

Japan's Country Assistance Program for Pakistan

February 2005

Government of Japan

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Attachment: Diagram of the Program Goal

Introduction

Japan has continued to provide cooperation to Pakistan since the 1960s through Official Development Assistance (ODA). Since the latter half of the 1990s in particular, this cooperation has been focused on the social sector, economic infrastructure, agriculture and the environment. Since 1999, towards the aim of building a ‘moderate and modern Muslim state,’ the Government of Pakistan has been making progress in various measures, including the reduction of the budget deficit, deregulation and privatization, the improvement of infrastructure and the activation of rural communities. Recognizing the considerable changes in the international environment around Pakistan, Japan has clarified the significance of economic cooperation to Pakistan (see section 1. below) and has analyzed development issues facing Pakistan and the direction of its development strategy (see section 2. below). With regard to the direction of economic cooperation to Pakistan, Japan has established its medium- and long-term goal as the ‘Construction and Development of a Sustainable Society.’ Under this goal, Japan has established three directions and priorities for economic cooperation as a guideline for the coming five years (see section 3. below). Japan will implement ODA to Pakistan in an efficient and effective manner based on the Japanese ODA Charter and the Country Assistance Program laid out in this paper.

1. Significance of Economic Cooperation to Pakistan

- 1) In broad terms, Pakistan, being the second largest country in South Asia and in the entire Muslim world with a population of 148 million people, requires international cooperation for the following two main reasons. First, Pakistan has been adversely affected by the emerging geopolitical instability in the region since the September 11, 2001 terrorist attacks in the United States. Second, socio-economic structural problems in Pakistan and the region remain at the root of this instability and, therefore, must be addressed.
- 2) The geopolitical problem requires reconsideration of several important factors and viewpoints. First, the maintenance of peace and the stable development in Asia, which contains the two largest countries, China and India—accounting for one-third of the world’s population—is becoming increasingly important for the stability and prosperity

of the international community, and is therefore also crucial for the foundations of Japan's peace and security in the 21st century. In relation to this, it must also be recognized that peace and stable development in Pakistan is inseparably-linked to peace and stability in whole of south Asia, including India. The reality of this was demonstrated in May 2002, when heightened tensions between India and Pakistan aroused great apprehension that they could lead to all-out war. Second, the U.S. attack on the Taliban in Afghanistan impelled Muslim Pakistan to make a very difficult choice, and as a result of Pakistan's decision to make a contribution to the international community as a front-line state in the fight against terrorism, the instability that Pakistan now faces has significantly increased.

- 3) Some of the elements of political instability that Pakistan is currently facing are shared with neighboring Afghanistan, given that two major ethnic groups (Pashtuns and Balochis) live on both sides of the border. A second factor has been the infiltration of terrorists and support for their activities from some local residents in the Federally Administered Tribal Areas (FATA) along the border with Afghanistan, areas in which the Pakistani government had maintained a position of non-interference. A third factor is the increasing presence of Islamic extremist groups, which have gained a strong foothold in the region in the years since the Soviet invasion of Afghanistan in 1979.
- 4) The deep-seated socio-economic structural problems, which will be explained more fully below, have been at the root of tendencies towards political instability in Pakistan and have been caused by the fact that the basic conditions necessary for sustainable development have not been sufficiently met, despite Pakistan's wealth of excellent human resources. The conditions that are required are: equality of access to social opportunities in real terms; consistency and continuity of development strategies; and a robust social monitoring capacity (e.g., countervailing forces). Unfavorable natural phenomena have also played a part, as economic growth, particularly in the agricultural sector, was slowed because of prolonged droughts that struck Pakistan during the latter part of the 1990's and continued till 2001. This resulted in lowered economic growth, the labor absorption capacity of Pakistan's economy declined and poverty levels increased. In addition, economic measures and sanctions were applied against Pakistan because of its nuclear testing, which dealt a blow to economic assistance and created disequilibrium in the balance of payments, culminating in a debt crisis.
- 5) Then Chief Executive General Pervez Musharraf, who took power in October 1999,

launched numerous reforms in various sectors in which the national prestige of the country was at stake, leading towards the building of a “moderate and modern Muslim state.” Representative of such initiatives is the formulation of various development plans, such as a Poverty Reduction Strategy Paper (PRSP), which incorporates changes in development strategies supported by international organizations (2001-04), a new 10-year Perspective Development Plan (2001-11), a 3-year Development Program, and an ambitious Devolution Plan. As will be explained below, some results of these reforms have already appeared, and they have led to the increased flow of assistance from the international donor community. Moreover, in regard to the domestic political situation, a general election was held in October 2002, and administrative authority was transferred to the Cabinet of Mir Zafarullah Khan Jamali. In June 2004, Prime Minister Jamali resigned and was succeeded by Prime Minister Chaudary Shujaat Hussain, and in September 2004 Mr. Shaukat Aziz was appointed as prime minister.

- 6) The present administration has achieved a number of tangible results not only in domestic administration but also in foreign affairs. Pakistan has built good relations with the Transitional Administration in Afghanistan led by President Hamid Karzai, and particular mention should also be made of the improvement in relations with India, which had been in a deteriorating state since December 2001, and with the industrialized countries, including the United States and European countries.
- 7) The Government of Pakistan’s various structural reforms and its policies and efforts for improving relations with other countries are essential for resolving the two broad problems the country is facing as mentioned at the beginning of this report, namely, its geopolitical instability and the basic socio-economic problems embedded at the root of this instability, and, in turn, for guiding Pakistan’s development into a sustainable society. Accordingly, staunch cooperation for this process will help lead to the stability of Pakistan and, further, to the stability of the entire region, which is a common goal for the donors supporting Pakistan to address.
- 8) In addition, the stable development of Pakistan as a “moderate and modern Muslim state” has great importance for the entire region, including Japan, which has friendly relations with Pakistan. First, Pakistan is in close proximity to China and India, as well as to Middle Eastern and Central Asian countries, and it is forging important relations with those countries. The stability, therefore, of Pakistan as a moderate and modern Islamic state will create stability throughout the entire Asian region, which will, as a

result, be beneficial for Japan.

