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Examining the potential and limits of subnational empowerment

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Dedicated to the loving memories of my father

**Shahid Mahmood
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CHAPTER 1

DECENTRALIZATION, DEMOCRACY AND DEVELOPMENT:

OVERVIEW OF THE RESEARCH

As the discourse on economic development has expanded its focus to a broader set of interrelated economic, social, and political variables, an important conclusion has been that sustainable and inclusive development requires not only economic and social policies, but also political empowerment to foster a deliberative and participatory development process. The state versus market led development debate has been increasingly conducive to the role of state since 1990s mainly due to the developmental state experiences in East Asia in particular, and the high social costs of pursuing market oriented reforms or Structural Adjustment Programs in many developing countries across Latin America, South Asia in particular under the Washington Consensus during the 1980s and 1990s (Williamson, 1990)¹. The growth spurts and the successive downturns delivered little on account of sustainable and inclusive growth.

The nature of an ideal state, in contemporary times, can be argued to be developmental and democratic; characterized by redistributive growth, broad-based participation, pro-poor policies, and responsiveness of public policy to local needs (Robinson & White, 1998). Furthermore, given the intricacies of the contemporary world where Keynesian and neo-liberal values contest for space simultaneously, the (re)configuration of the role of the state while fostering democratization is an important dimension to consider. In this context, it is increasingly argued that subnational democracy² is important in revitalizing and reinvigorating democratic systems, as well as promoting better public governance (Blokker, 2012).

¹ While the impetus for structural reforms came against the backdrop of globalization and the fiscal crisis (mainly the Latin American), the nature and nomenclature of these reforms remained largely the domain of the multilateral institutions, led by the World Bank and the IMF. The SAPs and other similar market oriented reforms initiated in this period were more targeted at liberalizing and promoting efficiency of markets rather than initiate a public sector reform/ state reform. The resurgence of interest in the state's role in the economy was reflected in the World Bank's 1997 World Development Report, where it stated that "the state is central to economic and social development, not as a direct provider of growth but as a partner, catalyst, and facilitator" (p.1); and that "the determining factor behind...contrasting developments (among regions) is the effectiveness of the state". The idea that subsequently took root was that reconciling the role of the state with its capacity to effectively deliver on its responsibilities (primarily through reinvigorating and reforming public institutions) was an important condition for sustained and inclusive socio-economic development.

² Subnational, in this research refers to both second (Provinces and Regions) and third (municipalities and local tiers of governments).

Nurturing democratic governance at the subnational levels has long been advocated as a strategy to not only foster democratization but also improved public management primarily in the realms of public service delivery, responsiveness of the public policies to local needs and accountability structures. In the context of subnational democracy and bringing governance structures to subnational space, decentralization emerges as one of the key reforms that reduces the concentration of power in general, by “fragmenting central authority and fostering greater intergovernmental competition, accountability and participation to make the public governance more effective, efficient and responsive” (P. K. Bardhan & Mookherjee, 2006)³. The World Bank (2006), for instance, highlights the importance of ‘empowerment through participation’, and asserts that while participation is a desirable outcome in its own right, it can also promote more just and efficient development outcomes. This increasing relevance of decentralization of economic and political authority to subnational levels also finds its roots in the changing global dynamics. The changing nature of the central state vis-à-vis growing supranational linkages under the global governance mandate, has made the role of the central governments as the ‘guardians of national sovereignty’ questionable and reinforced the democratic legitimacy of the subnational authorities (Kahler & Lake, 2012).

Decentralization of governance has been a key reform agenda, especially in the developing economies since the 1980s. While the advocacy in favor of decentralizing governance and public decision space, extols the benefits reaped through greater responsiveness, accountability, efficiency and a deliberative institutional framework (Crook & Manor, 1998; Heller, 2001); the empirical evidence in support of it remains mixed, at best.⁴

Amidst all the contrasting theories and results, the idea of decentralization as a key governance and public sector reform tool still dominates much of the academic and policy discourse. Given the ‘heterogeneity’ of form and impact surrounding decentralization and its

³ The main thrust is not to weaken central authority but to nurture subservient tiers government at local level that are more responsive to the needs of core constituents. Most of the arguments for decentralization focus on efficiency, especially on the comparative advantages of scale, information and accountability that come with having the proximity of the government to its constituents.

⁴ For instance, decision-making competence and resources to the local levels has been recorded to result in “local predatory capture”, i.e. a strengthening of prevailing networks of corruption, patronage and the rule of local influential circles, thus weakening state capacity and inhibiting democratization (Blair, 2000; Migdal, 1988). On the contrary, there are also instances where well-functioning local systems of governance have taken roots despite the structural adversities; infrastructural constraints, clientelism and corruption, low socio-economic development. (Ostrom, 1990, 2009; Tendler, 1998; Uphoff & Committee, 1986)

effect on facilitating a participatory development process (possessing both democratic as well as developmental attributes), this research aims to contribute to the debate by focusing on its political determinants by examining how the nature and content of the decentralization reform process, problems of incentive compatibility of the agents involved in the process, and the unique political, socio-economic and institutional factors in the design affect the scope for realizing effective decentralization to local tiers of government.

The developmental and democratic dimensions can also be conceptually located in the much advocated notion of ‘participatory development’. In addition to exploring the theoretical constructs on decentralization and its nexus with a participatory development process that encapsulates both democratization as well as developmental aspects, this research also engages in an empirical analysis of these dimensions in two contexts, Bolivia and Pakistan.

This chapter seeks to serve as an introduction to this research by putting forth a conceptual overview and the analytical parameters within which the research shall operate. The first section deals exclusively with a brief overview of decentralization and the developmental potential of subnational empowerment, including the role of the political dynamics governing decentralization reforms.

The second section pertains to the focus of enquiry of the dissertation, giving an expansive overview of the key questions this research endeavors to address, the sequential aspects of decentralization and the extent to which the ordinal prioritization of the forms change the nature of the reform outcomes. The ordinal prioritization deals with the fiscal, administrative and political forms of decentralization, and how these forms are ordered in succession as a consequence of interest articulation, contestation and bargaining procedures. In the analysis of the bargaining and contestation dynamics, a game theoretical model will be presented.

The final section of this chapter deals with the contexts chosen for exclusive case analysis, the periods across which the reform trajectories will be studied and finally the broader research methodology. It would, however, be pertinent to mention that while the case analysis remains centered around two contexts to reap the advantage of a Small-N study setting, it would still include various other contexts in its scope of analysis, albeit to a limited detail.

1.1 CONCEPTUAL AND ANALYTICAL OVERVIEW

Decentralization has lent itself to various conceptualizations and definitions, however, this research adopts its elucidation as “the process through which the central government transfers

responsibilities and political power to the state institutions closer to the population, granting them administrative independence and political legitimacy so that, with popular participation, the production of goods and services can be improved” (Oxhorn, Tulchin,& Selee, 2004). These policies have changed governance and political economy in fundamental ways, which amongst other examples is best manifested by an increasing share of subnational fiscal contribution around the world. This subnational allocation of fiscal resources and the discretion over their absorption has had a sizeable macroeconomic impact in some contexts⁵. This has also resulted in the delegation of key public services like education, health, social safety and poverty alleviation programs amongst others, to the subnational governments that are now responsible for their funding, delivery, management and quality (P. K. Bardhan & Mookherjee, 2006; Faguet, 1997). The most common advocacy in favor of decentralization reforms is that the proximity of the subnational governments (regional and local) to the broader citizenry enables greater responsiveness of service delivery and accountability; consistent with the ‘principle of subsidiarity’(Oates, 1999). There are various motivations behind the initiation of decentralization reforms that span across political, economic, social and in some cases even externally stipulated requisites. Table 1, provides an overview of some of the regions/countries undertaking these reforms and the underlying motivations.

From a normative standpoint, decentralization also brings government closer to the people. The existence of local political arenas makes it easier for ordinary citizens to participate and exert influence (P. Bardhan, 2005; Blair, 2000; Manor, 1999). Furthermore, the proximity of the incumbents to the constituents ensures greater accountability in a counter democracy fashion (Rosanvallon & Goldhammer, 2008); which pertains to a broader forum for the citizens for interest articulation and deliberation. Creating formal political forums in the local or more broadly subnational space, is also considered to be beneficial to pluralization of the political space and deconcentration of powers; a potent reform in the contexts characterized by elite capture (Hadenius, 2003). Decentralized governance structures are also argued to be more responsive to the local demands compared to a distant central level agency, which in most cases are central bureaucracies that may enjoy scale advantages but lack informational advantages. The scale

⁵ Calculations based on IMF Government Finance Statistics (GFS), reveal that the in 1980 the share of subnational revenues and expenditures was 14.9% and 19% respectively. By 1999, the share of subnational revenues and expenditures had increased to 23% and 30% respectively. Dataset can be viewed at : <http://www1.worldbank.org/publicsector/decentralization/fiscalindicators.htm>

advantage that centralized delivery of public services enjoy may make it more ‘productively’ efficient, but localized provision can have allocative efficiencies because of increased responsiveness to the needs and preferences of the local constituencies enabled by the information advantages. Another advantage of decentralized governance systems could be the potential of micro-level policy experimentation and innovation in individual subnational jurisdictions that could be potentially scaled up to national levels or just replicated horizontally across other subnational jurisdictions (Crook & Manor, 1998; Manor, 1999; Oates, 1999).

| | |
|---|---|
| Political and Economic Transformation | Central and Eastern Europe, Russia |
| Political Crisis due to ethnic conflict | Bosnia-Herzegovina, Ethiopia, Yugoslavia, Nigeria, Sri Lanka, South Africa, Philippines |
| Political Crisis due to regional conflicts | Indonesia, Madagascar, Mali, Senegal, Uganda, Mexico, Philippines |
| Enhancing participation | Argentina, Brazil, Bolivia, Colombia, India, Pakistan, Philippines |
| Accessionary Conditionalities (EU) | Czech Republic, Slovakia, Hungary, Poland, Slovenia, Croatia |
| Political Maneuvering | Peru, Pakistan |
| Fiscal Crisis | Russia, Indonesia, Pakistan |
| Improving Service Delivery | Chile, Uganda, Cote D’Ivoire |
| Shifting Deficits Downwards | Eastern and Central Europe, Russia |
| Shifting Responsibility for Unpopular Adjustment Programs | Africa |
| Prevent return to autocracy | Latin America |
| Preservation of Communist Institutional Legacy | China |
| Globalization and Information Revolution | Most Countries |
| Source: Shah and Thompson (2004) | |

Regardless of what the guiding impulse may be, decentralization reforms remain critically dependent on the political and institutional environment of the context they are introduced in. The main impulses for decentralization include democratization, development, and public service delivery improvements (efficiency and equity oriented improvements). However, there are other context-specific political and institutional factors that are even more influential in the design and implementation of the reforms. This also happens to be a factor commonly acknowledged but not evaluated as critically as it beckons, in the existing literature. This research explores this void to

critically evaluate and study the role of political incentives and governing dynamics in the design and outcome of the decentralization.

The recurring theme in most discussions and literature on decentralization is that it (like most generalized policy narratives) is no panacea for development policy. With a disaggregated governance and political structure, the political actors have a relatively diminished desire to pursue coherent and unified national policies, and find it of a greater providence to remain limited to their local constituencies. This has adverse implications on inter-regional equalization, uniform distribution of public services and uniform upholding of citizen rights – paradoxically, making a potent argument in favor of a greater centralization of political and administrative structures. From the governance perspective, there are various instances where decentralized state edifice has adversely affected an optimal exercise of political and administrative authority.

For instance, in some cases in South Asia, where corruption, mismanagement and patronage has deepened simultaneously with localized politics (P. K. Bardhan & Mookherjee, 2006). This adverse impact naturally has a similar bearing on the public sector efficiency, which in turn relays on the negative effects to the welfare of a country's citizens and also deepens clientelism. In the contexts already rife with clientelism, any attempt at decentralizing political or administrative functions would have a greater chance of inhibiting effective grass roots participation, and mostly replicate the 'elite capture' at the subnational levels (Hadenius, 1992; Hadenius & Teorell, 2007). As a consequence, the reforms deliver the exact contrary of what they are envisaged to – limiting democratic quality, weakening state capacity and reinforcing elite capture over the extended authority and resource pools. The idea of decentralization has also been a subject of intense debate on the structure and scope of the government at each level. This emanates mainly from the common criticism of an expanded centralized apparatus on the lines of inability, ineffectiveness, clientelism and political alienation, all considered "...as the natural by-products of a bureaucracy distant in space and rendered insensitive, inefficient, and inflexible by its size" (Williamson, 1995). As specified earlier, there is considerable heterogeneity surrounding the concept of decentralization that spans across both the form as well as the impact it delivers. One main explanation of the heterogeneity of form, and thus impact, of decentralization reforms has been the lack of consistency between the envisaged public policy goals and the diverging objectives and/or incentives of the political and bureaucratic players (Kaiser, Eaton, & Smoke, 2010).

This is largely due to the nature of the central governments who are responsible for the development and implementation of the decentralization reforms. Since they are not monolithic entities and often a coalition of different political parties, the homogeneity of their preferences and plurality of interests of the coalition members impairs the ability of the government to develop a policy mix and its consistent implementation. Furthermore, since the implementation of the reforms and their sequence remains largely a prerogative of the central authorities, it is imperative to consider what motivates the political actors at the central level to willingly relinquish and devolve their authorities to subnational levels which may or may not be conducive to their objectives.

Based on a review of literature and existing debates on decentralization reforms that will be covered in detail in the later chapters, this research identifies two main determinants of the effectiveness and potential for decentralization reforms to deliver on the developmental and the democratic dimensions:

1. Incentives of the Actors/ Agents involved
2. Sequencing of the Decentralization Reform

Incentives of Actors / Agents involved

One of the ways to interpret and operationalize the incentives of the political actors is the Political Economy Analysis Framework developed by Kaiser, Eaton,& Smoke (2010), where three forms of incentives for the political actors are identified: i) Electoral, ii) Partisan, and iii) Institutional. While this framework puts these three incentives forward as the broad classifications, their incidence varies in extent and nature across the contexts. These incentives are not of uniform salience across all contexts and are rooted in the specific characteristics of the contexts as well. The importance of this framework in the context of this research is only to interpret and operationalize the main generalizable forms of incentives that exist for the actors involved in the design and implementation of the decentralization reforms.

