well placed to absorb the provisions emanating from the regulatory framework.

ii. Regulatory Framework Prohibits the Development of Efficient Economic Units: Potential economies of scale are being distorted through regulations which prevent firms from developing in desired directions. First, labor legislation favoring very small enterprises has led to a horizontal sub-division of enterprises. Second, tax reliefs on particular production sub-processes (for example in the packaging industry) has resulted in sub-division of the enterprises in artificial boundaries.

iii. Regulatory Framework has not Realized the GOP Stated Objectives: Regulations, particularly concerning labor welfare, have often not been successful in meeting their stated objectives. Indeed, the net effect of some of the labor legislation may have been to increase insecurity of labor since owners are willing to go to substantial lengths to avoid giving permanent employment. The regulatory framework tends to reward those small enterprises who can successfully manipulate the system and handle officials from the regulatory bodies. Thus an important component of the success for some SSI is not related to efficiency or market responsiveness. A substantial part of the entrepreneur's time is spent in achieving successful manipulation rather than in concentrating on efficient business development.

c. Principal Recommendations

i. Increase the Threshold of Application of the Labor Laws and the Factories Act, 1934 from 10 to 50 Workers: This would release a substantial section of SSI from a maze of current regulations which are not enforced but provide avenues for corruption and is also unlikely to affect adversely tax collection or labor conditions.

ii. Regulate Enterprises through "One Window": All regulatory measures should be dealt with by a single public agency. This should make the system more efficient and more manageable.

iii. Establish Law Advisory Centers: Collective legal bodies should be established to strengthen the capacity of the small entrepreneurs to deal with the regulatory framework.

iv. Minimize Discretionary Powers of the Public Sector Functionaries: Discretionary powers cultivate an ethos of arbitrary authority which imposes a degree of fear among small entrepreneurs. It is vital to minimize discretionary powers of the public sector functionaries, especially in the taxation department.

v. Develop a List of SSI Sectors that do not Require No Object Certificate (NOC) from the Municipal Authorities: The current procedure for obtaining NOC from the municipal authorities is cumbersome with the result that a number of units do not get themselves registered and operate in a clandestine manner.

vi. Consistent Definition of SSI: Financial institutions, small industries corporations and other public sector agencies need to establish a consistent definition of SSI.

vii. Limit Sub-contracting to a Proportion of Work Force: A regulation which limits the scale of sub-contracting could contribute to better labor-management relations.

In summary, the regulatory framework needs major reforms. It must, however, be emphasized that reforms of the regulatory framework ought to focus more on the institutional mechanism for implementation rather than regulations *per se*.

2. The Financial Sector in Pakistan with Particular Reference to Investment Finance Banks and Development Finance Institutions (Economic Policy Research Unit, Lahore)

a. Scope of Work

This study is devoted to a review of the Development Financial Institutions (DFIs) and an assessment of the prospects of emerging private Investment Finance Banks (IFBs).

b. Principal Findings

Pakistan's financial sector is comprised of 5 nationalized commercial banks, 19 foreign private commercial banks, 14 DFIs, 7 leasing and modaraba companies, 2 stock exchanges and at least 2 (emerging) IFBs. The DFIs came into being largely in the 1960s to support GOP's sectoral, regional and large-scale import substitution development objectives. The DFIs are dependent on subsidized credit facilities, are management heavy at the top, have loan approval procedures which are not always governed by sound commercial principles, and, despite similar functions have hardly any competition among themselves. The upcoming private IFBs are a manifestation of the recent GOP policy of financial liberalization and are expected to undertake a variety of money market, project financing and corporate financing activities. The precise role and functions of these forthcoming IFBs are uncertain at the present but should get clarified as IFBs undergo an extended period of operation.

c. Principal Recommendations

Development Finance Institutions

i. Undertake Resource Mobilization: DFIs should be encouraged to undertake resource mobilization and, if needed, their charter should be amended accordingly.

ii. Assure Regional Dispersion: Concentration of DFI headquarters in Karachi has led to unequal distribution of services across regions. To assure equitable distribution of funds DFI headquarters must be dispersed at important regional centers across the country.

iii. Establish Technical Intelligence Units: DFIs should create Technical Intelligence Units and hire in-house technical consultants.

iv. Coordinate Loaning Activities with NCBs: DFIs must have on-line access to the credit information network of NCBs.

v. Employ Sound Loan Approval Criteria: Loan approval should be founded on sound commercial principles. The importance of post-disbursal evaluation and project monitoring must also be recognized.

vi. Discourage Trade of Sanctions: DFIs should assure that sanctions are not sold by the original sponsors to non deserving parties.

vii. Obtain Timely Financial Information from Borrowers: Certain preconditions must be imposed on borrowers such as the provision of audited financial statements in a timely fashion.

viii. Mandate Public Offerings: In order to play their due role in capital market development in Pakistan, DFIs should make it a precondition for borrowers to have a public offering.

ix. Revise Remunerations and Upgrade Staff Capabilities: Terms of conditions of the staff of DFIs should be revised and, ideally, brought in line with the practice prevailing in the private sector. Staff capabilities, especially of new entrants, should be upgraded through appropriate training

x. Undertake Financial and Administrative Restructuring: Over the long-term DFIs should be restructured administratively and financially. Measures for financial restructuring should include a thorough portfolio audit in each institution as a first step.