Second, Pakistan's geopolitical significance regarding the shipment of energy supplies is also an important factor. Not only is Pakistan's position next to the sea lanes from the oil and natural gas supply sources in the Middle East and Central Asia to Japan vital, but its location as a contact point between the Indian Ocean and the interior of East Asia will also grow in importance in the future.

Third, as Pakistan generates the momentum for its drive towards the goal of becoming a sustainable society, the economic opportunities created by its population of 148 million people will reach a scale that cannot be ignored by Japan and other countries.

Fourth, Pakistan has consistently been a friendly country to Japan, and it will be important for Japan to carefully foster the amicable feelings toward Japan that are widely shared by Pakistanis.

2. Development Issues and Direction of Pakistan's Development

2.1 Review of Pakistan's Development

The initial conditions in Pakistan at the time of its inception as an independent state in 1947 were certainly not very favorable. The Muslim League that formed the core of the Pakistan independence movement was politically inexperienced, and the number of Muslims equipped with a higher education working in the country's bureaucracies was limited. Pakistan, which at the time was no more than a supply base for raw cotton and wheat to India, had almost no foundation for secondary or tertiary industries. In the subsequent course of Pakistan's development, Pakistan performance does not however compare unfavorably to other developing countries, considering the various exogenous factors that hindered Pakistan's development. The following indicators show the achievements of Pakistan's development.

- Pakistan's real GDP for fiscal 2003-04 was 12 times greater than that for fiscal 1949-50, with an average annual growth rate of 4.8 percent.
- As a result of the Green Revolution in the 1960s, Pakistan has achieved self-sufficiency in food grains.
- Pakistan, which did not have a foundation for secondary or tertiary industries at the time of partition, now has a strong cotton textile industry and it has a burgeoning

small- and medium-scale enterprise (SMEs) sector, which now manufactures a variety of products such as medical instruments and sporting goods for export.

However, the potential for development above and beyond what has been achieved was certainly existent in Pakistan, considering the favorable conditions it enjoyed at the time of independence, including the excellent agricultural base, exemplified by its superior irrigation system (an irrigation ratio of 80 percent) and the high potential of its human resources. Why then did Pakistan not achieve the level of development that was expected? Three salient shortcomings seem to have marked the first fifty years of Pakistan's development.

- (1) Pakistan has not performed well in fostering the necessary human resources essential for development. Indicators related to education and health have also remained low, and a strong and enlightened middle class that can support the sound growth of democracy and market economy has not been cultivated.
- (2) Pakistan has not made serious enough efforts yet to diversify its industrial structure. Although the share of the agricultural sector, the largest sector in Pakistan, has declined to 23 percent of Pakistan's GDP, 42 percent of the country's labor force is still engaged in agriculture. What is more important is the fact that the decrease in agriculture's share in GDP has not been accompanied by a diversification of industry. In addition to the continued protection of the large-scale textile industry, the ad hoc nationalization of the non-agricultural sectors undertaken by the Bhutto government (1971-77) and the presence of an uncontrolled black economy have hindered sound industrial development.
- (3) Since the assassination of Pakistan's first prime minister, Liaquat Ali Khan, the political situation in Pakistan has been unstable, resulting in inconsistencies and lack of continuity in Pakistan's development policies and strategies during the course of its political history. Economic stagnation and the deterioration of law and order under civilian governments have invited military intervention. The development of a sound democracy and market economy has been markedly impeded by this uncertain political process.

The above represents a summary of Pakistan's development up to 1999; but how should the situation in Pakistan be evaluated since that time?

While it is premature to evaluate conclusively the impacts of the various reforms that have been introduced by the Pakistan government, the major macroeconomic

indicators seem to suggest the end of Pakistan's long period of stagnation. For example, Pakistan's real GDP growth rate jumped to 5.1 percent in 2002-03, and further to 6.4 percent in 2003-04. The inflation rate has dropped to less than 5 percent, and the budget deficit has been lowered to 2.4 percent of GDP. While improvements in trade accounts have also had an effect, the tremendous increase in overseas Pakistani workers' remittances from abroad, which were spurred by regulatory actions taken in the aftermath of the September 11 terrorist attacks (the strengthening of regulations against money laundering, etc.), created a surplus in Pakistan's current account for three years in a row for the first time in a quarter of a century. Pakistan's foreign exchange reserves now exceed more than 12 billion U.S. dollars (equivalent to 11 months' import).

In addition, improvements in Pakistan's investment climate (due to lower interest rates and a stable exchange rate) have been manifested in the increase in industrial production (18 percent increase) and the activation of the stock market. Along with its increases in expenditures for development and countermeasures against poverty, Pakistan can also be praised for its efforts at reducing government debt to a near sustainable level. All of these achievements are the realization of the Pakistani government's sound economic policies, which brought about the country's V-shaped economic recovery, together with changes in the international environment and the resumption of assistance from the international donor community.