Electoral incentives, for instance, are of a higher significance in the contexts characterized by relatively consolidated democratic systems. Even in contexts not characterized by consolidation, but instead transition, the core impulse remains resorting to electoral mechanisms to determine incumbency of public office in subnational space. This makes it imperative to consider the central political agents' incentives of using the subnational space to further their own strategic ambitions of securing/reinforcing gains at the centre. The introduction of electoral institutions in the local/

subnational space finds its roots in Huntington's '*third wave of democracy*' (Huntington, 1991). The idea behind supporting a process of successive and regular sub-national elections remains the liberalization of political space in general while also enhancing the possibility of plurality (in terms of the variety of political parties that assume the offices) in the subnational and central governments. This is a critical factor as it reduces the prospective rent-seeking and perversion that accompanies a central tendency to retain sub-national appointments as its exclusive domain.

As a product of these electoral systems, there is also an enhanced scope of the sub-national officials to utilize their individual mandates as well as pushing for a greater pool of resources and authority in a bottoms-up approach (Agarwal, 1999). Backed with electoral legitimacy, local governments can thus have a high influence over the traditional power structures at the local/subnational level (Burki, Perry, & Dillinger, 1999). Evidence of the aforementioned has been recorded in various cases. For example, in the case of Mexico, the plummeting public support of the incumbent political party (Institutional Reform Party|PRI) compelled it to acknowledge the of an opposition party (Party of Democratic Revolution|PRD) in the subnational elections in 1988. The PRD in turn used its newfound bargaining power to campaign for greater decentralization and winning the subsequent round of national elections due to a significantly higher consolidation of their voting base⁶. What this case also signifies is that with greater plurality and strong accountable regional governments, the central government may also be deterred in dominating the inter-governmental arrangements with the fear of 'nonconformist' potential that such regional governments hold.

Another potential pitfall to local governance reforms remains the pervasive strategic gameplay by the central political agents in the local space, where the privileges of incumbency enable them to unfairly support their own candidates in the subnational electoral rounds. Such behavior by the central government deepens the sub-optimality of the governance structures and nullifying the 'inclusive' dimension of political decentralization by sustaining the elite networks and hegemony of the central actors. An example of this can be found, especially in the case of Bolivia and Pakistan amongst others. In Bolivia, the MNR (National Revolutionary Movement / Movimiento Nacionalista Revolucionario) emerged victorious, albeit with a realization that their tenure would be short-lived because of a coalition presidency. Given its stable, significant support base and better organization at the

⁶ For more on the Mexican experience, see *Beer, Caroline. 2004. "Electoral Competition and Fiscal Decentralization* in *Decentralization and Democracy in Latin America* (eds.) Alfred P. Montero and David J.Samuel

subnational level, the MNR leaders endorsed a bold approach to decentralization under the 1994 Ley di Participación Popular (LPP)⁷.

Even before elections (subnational and/or national) are held, the expectations of the political actors of the electoral outcomes modify their preferences related to decentralization reforms. These are of particular importance in the context of managed political transitions from limited to greater democracy where the final victors and losers remain uncertain (Smith, 2008). The incentive-maximizing behavior then leads the political actors to evaluate their prospects ex-ante of the formal electoral rounds. Where a prior convention of competitive subnational elections existed, the central policy has been to roll it back and institute new electoral rounds under new rules or modalities that favor the incumbents in the centre. The guiding rationale remains rather intuitive: neutralize and dilute political opposition from the established interests at the subnational levels, and once this had been achieved, initiate a reform process that substantially empowers the subnational governments, most of whom comprise of actors with compatible interests to the centre. The case of Pakistan illustrates this trend. Every time an autocratic/ non-representative military regime overtook the government; major decentralization reforms were initiated to dislodge the entrenched support bases of the political parties. An interesting paradox that is thus observed in most developing countries is that authoritarian/ non-democratic regimes can be the source of substantive decentralization reforms, even though they are high on administrative and fiscal, but low on the political decentralization.

The next sets of incentives according to the PEA Framework are **partisan incentives**. Where political parties remain a primary platform to access any political office, the internal stance(s) of the party on such reforms is linked to the party structure as well as the nature and extent of competition within the party/(ies). Furthermore, one must also pay attention to whether the political capital of the involved parties is concentrated in specific subnational/ regional levels or distributed nationally. In the case of the former, decentralization may as well encourage or pose higher risks of ethnic conflict and secessionist tendencies (Brancati, 2006).

Furthermore, to gauge the support in favor of decentralization it is important to see the nature of political parties and whether the national or the regional preferential outlook dominates their political stance(s). This is an important factor as the contexts where the legislators or members of a political party had a more subnational/regional orientation instead of a structurally guided support to the national party leadership, the support to decentralization reforms is much higher (Willis, Haggard, & Garman, 1999). The direction of authority flow within the party (upwards to a central party

⁷ Chapter 3 engages with this in a greater detail

leadership or downwards to the broader party base) as well as the nature of the political party (personality-dominated/patronage based or a more participatory one), are important points to consider to gauge the extent to which effective decentralization reforms will be pursued. In contexts where the political space is not too pluralized, and is dominated by a single party, the overarching objective of any decentralization reform is to predominantly secure the interests of central leadership, leaving less space for the regional and pluralized interest articulation or representation. A related factor may also be the existing **institutional arrangements** in terms of national/subnational functional and fiscal authority distribution. While this in itself is linked to some level of decentralization already existing in the constitutional or functional modalities of the state apparatus, it has strong implications for the structures of the political parties as well. If these institutional mechanisms and functional modalities envisage a stronger subnational state, there is thus a greater impulse for a more participatory structure within the political parties and a dilution of central leadership's ability to coerce its own reinforcement from its party base. Sabatini (2003) presents an argument correlating (causally oriented) the degree of fiscal decentralization and the nature of the political parties across chosen contexts.

The main argument posits that where there is a greater fiscal centralization, the party systems are also more centralized and where there is a greater fiscal decentralization, the party systems are also more participatory and pluralized. This is more recently partially observed in the case of Pakistan, where post 18th Constitutional Amendment the provinces have been devolved a greater share of the administrative and fiscal responsibilities, leading to a greater subnational/provincial bargaining power vis-à-vis the centre. However, this has still not resulted in any substantive and observable shift in the political party organization as the leading parties like the PML-N, PPP, JUI-F who continue to be minimally institutionalized and remain a subject to a narrow central party leadership.

While the preceding discussion extolled the incentives present within the structure of a political party, there are also contrasting incentives in the broader political space and between the political parties. The discussion on how political parties deliberate and mediate with each other for/against decentralization is also an important variable in ascertaining how the envisaged decentralization reforms shall span out. Critical in this regard is to see the extent to which the political parties in a given political context vary in terms of their Institutionalization, Polarization and Fragmentation (Kaiser, Eaton, & Smoke, 2010). Institutionalization refers to the extent to which a political party exists with an identity of its own instead of being subservient to an individual party leader, and is rooted in the society it seeks to represent. Polarization refers to ideological divides between parties and the extent to which each political party bases its courses of actions according to its own manifesto. Fragmentation

pertains to the plurality of the political space in terms of the number of formal political parties catering to heterogeneous social groups. Any analysis of the extent to which the inter-party negotiations over the design and implementation of reforms in general (and decentralization in particular) needs to consider all of these elements.

The higher the fragmentation of the political space, the higher would the heterogeneity of political interests, and more so if there is a degree of polarization that also accompanies. In the contexts characterized by a higher degree of polarization, any consensus decision-making is arduous if each political party is credibly committed to its ideological stance. In the contexts characterized by greater fragmentation, the incentive maximization amid competition will be crucial in determining the design, rollout and implementation of the decentralization reforms, to ensure at the very least, a minimal common benefit. This can again be observed in the case of Pakistan, where decentralization reforms have frequently been a divisive issue between the political parties 2001 and 2012, and the delay in any further provincial to local decentralization can be largely attributed to the absence of a mutually beneficial arrangement between the political parties. In addition to the partisan and electoral dynamics, the PEA framework also identifies institutional incentives as major determinants of the trajectory and outcome of decentralization reforms.

According to Kaiser, Eaton, & Smoke (2010), regardless of the nature of the regime (autocratic, partially democratic or effectively democratic), the central incumbents will have strong incentives to preserve the influence of the central institutions. This is not necessarily an unwarranted and villainous pursuit by the centre, since it has the mandate of being the guarantor of the constituent entities' equality as well as being the unanimously agreed upon mediator of diverse subnational articulation. Not conceding too much of the central institutional influence and mandate to subnational levels remains an important imperative for a state resilience and cohesion. The problem is when such preservation is guided more by narrower political concerns by the central actors who may consider their 'wings clipped' with fewer instruments at their disposal to further their political agenda.

Sequencing of Decentralization Reforms

The second main determinant of potent and effective decentralization reforms is the *sequencing*. While this has also been highlighted in the framework discussed earlier, the importance of sequencing in decentralization was introduced by Falletti (2010), in a stark departure from the earlier norm of advocating a 'big-bang' decentralization reform that involved a rollout of all forms simultaneously or a form of decentralization (political, administrative, or fiscal) in a distinct and

disconnected manner. The sequential approach does not require the simultaneous approach to be applied across the three forms, necessarily. The sequencing patterns are the also of interest to political actors who are wary of relinquishing political control. The sequencing trajectories can be designed in any way; for example, instituting administrative decentralization in the absence of fiscal decentralization is bound to have limited success, or a political decentralization without any administrative and fiscal decentralization would largely be illusionary than anything else. There are cases when the central government does decentralize, albeit in a clientilistic manner and regional governments are elected in their own right, but these regional incumbents are constrained in the use of their incumbency e.g. Pakistan under the LGO 2001 during the Musharraf regime. Each of the possible trajectories results in the varying levels of regional government authority and autonomy.

The main idea of this put forth by Falleti (2010) is that there are distinct sequential preferences of the national and subnational actors. These preferences are discussed in a greater detail in the subsequent section. The sequential theory of decentralization remains the central analytical framework for this research as it enables an analysis of which level's interests (central or subnational) would dominate the decentralization reforms; thus helping explain the extent to which the decentralization reforms have actually yielded genuine subnational empowerment.

The sequential theory of decentralization put forth by Falleti (2010) considers the three main forms of decentralization:

a) Political:

Constitutional or electoral reforms designed to decentralize political authority to subnational actors (regional/provincial and local/provincial), with the intent of enhancing political participation and formal subnational political institutions.

b) Administrative:

Devolution of service delivery obligations and functions to subnational governments

c) Fiscal:

Decentralization of financial resources and discretion over their use to subnational governments.

How each of these types of decentralization fares individually and interactively can yield multiple degrees of empowerment for the subnational governments. Administrative decentralization can yield both positive and negative effects on the degree of subnational empowerment. If the decentralization of functions and responsibilities to subnational levels improves subnational administration, fosters skill and capacity building of local officials and bureaucracy once delivering expanded functional

responsibilities; it could improve the policy implementation and broader public governance. However, administrative decentralization alone would be of a limited effect if it is not accompanied by a corresponding devolution of fiscal resources and privileges. In the absence of additional fiscal resources to meet the enhanced functional responsibilities, the degree of subnational empowerment and autonomy would remain limited as the subnational governments would have to rely on the superior levels for fiscal transfers to perform the assigned functions. Furthermore, raising the requisite finance to deliver on their administrative obligations may also be met by soliciting debt finance for which the central government's sponsorship is required.

Similarly, fiscal decentralization can also go both ways. The outcome remains largely contingent on the 'design of the fiscal decentralization' policy (Falletti, 2010). If the fiscal decentralization involves handing down of guaranteed (scale and criteria of which is in turn dependent on inter-governmental institutional arrangements that take account of regional needs and their contributions to the central pool) transfers from the central exchequer, it would enhance the subnational autonomy over where they can allocate these resources, or in line with regionally responsive policies and priorities. This is also enabled as a result of them not participating in the process and costs of mobilizing those fiscal resources through taxes. The downside to decentralization of revenue collection or subnational resource mobilization functions is the lack of subnational administrative capacities. The revenue base for local/Subregional taxation is limited and to deliver on their obligations, the subnational governments have to seek central handouts or revenue transfers. This could also bolster inter-regional inequality as the relatively affluent (owing to mineral rents, geographical, and/or infrastructural advantages) subnational governments would find it much easier to mobilize the fiscal resources even if constrained by the administrative capacities, vis-à-vis other less affluent regions. This horizontal imbalance would have to be corrected either by vertical transfers (from the central government, which may have absorption conditionalities), or a horizontal redistribution mechanism (fiscal transfers from richer regions to poorer regions, which can be highly contentious). Of the three types, political decentralization will necessarily have a positive effect on empowering the subnational government, primarily because the subnational entities enhance their bargaining power in subsequent negotiations over further types of decentralization.

Politically empowered subnational governments are likely to pressure for higher shares of subnational resources, or greater administrative discretion suiting the preferences of their respective constituencies. It must be noted that political decentralization transcends mere electoral processes at

the subnational level and also pertains to formal institutional support in the form of legal and constitutional provisions that support and foster genuine subnational empowerment.

This sets the grounds for exploring another strand of argument - the nature and content of the decentralization reform is dictated at its outset by the territorial interests of its protagonists. This argument seeks to identify the social and political actors that form the decentralizing coalitions and subsequently classify these actors and the resulting coalitions according to their level (national or subnational) and partisan (ruling or opposition) interests. The preferences of the political actors at each level with regard to the type of decentralization result in distinct outcomes for subnational empowerment and autonomy. A summary of this is presented in Figure 1 below and subsequently discussed:

Figure 1: Mapping the Incentives of National and Subnational Actors

| Main Protagonist | Causal Mechanism | |
|--|--|--|
| | <i>Self-Reinforcing</i> | <i>Reactive</i> |
| National Level <i>Hypothesized Degree of Change</i> | National Dominance Path (A->F->P) <i>HDC:Low</i> | Subnational Response Path (A->P ->F) <i>HDC:Medium</i> |
| Sub-National Level <i>Hypothesized Degree of Change</i> | Subnational Dominance Path (P->F->A) <i>HDC:High</i> | National Response Path (P->A ->F) <i>HDC:Low/Medium</i> |

A: Administrative Decentralization F: Fiscal Decentralization P: Political Decentralization

Source: Falleti [2004, 2010]

The sequential argument furthers the enquiry that most comparative studies of decentralization have not, as their focus remained on the bargaining process at the central level (Eaton, 2008; Garman, Haggard, & Willis, 2001; Kaiser, 2006). This research alludes to the incentive dynamics and preferential mix developed by Falleti (2010) and employs these as the main analytical framework in the subsequent chapters as well as the grounds for selecting the two contexts for case studies.