Investment Finance Banks

i. Simplify Approval Process: Approval process should be simplified and made more transparent.

ii. Simplify Procedures for Public Offerings: Approval process should be simple so as to allow transaction to proceed before market conditions change. A step beyond this could be a blanket approval for IFBs to undertake issues on behalf of clients on their own books or by directly placing them in the market.

iii. Allow Membership of Stock Exchanges to the IFBs: IFBs are allowed to act as traders and brokers of listed securities. At the present, however, stock exchanges are not allowing new membership with the result that the only way out for IFBs is to purchase a membership card from an existing member at exorbitant prices.

iv. Amend Existing Regulations to Allow Issuance of Term Finance Certificates in Favor of IFBs: IFBs are allowed to issue short and long-term redeemable capital which includes Participation Term Certificates (PTCs) and Term Finance Certificates (TFCs). However, under section 120 of the Companies Ordinance a company can issue any instrument in the nature of redeemable capital in favor of scheduled bank, financial institution, or other persons as may be specified for the purpose by the Federal Government. As an IFB is neither a scheduled bank nor a financial institution, companies cannot issue TFCs in their favor. This situation can be altered only if the Federal Government issue a notification that will amend the existing regulations.

v. Permit IFBs to Functions as Foreign Exchange Dealers: IFBs should be allowed to act as authorized foreign exchange dealers.

vii. Install a Recovery Mechanism for the IFBs: IFBs must be eligible for remedies available to commercial banks in cases of default such as access to the banking tribunal. Further, the existing law regarding foreclosures and taking possession of assets which are pledged as security leave a lot to be desired. Thus recovery mechanism must be put in place before IFBs can be expected to take on risk of credit and new ventures.

viii Permit IFBs to Take Deposits of Less than 90 Days Maturity: At the present IFBs are not allowed to take deposits that are less than 90 days maturity. IFBs want to provide all services under the same roof for their corporate clients including raising short term funds which may be of less than 90 days maturity.

ix. Ensure Access of IFBs to Specialized Credit Lines of the State Bank of Pakistan: IFBs are excluded from specialized credit lines, such as concessionary credit for locally fabricated machinery, available to NCBs and the DFIs.

x. Remove Stamp Duty on Paper Products of IFBs: Stamp duty on the paper products of IFBs should be removed to provide the necessary incentive for development of paper instruments.

xi. Create Fair Competitive Environment: To have IFBs competing with other institutions on a level playing field certain conditions have to be created. Liquidity and tradeability form the critical mass of capital markets. The GOP will have to take committed steps to fuel this market. For instance, the crowding out effect due to unnecessarily advantageous features of certain instruments (such as WAPDA bearer bonds) should be avoided. Again modaraba companies should be disallowed investment banking functions or should have similar guidelines as those provided to the IFBs.

xii. Clarify Tax Status of IFBs: The tax status of the IFBs is still not very clear. If the IFBs are taxed like other banks it will be unfair since the quality of the portfolio of the two types of institutions will be very distinct. Secondly, the amount of money that the IFBs are spending on the research and development of new products will have an impact on their income thus rendering them incomparable to other banks.

Investment banking is a new concept in Pakistan which requires active support not only from the GOP but also from the international donor community. The donor community can play a positive role in the development of IFBs by sponsoring workshops aimed at public education, by making available overseas training facilities for the staff of IFBs, and by providing credit lines.

3. Pakistan Informal Sector Study (Development Research and Management Services, Islamabad)

a. Scope of Work

This study is the first broad description of the informal sector from the perspective of the "de Soto problem". Its primary purpose is exploratory and descriptive, rather than prescriptive. It seeks to review the main theses of Hernando de Soto's book The Other Path, analyze their relevance to Pakistan's political, economic and administrative environment, and document specific examples in Pakistan where legalization of informal activity would result in major improvements in economic efficiency. The study examined seven subsectors (housing and human settlements, financial and commodities market, manufacturing, trade and commerce, health, education, and transport) of the urban informal sector in eight cities of Pakistan.

b. Principal Findings

i. Housing and Human Settlements: The major observed sources of illegal activity in housing are: (a) the general shortage of serviced plots that are legally available in planned settlements; (b) the allotment of plots at a price that is considerably lower than its market value; and (c) costly standards and procedures for regularization of kutchi abadis.