However, if the only indicator considered is V-shaped economic recovery, Pakistan has experienced two similar recoveries in the past; the recoveries during the Ayub government (1958-1969) and the Zia government (1977-1988). Two similarities with these past two economic recoveries are the restoration of law and order and the consistency and continuity of the country's development policies and strategies. But the fundamental reasons for the unsustainability of the past two recoveries can be found in two factors mentioned above—the slowness of human resources development and the lack of diversity in the industrial structure. Based on this experience, it is clear that concerted efforts have to be made in human resources development, diversification of industrial structure and political stability in order to ensure the sustainability of the current economic trend

2.2 Development Strategy of the Government of Pakistan

As mentioned above, since he assumed power in October 1999, President Musharraf

and his government have made concerted efforts for the development of Pakistan. Examples of these efforts have been the formulation of the government's 10-year Perspective Development Plan and the 3-year Development Programme announced in September 2001, the Interim Poverty Reduction Strategy Paper (I-PRSP) announced in November 2001, and the Full-PRSP announced in December 2003. From these policy documents it is evident that the Musharraf government is taking direct steps for the acceleration of economic growth, poverty reduction, and improvement of governance. These strategies are in line with the medium- and long-term direction of Japan's ODA framework. Outlined below are the development strategies the Government of Pakistan has undertaken for implementation.

2.2-1 Acceleration of economic growth

While it is making efforts to reduce the budget deficit, strengthen its debt management capabilities, rationalize government expenditures, and carry out other fiscal reforms, the Government of Pakistan is also promoting privatization as well as financial and trade deregulation and liberalization, positioning the private sector as the country's engine of growth. Another high priority is the improvement of infrastructure to facilitate the smooth execution of economic activities and the harmonious development and integration of underdeveloped regions. The government is also fostering SMEs with high labour absorption capabilities, bringing in foreign direct investment (FDI) to the oil and gas, IT and telecoms sectors, and promoting the housing construction industry, which has strong forward and backward linkages. Through the revitalization of the agricultural sector (crop, livestock, and fishery sub-sectors), the government is making efforts to activate rural communities, where serious poverty issues remain.

2.2-2 Poverty reduction

As it increases government investment for the improvement of Pakistan's social indicators, the Government of Pakistan is also working out plans to strengthen collaboration with non-governmental organizations (NGOs) and the private sector, with the aim of diffusing more widely, and improving the quality of, social services. In line with its devolvement of authority to the local governments, the Federal and provincial governments are making efforts to provide social services that meet the real needs of

recipients by transferring authority for the provision of these services to the actual implementing agencies at the grassroots level. Moreover, aiming to achieve the Millennium Development Goals, Pakistan is instituting comprehensive reforms to improve access to social services, the service-delivery capability of implementing agencies, and the quality of the services themselves, based on the government's Education Sector Reform in the field of education and the National Health Policy in the field of health care. Furthermore, in order to be effective in tackling poverty, the government is implementing, as policies specifically targeting the poor, micro-financing facilities to foster entrepreneurship among the poor and the Khushal Pakistan/Tameer-e-Pakistan/DERA programs to improve and develop infrastructure and create income-generating opportunities in rural districts.

2.2-3 Improvement of governance

The central government is moving forward with its devolvement of authority, which includes the decentralization of political and administrative authority to revenue mobilized districts. Direct elections are being held at the union level to devolve political power, and one-third of the local council seats are allocated for women. Moreover, the government is implementing legal reforms and reforms of the police force in order to thoroughly ground authority in the rule of law, civil service reforms with the aim of ensuring the efficient and effective formulation and execution of government policies, anti-corruption policies and procurement reforms to improve transparency and prevent corruption by politicians and civil servants, and reforms in fiscal accounting, auditing, and reporting practices.

2.3 Framework for Medium - and Long-term ODA Strategies

2.3-1 Goals of ODA

Based on discussions with the Government of Pakistan to date, Japan has made the “construction and development of a sustainable society” the uppermost goal of its ODA to Pakistan. This development is centered on the building of a national identity based on “dignity and pride” and ensuring the sustainability of development through the effective fostering and utilization of Pakistan's potential. For this, a “sustainable society” must at least be able to satisfy the following three fundamental conditions. First, a sustainable society must maintain law and order and remain committed to the consistency and

continuity of its development strategies. Second, such a society must ensure equal access to social opportunities in real terms and provide ample choices for its citizens. Third, it should be a just society that has the capability for social monitoring. It is of course difficult to say that these three conditions are absolutely necessary and sufficient conditions allaying the foundations for a sustainable society, but it is equally difficult to claim that a society that does not fulfill these conditions is labeled a sustainable society. In this context, these conditions can be considered necessary and fundamental.

2.3-2 Three priority directions in ODA strategy

In order to build a sustainable society in Pakistan, a medium and long-term strategic framework should be articulated beyond the short-term strategies in which the institutional and technological conditions are provided. In reviewing Pakistan's 50 years of development experience and in consideration of the various endogenous problems that Pakistan is currently facing, Japan has set forth three priority directions for cooperation, which are explained in detail below. These three strategies are: ensuring of human security and human development; development of a sound market economy; and achievement of balanced regional socio-economic development. The direction of these cooperation strategies provides a roadmap for meeting the necessary fundamental conditions for building a sustainable society as mentioned above.

2.3-2-1 Ensuring human security and human development

To date, Pakistan has not been able to develop its human resources to the desirable extent, one of the most fundamental conditions for building up a sustainable society. Not being adequately afforded the opportunities to exercise their capabilities, the earnings of many Pakistani citizens possessing latent capabilities are not consistent with their talents. Shadowing the problems of poverty and unemployment, low income and consumption levels are also issues intrinsically linked to basic human rights and human dignity. The problem of lack of access to health care is also on a similar level. Equal access to social opportunities, hindered in Pakistan's case by various structural impediments, is the most unavoidable and important development issue when creating sustainable development. It should be well recognized that these perspectives are also reflected in the Government of Pakistan's own Poverty Reduction Strategy Paper. The three priority areas given below are essential for achieving the goal of ensuring of

human security and human development. Among them, the importance of reducing various social disparities, including the serious gender disparities in education and health care, and of providing support for higher education and technical training to promote the expansion of social monitoring capacity, which also involves expanding the middle class, should receive special attention. The priority areas in this respect are delineated as follows:

- Improvement of basic education and reduction of various social, economic and other disparities
- Support for higher education and technical training to promote the expansion of the middle class
- Ensuring access to primary health care, safe water and sanitation and the reduction of various other disparities.