As presented in Table 2, both tiers of the state governance, i.e. national and subnational (includes both regional/provincial and local/municipal governments), enter the policy discourse with a

view to preserve and/or expand their discretion over their specific jurisdictions. The preferences that each of the two tiers of the state has, is a function of which form of resources enable them to have a greater bargaining power in the post-reform scenario. As per Falleti (2010), central actors place the foremost preference on administrative decentralization, followed by fiscal and least preferred being political decentralization. The underlying idea is that the central government would choose to devolve functions and administrative responsibilities to the subnational levels, and in the event of a subsequent round of reform devolve finances to the subnational levels to deliver on their functional obligations. The fiscal decentralization is resisted in the primary preference mix because the fiscal instruments are used as a bargaining tool to keep the subnational policies consistent with the priorities of the central government. Political decentralization is the least preferred sequence to enable the central actors to retain greater political control over the subnational governments.

Looking at the flip side, the subnational preference set, according to Falleti (2010) is Political, Fiscal and Administrative. The subnational actors prioritize political decentralization for enhanced autonomy and bargaining power in the subsequent reform rounds. Greater political autonomy of subnational governments enables them to pursue issues and concerns of their respective territorial jurisdictions without any preference articulation, distortion, or credible threat of punitive action(s) from the central levels. The secondary preference of the subnational actors remains fiscal decentralization as they would demand access to an expanded fiscal pool at their disposal to deliver on their mandate, contrary to the ‘finance to follow function’ advocacies. An expanded fiscal pool will also enable the subnational governments to be in a better position when choosing which functional responsibilities and service delivery obligations to assume, and build up local delivery capacities in advance of additional functional allocation. It must also be noted that pursuing access to an expanded fiscal pool is not devoid of rent-seeking impulses of the subnational political actors and officials, however, this research keeps this consideration extraneous to the current scope of analysis.

With regard to the dominance and reactive paths as highlighted by the sequential theory, the idea is that the tier (national or subnational) whose interests dominate the first round of reforms will have implications on the subsequent reforms and the preference articulations of all participating actors. The distortive effect of the level dominating the first round of the reform, shall lead to a reactive strategy by the one losing whereby the agenda shall be to wither continue articulating its initial preference sequence or choose the second best strategy. The dominant tier shall continue to pursue same preferential sequence in the subsequent rounds. This is consistent with the *‘ratchet effect’* – continued support to the initial direction/sequence/modalities of a reform as it remains an incentive

maximizing strategy to do so (Huber & Stephens, 2001). Going back to Falleti (2010) framework summarized in Figure 1, sub-national preference domination will deliver political decentralization reform at first. The resulting enhancement in their bargaining power and greater relative autonomy in policy development and implementation shall enable them to pursue access to additional fiscal resources (in line with their ordinal reform preferences). The degree of influence that the subnational actors will have in defining the scale and modalities of the fiscal decentralization shall also be greater, in addition to framing the parameters of administrative (functional) decentralization. The preference mix under the Falleti framework for the central actors is the reverse of the subnational mix discussed above. The first preference of the central actors is, according to this framework, administrative decentralization. The underlying motivations could be that transferring functional responsibilities to subnational levels could yield advantages that localized provision yields (e.g. responsiveness, effectiveness, etc), as well as the central impulse to devolve functional responsibilities as a conditioning mechanism for subsequent fiscal decentralization.

In a *de-facto* sense, the central government has the privilege of stipulating or enacting any structural and institutional change, regardless of where the roots of the primary reform articulation lie. When in addition to this, the central levels also enforce their preference set in the first round of reforms, the logical recourse for subnational actors remains the articulation for greater fiscal resources to deliver on the functional responsibilities assigned to them in the first round. Thus, the primary preference of the subnational agents of gaining greater political autonomy gets relegated to a last pursuit. Political decentralization, when instituted, will not be of any substantive benefit for the subnational levels since most of their institutional capacities and bargaining power has already been tweaked in the preceding reform rounds. However, there is also an element of non-conformity that must be considered, whereby a reactive course by the ‘losers’ of the first round of reform would continue to articulate its primary preferences instead of situationally imperative compliance with the preferences of the ‘winners’ of the first round. Put in the context of the framework, if the central interests dominate the first round and administrative decentralization occurs, the subnational reactive strategy would not be an adjustment of its preferences in the subsequent round but instead, a continuing articulation of their primary preference mix, i.e. Political, Fiscal, and Administrative. Contrarily, if the subnational preferences dominate in the first round, the reactive trajectory available to the central actors could be one of compliance (as covered above, in the context of subnational dominance) or that of non-compliance (continue pursuing its preferences regardless of the outcomes

of the first round). Considering the latter, the central actors shall continue articulating their most preferred form of decentralization – administrative decentralization.

Going back to what was earlier discussed as a central privilege; the central agents retain a considerably higher degree of leverage in articulating their preferences even if they were not successful in the first round of reform. Not deviating from their primary preference set, the central actors will articulate for administrative decentralization, so that they can condition the subsequent decentralization of the fiscal resources upon the functions devolved to the subnational levels. The degree to which it would substantively alter the inter-governmental balance of power would be limited at best.

In the context of this research, the main focus shall be on the distinct dominance paths as they necessarily have the greatest effect, to either direction, on subnational empowerment.

1.2 KEY FOCUS OF ENQUIRIES

Building upon the importance of the stakeholder incentives and the sequential theory of decentralization, this research explores two main arguments:

1. The substantiveness of subnational empowerment is dependent on the form of decentralization being pursued and how the reform was sequenced, subject to all incentive maximization and preference articulations of the stakeholders involved. The content and quality of the overall decentralization reform remains a function of which tier dominates the initial articulation for reform. Regardless of the system of government, reform processes that follow subnational dominance trajectories have a greater degree of effectiveness and sustainability.
2. The experiences of successful developmental states in East/South East Asia illustrate characteristics contrary to those of a decentralized democratic polity. However, decentralization reforms can be genuinely conducive and reinforcing to the establishment of a *‘Democratic Developmental State’*.

1.3 RATIONALE FOR CHOOSING THE CASE STUDIES

While this research endeavors to draw the connections across multiple contexts globally that have undergone some form(s) of decentralization, the overarching focus will be placed on two

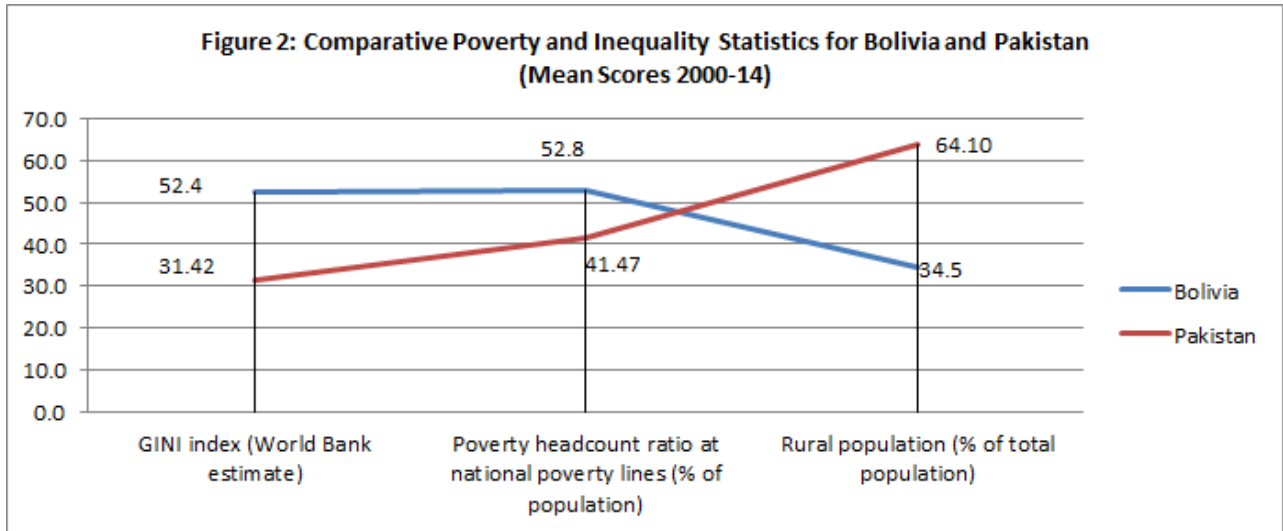
contexts; Bolivia and Pakistan. The primary reason for the choice of these two contexts is because they enable an analysis of the two distinct typologies of subnational and national dominance (in the context of the reform sequencing), and how they affect the final outcomes of the reform process. The case of Bolivia presents an example of subnational domination in the interest articulation and reform design, whereas the case of Pakistan presents the case of dominance of central interests and preference articulations.

Both countries have different state structure, with Bolivia being a Unitary State and Pakistan being a Federation. This on one hand enables the broader study of decentralization and its implications for democracy and development across two systems of government and state-structure, but at the same time enables the analysis of an interesting paradox. The structure of the state in Pakistan has been Federal in its form, but unitary in function up until the constitutional reform of 2009 following which it has been making leaps towards being federal in function as well. The structure of the Bolivian state has been unitary both in form and in function, and continues to be so after the promulgation of the new constitution in 2009. However, with the departments getting more autonomy vis-à-vis the centre, and a greater space for preference articulation in the decision-making space in the now Plurinational State of Bolivia, it is often considered as emerging federation⁸. This will be examined in detail in the relevant chapters.

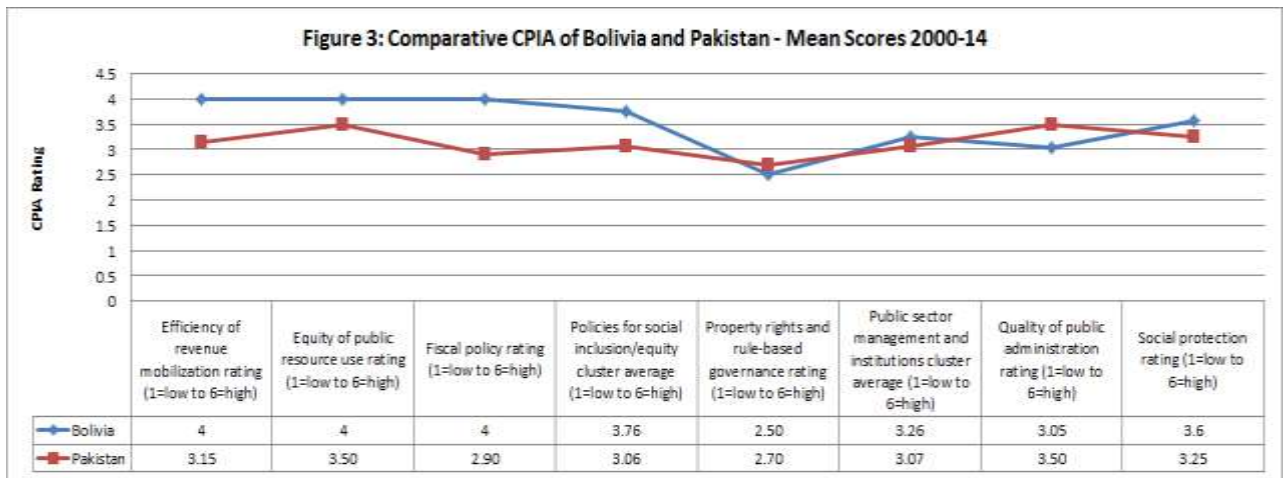
Bolivia and Pakistan are comparable countries not just in their political dimensions but also in their socio-economic dimensions. Both countries are classified as lower middle income countries by the World Bank, with a high but decreasing poverty headcount (as per national poverty lines), a high level of inequality (regional, urban-rural and income), and public management inadequacies. Moreover, the Country Policy and Institutional Assessments⁹ of the two countries also exhibit comparable attributes and trends. This can be seen in Figures 2 and 3, drawn from the World Development Indicators, below:

⁸ For details see, Faguet, J.P (2013) Can Subnational Autonomy strengthen Democracy in Bolivia? <http://publius.oxfordjournals.org/content/early/2013/05/09/publius.pjt020.full.pdf+html>

⁹ Based on World Bank – World Development Indicators. CPIA is a rating of countries against a set of 16 criteria grouped in four clusters: economic management, structural policies, policies for social inclusion and equity, and public sector management and institutions.



Data Source: WDI



Data Source: WDI

Both Bolivia and Pakistan have had considerably long periods of authoritarian rules and are at relatively nascent stages of democratic consolidation and in pursuit of a stable equilibrium in terms of state management and governance following the political and institutional reforms. The decentralization reforms, particularly the recent ones, in both the countries have also been rather radical yet sustainable in terms of the institutional and constitutional cover that they are accompanied with.

Owing to the economic crises of the 1980's, and what is referred to as a 'Lost Decade for Latin America'¹⁰ waves of decentralization and democratic movements have significantly altered the political landscape of Latin America including demands for a greater efficiency, effectiveness and

¹⁰ Bértola and Ocampo (2013)

responsiveness of the state. These changes in the political space compelled the governments to pursue governance reforms and renegotiate the centre-subnational arrangements on issues of taxation, revenue-sharing, accountability, discretion, and service delivery. Bolivia also witnessed a similar series of transitions. The first main decentralization reform in Bolivia was the 1994 *Ley de Participación Popular (LPP)* or the *Law of Popular Participation* which was promulgated as a part of the neo-liberal reform strategy of President Gonzalo Sánchez de Lozada (Faguet, 2002). While this reform was massively criticized by the opposition and simultaneously lauded by international development agencies, it was aimed at incorporating the marginalized indigenous groups into the political and economic development processes.

Before this reform was introduced, Bolivia was amongst the most centralized states of Latin America and had no subnational governance structure or institutions in place. The public service delivery functions were mainly the discretion of the central government. With the introduction of the LPP, there was a significant transformation in the state structure primarily through the establishment of subnational governance structures and the assignment of functional responsibilities to the subnational level. A radical reform that it was, it involved the decentralization of the some public services more suitable for local provision (primary education, health, basic infrastructure, sanitation etc) as well as decentralization of 20% of all national tax proceeds to 311 newly created municipalities(Faguet, 2002).