The major dynamic factor seems to be the inability of state systems to come anywhere close to the demand for housing associated with urbanization and raising incomes. The high cost of understanding and following official procedures is also relevant as a factor that affects the formal and informal sectors differentially.

ii. Education: It appears that the major long- term constraint on formalization is the unrealistic and prohibitively expensive standards for registration of schools. In order to register, a school has to fulfill the requirements for provision of playgrounds, laboratory, physical space, teachers qualifications, uniform curriculum standards, toilets, financial statements and solvency, may of which are impossible for most schools to fulfill. As a result, only a handful of schools have registered as required. The problem is compounded by the inability of the formal sector schools (largely state sponsored) to keep pace with the rapid increase in demand for schooling that has come about due to increases in urban population, incomes and the age structure of the population.

iii. Health: In common with housing and education, the health sub-sector has been experiencing large increases in demand associated with rapid urbanization and increases in incomes. Unlike those sub-sectors, however, informal health services do not appear to be creative or manipulative response to over-regulation. They appear, instead, to be responses to deficiencies in the availability of services in specific professional and locational categories, primarily nursing care, rural areas and poor urban areas.

iv. Trade and Commerce: The informal trade and commerce sector caters to low income groups. The dynamic factors behind its growth is a combination of two forces - growing market demand and supply restricted explicitly by administrative means. The source of growing demand appears to be the growing number of urban low income households, which generate the demand for informal trade and commerce in the cities. The restriction on supply emanates from administrative restrictions (often complete bans) imposed by local governments on the right to vend and set up markets in the numbers demanded, and at locations that are in great demand.

v. Transport: In common with the housing, education, and health sub-sectors, the urban transport sector has been witnessing growing demand in recent years. In addition, inter-city transport, has provided an attractive source of investment for illegally obtained money. From the administrative point of view, the supply of legal transport services has been restricted in two ways: first, the government has been slower than the private sector and the consumer in accepting new forms of transport; and, second, government at the provincial and the local levels has been restricting the availability of permits for various forms of transport.

Unlike all other elements of mechanized road transport, trucking is an almost completely deregulated, competitive and legal enterprise: truck permits have been freely available since deregulation in the 1970s, and what illegality there is, does not appear to be a "de Soto problem".

vi. Manufacturing: The immediate source of informality, in the de Soto sense, appears to be the incentive to avoid legal costs for inputs and taxes given, particularly, the broad and discretionary powers of government functionaries. This could be a major source of cost differential between formal and informal sectors.

Some of the costs of legality originate with legislation from colonial times; others are costs of administrative procedures (particularly, the approvals and No Objection Certificates required to set up business legally). To summarize, the source of illegality appears to be: (a) costly and time consuming procedures for registration; (b) the interest of the enforcing agencies to prevent registration and look the other way for illegal payments; (c) legislated costs, such as those of the labor and social security laws under the Factories Act, 1934 and the Shops and Establishments Ordinance 1969; and (d) broad and discretionary powers of the government functionaries charged with enforcement.

vii. Informal Financial Sector: The formal financial sector in Pakistan presents, in general, a picture of stagnation and inefficiency in the provision of financial services. On the demand side, Pakistan has been witnessing an explosion in the demand for an increasingly diversified set of instruments for savings, loans, foreign exchange, and insurance against risk. The dynamic factor in the growth of the informal sector is its responsiveness to this demand.

c. Principal Recommendations

i. Make the NOC Pro-active: There are two sets of possibilities for making the NOC more pro-active and less reactive: first, draw a "negative list" of a small number of activities for which NOC would be required for purposes of public interest; and, second, if an NOC is required in the public interest, whether from one or more agencies, only one agency should be designated as "concerned agency".

ii. Simplify Requirements for School Registration: The registration standards in the West Pakistan Registration of Unrecognized Educational Institutions Ordinance, 1962 should be aligned more closely with the prevailing reality.

iii. Simplify Procedures for Regularization of Kutchi Abadis: Since 1986, the Federal Government has had the stated policy of regularizing kutchi abadis, but the policy has been implemented through cumbersome and costly procedures. As a result, large numbers of low income dwellings remain in the informal sector, without the benefit of secure ownership and municipal services, and subject to the extortion and victimization that accompanies informal human settlement.

iv. Allot Residential Plots at Market Prices: Greater market orientation in the allotment of plots would tend to reduce illegal activity in the housing sector and serve to integrate the formal and informal components.

v. Abolish Foreign Exchange Controls: Existing exchange control regime seems to increase the cost of transactions, particularly to small customers and ordinary citizens, and put substantial foreign exchange flows into informal system (such as the hundi).

vi. Eliminate the Permit Control Over Mechanized Road Transport: The permit control system inhibits competition, promotes illegal rent seeking activity, and strengthens the influence and nuisance value of transporters. Regulation would still be needed in respect of standard of operations, but it cannot be justified as a means of restricting entry into the transport sector.

vii. Eliminate Subsidized Housing Finance: The elimination of subsidized housing finance in the public sector, greater market orientation in housing finance, responsiveness to low income groups, and modification of collateral arrangements are likely to increase investments in the sector, increase overall productivity, and undermine incentives for informality.