2.3-2-2 Development of a sound market economy

With its economy excessively dependent on the country's excellent agricultural base, Pakistan has not made sufficient effort to diversify its industrial structure. The food processing, tobacco, and cotton textile industries still account for 40 percent of Pakistan's industries, and Pakistan has not been able to extricate itself from an agriculture-based industrial structure. The protectionist industrial policies of successive governments in the past have induced excessive investment in designated industries like cotton textiles and sugar refining. The ad hoc nationalization policies of the Bhutto government and the subsequent delay in privatization retarded the mobilization of industry, and shifts in policy caused by repeated changes of government discouraged private investment and thus hindered the diversification of industry. In addition, the influx of cheap contraband goods stifled the growth of the consumer durables manufacturing industry. Although regulations encouraging investment were instituted, law and order problems, frequent policy changes, procedural delays, and infrastructure inadequacies raised production costs and limited new investment. More seriously, the significant decline in the growth rates of agriculture and agro-based industry during the latter part of the 1990s resulted in a significant downturn in the absorption of labour force in these sectors. Evidently, these are the two major labour absorption sectors in the country. The employment generating capacity of manufacturing industries has also been sluggish since the 1980s. While the population and the labor force increased, the

capital-intensive nature of the development of Pakistan's main industries was also related to the rise of poverty levels in urban areas in the 1990s. Based on the conditions described above, Japan has set the following vital priority areas for its cooperation.

- Expansion of labor absorption capacity and development of the agricultural and rural sectors to reduce poverty
- Ensuring sound development of a market economy and promoting the diversification of industries
- Development of economic infrastructure to support the activation of a market economy and the reduction of poverty

2.3-2-3 Achievement of balanced regional socio-economic development

Regional disparities in Pakistan are increasing. While 56 percent of Pakistan's population is concentrated in Punjab province, which occupies 26 percent of the national land area, only 5 percent of the population lives in Balochistan province, which makes up 44 percent of the total land area. Regional concentration is very much prominent in the agriculture sector, the country's largest sector of economy. Punjab province has 56 percent of the country's arable land, and public as well as private investment is concentrated in the province. Seventy-three percent of public canal irrigation and 91 percent of tube-wells are concentrated in Punjab. Eighty-one percent of wheat production, 100 percent of the superior variety Basmati rice production, 80 percent of cotton production, and 50 percent of cattle and 71 percent of buffalo are in Punjab. Moreover, this trend has been gradually accelerating. Regional concentration in the manufacturing sector is not as prominent as it is for agriculture, but here again there is a trend towards concentration in Punjab province, this trend being strengthened by the deterioration of law and order situation in Sindh province. Karachi, which could boast of its prosperity as a vital economic centre of the country, has been suffering mainly due to the deterioration of law and order situation and the lack of business confidence. In addition, the underdeveloped region wedged between the Indus River and the border with Afghanistan not only provides much less income opportunities, resulting inevitably in high poverty levels and the worsening of other social indicators, but it has also become a hotbed for smuggling and a center for the black economy. Based on the situation described above, Japan has set the following as important priority areas for its cooperation.

- Expansion of public investment to provide externalities to private sector investment that will lead the development of underdeveloped regions
- Development of attractive regional economic centers

2.4 Strategies of Major International Organizations and Other Donor Countries

While bilateral donors curtailed their assistance and concentrated their assistance in social sectors due to the economic sanctions imposed after Pakistan's nuclear testing, international financial organizations continued their funding to Pakistan and thus their influence on the country has increased considerably.

Of these international financial organizations, the IMF supported Pakistan in achieving macroeconomic stability and strengthening the efficiency of its government, while the World Bank and the ADB helped Pakistan in improving its business environment in order to promote economic growth, introducing reforms for rectifying income and gender disparities and providing assistance for pro-poor economic growth, social development, and governance reforms based on Pakistan's PRSP and devolution programs. For all organizations, common elements are the provision of comprehensive assistance that extended to many sectors, the expansion of assistance for the improvement of infrastructure that spurred Pakistan's recent favorable economic performance, and the strengthening of assistance to provincial governments in line with the movement toward the devolution of authority (Pakistan was exempted from the IMF's Poverty Reduction and Growth Facility (PRGF) Program until the end of 2004).

Concerning bilateral donors, while other donors were imposing economic sanctions after Pakistan conducted its nuclear tests, China increased its presence in Pakistan through its assistance for infrastructure development. With the growing importance of the stable development of Pakistan, which became a frontline state in the battle against terrorism in the aftermath of the September 11 attacks in the United States, donors began to successively lift the economic restrictions they had imposed after the nuclear tests. The actions of the United States, which resumed its large-scale assistance to Pakistan, captured the particular attention of other donors. Most of this assistance was earmarked for debt relief, efforts to improve social services through local NGOs, and the strengthening of governance, with regional priority being given to the Balochistan and Sindh provinces. The United Kingdom concentrated its assistance in the social

sectors, putting priority on the North West Frontier and Punjab provinces.