The developmental implications of the decentralization reform were also profound as the national public investment patterns witnessed a shift from economic production to human capital development, efficiency improvements in public service delivery and capacity enhancement of subnational public service delivery systems, and mitigating regional inequalities (Faguet, 2002). In addition, the local governance institutions also illustrated a higher degree of responsiveness as compared to the central executive in sectors including education, agriculture, water and sanitation, health, urban development, and transport (Faguet, 2002).

The 1990s saw an increasing mobilization of indigenous groups and social movements that challenged the status-quo or the ‘coalition of elites’ (in terms of North, 1990) for failing to respond to the genuine needs and demands of the citizenry. The LPP was seen as an administrative decentralization, and the strong momentum of the indigenous movement at the subnational level all through the 1990s continued to articulate the need for greater political and fiscal autonomy. Between the years 2000 and 2005, the political climate worsened with massive protests and social mobilization which saw the end of tenures of Presidents Lozada (in 2003) and Mesa (in 2005) respectively. In the

subsequent round of elections, the Movement for Socialism (*Movimiento al Socialismo, MAS*) head Evo Morales established himself as the common representative of all the dissenting groups.

Given the rise of the MAS party from subnational political space to the central level, the main political mandate of the new Morales regime was to initiate a process of substantive political change that at its outset focused on forging a new constitution and state structure. An important point to note here is that the preference and order of decentralization reforms pursued by the MAS government were totally reflective of the Subnational Self-reinforcing nature as elucidated in the Sequential Theory, primarily because all these preferences were developed and amply articulated by MAS at the subnational level before they assumed the national stage. Therefore, this round of decentralization reforms will be considered by this research as following a subnational dominance path. Political decentralization was the top of the agenda of the Bolivian decentralization following 2006, with even greater pressure coming from the subnational level for greater autonomy¹¹. The subnational political space has, since the first election of MAS to the central government in 2005, become the most vibrant arena for political contestation and preference articulation.

The referendum of 2006 was held for greater regional autonomy, against the backdrop of the Bolivian Constituent Assembly deliberating over a new model of regional autonomy that was subsequently incorporated into the new national constitution in 2009/10. However, even after the introduction of the new constitution that involved a substantial relocation of functions and authority to the subnational levels, there continues to be a high degree of contestation on the nature and extent of regional autonomy, especially in the area of fiscal resource distribution. An ongoing agenda since, is the establishment of a fiscal pact that maximizes regional equalities and that distinctly stipulates inter-governmental revenue sharing mechanisms, particularly the distribution of mineral and hydrocarbon rents (envisaged under the Hydrocarbon Nationalization Law). Other contentious agendas include the functional responsibilities at each administrative tier, local revenue generation, subnational debt and fiscal responsibility.

Finally, the case analysis of Bolivia affirms the subnational dominance trajectory as a subnational dominance path even though the centre remained the protagonist of the initial reform, and the consolidation of the decentralization exercise hinges on the fiscal dimensions (in accordance with the sequentialism of subnational dominance).

¹¹ Along with issues of land distribution, indigenous rights, distribution and use of hydrocarbons revenue, the issue of greater regional autonomy was the key element of this new social contract in Bolivia.

The second country of analysis is Pakistan, where the decentralization reforms have been significantly different in terms of the trajectory, but similar with the Bolivian case especially in terms of negotiated bargains between established political elites¹². The main difference being that in case of Pakistan, paradoxically most of the decentralization reforms were initiated during autocratic regimes. The incentive of the protagonists was the further centralization of powers in the non-representative centre, which was also amongst the reasons they were rolled back by the democratically elected incumbents. There have been multiple substantive attempts at decentralization in Pakistan since its independence in 1947, primarily through the different administrative structures of the government; national to provincial, national to local, and provincial to local. While all these three manifestations differ with each other, the main similarity between each of them remained in the underlying motivation. The first three attempts at governance reform through decentralization had been made by a non-representative, autocratic, unelected centre whereas the current reform process (though still in evolution) is the first one to be instituted under elected governments. The irony, as stated earlier, surrounding the local governance reforms in Pakistan is that the three military regimes directly in government for 34 years, have actively pursued decentralization and devolution of power, whereas all elected governments have deliberately subdued subnational politics and governance. This paradoxical situation between authoritarian and democratic politics in Pakistan, presents an interesting avenue for research not only in terms of decentralization and local governance but also in terms of the bargaining strategies employed by the ruling elite¹³.

The most comprehensive decentralization reform process was the 2001 as it involved changes in the “administrative level of decision-making, the accountability of the decision-making authority (political or bureaucratic), and the nature and amounts of the available fiscal pool” (Cheema, Khawaja and Qadir, 2005). This reform was a radical one, under an autocratic regime, and without an adequate constitutional cover. It also involved a great deal of decentralization of provincial powers to local levels, without any decentralization of the federal powers to the lower tiers. As a consequence, the sustainability of these reforms was low despite yielding delivering service delivery improvements and empowerment to local governments¹⁴. In 2008, this arrangement was rolled back following a ‘democratic transition’ as the Pakistan People’s Party assumed the government. While very important

¹² For more on this, see Hussain, A and Hussain, S (2009), Poverty, Power and Local Government in Pakistan. In ‘Economic Democracy through pro-poor growth’ Wignaraja, Sirivardana, Hussain (eds).

¹³ More details can be found in Aslam, G (2010)

¹⁴ Aslam, G. and Yilmaz, S. (2011), Impact of decentralization reforms in Pakistan on service delivery—an empirical study. *Public Administration and Development* 31: 159–171. doi:10.1002/pad.591

constitutional changes were passed in 2009 and 2010, primarily dealing with the fiscal and administrative decentralization from the centre to the provincial level, the grassroots governance infrastructure remained ignored. Currently, there is a massive process of contestation and bargaining underway for a revival of the decentralization reforms that empowers the municipalities and follows a ‘grassroots’ approach. Owing to the inadequate quality of public policy response to the citizen demands, the 2013 elections (historical elections as it was the first time a transition between two elected governments took place following a completion of mandated tenure) saw the reinvigoration of the local governance as one of the popular electoral slogans. However, the electoral slogans actually lacked the ‘credible commitment’ attribute and actual local governance elections and structures were not established until 2015 and 2016 despite commitments to do so much sooner. The cause of this delay was that major political parties were engaged in a process of bargaining to save their respective ‘support bases’ and secure their positions against any threat of dislodging.

Finally, the case of Pakistan illustrates the National Dominance Path with the ‘*intra-elite bargaining*’ at the centre (in both representative and non-representative incumbencies) precede the citizen interest articulation. As a consequence, the process of reform design and its implementation turns out to be a self-reinforcing mechanism that affects not only the institutional evolution, but also affects the democratization and developmental indicators.

Considering the comparability of both these cases, it would also be important to look at their transformation experiences across the variables identified by the Bertelsmann Transformation Indices for the periods preceding the last rounds of decentralization reforms and trace the progress to 2015. Figures 4 and 5 below illustrate the transformation trends exhibited by both Bolivia and Pakistan in the areas of Democracy, Economy and Public Management¹⁵.

¹⁵ Details on the methodology and the variables employed under each of the dimensions can be accessed at <http://www.bti-project.org/en/index/methodology/>

Figure 4: Transformation Trends Pakistan



Figure 5: Transformation Trends Bolivia



Source: Compiled and generated from the Bertelsmann Transformation Indices 2016

Reviewing the transformation trends across both the countries, it can be seen that they have been more favorable for Bolivia than for Pakistan especially in the realms of Democracy and Management Performance. While the factors contributing to these will be discussed in a greater detail in the relevant chapters, this can be considered as a support to the main argument made in the preceding section. Finally, the choice of these two contexts is also rooted in my own first-hand exposure to them, and to an extent that allows a more in-depth and contextually specific analysis.

1.4 METHODOLOGY AND ANALYTICAL FRAMEWORK

This research has engaged in a mixed-method approach in identifying and developing the main research arguments, data collection and interpretation. This has included an extensive review of secondary literature, databases, reports and journal articles. Most of the primary research was carried out in the form of interviews and in depth unstructured interviews with various thematic experts as well as country experts which was aimed at validating the questions identified and getting an insight into the context specific dynamics that would otherwise be difficult to generate from the secondary sources detailed earlier. These included respondents that have served in research and international organizations monitoring and advising on these reforms, officials of Ministries and Task Forces of the two countries chosen for case studies, various independent experts and members of the civil societies from both the countries¹⁶. Owing to the nature of the solicited inputs, questionnaires and written responses to the enquiries could not be sought primarily because of attribution concerns of those interviewed.

In terms of formal research methodology, and given the scope of the enquiry finding a single model or approach that could offer the purpose of explaining the complexities involved in interest articulation, empirical analysis, and a tenable explanation for the events and mechanisms of relevance was difficult. Following on some of the related works notably Falleti (2010) and Eaton et al (2010), two mutually reinforcing frameworks were identified to operationalize the research questions and guide the analysis. The Political Economy Framework (Eaton, Kaiser and Smoke, 2010) was used to identify the types of incentives that political stakeholders face in the design and implementation of decentralization reforms. The framework presented in the Sequential Theory of Decentralization (Faletti, 2010) enabled

¹⁶ Of particular importance was my research mobility at the United Nations Research Institute for Social Development, Geneva where I had a chance to work on a project that dealt with the Politics of Domestic Resource Mobilization and another one that dealt with financing social policies in developing countries. By virtue of this engagement, I had the opportunity to interact and solicit inputs from some of the key actors in the decentralization reforms in Bolivia and other thematic experts.

a structured approach to distinguish between subnational and national level incentives and preference mix. Given these mutually reinforcing analytical frameworks, looking at the sequential aspects of decentralization and their impact on the reform outcome required the use of an in-depth review of secondary literature, online articles, policy reviews and news items to trace the processes, analyze the context and identify mechanisms that led to the outcomes or the stage of the reforms in each country chosen for analysis (Falleti & Lynch, 2009; James Mahoney & Rueschemeyer, 2000). The process tracing technique implicit in the broader sequential analysis methodology enables the reconciliation of the theoretical constructs on incentive maximization, interest articulation and bargaining, with the actual stages of the reform and the associated causal mechanisms. Identification of causal factors within each reform context was also enabled by tracing the processes involved in the prelude and the rollout of the reforms and help explain the ‘sources of variance in the outcomes of interest’ (Blanchard, 2011). Proceeding with the context analysis by reviewing each reform stage and the corresponding interests of the participating actors, enables the identification of the ‘winners’ of each round of reform and how the outcomes of one round affect the subsequent ones. In the detailed contextual analysis, the relatively temporally stretched structural and institutional constraints that shape the contents of decentralization policies (e.g. those derived from the distinct historical evolutions of the political system in Bolivia, or the patronage politics in Pakistan) are also brought under consideration. Furthermore, the comparative sequential methodology also offers a reconciled explanation of the ‘macro-social comparative historical discourse’ with the relatively micro-oriented process, which is a potent tool of analysis for the kind of enquiry this research seeks to embark upon.

While the historical context and the distinct dynamics are influential in developing an explaining the reforms and the associated processes, there was also a need to identify a theoretically grounded interpretive tool which could help in explaining a sustainable institutionalization of decentralization reforms in the presence of an impulse of the involved stakeholders in maximizing their divergent interests. To this effect, using a game theoretical model to explain the interaction and bargaining of the stakeholders to rationally maximize their own interests when framing the subsequent course of the reform, was employed. This is of particular importance in analyzing the impulses of national and the subnational actors for power acquisition/retrenchment (James Mahoney & Rueschemeyer, 2000; Pierson, 2000; Thelen, 2004).

One of the game-theoretical models applied here follows Aslam (2010), where a bargaining process was postulated as a way of ensuring regime survival by a dictator. However, its application here differs from that in Aslam (2010) as it is not about a dictator and citizens, but between the centre and

the subnational agents. This model can also incorporate bargaining practices, particularly cooptation and consociational bargaining, either by the CG or at a lateral level amongst the regions to enhance their collective bargaining. It is presented as follows:

Model 1: Basic Bargaining Dynamics between National and Subnational Political Agents

This model presents a basic dictatorship game to analyse the incentives and interest articulation processes underlying decentralization reforms. An analytical proxy of a ‘dictator’ shall be applied to the ‘status-quo’ preceding the reform at $t=0$. The objective is to frame the analysis operating on Schelling’s idea of free activity in a strategic interaction context; the dynamics of “bargaining, of arriving at understandings and misunderstandings, for accommodation and co-operation and for conjectures about each other’s decision processes, value systems and information” (Schelling, 1961). Following on Aslam (2010), the analytical focus is on how the surplus is divided, what strategies are employed to secure preferred outcomes, critical factors behind their bargaining power and the exogenous factors that have a bearing on the outcome.

In particular, the strategies analyzed and linked to the design and implementation of decentralization reforms would be; a) changing opponent’s payoffs (co-optation), b) explicit signaling by a participant to signal credible intent about the future action, and c) ‘brinkmanship’/ repression strategies (Aslam, 2010)¹⁷. The basic setup of the game is as follows:

- A group of regions yield a total product, a proportion of which is taxed by the Central Government who exercises full discretion over its use for redistribution or retention. In the status quo the tax rate is $0 < T < 1$.
- The total income generated for this tax rate is Y .
- The total tax revenue that the CG receives equals TY , while the disposable income of the regions collectively is $Y(1 - T)$.