The Pakistan Informal Sector Study also suggest four priority research areas: cost-benefit of laws and procedures affecting manufacturing; comparisons of efficiency, productivity and transfer payments, assessing education standards in terms of output, and allowing organic development of local communities.

4. Privatization in Pakistan (MTech, Islamabad)

a. Scope of Work

The scope of work of this study include a review of the history of public and private sector roles in the national economy over the last two decades; an assessment of the GOP's current privatization policies; and, identification of the potential future policy directions for improved private sector participation in the economy.

b. Principal Findings

Public sector contributes about 49 percent to Gross Fixed Capital Formation (GFCF). State-owned enterprises (autonomous and semi-autonomous GOP sponsored agencies) account for around 60 percent of GFCF in the public sector. There are around 75 holding companies in which the Federal Government has an equity interest and management control with total assets of over 800 billion. In addition to this Federal Government sponsored corporate sector, there is also sizeable direct participation in economic activities by the four provincial governments.

There is a growing realization within the GOP of the need to shed the large and inefficient empire of public enterprises. However, while the GOP concede that privatization will improve economic efficiency, encourage increased private participation in the economy, and generate budgetary support, it has not yet demonstrated firm commitment to a widespread privatization program. The GOP policy combines elements of simultaneous strengthening and expansion of the public sector as well as selected privatization to promote more equitable asset distribution.

c. Principal Recommendations

i. Develop Privatization Policy: The presence of a comprehensive privatization policy encourage the functionaries at the operational level to take privatization decisions.

ii. Restrict Expansion of State Sponsored Enterprises: State owned enterprises should be restricted to undertake new investment except for modernization and rehabilitation of existing facilities; for activities in which private sector is not forthcoming; and for considerations of (demonstrable) public interest.

iii. Divestiture through Capital Markets: The GOP should annually offer shares worth at least Rs 1 billion of profitable enterprises to public for the next three years. The minimum proposed limit of Rs 1 billion may be revised thereafter.

iv. Establish a Privatization Fund: For meeting the cost of privatization, especially for developing "golden handshake" programs for employees of non-profitable enterprises, the GOP should set up a non-lapsable revolving Privatization Fund of at least Rs 100 million.

5. Industrial Investment Approval System in Pakistan (Mtech, Islamabad)

a. Scope of Work

This study is intended to provide documentation and clarification of issues relating to industrial investment approval procedures in Pakistan; to propose Government, or preferably non-Government assistance to promote increased investment (local and foreign); and, to suggest improvements in or alternatives to the current industrial investment approval procedures.

b. Principal Findings

Pakistan has in place a licensing regime whereby the GOP regulate the entry of new industrial investment in an attempt to avoid excess capacity; increase indigenization; direct resources to priority areas; and ration scarce foreign exchange, infrastructure and utilities. This investment approval process may broadly be seen as consisting of "primary" approvals of investment sanctioning, financial package approval, and location clearance and "secondary" approvals principally of registration with the Registrar Joint Stock Companies, registration with the Provincial Chief Inspector of Factories, tax and custom exemptions from the Central Board of Revenue, import license from the Chief Controller of Imports and Exports, and provision of utilities. This complex system of "primary" and "secondary" approvals require the investors to satisfy approval criteria of each of the concerned public sector agency which cause costly delays. Additionally, available evidence suggest that the approval system has not been successful in realizing the GOP's stated objectives.

In recent years the GOP has moved to streamline the approval system through liberalization of the sanctioning criteria and reform of the institutional mechanism for sanction and post- sanction formalities. A Federal Government sanction is now required only for investment of Rs 1,000 million and above, or if the investment concerns seven industries (arms and ammunition; security printing, currency and mint; high explosives; radio- active substances; alcohol and beverages based on imported concentrates; manufacture of automobiles, tractors and farm machinery; and petroleum blending plants). The institutional changes include the establishment of a Board of Investment (BOI) to evaluate and expedite investment sanctions; creation of a Committee on Investment (COI) to facilitate post-sanction formalities for BOI- sanctioned projects; and initiation of a "one-window" approval facility at the industrial estate level.