Among donor collaboration efforts, the World Bank and the UK led other donors in participating in the Social Action Programme (SAP), which was implemented from 1994 to 2002.

3. Direction of Japan's ODA to Pakistan

3.1 Past Record and Current Status of Japan's ODA to Pakistan

3.1-1 During the 1990s, while other donors were decreasing their assistance to Pakistan year by year, Japan maintained its position as the top donor to Pakistan. Particularly from the latter half of the 1990s, Japan focused its cooperation on the social sectors, economic infrastructure, agriculture, and the environment. But after the May 1998 nuclear testing, the Japanese government decided to freeze grant aid and yen loans to Pakistan for new projects (excluding emergency or humanitarian assistance and grassroots grant aid), and cautiously examined the provision of funding to Pakistan by international financial organizations. Japan subsequently concentrated its cooperation to Pakistan on the continuation of existing projects, technical cooperation aiming at poverty reduction and human resources development, emergency and humanitarian assistance, and grassroots grant aid for promoting human security. During this period, Japan repeatedly made its position clear to India and Pakistan regarding nuclear disarmament and non-proliferation. In part because of this influence from Japan, both countries have maintained their moratoria on nuclear testing and stated that they will continue to do so in the future. Both countries have also declared strict implementation of controls on the export of nuclear- or missile-related materials and technology. Pakistan has recently passed a law to control the export of nuclear related materials and technology.

3.1-2 As one of the measures announced by Prime Minister Koizumi in September 2001 that Japan adopted in response to the September 11 terrorist attacks in the United States, Japan took the initiative in announcing that it would extend 40 million U.S. dollars in emergency economic assistance to Pakistan. Further, in October of the same year, Japan announced that, in view of the continuation of the above-mentioned moratoria on nuclear testing and other developments, it would discontinue the economic

measures it had imposed in response to the testing. In November, Japan announced additional assistance of 300 million U.S. dollars (which included the above-mentioned 40 million U.S. dollars) in grant aid to be extended over approximately a two-year period in order to assist Pakistan's efforts for poverty reduction, including in the fields of education and medical care. In December, Japan agreed to the Paris Club's rescheduling of Pakistan's official debt (amounting to approximately 4.5 billion U.S. dollars in the case of Japan). With the international donor community uniting in the war against terrorism, this debt relief measure was an indication of the high regard for Pakistan's efforts in this regard. Based on the recognition of the importance of extending medium and long-term cooperation for Pakistan's stable development and thus rectifying the various social disparities in Pakistan and reducing poverty, which creates a breeding ground for terrorism, in August 2004, Japan declared that consideration would be initiated on the resumption of yen loans to Pakistan for new projects.

3.1-3 As Pakistan's top donor, Japan has succeeded in developing ties of genuine trust with Pakistan through its development cooperation. Japan's cooperation can be seen in the development of regions considered particularly underdeveloped in Pakistan. Because of the need to boost the development of the underdeveloped region between the Indus River and the border with Afghanistan, the upgrading and rehabilitation of the Indus Highway, which will function as an important economic artery extending across the length of Pakistan to connect Karachi and Peshawar, and the construction of the Kohat Tunnel have been highly evaluated by the Government of Pakistan, both projects being financed by Japanese ODA. Japan has also contributed greatly to poverty reduction in Pakistan, providing extensive cooperation for rural electrification, terminal irrigation facilities, rural roads, safe water supply, construction of school buildings, and so on, in order to promote regional development and improve living conditions.

The Government of Pakistan has also been highly appreciative of Japan's efforts to respond positively and actively to the various urban problems Pakistan is facing due to hyper increases in urban populations. For example, the Ghazi Barotha hydroelectric power plant, construction of which is intended to address the increasing demand for electricity, will play a major role as a key supplier of hydroelectric power in Pakistan, contributing significantly to the country's stable supply of electricity, in tandem with

the related project for strengthening the electric power transmission grid. Japan's extensive support for the improvement of urban water supplies and sanitation has also highlighted Japan's cooperation to Pakistan.

In the field of health and medical care, cooperation not only for the provision of facilities and equipment for hospitals, but also for expanding basic medical services is also an important concern, and since the latter half of the 1990s, Japan has been making vigorous efforts for the improvement of mother and child health care and the furthering of countermeasures against infectious diseases. Japan has also extended grant aid for the construction of the Mother and Child Health Center, the Children's Hospital, the College of Nursing, and the Paramedical Institute, as well as technical cooperation for the training of human resources. All of these projects are located within the premises of Pakistan Institute of Medical Sciences.

In the field of education, Japan originally placed emphasis on the improvement of higher education, focusing its assistance on supporting science and engineering universities and colleges, but recently, from the perspective of poverty reduction, Japan has been strengthening its cooperation for basic education, particularly literacy and numeracy education. Japan has also been making active efforts for the support of educational policy formulation through the dispatch of specialists, the enhancement of the Punjab province government's literacy monitoring capabilities, support for secondary education in Balochistan province, the construction of schools in tribal regions, and the promotion of distance learning.

Japan's technical cooperation and grassroots human security grant aid cooperation were carried out without interruption during the period of the imposition of economic measures beginning from 1998, and this assistance has been highly appreciated by the Pakistani people as being very need-specific and meticulous in its implementation. The contribution made by Japan's yen loans and grant aid for the construction and improvement of economic and social infrastructure has also been highly evaluated by Pakistan. In recent years, Japan has been actively pursuing attempts to consolidate these various assistance schemes, with the aim of achieving even more effective results.