¹⁷ More detailed version of this model can be seen in Aslam, G., Dictatorship as a Bargaining Process. George Mason University Doctoral Student Working Paper Series:

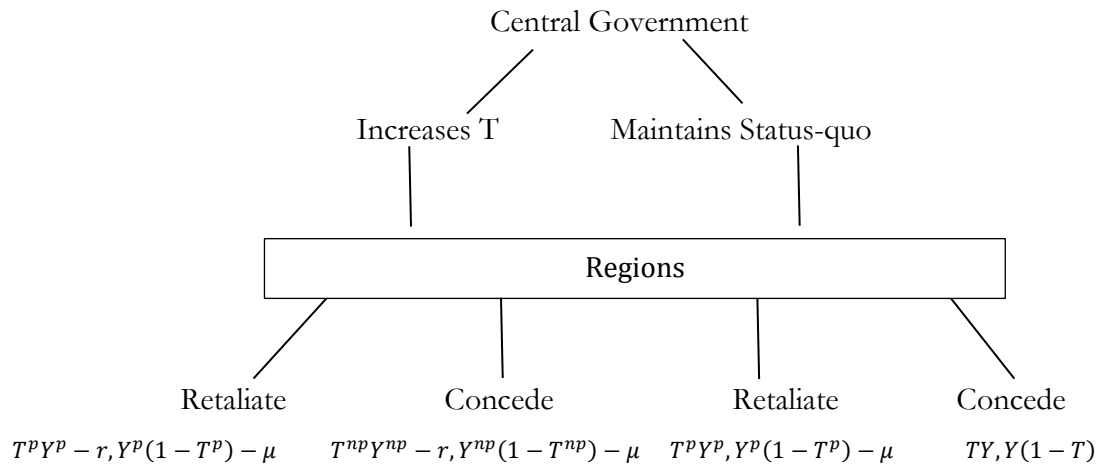
(https://www.google.de/url?sa=t&rct=j&q=&esrc=s&source=web&cd=7&ved=0ahUKEwjI3-r4md7JAhVDuhQKHcj5CMMQFgg9MAY&url=http%3A%2F%2Fgeobot.gmu.edu%2Fbitstream%2Fhandle%2F1920%2F5697%2FAslam_Dictatorship%2520Paper%2520Feb%25202010.doc%3Fsequence%3D1%26isAllowed%3Dy&usg=AFQjCNHCaUbSfkq22BoCtYBdKtp7kkwozg&sig2=gU2XnKVfWeUc0jv_FfHoSw&cad=rja)

- In each period, the CG has two strategies. It either maintains the status quo, which means that the tax rate does not change or it can retaliate by increasing the tax rate to T^{np} so that $T^{np} > T$.
- For the tax rate T^{np} , the income generated is Y^{np} and the disposable surplus/income of the regions is $Y^{np}(1 - T^{np})$.

From the perspective of the regions, they have two strategies. They can either concede to the tax rate proposed by the CG or they can retaliate and demand for T^p such that

$$0 < T^p < T < T^{np} < 1.$$

The total income generated for this tax rate is Y^p . At all times, the cost of retaliation of the regions is μ , where $0 < \mu < 1$, whereas the cost of increasing T for the CG is r where $0 < r < 1$. A one off game would play out as follows:



Based on the costs of repression by the CG and the costs of retaliation by the regions, the threat of retaliation shall persist as long as the following inequalities hold:

- i. $\mu < Y^p(1 - T^p) - Y^{np}(1 - T^{np})$
- ii. $Y^p(1 - T^p) - \mu > Y^{np}(1 - T^{np})$
- iii. $\mu < Y^p(1 - T^p) - Y(1 - T)$
- iv. $r < T^{np} Y^{np} - TY$

The regions will only retaliate if the cost of retaliation is less than the loss in their collective share of the surplus when a higher tax is imposed by the CG. Similarly, the CG would continue to

retaliate until the point as long as the cost of repression is less than the additional income made from imposing higher taxes.

In order to bring in bargaining into this model, let's assume that every region has its own share of contribution to the total disposable income individually given by $\emptyset(Y - YT)$ where $0 < \emptyset < 1$. In the previous setup, it was assumed that at $t=0$, all regions operate collectively and no contestation over individual shares exists. However, if there is a disparate contribution of the regions to the collective output yield Y , then there are different constraints that face individual regions in their bargaining processes with the CG. The higher the \emptyset , the greater would be the bargaining power with the CG as the potential increase in surplus due to favorable bargaining results would still be higher than the cost of retaliation μ .

This model will be subsequently developed in a greater, more specific detail in the case studies to illustrate the different bargaining scenarios and interest articulation by the CG or the regions within the chosen cases.

Finally, the sources for statistical data and other quantitative ratings are predominantly secondary and includes World Development Indicators, IMF Article IVs, World Governance Indicators (WGI), Polity IV, Bertelsmann Transformation Index and national social and economic surveys. The modalities and parameters of their usage will be explained once and where employed.

CHAPTER 2

DECENTRALIZATION AND DEMOCRATIC DEVELOPMENTALISM

2.1 GOVERNANCE, STATE AND PUBLIC SECTOR REFORM: AN OVERVIEW

Public sector reform, and more importantly, governance reform in developing economies has been a dominant agenda item in the global development narrative. The existence and persistence of dysfunctional and ineffective public institutions coupled with weak governance mechanisms have been the main constraints to socio-economic development in developing contexts. During the 1980s-1990s, international donors and development agencies witnessed the failure of potentially high benefit projects in poor policy environments which in turn were a product of inadequate public institutional effectiveness and poor public governance (World Bank, 2000). Thus, fostering effective, efficient, responsive and accountable public institutions is arguably the main challenge for making any inroads into sustained socioeconomic development.

Globally, the public sectors witnessed a significant expansion (albeit to varying extents) between 1945 to 1980s despite the plurality of economic structures and development stages. With increased global integration, economic growth and varying levels of socio-political modernization, the conventional role of the state in the socio-economic and political management became more complex. In a way, the growth in the public sector was also motivated by the conceived benchmarks of the nature of the society that the governments envisaged. For example, post 1945 the commitment of the OECD countries (European countries in particular) to welfare regimes and macroeconomic stability paved a way for the acceptance of the state as a central institution for income redistribution, support to vulnerable groups and a stimulant for aggregate demand (World Bank, 2008). The developing countries followed a similar suit, many of them emerging after the decolonization and nationalist movements, in their efforts to promote social cohesion and establishing growth trajectories. The emergence of parastatals (especially in Africa) in the realm of poverty alleviation, health service delivery and other public service delivery sectors, was also witnessed owing to the absence of requisite incentives for private enterprise in the provision of these services and engagement in the preferred sectors of the economy.

The notions of participation, accountability, representation and responsiveness remained secondary concerns in most countries for a major part of the 20th century, with the exception of some

states where democratic norms and market structures were already well developed. The major transformation in the understanding of the role of the state occurred in the 1980s and 1990s especially in the developing countries, that put forth an alternative view of creating a ‘market-friendly, transnational, decentralized, citizen oriented and democratic state’ (World Bank, 2008). Dichotomous imperatives subsequently came to surface where the concerns included efficient use of economic resources, making economic structures and institutional mechanisms more conducive to markets, on one hand, and notions of public accountability, representation, equity and responsive service delivery, on the other.

Not disavowing the importance of the technical dimensions of reform design, ensuring suitable institutionalization and maximizing public welfare requires a ‘*factoring in*’ of the pressures the reform brings upon those tasked with public service delivery and those administering them. In order to foster a ‘stakeholder’ spirit amongst the citizenry, the issues of representation and accountability at national and subnational levels are critically important. In ‘*principal agent*’ theory terms, the result of accountable and representative structures will be that the principal (citizens) will be effectively empowered to reward or penalize the agent (the government and state institutions) by revealing their preferences either through fiscal cooperation or through electoral mechanisms. This chapter aims to provide an overview of the broader public sector reform narrative, how the role of the state can be reconfigured to yield development conducive outcomes, the notion of developmental state and its interplay with democratization, and finally how decentralization reforms can be designed such that the democratic developmentalism can be instituted for a broad-based inclusive process of development.

While the preceding chapter covered the centrality of political processes to decentralization, this section outlines their role in the broader public sector reform processes (which include, but are not limited to, decentralization). Public sector reforms (hereon referred to as PSR), shall be of limited utility and effectiveness if the political actors (agents) and the broader citizenry (principal) have not established a clear framework for the distribution of public authority and power to achieve a ‘minimum consensus’ on the public policies. This is most pertinent in cases where there is either a high level of contestation or/and a related yet distinct aspect of regime instability¹⁸. Instituting these reforms in such contexts makes them more of an imposition or a technocratic exercise rather than an organic and

¹⁸ Most of the developing economies are also faced with either transitional or limited democracy, which is most often rooted in the ‘limited access social order’ or an at best, procedural nature of democracy. When coupled with ethnic plurality, disparate socio-economic development or endemic poverty, an inference about the extent of contestation (even if it is latent because of inadequate articulation mechanisms) can be made. An elaborate account of this limited democracy can be found in Robinson and White, 1998.

deliberative process. As a consequence, the sustainability of the reform is questionable in the wake of opposition, rollback in case of regime change, or implementation inconsistencies.

Public sector reforms can be diverse in terms of forms, however, the common objective remains improving public sector effectiveness and efficiency, accountability to the citizenry, and broader macroeconomic stability. Reforms geared towards the capacity enhancement of state and state institutions mandated for Public Service Delivery (PSD) remain largely a concern for the developing economies primarily due to donor advocacy across Latin America, South Asia and Africa. The main purview of such reforms is enhancing the technical capabilities of the bureaucracy in terms of serviced delivery design and delivery, managing recurrent public expenditure and remunerative reforms. PSR dedicated to enhancing public accountability are geared towards participatory and transparent public policy and service delivery. Such reforms also consider issues related to political (and hence, parliamentary/legislative) plurality, independent media, social mobilization and independent judicial systems. In contexts that are multi-ethnic or where state cohesiveness is weak, such governance reforms are also geared towards promoting greater plurality and equitable participation in the central institutions of the government or the distribution of authority to lower levels of the government through decentralization reforms. As covered in the prior chapter, decentralization in itself is targeted at pluralizing political space and preventing power consolidation, and the reforms have predominantly been undertaken at the behest of the donor agencies.

The Narrative on State-led Development

From 1950s to the mid of 1980s, most developing countries followed a state intensive development policy. As a result, there was an expansion in the size and mandate of the public sector whereby state policy encouraged private investment while also engaging in the sectors that held limited incentive for private sector operations. Success thereof, remained constrained (in the developing economies in particular) by the limited state capacity. The question that arises is what does 'state capacity' connote? A review of literature reveals the subjective nature of this concept, however there are common denominators across most definitions of state capacity, that include the ability of the state to rectify market failures, domestic resource mobilization, effective and efficient absorption of state resources to productive sectors, develop conducive institutional and enforcement mechanisms, higher social cohesiveness, stable fiscal management, and deliver public services and social benefit programmes (Burki, Perry, & Dillinger, 1999; Fukuyama, 2004; Huang, 2008a; Leibfried & Zürn, 2005). Other attributes have also been provided, albeit with less consensus, one that is most relevant to the purview of this research is the ability of the state to extend its writ across the territory; negotiate,

enforce and credibly commit to political settlements with (sub) national actors in the subnational arena, all the while creating a developmentally oriented public policy and welfare enhancing public institutional framework.

However, these settlements may vary across contexts primarily depending on the nature of the political setup; democratic or autocratic¹⁹. The state led growth and development model, drew its criticism not only from the dominant assertions of the Neo-classical framework but more on the structural and institutional capacity of the states to act as agents of development in the developing contexts. While there is a considerable thematic breadth in the literature on public sector reforms and role of the state in particular, this section shall engage with two of the recurrent themes. The broader notions overlap but given the heterogeneity of experience in diverse regional contexts, there is a corresponding plurality in the theoretical positions that have emerged. The first one emanates from the international development assistance across the global spectrum during the 1950s and 1960s, whereby the role of the public administration was considered to be of limited utility in growth and development (Eaton, 2008; Ferguson, 1990).

The main argument in this case was based on the role of the public sector institutions and bureaucracies being engaged with stable incremental reforms and stability rather than pursuing deeper structural reforms hence being anti-developmental and inhibitive to private entrepreneurial activity. Another argument extolled the fallacy of ‘rational bureaucracy’ as the bureaucratic service was considered subservient and aligned to particular vested interests that were contextually unique. The second one has been rooted mainly in the experience of developing countries, primarily across Sub Saharan Africa and Asia, arguing that where the state institutional structures are ‘weak’, state has low legitimacy and laden with patriarchal political norms; the capacity of policy enforcement and sustainable reform remains limited. These attributes were considered typical of contexts with autocratic political regimes, lack of social cohesion and an exploitative policy framework.

Structural Adjustment and the role of state under Neoliberalism

Towards the end of the 1970s and the beginning of the 1980s, an international recession in the backdrop fueled further by the Latin American debt crisis and exploitative autocratic regimes in Africa, promoted the skepticism of the developmental narrative as well as the role of the state. As a consequence, two dominant ways of thinking came into the narrative; the Developmentalism in newly industrializing states in Asia (Singapore, Malaysia, Taiwan, China, South Korea), and neoliberalism

¹⁹ The nature of political setup is not defined in binary terms but implies a spectrum that lies between the two.

championed by the US and the UK amongst others. The East Asian developmental policy illustrated a significant departure from the narrative of the radical leftist thinking, by showing that developing economies at the lower end of the income quintiles could manage sustainable inclusive growth without disengaging from the international economy. This developmental policy was also a significant departure from the neoclassical narrative that extolled the inhibitive nature of state activity on economic growth and development. The developmental model put forth by the East Asian economies was characterized by a state led institutional framework that had necessary functional authority, responsiveness and capacity to steer market development. This approach is cited in the literature as a 'governed market' (Wade, 1990). In another addition to the development policy narrative, it was argued that such a framework may be of good utility in managing relatively closed economies it cannot be sustained in a context of 'global liberalization of financial and capital markets' (Flynn, 2007a). This argument was further substantiated with the East Asian financial crisis in the later part of the 1990s that was caused primarily by the instability of capital flows.

The consistent critique of the state led development model was that in the absence of certain requisites of state capacity and context specific conditions, there existed a latent tendency of the state to become 'predatory'; rent-seeking, patrimonial, and fostering a limited access order. However, the neo-liberal paradigm harbored a greater skepticism of the state capacity to actively pursue a developmental policy under any circumstances (Friedman, 1993; Friedman & Friedman, 1962; Leibfried & Zürn, 2005). The main impetus for the neoliberal resurgence found its roots in the oil crisis of the 1970s occurring in the developed economies like the UK and the USA before being mainstreamed into the global development narrative²⁰. The United Kingdom was in effect the protagonist of implementing neoliberal reforms when it undertook its structural adjustment program as part of a financing agreement with the International Monetary Fund, after consistently posting low investment rate and, fiscal and trade deficits. Under this SAP, the UK government had to slash public expenditure and divest its stake in the Public Sector Enterprises to regain fiscal space, while also enacting a floating exchange rate regime and a contractionary monetary policy. These strategies then evolved into the standard SAP policy milieu that was subsequently applied across the globe including

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mainly the developing economies and the Highly Indebted Poor Countries (HIPCs). The imperatives of the economic liberalization led many of the developing economies into macroeconomic imbalances primarily in terms of inflation, debt management, fiscal and trade balances. In order to deal with these imbalances, they had to solicit IFI support for which the World Bank and the IMF were the primary resort. The policy mix pushed through as part of these financing and stabilization programs included fiscal austerity, divesting public stake through privatization of PSEs, and broader structural adjustment and economic liberalization.