An assessment of the recent changes can be summarized as follows: progress in liberalization of the sanctioning criteria is encouraging, initiation of the one-window facility at the industrial estate level is of limited practical value, the impact of the creation of BOI and COI is difficult to ascertain at this stage, and in the remaining areas there has been, generally, no notable improvements. In short, the GOP's response thus far has not been commensurate with the size of the problem and significant reforms are needed to overhaul the investment approval system.

c. Principal Recommendations

i. Liberalize Sanctioning Criteria: Remove "Petroleum Blending Plants" and "Manufacture of Automobiles, Tractors and Farm Machinery" from the Federal Specified List. Also amend "Alcohol and Beverage Industry Based on Imported Concentrates" to allow investment in non-alcoholic beverages based on imported concentrates without sanction.

ii. Eliminate Sanctioning Requirements Based on Investment Size of Rs 1,000 Million and Above: Investment size considerations should not figure in GOP's calculus of investment controls and appraisal should be left to financial institutions.

iii. Eliminate Punjab Specified List: Provincial sanction requirement for cotton ginning, flour mills and sugar units in Punjab should be eliminated.

iv. Increase reliance on Prices to Direct Industrial Location: Existing location policies may be complemented with policies reflecting economic prices of industrial infrastructure.

v. Eliminate Licensing Requirement for Import of Machinery and Industrial Raw Material: Improved access to capital goods and industrial raw material will encourage new investment and improve capacity utilization.

vi. Energize Provincial Facility Boards: Vigorous Provincial Facility Boards could serve as useful expeditor of "secondary" approvals.

6. Pakistan : Private Investment Promotion and Investment Promotion Bureau (MTech, Islamabad)

a. Scope of Work

This study focus on the history, evolution and existing structure of the Investment Promotion Bureau (IPB); the investment promotion role of IPB in relation to its charter of objectives; and, the nature of IPB's investment promotion activities.

b. Principal Findings

A historical examination of the functions of IPB reveal that the Bureau has served as investment facilitator only marginally and has virtually not performed direct investment promotion functions. The Bureau has functioned primarily as an investment sanctioning agency and it is probably because of overwhelming focus on sanctioning that the private sector has often labelled IPB as an "Investment Prevention" rather than an "Investment Promotion" organization.

In February 1990, the Government of Pakistan (GOP) transferred the administrative control of IPB from the Ministry of Industries to the newly established Board of Investment (BOI) within the Prime Minister's Secretariat and is currently in the process of reorganizing and reorienting the role of IPB towards a mix of investment sanctioning, investment information dissemination and investment promotion. The reorganization plan envisages three wings, each headed by a Director General, for appraisal and regulations; monitoring and one-window facility; and, planning, promotion and publicity. The Director General for Planning, Promotion and Publicity will be responsible for identifying new areas for potential investment, preparing project profiles, developing investment related literature, organizing seminars, counselling prospective investors, and opening of investment centers both at home and abroad. The GOP has also established an Advisory Committee, consisting of public and private sector representatives to guide IPB, among others, in developing and implementing promotional programs. The GOP's proposed reorganization of IPB, however, suffers from two apparent weaknesses: it is likely to transform IPB into a larger organization with increased budgetary costs; and, it has a too little private sector participation.

c. Principal Recommendations

i. Alternatives to IPB's Reorganization: Two alternatives to the proposed reorganization of IPB may be considered: first, delinking IPB from sanctioning and promotion functions; and, second, abolition of IPB. While the first alternative allows the IPB to develop into an expeditor of post- sanction formalities, the second option permits the development of a private sector led promotion system.

ii. Encourage Private Sector Led Promotion: Regardless of the future shape of IPB, the GOP should encourage a more vigorous private participation in investment promotion through sub-contracting and through institutional development of business forums like Federation of Pakistan Chambers of Commerce and Industry.

7. **Financial Sector Development Program : Pakistan Capital Markets (Price Waterhouse, Washington D.C.)**

a. Scope of Work

This study analyzes Pakistan's capital markets in order to identify those areas in need of policy reforms or technical assistance. The study has been conducted with the goal of improving the domestic and foreign investment climate in Pakistan and, in particular, creating a more efficient and competitive financial sector.

b. Principal Findings

i. Distorted Interest Rate Structure: Generally, interest rate on government debt establish the reference rates for all other types of short and long-term obligations. In Pakistan, all rates on Government debts are administratively determined and the interest rate structure is distorted. The situation is complicated further by the GOP policy of "credit ceilings" where credit targets are established for individual banks and for small loans to agriculture, business, industry and low cost housing.

ii. Public Sector Dominated Financial System: The financial sector is centrally controlled system of directed credit, dominated by the Government ownership of commercial banks and DFIs. Although there are 19 foreign commercial banks, they do not provide competition due to the limited size of their resources and statutory limitation on their activities. Private IFBs are beginning to emerge though their precise role and functions are unclear at the present.