3.2 Direction and Priority Areas of Japan's ODA

The account given above is a broad description of Japan's medium and long-term assistance strategy that will underpin Japan's efforts to cooperate with Pakistan towards

the ultimate goal of constructing a sustainable society. It is also necessary to set a specific direction for Japan's cooperation in due consideration of Japan's comparative advantages, and constraints in terms of time and resources, subject to active policy dialogue with Pakistan. Such considerations are important because any project, however relevant it may be, could not be effective unless positioned in a medium to long-term cooperation framework. In this sense, consistency and continuity in cooperation are essential factors for bilateral cooperation. There are also two other considerations important for Japan to bear in mind. First, Japan's ODA covers only a fraction of the total development expenditure required by Pakistan. Second, in order for the development problems facing Pakistan to be addressed once and for all, long-lasting and persistent efforts are required. From these perspectives, Japan has set the following priority areas for its cooperation in accordance with its overall ODA framework.

3.2-1 Cross-cutting issues

In formulating its ODA policy for Pakistan, Japan considers gender, the environment, and governance as cross-cutting issues. In other words, there should be an awareness of these issues in the formulation, processing and implementation of all projects. This awareness should be an integral and institutionalized part of any ODA project, and appropriate consideration should always be given to cross-cutting issues.

Particularly regarding gender, the gender disparity in the area of human development is conspicuous. The ratio of females to males in Pakistan is less than one and women's life expectancy is less than men's. It should be emphasized that gender disparity is an issue that requires urgent amelioration.

Pakistan has recently been faced with the rapid deterioration of the environment, with ongoing pollution of air and drinking water in cities, land degradation, and alarming depletion of natural resources such as ground water and forests. Thus the improvement of the urban environment is an urgent issue. In implementing individual projects, careful consideration also needs to be given to the environment and the participation of local residents.

Concerning governance, Japan's ODA should contribute to the smooth progress of devolution, the upgrading of administrative capabilities, and the maintenance of law and order.

3.2-2 Ensuring human security and human development

3.2-2-1 Improvement of basic education and reduction of various social, economic and other disparities

In order to enhance basic education and reduce disparities caused by regional and socio-economic factors or gender, improving access to basic education and raising the quality of education are essential. Enhancing the capability of district governments, which have now become responsible for education administration as a result of devolution, is also an urgent issue. Priority issues are:

- Provision of quality education (improvement of teacher training and reeducation, the educational environment, including of school luncheon program, etc.)
- Enhancement of administrative functions in education
- Improvement of access to basic education (Expansion of correspondence education and adult literacy education)
- Promotion of secondary education

3.2-2-2 Support for higher education and technical training to promote the expansion of the middle class

In order to promote the expansion of a middle class that possesses the broad vision and social monitoring capacity needed to support a sustainable society, the qualitative improvement of higher education, inadequate addressed till now, is a pressing demand. In addition, based on the “Japanese experience,” the expansion of technical education and skills training at the secondary school level will also contribute to the formation of the middle class by enhancing vocational skills and increasing employability, particularly in the low-income class. Accordingly, the priority issues are:

- Qualitative improvement of higher education
- Expansion of technical education at the secondary level

3.2-2-3 Ensuring access to primary health care, safe water, and sanitation and the reduction of various other disparities

In order to build a sustainable society, making an environment in which people can live without anxiety by providing trouble-free access to health and medical care services and safe water and improvements in sanitation are essential. It is also necessary to reduce disparities in access caused by regional or socio-economic levels or gender

imbalances are a vital factor in efforts to create a sustainable society. To create such a conducive environment, providing primary health care services and ensuring links with secondary health care services, as well as adequate training of health care providers including paramedics and administrators, is also essential. Of equal importance are the stable provision of safe water and improvements in sewerage and the waste management systems. Thus priority issues are:

3.2-2-3-1 Ensuring primary health care services

- Ensuring access to health care services in rural areas
- Training of health care providers
- Reduction of regional disparities in primary health care and improving links with secondary health care services

3.2-2-3-2 Provision of safe water and improvement of sanitation

- Improvement of waterworks facilities
- Improvement of sewage and waste management

3.2-3 Development of a sound market economy

3.2-3-1 Expansion of labor absorption capacity and development of the agricultural and rural sectors to reduce poverty

Considering sector-wise employment elasticity and trends, it is most likely that agricultural and rural sectors could assume a major responsibility in absorbing increases in the population and labour force, at least in the short and medium term. It is for this reason that the development of the agricultural and rural sectors is a high priority issue from the perspective of employment policy and poverty reduction. The policy measures that should be undertaken for this purpose include the securing of water resources and the maintenance of irrigation facilities to improve agricultural productivity, the preservation and rehabilitation of forests which helps the sustainable development of agriculture and rural districts, the improvement of income for farm households through extension of agricultural technology, and the creation of employment for non-farm households which make up close to half of the rural population. Priority issues are as follows.

- Securing of irrigation water resources, rehabilitation of irrigation facilities, and

sustainable water utilization and management

- Improvement of the agricultural technology extension system
- Promotion of agro-processing and agro-based industries (including forestry and fisheries industries)

3.2-3-2 Ensuring sound development of a market economy and promoting the diversification of industries

The maintenance of law and order is a prerequisite for the healthy growth of a market economy and diversification of industry, together with other systemic improvements such as deregulation and control of the black market economy, etc. All of these are important elements for the improvement of the investment climate. The development of industries other than the cotton textile industry and the further expansion of export-oriented SMEs are also desirable. Priority areas are as follows:

- Improvement of production management and quality control of export-oriented businesses and SMEs
- Fostering of the information and communications industry and expansion of distribution infrastructure
- Improvements in basic financial and systemic conditions for promoting industrial diversification (including maintenance of law and order, policies for attracting foreign direct investment, and control of the black market economy)

3.2-3-3 Development of economic infrastructure to support the activation of a market economy and the reduction of poverty