This advocated policy milieu was also known as the '*Washington Consensus*'²¹. A few common denominators can be identified with public sector reforms and structural adjustment in developing contexts. The first among these is the question of ownership which deals with the protagonists and executors of the reform process. In the case of advanced economies of the developed world (mainly the high income OECD countries), the reform processes were tailored and phased consistent to the local imperatives and compliance of the local constituencies. In the case of the developing countries, the adjustment and sectoral reforms has been a product of donor agendas thereby limiting their legitimacy and sustainability in the absence of corresponding mandates. The PSR agenda consisted, more or less, a uniform agenda that involved withdrawal of the state through privatization, divestment and functional readjustment mechanisms.

Given the widely divergent outcomes of the economic liberalization, primarily from the PSR viewpoint, the international reform agenda witnessed significant modifications in the later part of the 1990s which are still ongoing, to focus simultaneously on seemingly opposing pursuits of poverty alleviation and efficiency, and building state capacity while also fostering market development. The objective of this realignment of the development narrative was initially brought on in the form of augmented policy frameworks that squared on the enactment of social safety and support mechanisms for the groups adversely affected by the liberalization reforms. By the end of the 90s, an explicit focus on the poverty alleviation (at least in the context of (HIPCs) led the donor assistance and the supported governments to coordinate the development policy through agreed international development targets, like the United Nations Millennium Development Goals, as well as comprehensive development frameworks. These comprehensive development frameworks included the oft cited imperatives of securing development assistance such as the country specific 'Poverty

²¹ Based on review and notes from World , B. (2008). Development Economics through the Decades. Washington D.C.: World Bank.

Reduction Strategy Papers' (PRSPs), that were nationally devised comprehensive development strategy papers that gave the borrowing economies some degree of ownership over the economic policy.

The main departure from the neo-liberal paradigm in the international development policy narrative came in the form of recognition from the IFIs that market development and poverty alleviation depended on effective and capable states. The World Bank articulated this change in the policy narrative first in the 1997 World Development Report titled 'State in a Changing World', stating that 'State-dominated development has failed, but so will stateless development' (Bank, World Development Report 1997 : The State in a Changing World, 1997). This was subsequently reiterated thematically in the subsequent reports by the World Bank in 2000, 2001 and 2004.

The new development agenda from 2000 onwards, especially in the aftermath of the Monterrey Consensus 2002 reinvigorated the role of state in the development policy narrative²². In the Section II (A) of the Monterrey Communique, Paras 10-16 detail the imperatives of state activity that span governance reforms, public policy formulation that is growth stimulating and redistributive, and a reform of public service delivery on grounds of efficiency, effectiveness and responsiveness (See Box 1). State operations in the economy can be detrimental and inhibitive to economic development (through markets), nevertheless the state has a critically important role to play in the process of economic development and structural transformations. In some contexts, especially in South Asia and Sub Saharan Africa, the lack of economic development and erratic growth patterns can also be attributed to the inhibited government capacity to formulate policy, perform basic administrative functions, synergize with private and semi-public sectors, and ensuring the provision of basic physical infrastructure and public services. This is what is also known as the 'too much state and too little state' dichotomy (George, 1999).

Under the fold of the 'Good Governance' narrative that emerged as an influential subset of the new development paradigm in the 2000s, a major departure from the narrative of two decades of reducing the role of the government occurred that highlighted the importance of strengthening the governments. This can be attributed mainly as a consequence of the failure of the Structural Adjustment regime under the broader neoliberal agenda. While the first half of these structural liberalization reforms during the 1980s and the greater part of the 1990s were articulated, designed and

²² Representatives of all countries of the world gathered in Monterrey, Mexico, on 21 and 22 March 2002, with resolve to address the challenges of financing for development around the world, particularly in developing countries. The objective was primarily to evaluate the demand and supply of financial resources to pursue the globally agreed development goals of poverty eradication, sustained economic growth and economic development, and fostering an inclusive and equitable global economic system.

implemented by a ‘technocratic élite’, the second round that began in the later part of the 1990s and continues till now gave a lot more attention to the transformation of institutions that structure political and economic activities in the reformed context (Bank, 2005; Chatterjee, 2004). The premise of this stance was on creating an institutional framework that ensured rule of law, safeguarding property rights, mitigate adverse exploitation and corruption, and enhancing regulatory quality (North, 1990). These policies also led to the development of the ‘good governance’ agenda that dominated much of the policy reform advocacy since the mid-1990s onwards.

Box 1 : Section II (A) Monterrey Consensus Communiqué - United Nations 2003²³

10. In our common pursuit of growth, poverty eradication and sustainable development, a critical challenge is to ensure the necessary internal conditions for mobilizing domestic savings, both public and private, sustaining adequate levels of productive investment and increasing human capacity. A crucial task is to enhance the efficacy, coherence and consistency of macroeconomic policies. An enabling domestic environment is vital for mobilizing domestic resources, increasing productivity, reducing capital flight, encouraging the private sector, and attracting and making effective use of international investment and assistance. Efforts to create such an environment should be supported by the international community.

11. Good governance is essential for sustainable development. Sound economic policies, solid democratic institutions responsive to the needs of the people and improved infrastructure are the basis for sustained economic growth, poverty eradication and employment creation. Freedom, peace and security, domestic stability, respect for human rights, including the right to development, and the rule of law, gender equality, market-oriented policies, and an overall commitment to just and democratic societies are also essential and mutually reinforcing.

12. We will pursue appropriate policy and regulatory frameworks at our respective national levels and in a manner consistent with national laws to encourage public and private initiatives, including at the local level, and foster a dynamic and well-functioning business sector, while improving income growth and distribution, raising productivity, empowering women and protecting labour rights and the environment. We recognize that the appropriate role of government in market-oriented economies will vary from country to country.

13. Fighting corruption at all levels is a priority. Corruption is a serious barrier to effective resource mobilization and allocation, and diverts resources away from activities that are vital for poverty eradication and economic and sustainable development.

14. We recognize the need to pursue sound macroeconomic policies aimed at sustaining high rates of economic growth, full employment, poverty eradication, price stability and sustainable fiscal and external balances to ensure that the benefits of growth reach all people, especially the poor. Governments should attach priority to avoiding inflationary distortions and abrupt economic fluctuations that negatively affect income distribution and resource allocation. Along with prudent fiscal and monetary policies, an appropriate exchange rate regime is required.

15. An effective, efficient, transparent and accountable system for mobilizing public resources and managing their use by Governments is essential. We recognize the need to secure fiscal sustainability, along with equitable and efficient tax systems and administration, as well as improvements in public spending that do not crowd out productive private investment. We also recognize the contribution that medium-term fiscal frameworks can make in that respect.

²³ Excerpt taken verbatim from the Monterrey Communiqué 2003

Source: <http://www.un.org/esa/ffd/monterrey/MonterreyConsensus.pdf>

16. Investments in basic economic and social infrastructure, social services and social protection, including education, health, nutrition, shelter and social security programmes, which take special care of children and older persons and are gender sensitive and fully inclusive of the rural sector and all disadvantaged communities, are vital for enabling people, especially people living in poverty, to better adapt to and benefit from changing economic conditions and opportunities. Active labour market policies, including worker training, can help to increase employment and improve working conditions. The coverage and scope of social protection needs to be further strengthened. Economic crises also underscore the importance of effective social safety nets.

While this new paradigm greatly downplayed the anti-statist approach of the liberalization and structural adjustment agenda, it did however lead to a spillover of the liberalism agenda into the process of governance. The preceding agenda was dominated by the reversal of government/public sector growth, liberalizing the regulatory frameworks and divesting state stakes in enterprises, this new development paradigm considers liberalization of governance, including public sector management and public service delivery. Intertwined with the broader notion of *'good governance'* was a new approach to public sector reforms, mainly managerial reforms that promoted market principles in governance of the public sector, known as the *'New Public Management'*. The main premise of the NPM is to revisit public administration frameworks characterized by centralized procurement, provisioning and policy formulation, in favor of more decentralized, responsive management. These reforms can be considered as 'market enhancing governance reforms', given their accountability, efficiency and participation enhancing attributes, they cannot necessarily yield sustained growth or improvement in the state capacity to produce equitable socio-economic results. However, if we evaluate the growth and welfare strategies that were adapted as part of the growth and welfare enhancing strategies adapted by the early industrializers as well as the successful developmental regimes, their public management approaches were significantly different.

While this chapter shall engage in a greater detail with the notion of developmentalism, NPM and decentralization in the subsequent sections, the constructs find their base in the following assertions:

- a) The contexts that have been successful in managing a high growth trajectory along with a structural change did not have the requisite capacity at the outset of the reform process. This capacity building process is organic and temporal;
- b) Coercive recourses are insufficient in building effective state capacity even where the nature of the political system is authoritarian, apart from being unsustainable. Building state capacity in this course deems imperative the state's ability to deliver broad-based and efficient, effective and responsive services;

- c) Enhancing DRM in order to foster greater policy autonomy by the developing countries in establishing development targets and the modalities to achieve them, foster greater accountability and responsiveness, and (re)align the strategies of economic and social stakeholders with the national development agendas;

Section 2, 3 and 4 of this chapter analyze the notion of a developmental state, its imperatives and nexus with democratization in the establishment of a democratic developmental state. These sections while outlining the theoretical constructs also engage in analyzing the experiences of the highly successful and less successful states in three main capacity realms: political, domestic resource mobilization, and allocative and enforcement. Section 5 examines the prospects of the compatibility of decentralization reforms with the establishment of a democratic developmental state.

2.2 CONCEPTUALIZING A DEVELOPMENTAL STATE

As the preceding section has exhibited, there is significant ongoing contestation about the ambit of the state and the way it is structured. The debate on the scope of state authority finds itself oscillating between two extremes – the minimalist one that requires the state to limit its action to a limited set of functions that cannot be performed by any other entity but the state, and the other view places argues for the state taking a lead role in improving the economic and social development of its citizens. This research engages with the latter end and its overarching focus remains on fostering a democratic developmental state, of which decentralization is an important requisite. This section puts forward a conceptualization of the developmental state and its interplay with democracy, the notion of good governance, and the attributes essential for the creation of a democratic developmental state.

The notion of a democratic developmental state has been considered as ‘a rare bird on the developmental scene’ (Robinson & White, 1998), which leads to the arguments of incompatibility of developmentalism and democracy. The arguments against the notion of a Democratic Developmental state extol the mutual incompatibility of the key features of the individual constructs of democracy and Developmentalism; e.g. autonomy of policy making is critical to developmental policy and accountability is a critical requirement of democratic norms, but under a DDS making the policy framework accountable may compromise the autonomy of developing one. For the sake of a cogent analysis, it would be best to examine the concepts of developmentalism and its democratic variant independently before analyzing the connection points. The notion of democratic developmental state will be discussed in exclusive detail in Section IV, and this section and the subsequent one shall engage with the concepts, requisites and experiences of developmentalism.

Developmental state has, like decentralization, enjoys a significant heterogeneity in its conceptualizations. One definition considers a developmental state as one that:

‘..puts economic development as the top priority of governmental policy and is able to design effective (policy) instruments to promote such a goal’ (Bagchi, 2000).

Bagchi’s conceptualization as a broad definition does justice, but in terms of the attributes a developmental state eschews, Leftwich argues that a developmental state:

‘concentrates sufficient power, autonomy and capacity at the centre to shape, pursue and encourage the achievement of explicit developmental objectives, whether by establishing and promoting the conditions and direction of economic growth, or by organizing it directly, or a varying combination of both’ (Leftwich, 1996).

The pioneering conceptualization of a developmental state was presented by Johnson (1982) in his analysis of the rise of industrial Japan. The main premise of his arguments therein was that the Japanese success in catching up with the West in terms of its technological endowment as well as the economic wealth was rooted in a strong, capable and merit oriented state bureaucracy coupled with the state’s policies on export promotion, policy consistency regardless of the change in the government incumbency, domestic growth orientation and a strategically oriented industrial coordination policy where the state acted as a guiding and coordinating agency. The Japanese policy framework, at least in principle, was subsequently adopted by most of the South East Asian economies whose sustained growth and industrial advancement was attributed to the developmental stance of their respective governments and the establishment of a developmental public institutional framework (Ayres & Freire, 2012; Ferguson, 1990; Joshi, 2012; Robinson & White, 1998; Wylde, 2012). The DS model has had limited success in being a mainstream strategy in the international economic policy narrative, primarily because of the dominance of the neoliberalism as the core model of economic organization and development for the 21st century (Lee & Han, 2006; Stubbs, 2009). Owing to this dominance, an argument can also be made that in the context of developing countries where domestic resource mobilization and the fiscal resource pools are strained, there is a reliance on donor or international bilateral assistance to bridge the resource gaps and since the donor policy mix acts in consistency with

the neoliberal paradigm, the scope for establishing a DS in such contexts can be a daunting task. While this argument is quite valid, a contrasting argument can be made on the grounds of ‘agency’.