iii. Inefficient Tax Policy: The failure to operate and effective tax collection system distorts capital markets primarily by encouraging companies to under report income and thus provide inadequate disclosure. Companies that are free from tax (such as modarabas) and multinationals that pay their taxes generally disclose more accurate information and their securities have developed active trading markets. Where tax systems are relatively effective more companies go public.

iv. Assets Distribution through Capital Markets: To achieve a more equitable distribution of assets, current GOP regulations require companies with over Rs. 50 million paid up capital become public limited companies and offer 50 percent of their shares to public. Further, the amount that can be charged by companies for their shares is limited to book value to effect a redistribution of wealth. The GOP has also created National Investment Trust (NIT) to serve as an open ended mutual fund to encourage indirect investment in the market by small investors. NIT has the unique option to acquire 20 percent of all new security issues. While these measures are intended to address important social problems, they distort a free market.

v. Limited Investor Confidence: Investor confidence in the capital markets is limited due to: lack of timely and accurate financial disclosure; insider training and market manipulation; limited capacity of Corporate Law Authority (CLA) to enforce security laws, including disclosure and insider trading; and, family domination of enterprises, which works against the interest of minority shareholders.

vi. Inadequate Institutional Mechanism for Investor Participation: There are no entities in Pakistan that provide investment advisory services; the potential for increased trading at the Stock Exchanges remains unexploited; settlement and clearance procedures need modernization; and, brokers are self-regulated and have not inspired investor confidence.

vii. Limited Liquidity of the Market: Market depth, in the form of an active secondary trading market, is one of the most important functions of a stock exchange. Without an active secondary trading market to assure investors of liquidity, it is difficult to effect primary distributions. In the U.S. markets this function is generally performed by specialists or market makers. There are no specialists or market makers on the Karachi Stock Exchange (KSE), and historically the Exchange has not provided a good secondary market.

c. Principal Recommendations

i. Minimize Distortions in the Interest Rate Structure: The GOP should reduce budgetary deficits, gradually shift to the securities market for its financing requirement, and conduct true auction of treasury bills for raising the needed funds thereby establishing reference rates for other debt instruments. Also, the GOP should reduce the number and proportion of total credit for directed credit programs; eliminate the degree of interest rate subsidization; and specify and define priority sectors narrowly.

ii. Deregulate Financial Sector: Foreign banks and the newly established IFBs should be permitted to compete with NCBs in all aspects of banking except in taking short-term (30 days or less) deposits; government intervention in the day-to-day affairs of the NCBs should be curtailed; state-owned credit institutions that overlap one another should be consolidated; privatization of NCBs should be implemented; and, government and legislative bodies should assure autonomy for the State Bank of Pakistan.

iii. Improve Tax Administration: Improvements in the tax collection system will not only contribute to a reduction in the GOP's budgetary deficit but also will assist in the expansion of capital markets.

iv. Strike a Balance Between Social Goals and Free Market Principles: Encourage establishment of private mutual funds to compete with NIT; provide tax and other incentives to encourage the creation of stock option plans; gradually eliminate the requirement to become public but only in conjunction with changes in interest and financial sector pricing policies that encourage companies to become public; permit companies to receive market-determined prices for their securities; permit private institutions to determine the types of securities they will issue; and, change the legal system to encourage the development of a mortgage loan market.

v. Improve Investors Confidence: Improve investors confidence through strengthening application of disclosure requirements and enforcement capabilities of CLA; and, by encouraging the Institute of Chartered Accountants (ICA) in establishing an effective self-regulatory body of accountants.

vi. Encourage Development of Private Investment Advisory Services: The GOP should encourage the development of private advisory organizations, mutual funds, credit rating agencies and other institutions to act on behalf of small investors.

vii. Improve Liquidity of the Market: Efforts should be focused primarily on improving the liquidity of market through rationalization of interest rate structure.

The Price Waterhouse report also identifies several technical assistance areas such as public education, securities market development, financial regulation, development of private non-bank financial institutions, and privatization.

Annex N

Training Cost Analysis Budget Worksheets

The following pages present the-participant Training Cost Analysis (TCA) budget worksheets for this project. Individual budget worksheets are presented for One Month of Training, the Entrepreneurs International program and for Three Months of Training.