The development of secondary and tertiary industries forms the nucleus of economic growth in the long-run and through the creation of national wealth can also be expected to contribute to poverty reduction. However, to enable this development, the improvement of economic infrastructure, which provides the run-way for “take-off”, and the continuous maintenance and management of this infrastructure are essential. In this area, Japan’s experience and expertise are highly appreciated by Pakistan. Accordingly, priority issues are as follows:

- Development and upgrading of infrastructure to improve the living conditions of the poor and to provide better access to public services and markets
- Efficient development of infrastructure and the sustainable utilization and

maintenance of that infrastructure, accompanied by improvements in administrative policy and systems and the strengthening of relevant organizations

- Improvement of infrastructure that will contribute to the development of neighboring countries, in view of Pakistan's position as a gateway to Central Asia

3.2-4 Achievement of balanced regional socio-economic development

3.2-4-1 Expansion of public investment to provide externalities to private sector investment that will lead to the development of underdeveloped regions

The presence of large regional disparities creates obstacles for social stability. Pakistan recognized this reality with the spread of international security problems after September 11. From this perspective, the leading role public investment plays in developing underdeveloped regions is very important. Accordingly, a priority issue is:

- Expansion of public investment which provide externalities to private sector investment to contribute to the comprehensive development of the underdeveloped areas extending west from the Indus River to the border with Afghanistan

3.2-4-2 Development of attractive regional economic centers

To date, Punjab has attracted the lion's share of development efforts by the Government of Pakistan. However, there is every expectation that the economic vitalization of Karachi, Pakistan's metropolitan city and economic hub, can be the multiplier for stimulating Pakistan's economic growth, including Punjab.

Moreover, the fostering of the Peshawar economic zone, including the Federally Administered Tribal Areas (FATA) of N.W.F.P. will contribute to poverty reduction and, at the same time, the maintenance of law and order and the control of the black market economy. The priority issues are:

- Vitalization of Karachi as a leading economic center of Pakistan.
- Development of Peshawar economic zone including FATA.

3.3 Considerations in the Implementation of ODA

3.3-1 Urging weapons disarmament and non-proliferation

When Japan discontinued its economic measures in 2001, it was made clear that it would consider taking appropriate actions, including restoring of the discontinued measures, if the situation regarding nuclear non-proliferation were to deteriorate. Since

then, Japan has been strongly urging Pakistan to move forward with disarmament and non-proliferation of nuclear weapons and other weapons of mass destruction and their means of delivery, including calling on Pakistan to maintain the moratorium on nuclear testing and to strengthen controls on nuclear exports, to become a State Party to the NPT and to sign and ratify the CTBT. Japan will continue to observe closely Pakistan's responses to these calls. In 2004, information concerning the outflow of nuclear-related material, equipment and technology from Pakistan by Pakistani scientists emerged. This incident could pose significant implication on the security of Japan, and has prompted Japan to urge Pakistan to provide more information concerning the incident and to strengthen its efforts for nuclear non-proliferation. Japan has since been closely monitoring Pakistan's responses in this respect and will continue to do so. Japan will consider active assistance for Pakistan's efforts toward enhancing the framework for nuclear non-proliferation including controls on nuclear exports. Moreover, in order to raise Pakistan's awareness and understanding of the main principles of Japan's ODA Charter, Japan will use various opportunities, including policy discussions on the provision of assistance, to raise these concerns. From the perspective of maintaining and strengthening international peace and security through the prevention of terrorism and the proliferation of weapons of mass destruction and their means of delivery, Japan also pays close attention to Pakistan's military expenditures, development and production of weapons of mass destruction and ballistic missiles, and export and import of weapons.

3.3-2 Collaboration with other bilateral and multilateral donor agencies

In Pakistan assistance coordination meetings are held on a regular basis among donors for each sector. For the past several years, open discussions have also been held between the donor side and Pakistan at the Pakistan Development Forum and at other similar fora. Japan believes it is essential to continue to participate actively in these discussions and to extend mutually complementary assistance through aid coordination with the various donor organizations. Moreover, in addition to close cooperation with international organizations, it is important to place further emphasis on cooperation with other donor countries that are playing a significant role in Pakistan.

It is important for Japan to keep encouraging the Government of Pakistan to maintain and adhere to the comprehensive and consistent development strategy which is contained in the PRSP. Japan, together with other donors, should also consider

necessary assistance to Pakistan so that the development strategy can be implemented effectively.

3.3-3 Collaboration with international and local NGOs

At present over 20 international NGOs are providing highly reliable services in Pakistan, and even among the diverse numbers of local NGOs, there are some groups capable of providing services in place of the government in specific regions. In 1999 the Pakistan Poverty Alleviation Fund was established to fund NGO projects, and NGOs are being clearly recognized as new pillars of development. Moreover, many donors are actively utilizing NGOs as a means of extending the benefits of development at the grassroots level. Collaboration between donors and NGOs is being strengthened in many fields, and Japan's increase in recent years of its grassroots and human security grant aid exemplifies this trend. In the future, further collaboration with NGOs will be sought, through project commissioning or assistance to NGOs with extensive experience in specific fields as a means of further clarifying and enhancing the effectiveness of assistance.

3.3-4 Strengthening of Japan's system of ODA implementation

Japan's ODA is carried out under a complex system, in which several relevant organizations, including the Japanese embassy, Japan International Cooperation Agency (JICA) and Japan Bank for International Cooperation (JBIC), and also the Japan External Trade Organization (JETRO) (for cooperation and assistance in the private sector) participate through their respective cooperation schemes. Although Japan's ODA system can widely address an extensive range of needs, it has been pointed out that more systematic coordination among the respective agencies is required to make the aggregate impact of Japan's ODA more pronounced. In response to this demand, Japan has now established a local ODA Task Force in Islamabad in which regular and close exchanges of views can be held and better coordination realized among the Japanese embassy, JICA, JBIC and JETRO. Japan will also promptly move to improve and strengthen local implementing capabilities, including increasing the number of relevant staff, as the scale of Japan's ODA to Pakistan increases.