Even though the exigencies of the international strategic and economic order may pose a structural constraint to the policy choices imperative for a developmental path, the implementing agencies in the local context (primarily the government and the political elites in the domestic sphere) continue to command a high degree of autonomy that can also be used to pursue a developmental trajectory as a key prerogative (Burki et al., 1999; Crewe & Harrison, 1998; Fukuyama, 2004). Another feature of a developmental state has been the ‘embedded autonomy’ of the state and the primacy of strategically oriented targeted intervention of the state (Evans P., 1995). In Evans’ (2012) view the notion of embeddedness implies that the governments or the state authorities cannot venture into economic matters without incorporating the information obtained from the non-government actors in that particular polity. The notion of autonomy implies the independence or non-reliance of the state on private interests in the undertaking of any economic policy. Considering these two constructs together highlights legitimacy aspects and the integration of the populace in the public policy-making that keeps the broader interests of the constituents in mind instead of being held hostage to narrower private incentives of a select few. An associated attribute of a DS is the state’s ability to regulate agencies (private or in some cases public) that do not conform to the imperatives of the socio-economic development envisaged, while also limiting the influence of elite groups or vested interests to manipulate the political process to secure their own gains. Doing this deems imperative that the state be in possession of a capacity that is adequate enough to neutralize the influence of the entrenched interest groups, mostly feudal in the context of developing economies (Migdal, 1988).

Such a capacity can only be acquired if the state enjoys a thorough control over the resource mobilization, allocation and assimilation that takes place through a politically insulated bureaucratic structure. A developmental state can thus, in the presence of these attributes be able to exercise a considerable leverage over the endowed classes as well as the flow of international capital in the economy. It must be noted that in spite of having a greater role of the state, the DS model does not advocate state exclusivity in economic operations as in the planned economy systems. The DS model that has been seen during the 1980s and 90s in South and South East Asia presents quite a contrary picture i.e. state and market agencies operating simultaneously. Significantly different from the polar systems of economic organization at the time, the Asian development model presented a centrist approach that seemed more pragmatic and sustainable than that on the extremes. The arguments for the DS model argued that such a state would, in its ideal conduct, ‘combine authoritarian technocracy

with a relatively egalitarian distribution of income and wealth' as it bridled (with rational confines) instead of outright suppression of the private enterprise or the profit driven market impulses (Radice, 2008).

Contrary to the neoliberal discourse that argues for the market forces' command of the social organization and economic affairs, a developmental state has more of a 'neo-mercantilist approach to economic relations', both internationally and within the national confines (Ghani, 2005). Furthermore, such a state is also characterized by the primacy of political realms and the state in command of the domestic social structures targeted at bridling both the civil society as well as the elite influences subservient to the whims or the writ of the state (Leftwich, 2001). Another feature central to the idea of a DS is that in addition to the institutional and political framework, it also derives its 'legitimacy' from a strong ideological component that has at its core nationalism (Bagchi, 2000), a collective belief in the 'development urgency'(Leftwich,1996), and confidence in the state's role in ensuring the well-being of its constituents.

In the course of establishing a DS, the state must possess the 'determination and ability to stimulate, direct, shape and cooperate with the domestic private sector and arrange or supervise mutually acceptable deals with foreign interests' (Leftwich, 2001). A synthesis of the conceptualizations and definitions of a developmental state can be that a DS is committed to a national development agenda that has at its core capacity and outreach, and geared towards an inclusive growth trajectory that targets poverty alleviation and, effective and efficient public service delivery. Furthermore, the recent literature on the notion of developmental states also places a great attention on the state's infrastructural power and political commitment to the developmental objectives. According to Ghani (2005), a developmental state ought to be essentially characterized, at the very least, by the following two attributes:

- a) The state must have the capacity to have an established writ in a significant majority of its territorial boundaries that enables the formulation and implementation of public policy frameworks.
- b) The developmental vision must entail greater outreach and inclusiveness, whereby the vision is targeted at long term objectives that are not limited to one political tenure/ regime or have limited political ownership.

With these conceptualization and attributes of the DS, one must also acknowledge that the developmental policy stances can be quite heterogeneous in terms of what they seek to pursue. Joshi

(2012), identified three specific varieties of developmental states: Human Developmental State, Resource Developmental State, and Social Developmental State. This disaggregation by Joshi (2012) is especially relevant to the purview of this dissertation as it enables a consideration of the DS concept as a broader policy orientation of the state instead of a narrow set of bureaucratic or policy initiatives, to foster an inclusive process of socio-economic development. This is also different from most of the existing conceptualizations of the DS that generally extol the growth orientation of a policy regime that operates in a close collaboration of the political incumbents and the state bureaucracy.

A *'Human Developmental State'* is considered as one that engages in the human capital emancipation for its constituents. This model has been evident in the East Asian developmental experience, whereby there was significant public investment in universalizing primary education and subsequent levels to develop the 'human capital' necessary for the economic and sectoral development as envisaged. Given that most of the East Asian countries had a low natural resource base (particularly Japan and South Korea), the impetus for economic development comes through a knowledge base that comprises of high technical expertise, innovation, skills and training of their constituents.

A *Resource Developmental State (RDS)* is one that bases its development agenda on the exploitation of its natural resource capital. States in the Middle East (UAE, Saudi Arabia, to some extent Libya), Africa (Uganda, Zimbabwe, Botswana), and Latin America (Bolivia, Venezuela, Guatemala) are prime examples of an RDS where the states' developmental orientation is grounded in the exploitation of their 'natural capital' to generate the wealth. Creating wealth or economic progress, in the absence of a domestic capacity (both technological and human resource), have a dependence on external partners (states, as well as enterprises) in the resource exploitation process. Once the fiscal resource base of the state expands to a sizeable degree, the reinvestment of the gains from the resource exploitation is made into social welfare and human development areas.

The third of Joshi (2012)'s conceptualization of a DS is the *Social Development State (SDS)*. Such states are oriented toward an active pursuit of promoting 'cross-class coordination, mutual trust, and social cooperation without necessarily exploiting an abundance of natural resources or investing heavily in human capital' (Joshi, 2012). The orientation for socio-economic egalitarianism through public investments and redistributive policy regimes are the hallmark of an SDS, and unlike the RDS and HDS, an SDS also actively fosters an inclusive political space. Viewing in a purely economic context, distinguishing between growth and development mirrors the difference between the orientation of the *'laissez-faire'* orientation of profit maximization and free markets, and a rational judgement of its potential pitfalls for serious shocks resulting from market naturalism. While the

former considers any incoming action from beyond the realms of the market inhibitive to growth (and by extrapolation, development), the latter pertains to establishing corrective mechanisms for the predictable and inherent shocks as a consequence of market naturalism through a regulatory or active agency role of the state in the economic ensemble. This regulatory, oversight or productive functions of public policy comes as a consequence of predominantly institutional and political responses to the market dysfunctions.

Wrapping up the conceptualization that this section has endeavored to deliver, developmentalism implies, by virtue of the 'ism' suffix: a process of progression and development with a social dimension instead of narrow economic dimensions, generating historical paradigms and configurations. Setting the perimeters of the notion minimally, it can be associated with the theme of heterodox economic organization or what is broadly considered the capitalist periphery. It can thus, be considered as a process of deep social transformation, rationally operated against a politically committed state, to bridge the economic and social progress gaps. Extrapolating from this premise, developmentalism finds an ideal context in chronic structural and distributive imbalances whereby its transformative conduct needs to be systematic, socially oriented and politically sustained change.

2.3 BUILDING A DEVELOPMENTAL STATE: LESSONS FROM THEORY AND POLICY

Given the purview of this dissertation, the following section identifies and explains the key imperatives for the establishment of a developmental state. Having gleaned the findings from most of the available literature on the notion of DS, this research puts forth three key attributes that must be the objective of any public reform geared towards the establishment of a DS (particularly in the developing countries context), going beyond what has previously been identified. These are:

- a) State Resilience and Social Cohesion
- b) Enhancing the Allocative and Enforcement Capacity of the State
- c) Enhancing capacity for resource mobilization

State Resilience and Social Cohesion

Perhaps the most important aspect in establishing a successful developmental state is the notion of state resilience, which is inextricably linked to the notion of social cohesion, as the former operates as an aggregation of the latter. State resilience happens to be a highly subjective concept that finds its roots in the notion of 'state building' and spans social, political and economic realms. While

the economic dimension of state resilience is better expressed in the context of resource mobilization (both domestic and external), this section would deal predominantly with the socio-political aspects.

Social cohesion is ‘the nexus of vertical and horizontal social capital and the balance of bonding and bridging social capital’ (Colletta & Cullen, 2000). Social capital, being a fairly subjective concept, enjoys considerable heterogeneity in terms of its definitions and conceptualization. However, for the purpose of the current endeavor, Putnam’s definition of social capital as ‘networks, norms, and social trust that facilitate coordination and cooperation for mutual benefit’, is the most consistent (Putnam, 1993). ‘Bonding’ social capital implies the intra-group linkages and the ‘bridging’ capital refers to inter-group links. While there is no concrete evidence on whether social cohesion and the extent of state resilience are correlated positively or adversely, given that both are not easily quantifiable and neither is an independent analysis of the other factors that could have an impact on state resilience. Nevertheless, there is a strong consensus on the notion that social cohesion is an important determinant of state resilience in the policy and academic debates (Kaplan, 2008; Marc, Willman, Aslam, Rebosio, & Balasuriya, 2013; GIZ, 2012; Easterly, 2000).

With the role of social cohesion as an influential factor for fostering state resilience established, attention shall now be devoted to a more intermediary factor that succeeds the former and precedes the latter: the notion of state building. Most of the contemporary states, especially in the developing world, find themselves engaged in the state-building process in either post-colonial or newly autonomous contexts. This is an important fact that needs to be taken into cognizance because the context of each state engaged in the state-building process is instrumental in framing the social expectations. For instance, under colonial regimes most of the pre-existing relationships between the state and the citizens were dismantled. Consequently, post-colonial transitions were marred by fissures, violence and most commonly a systematic elite capture. In many such contexts, the process of state-building involved sidelining ethnic or religious identities, and coerced compliance to the institutional order promulgated by a non-representative at worst and a non-responsive elite or a coalition of the elite (Latour, 2005; North, 1990; Pierson, 2004; Robinson & White, 1998).

It can thus be argued that there will be heterogeneity of both the expectations as well as the experiences of the constituents with the state. Hence, for any analysis on the state resilience, an analysis of the processes of reconciling societal expectations with the state functioning and state capacity is imperative. Therefore, the discussion from here on shall focus on an approach to state

resilience that focuses on the processes for articulating and reconciling this ‘capacity expectation’²⁴ gap that can also be considered a conceptual equivalent of negotiating a new ‘social contract’. It is the degree of inclusiveness and the strength of this articulation and reconciliation process that shall determine the extent to which the state improves its responsiveness, effectiveness, efficiency and cohesiveness and resilience. In order to examine this articulation process, it would be more analytically convenient to employ a reverse induction approach to the notion of state resilience by looking at state fragility instead.

Approaching it this way not only entitles the analysis to be more expansive but it also has a greater explanatory power with respect to the two cases this dissertation seeks to examine in the next chapters; Bolivia and Pakistan. The notion of ‘state fragility’ is a polar opposite of a resilient state, and is said to arise amid the “state’s ineffectiveness in enforcing contracts, protecting property, providing public goods and raising revenues”; or when “political violence either in the form of repression or civil conflict”; or a simultaneous existence of both (Besley and Persson, 2011: 373).

While a detailed analysis and review of the notion of state fragility is beyond the scope of this research, the analysis shall be limited to secondary conceptualizations such as the following disaggregated into five distinct forms presented below:

| Types of Fragility | Characterized by |
|-----------------------------|---|
| Weak States | Low level of administrative control either across the entire territory or in sections |
| Divided States | Substantial ethnic, religious and/or social cleavages |
| Post Conflict States | Experienced protracted periods of violence |
| Semi-authoritarian States | Imposition of order through coercion, lack of legitimacy |
| Collapsed States | Core national institutions such as defence, parliament, judiciary and the executive, do not function at all |
| Source: Call & Wyeth (2008) | |

Building upon this conceptualization, one can also consider highly authoritarian states as an addition to those provided by Call & Wyeth (2008). Furthermore, while the aforementioned have been considered as categorizations of state fragility, this research considers them as attributes or

²⁴ It must also be noted that when considering the citizen expectations with the state, one must acknowledge that the importance of retrospection. A retrospective citizen or group shall frame its expectations in accordance with the experience of interaction with the state. For instance, in contexts where the state is characterized by non-responsive service orientation, exploitation through coercion and over-taxation, the citizen perception of the state would most likely be that of a distant, non-responsive entity which would have its implications (neutral at best, but most likely adverse) on their compliance with the state’s promulgations.

characteristics that may not be distinct and can also occur simultaneously in a particular context²⁵. Moreover, these attributes or dimensions can also be considered as a spectrum whereby states do not exclusively rest on these conditions but instead have degrees of division, weakness and authoritarianism. Given that various interacting factors, operating independently or in tandem, have a bearing on the nature of the social contract, it is not an easy endeavor to stipulate a framework to see which contexts can deepen the fragility or which may see it being mitigated. While the importance of the ‘expectation and capacity’ gap in the articulation and deliberation of a new social contract have been outlined earlier, attention will now be devoted to the procedural dimensions, primarily the political processes in place through which the state-society bargaining takes place and is institutionalized. Of a critical importance to the political processes are two factors; a ‘credible commitment’ of the domestic elite networks to channel the state resources and capacity for meeting the constituents’ expectations, and the legitimacy of the state or the incumbent political regime in participating or initiating the political processes. The legitimacy of the incumbent regime or the state manifests in various domestic forms that may be distinct and non-mutually enforcing; it could be embedded or residual (rooted in historical events or bequests of a preceding system), or procedural legitimacy (often a scenario found in procedurally democratic contexts that will be discussed in length in the country analysis of Pakistan in the subsequent chapters). In addition to the domestic forms, legitimacy of the incumbents may also stem from the external/international arena in the form of recognition or reinforcement from multilateral agencies or even states.

Consistent and continuing negotiations between the state and the society positively refine and institutionalize the social contract, and a dynamic equilibrium in this regard is an important requisite of fostering state resilience. Therefore, resilience can be considered as the ability of the state to bridge the expectation-capacity gap, changes in the nature of its legitimacy as well as its functional effectiveness. The question that now arises is, how can state resilience be achieved in the contexts characterized by weak political processes that are inadequate in a dynamic negotiation of the state-society contract? This research identifies two main strategies to foster state resilience discussed as follows:

²⁵ In a context where the state institutions find themselves limited in their ability to exercise their writ over the entire territory or geographical scope of the state, one can also find ethnic, social or religious groups that challenge the state’s legitimacy which may result in semi-authoritarian practices to reinforce the state’s which in turn adversely affects the nature of the state-society contract. The classifications need to be considered as illustrative of a non-binary continuum.