Annex N

PIE Training Plan
One Participant Budget Based on TCA Worksheets

Training	One Mth General	EI	Three Mth General	Two Yr Masters	Total
Part Yr	75	55	45	20	195
	$				
Educational Cost	3,000	4,000	9,000	18,000	34,000
Allowances	3,195	4,695	6,165	21,210	35,265
Travel	3,000	4,000	4,000	3,500	14,500
Insurance	34	34	102	714	884
Supplemental Cost	60	480	205	210	955
Total	9,289	13,209	19,472	43,634	85,604

PIE Training Plan Budget
(Combined)

Training	One Mth General	EI	Three Mth General	Two Yr Masters	Total
Part Yr	75	55	45	20	195
	$				
Educational Cost	225,000	220,000	405,000	360,000	1,210,000
Allowances	239,625	258,225	277,425	424,200	1,199,475
Travel	225,000	220,000	180,000	70,000	695,000
Insurance	2,550	1,870	4,590	14,280	23,290
Supplemental Cost	4,500	26,400	9,225	4,200	44,325
Total	696,675	726,495	876,240	872,680	3,172,090
Per Person	9,289	13,209	19,472	43,634	15,267

Annex N

TRAINING COST ANALYSIS FOR TECHNICAL 30 DAYS U.S. TRAINING
Budget for One Person

A. EDUCATION / TRAINING COST

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Tuition/Fees						
Regular Session	0	0	0	0	0	0
Summer Session	0	0	0	0	0	0
Training Costs	3,000	0	0	0	0	3,000
Packages Prg. Costs	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	3,000	0	0	0	0	3,000

B. ALLOWANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Maintenance Adv	0	0	0	0	0	0
Living/Maint.	0	0	0	0	0	0
Per Diem	3,000	0	0	0	0	3,000
Books & Equipment	60	0	0	0	0	60
Book Shipment	60					60
Typing	0					0
Thesis	0					0
Doc. Dissertation	0					0
Prof. Membership	75					75
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	3,195	0	0	0	0	3,195

C. TRAVEL

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
International	3,000	0	0	0	0	3,000
Local (U.S.)	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	3,000	0	0	0	0	3,000

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D. INSURANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
HAC for U.S.	34	0	0	0	0	34
Required by Inst.	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	34	0	0	0	0	34

E. SUPPLEMENTAL ACTIVITIES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
ELT, in-country	0					0
ELT, U.S.	0					0
Academic up-grade	0					0
Reception Services	60					60
WIC Orientation	0					0
Other Orientation	0					0
Interpreter/Escort	0	0	0	0	0	0
Internship/Coop.	0	0	0	0	0	0
Enrichment Prg.	0	0	0	0	0	0
Mid-Winter Seminars	0	0	0	0	0	0
Foolowup/Career Dv	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
TOTAL COST	60	0	0	0	0	60

TOTAL PARTICIPANTS COSTS (A+B+C+D+E)

Year 1	Year 2	Year 3	Year 4	Year 5	Total
9,289	0	0	0	0	9,289

Total Number of Participants: 1

PARTICIPANTS MONTHS PROJECTED

Year 1	Year 2	Year 3	Year 4	Year 5
1	0	0	0	0

Annex N

TRAINING COST ANALYSIS FOR
ENTREPRENEURS INTERNATIONAL 30 DAYS U.S. TRAINING
Budget for One Person

A. EDUCATION / TRAINING COST

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Tuition/Fees						
Regular Session	0	0	0	0	0	0
Summer Session	0	0	0	0	0	0
Training Costs	4,000	0	0	0	0	4,000
Packages Prg. Costs	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	4,000	0	0	0	0	4,000

B. ALLOWANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Maintenance Adv	0	0	0	0	0	0
Living/Maint.	0	0	0	0	0	0
Per Diem	4,500	0	0	0	0	4,500
Books & Equipment	60	0	0	0	0	60
Book Shipment	60					60
Typing	0					0
Thesis	0					0
Doc. Dissertation	0					0
Prof. Membership	75					75
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	4,695	0	0	0	0	4,695

C. TRAVEL

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
International	3,000	0	0	0	0	3,000
Local (U.S.)	1,000	0	0	0	0	1,000
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	4,000	0	0	0	0	4,000

Annex N

D. INSURANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
HAC for U.S.	34	0	0	0	0	34
Required by Inst.	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	34	0	0	0	0	34

E. SUPPLEMENTAL ACTIVITIES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
ELT, in-country	0					0
ELT, U.S.	0					0
Academic up-grade	0					0
Reception Services	0					0
WIC Orientation	60					60
Other Orientation	0					0
Interpreter/Escort	0	0	0	0	0	0
Internship/Coop.	0	0	0	0	0	0
Enrichment Prg.	0	0	0	0	0	0
Mid-Winter Seminars	0	0	0	0	0	0
Foolowup/Career Dv	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
PIET Prg. Fee	420	0	0	0	0	420
TOTAL COST	480	0	0	0	0	480

TOTAL PARTICIPANTS COSTS (A+B+C+D+E)