3.3-5 Enhancement of Pakistan's capacity and effectiveness to receive ODA

In Pakistan the implementation of ODA based on a longer-term perspective has been impeded by factors related to political instability, discontinuity of policies and the deterioration of law and order and security. Moreover, inefficient administrative structures, delays in decision-making due to the centralization of authority, and other inadequacies in ODA executing capabilities hamper the smooth implementation of ODA. Indeed the period during which economic measures were in place due to Pakistan's nuclear testing, awareness and understanding of the modalities and procedures related to Japan's ODA further deteriorated. In the future, effectively raising the implementing capabilities of the Pakistani side, including improving the coordination between financial cooperation and technical cooperation, will be an important step for facilitating the implementation of Japan's ODA. In addition to making the best use of Pakistan's human resources and linking Japan's ODA with other donors, it will also be of paramount importance to more actively utilize the network of Pakistan nationals who have received training in Japan through the various training schemes implemented by the Japanese government to date, and who therefore have a good understanding of both Japan and Pakistan.

3.3-6 Improvement of publicity operations

Japan has extended significant cooperation in a variety of fields to date, but in view of the fact that not only Japan but also other donors have extended full-fledged cooperation to Pakistan and are making efforts to further expand it, concerted efforts must be made to elevate the presence and visibility of Japan's ODA. For this, while some of the independent publicizing activities implemented by the Japanese embassy, JICA, and JBIC may be left to continue, coordination among concerned agencies should be given priority so as to more effectively demonstrate Japan's ODA measures. Second, efforts should be made to diversify the dissemination of information, making use of not only the mass media but also publicity information through local communities and the Japanese community. Third, an effort to add more accountability to these publicity activities should be made.

3.3-7 Introduction of an ODA monitoring system

This Country Assistance Program outlined above, covers approximately a five-year period. In order to ensure its effective and efficient cooperation, a verification system

for the program will be established. The local ODA Task Force will examine and verify the implementation of this program through policy discussions, focusing on the formulation and implementation of individual projects in each priority sector and the special considerations regarding implementation described earlier. The results of this verification will constitute an important input when the Country Assistance Program is reviewed.

Japan's Country Assistance Program for Pakistan: Goals and Directions Matrix

Assistance Goals	Directions of Assistance Strategy		Priority Issues for Economic Cooperation		Areas	
Construction and Development of a Sustainable Society	Ensuring human security and human development	Improvement of basic education and reduction of various social, economic and other disparities	• Provision of quality education (improvement of teacher training and reeducation, the educational environment, including of school luncheon program, etc.)		Social Sectors (Education, Health, Waterworks and Sewage Facilities)	
			• Enhancement of administrative functions in education			
			• Improvement of access to basic education (Expansion of correspondence education and adult literacy education)			
			• Promotion of secondary education			
		Support for higher education and technical training to promote the expansion of the middle class	• Qualitative improvement of higher education			
			• Expansion of technical education at the secondary level			
	Ensuring access to primary health care, safe water, and sanitation and the reduction of various other disparities	Ensuring primary health care services	• Ensuring access to health care services in rural areas			
			• Training of health care providers			
		Provision of safe water and improvement of sanitation	• Reduction of regional disparities in primary health care and improving links with secondary health care services			
			• Improvement of waterworks facilities			
			• Improvement of sewage and waste management			
	Development of a sound market economy	Expansion of labor absorption capacity and development of the agricultural and rural sectors to reduce poverty	• Securing of irrigation water resources, rehabilitation of irrigation facilities, and sustainable water utilization and management		Agriculture/Irrigation	Gender Environment Governance
			• Improvement of the agricultural technology extension system			
			• Promotion of agro-processing and agro-based industries (including forestry and fisheries industries)			
		Ensuring sound development of a market economy and promoting the diversification of industries	• Improvement of production management and quality control of export-oriented businesses and SMEs		Investment/Industry	
			• Fostering of the information and communications industry and expansion of distribution infrastructure			
• Improvements in basic financial and systemic conditions for promoting industrial diversification (including maintenance of law and order, policies for attracting foreign direct investment, and control of the black market economy)			Economic infrastructure			
• Development and upgrading of infrastructure to improve the living conditions of the poor and to provide better access to public services and markets						
Development of economic infrastructure to support the activation of a market economy and the reduction of poverty		• Efficient development of infrastructure and the sustainable utilization and maintenance of that infrastructure, accompanied by improvements in administrative policy and systems and the strengthening of relevant organizations				
		• Improvement of infrastructure that will contribute to the development of neighboring countries, in view of Pakistan's position as a gateway to Central Asia				
Achievement of balanced regional socioeconomic growth	Expansion of public investment to provide externalities to private sector investment that will lead to the development of underdeveloped regions	• Expansion of public investment which provide externalities to private sector investment to contribute to the comprehensive development of the underdeveloped areas extending west from the Indus River to the border with Afghanistan		Comprehensive regional development		
		• Vitalization of Karachi as a leading economic center of Pakistan				
	Development of attractive regional economic centers		• Development of Peshawar economic zone including FATA.			

* Priority areas: social sector, agriculture/irrigation, economic infrastructure, investment/industry, comprehensive regional development

* Cross sectoral issues: gender, environment, governance