Year 1	Year 2	Year 3	Year 4	Year 5	Total
13,209	0	0	0	0	13,209

Total Number of Participants: 1

PARTICIPANTS MONTHS PROJECTED

Year 1	Year 2	Year 3	Year 4	Year 5
1	0	0	0	0

Annex N

TRAINING COST ANALYSIS FOR
TECHNICAL 3 MONTHS U.S. TRAINING
Budget for One Person

A. EDUCATION / TRAINING COST

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Tuition/Fees						
Regular Session	0	0	0	0	0	0
Summer Session	0	0	0	0	0	0
Training Costs	9,000	0	0	0	0	9,000
Packages Prg. Costs	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	9,000	0	0	0	0	9,000

B. ALLOWANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Maintenance Adv	0	0	0	0	0	0
Living/Maint.	0	0	0	0	0	0
Per Diem	5,850	0	0	0	0	5,850
Books & Equipment	180	0	0	0	0	180
Book Shipment	60					60
Typing	0					0
Thesis	0					0
Doc. Dissertation	0					0
Prof. Membership	75					75
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	6,165	0	0	0	0	6,165

C. TRAVEL

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
International	3,000	0	0	0	0	3,000
Local (U.S.)	1,000	0	0	0	0	1,000
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	4,000	0	0	0	0	4,000

Annex N

D. INSURANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
HAC for U.S.	102	0	0	0	0	102
Required by Inst.	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	102	0	0	0	0	102

E. SUPPLEMENTAL ACTIVITIES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
ELT, in-country	0					0
ELT, U.S.	0					0
Academic up-grade	0					0
Reception Services	60					60
WIC Orientation	0					0
Other Orientation	145					145
Interpreter/Escort	0	0	0	0	0	0
Internship/Coop.	0	0	0	0	0	0
Enrichment Prg.	0	0	0	0	0	0
Mid-Winter Seminars	0	0	0	0	0	0
Foolowup/Career Dv	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
TOTAL COST	205	0	0	0	0	205

TOTAL PARTICIPANTS COSTS (A+B+C+D+E)

Year 1	Year 2	Year 3	Year 4	Year 5	Total
19,472	0	0	0	0	19,472

Total Number of Participants: 1

PARTICIPANTS MONTHS PROJECTED

Year 1	Year 2	Year 3	Year 4	Year 5
3	0	0	0	0

Annex N

TRAINING COST ANALYSIS FOR TWO YEAR MASTERS DEGREE
Budget for One Person

A. EDUCATION / TRAINING COST

Activity Year 1	Year 2	Year 3	Year 4	Year 5	Total	
Tuition/Fees						
Regular Session	9,000	9,000	0	0	0	18,000
Summer Session	0	0	0	0	0	0
Training Costs	0	0	0	0	0	0
Packages Prg. Costs	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	9,000	9,000	0	0	0	18,000

B. ALLOWANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Maintenance Adv	0	1,950	0	0	0	1,950
Living/Maint.	800	9,650	7,200	0	0	16,500
Per Diem	0	650	0	0	0	650
Books & Equipment	0	780	585	0	0	1,365
Book Shipment	0		120			120
Typing	0	200	200			400
Thesis	0		500			500
Doc. Dissertation	0					0
Prof. Membership	0		225			225
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	800	13,180	8,830	0	0	21,210

C. TRAVEL

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
International	0	1,500	1,500	0	0	3,000
Local (U.S.)	0	500	0	0	0	500
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	0	2,000	1,500	0	0	3,500

Annex N

D. INSURANCES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
HAC for U.S.	0	408	306	0	0	714
Required by Inst.	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
Total Cost	0	408	306	0	0	714

E. SUPPLEMENTAL ACTIVITIES

Activity	Year 1	Year 2	Year 3	Year 4	Year 5	Total
ELT, in-country	0					0
ELT, U.S.	0					0
Academic up-grade	0					0
Reception Services	0	60				60
WIC Orientation	0	150				150
Other Orientation	0					0
Interpreter/Escort	0	0	0	0	0	0
Internship/Coop.	0	0	0	0	0	0
Enrichment Prg.	0	0	0	0	0	0
Mid-Winter Seminars	0	0	0	0	0	0
Foolowup/Career Dv	0	0	0	0	0	0
Other (Mission Opt)	0	0	0	0	0	0
TOTAL COST	0	210	0	0	0	210

TOTAL PARTICIPANTS COSTS (A+B+C+D+E)

Year 1	Year 2	Year 3	Year 4	Year 5	Total
800	24,798	19,636	0	0	43,634

Total Number of Participants: 1

PARTICIPANTS MONTHS PROJECTED

Year 1	Year 2	Year 3	Year 4	Year 5
0	12	9	0	0

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Annex O

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