I. Reforming the Political Processes

One of the ways forward in this regard is a reform of the exigent political processes. The most important political processes in the context of state fragility or resilience are the nature of competition in the domestic political space, and the degree and/or nature of mechanisms enforced for the state's/incumbent executive's accountability. This assertion is substantiated by the findings of Goldstone, et al.. (2005) study, that where the political space is more factionalized, restricted or repressed the vulnerability to fragility and instability is high. The reason is that the political parties' failure to mediate conflicts between different social groups primarily because their legitimacy and support base is linked to these divisions, and as a consequence amplify rather than exacerbate the differences.

Legitimacy is also enhanced by making the political processes more inclusive, deliberative and participatory. The participatory and deliberative aspects pertain to the consultative mechanisms embedded in the political process that put forth a forum to negotiate and articulate diverse interests. These consultative mechanisms, especially when done at the elite levels of a socio-political order, enables the incorporation of the previously excluded groups into the political space and interest articulation by these groups thereby making them active stakeholders than mere subjects. This brings into the spotlight an associated stream of literature on the theme of state resilience, the role of elite pacts in a context characterized by a political transition (more specifically between an autocratic to a democratic regime). Negotiated contracts between the elites and their subject social groups, in the absence of a broader harmonization of concessions across the entire national constituency can result in generating contradictory outcomes that could also result in polarizing the political space.

This is especially true in contexts where the elites or a coalition of elites, are benefitted by retaining their focus on their traditional constituencies. In order to grapple with this problem, there ought to be an institutional mechanism that incentivizes elite coalitions and the development of a common agenda that is not rooted squarely in their own constituencies but transcends into a broader socio-political priorities of the polity. An example of this can be found in the case of Nigeria, where the political parties need to have their executive bodies comprising of 2/3rd of the country's regions with no allowance for any regional or social preferences in their political campaigns. In addition to a stipulated regional representation in their executive councils, the political parties are also required to have their membership base of at least a 1000 individuals in 2/3rd of the districts and municipalities. (Edigheji,2005).

Another way to institute political reforms is to establish accountability mechanisms for the incumbent governments' and their exercise of their executive authorities. The key institution in this

case, especially in the absence of decentralized governance, would be the judiciary and its autonomous conduct to uphold the rule of law. However, judicial empowerment alone cannot be an adequate guarantor of sustainable and strong accountability mechanism, and the decentralization of governance will be a strong guarantor of the executive's decisions.

II. Fostering Democratization and Economic Progress

Globally there has been an enhanced focus on democratization, especially so in the developing countries that have historically been host to either authoritarian regimes or an imperfect democracy at best. Owing to internal and external pressures for a more inclusive domestic political space in non-democratic or quasi-democratic states, the notion of hybrid regimes has taken roots (Ottaway, 2003). Hybrid regimes are those political regimes that are attributed by some procedural democratic norms but fall short on the substantive requisites of liberal democratic ideals. It must also be noted that the hybrid regimes cannot be considered as distinctive absolutes as they are characterized by varying levels of democracy and autocracy, so at best, they can be considered as 'transitional' polities. While the hybrid regimes have been existing in a lot of contexts in the developing world and have exhibited a fair degree of stability, they are also characterized by a significant latent instability (Mansfield & Snyder, 2002). Hence, any attempt to foster democratization in such contexts involves intense contestation across the social groups as well as in the process of interest articulation.

Furthermore, in the contexts where there is a paucity of institutions that can potentially manage mass participation, mobilization and political competition, there is an incentive for the established elite networks in the domestic context can resort to their conventional strategies to retain their influence. Thus, for a democratization initiative to succeed, it is imperative that not only should the reform process be accompanied by credible commitment of the existing institutional framework but also be credibly directed towards the establishment of strong democratic organizations. This is again a notion that will be discussed in the section on decentralization and its interplay with democratization. Such a credible commitment and direction ought to come from state institutions committed to uphold the rule of law, impartial judiciary and electoral commissions, active civil society and a competent bureaucracy acting as an executor of the executive's policies.

Finally, a key imperative for promoting state resilience is stable and progressive economic performance ideally with a democratization process in the backdrop. While the empirical data on the connection between democracy and economic development (including the direction of causality) remains mixed at best (as discussed in Chapter 1), there are quite a few normative advocacies that extol the importance of the economic performance on the government's legitimacy and the extent of socio-

political inclusion; both of which are important determinants of state resilience. When characterized by poor economic performance, both at the macro level and also in terms of the 'pro-poor' dimensions of economic growth, autocratic regimes can confront weaker legitimacy and growing pressures for a democratic transition (Arab Spring being a case in point). However, the transition to a more democratic regime has a similar latent instability and can find its legitimacy depreciating in the wake of poor economic performance (Ghani, 2005). According to Przeworski (2002), democratic norms as well as the sustainability of a democratic system is more frequently found in economically developed contexts, not because democracies are more likely to emerge as a consequence of economic development but because their sustainability is defined by the economic performance. Furthermore, democratization comes in various forms and manifestations, but once a democratic transition has been made its survival is inextricably linked to the economic development.

Going back to the 'state capacity-citizen expectation' dynamic equilibrium as a key determinant of state resilience as presented earlier, one can observe that with a greater democratization comes a greater citizen expectation of what the state must deliver to its constituents, and if the expectations are not adequately matched then the resulting instability can make the state's resilience a distant dream.

Enhancing Allocative and Enforcement Capacity of the State

A key feature of an effective developmental state is its capability to deliver responsive and effective public services, for which its capacity for allocating resources for PSD and establishing potent enforcement mechanisms are important (Radice, 2008). The allocation and enforcement functions of state policy remain the prerogative of the executive, of which the bureaucratic edifice remains a key agency as it is responsible for the policy implementation. This section shall engage firstly with a normative discussion on how the nature and orientation of the bureaucratic institutions need to be reformed, followed by an analysis of the policies adapted across different contexts in this regard.

The establishment of a DS in general, takes us back to the concept of a 'rational bureaucracy' and the tenets of the New Public Management discourse, and this research contends that enhancing the effectiveness and the efficiency of the bureaucracy can be brought about through a selective amalgamation of their attributes instead of an expansive and exclusive subscription to either of them. However, this research engages at a greater length with the NPM concept and how it can be instituted in developing contexts, with the Weberian rational principles only serving to define the normative character of the bureaucratic structures. This approach is chosen primarily because the contemporary discourse in both the policy and academic discourse on reinventing governments for greater public

effectiveness and efficiency, extols the NPM as a means of putting the tenets of the good governance agenda into action (Blair, 2000; Fukuyama, 2004; Grindle, 2004, 2011; Oxhorn, Tulchin, & Selee, 2004; Turner & Hulme, 1997). Before dwelling on the NPM and its relevance in the establishment of a developmental state, it is important to briefly examine the notion of ‘rational bureaucracy’ rooted in the Weberian conceptualization of bureaucracy (Weber, 1990). Weber argued that a rational bureaucracy is one that is organized according to rational principles characterized by: a) Hierarchy of authority; b) Impersonality; c) Formal and established rules of conduct; d) Merit oriented progression of the incumbents; e) Specialized division of labor and resources; f) Efficiency. Following on his conceptualization, bureaucracies can be taken as goal directed organizations designed on rational principles for the efficient attainment of the assigned goals. A hierarchical bureaucratic structure allows for an upward mobility of information and a downward mobility of directives and orders.

The operations and conduct of the mandated activities are guided by formally established and written rules that clearly demarcate the responsibilities and functional aspects of exercising authority by the incumbents. The appointments in the structure are based on specialization of the appointees rather than an ‘ascriptive criteria’ whereby appointments are made on the basis of the candidates’ association with a particular social group, political party or ideology. All of these characteristics are guided towards the efficient attainment of the goals assigned. The point to be noted, however, is that the Weberian conceptualization did not disavow the latent propensity of dysfunctionality of these structures, and aimed to present an ‘ideal type’ bureaucracy²⁶. Most of the criticisms of the Weberian bureaucratic model were based on its rigidity, excessive rule-compliance, lack of public accountability, cost inefficiency of elaborate bureaucratic structures and the lack of responsiveness as the public services ended up being ‘provider-dominated’(Ferguson, 1990; Flynn, 2007a; Zamor, 1985; Pollitt & Summa, 1997). With this in the backdrop, the 1980s witnessed a new wave of public sector reforms that since then have been at the core of the public sector organization in developed, transitional and developing countries alike. As the neo-liberal economic doctrine took roots in the global economic policy, the role and the institutional form of the state and its operations faced the need to be more market oriented in outlook, and private sector-oriented in their organization (George, 1999). This was initially witnessed in the developed OECD countries, and later in the developing countries that were collaborating with the IFIs (World Bank and the IMF, and others) in financial arrangements or structural adjustment programs. This revisit of the role of the state and public sector organization also finds its roots in the

²⁶ The Weberian conceptualization of bureaucracy has often been misconstrued as one that considers bureaucracy as an ideal form of organization. There have been other criticisms of his conceptualization that the real world bureaucratic structures are incapable of fitting well with his ‘ideal’ characteristics.

fiscal crises witnessed in the 1970s and the 1980s, and more recently post 2008 whereby the scope and size of the public sector and bureaucratic operations were considered for a scale-down. The contemporary discourse on public sector organization and management focuses on incorporating private enterprise styled management techniques and mechanisms in the public service delivery, given that PSD in the contemporary state has gone beyond the state's exclusive jurisdiction especially with the emergence of CSOs and para-statal organizations (Burki et al., 1999; Leibfried & Zürn, 2005; Oxhorn et al., 2004).

This is considered as the New Public Management or neo-managerialism in the public administration literature (Pollitt & Summa, 1997). While a consensus on what the elements of NPM need to be have so far evaded a consensus, a common denominator identifiable from all the conceptualizations surrounding the notion has been the introduction or emulation of the performance incentives and organizational design of the market-oriented agencies, in those realms of public service that exclusively remain in the public-provisioning domain. Table 2 outlines few of these oft cited conceptualizations of NPM. A common denominator across all advocacies in favor of the NPM oriented PSRs has been that exposing the public sector operations to the market dynamics and a more private-sector styled orientation to service delivery shall result in improved efficiency and effectiveness²⁷. The discussion will instead be directed to a brief overview of the critique that the superior effectiveness and efficiency yield advocated by the NPM advocates has received. One of the most seminal works in this regard is by Batley (1996), who studied the introduction of competitive norms and private provisioning of public services across a pool of 6 developing countries and concluded that this remains a 'presumption' that can only be 'partially supported by evidence' (Batley, 1996).

Bolstering efficiency of service may result in an increased focus on cost efficiency, which could undermine the state capacity in pursuing a long term perspective on issues such as education, health and technology, in the interest of those with short term gains such as infrastructural development. Amongst other critiques of the NPM agenda, it has been argued that it may result in promoting self-interest as the public agencies may favor outsourcing or privatization due to higher opportunities of rent seeking. This is particularly in the developing countries, with well entrenched systems of patronage and limited accountability, and the discretionary space that the NPM strategies allow the public agents are susceptible to abuse. Furthermore, with a greater 'fragmentation' of public service

²⁷ While a more substantive elaboration of this remains beyond the purview of this dissertation, support of the efficiency and effectiveness improvements can be found in the works of Pfiffner (2004), Stewart and Walsh (1992), Walsh (1995), Flynn (1993).

delivery channels, monitoring and accountability challenges may end up adding to the transaction cost of the service provision. While, NPM has significant potential merits in the realm of public sector reform, it can by no means be considered as a panacea. This line of argument also dominates the decentralization debate, and the response also remains similar – there is no specific set of reforms that can be implemented in all contexts, and can at best be selectively applied after taking stock of the local dynamics of the reform context.

Given the main critiques in the preceding paragraphs and the oft-cited attributes/components of NPM, this research identifies some of these components that could be of essence in enhancing bureaucratic effectiveness, efficiency and responsiveness in line with the requisites of establishing a democratic developmental state. Given that the purview of this dissertation spans the realm of governance decentralization as well, the analysis from hereon shall be focused on the decentralization of public service delivery that pertains to the fiscal and administrative dimensions of decentralization from a broader lens of ‘managerialism’ as envisaged by the NPM conceptualization. When the administrative and fiscal decentralizations exist in a context of effective political decentralization to the local levels, it would also enhance the accountability in addition to the responsiveness, effectiveness and efficiency (REE) dimensions. It would further facilitate, if not ensure, the Weberian ‘rationality’ in the bureaucracy. In the following discussion on the decentralization²⁸ of public service delivery, aspects pertaining to enhancing the bureaucratic quality (including REE) include:

a) Disaggregation of ‘monolithic’ bureaucratic structures into specialized agencies:

Traditionally large and monolithic, both in functional scope as well as size, public bureaucracy needs to be scaled down in size as well as functional domain through functional outsourcing, and division into smaller and specialized role executive agencies. Evidence of this can be found in most of the developed contexts in the OECD countries, but also increasingly in the developing world albeit to a varying degree (George, 1999; Pollitt & Summa, 1997; Pfiffner, 2004). This entails the functional a separation of the policy development and the implementing/operational aspects of the service delivery and design process. The greater operational autonomy as well as distinctly drawn ambits enable these specialized agencies to operate with synergies instead of abiding by traditional hierarchical structure. While this remains the theoretical elaboration of the arrangement, the policy response ought to be a structural

²⁸ Decentralization in this discussion deals exclusively to the managerial dimensions instead of the broader governance decentralization.

reorientation of the government towards a leaner hierarchical model. The proponents of the executive agency model have extolled the enhanced operational flexibility of these specialized agencies in terms of resource allocation and distinctive role specification attributes to positively reinforce the accountability of these agencies (Jervis & Richards, 1995). The development of specialized agencies from a prior centralized framework of governance also enables the insulation of the bureaucratic agencies from the political contestation and preferential political interest articulation.

b) Devolution of Fiscal Resources and Budgeting to Local Levels:

A complementary requisite to the establishment of the executive agencies is the fiscal devolution to these specialized agencies. Though more of a procedural aspect in terms of creating budgeting and financial control with these agencies, the more substantive dimension to the fiscal devolution is the fiscal resource allocation corresponding to discretionary authority to the subnational tiers. While the fiscal devolution at the local/regional governmental level shall be dealt in a greater detail in the subsequent section, the allocation of devolved fiscal pool to these executive agencies shall be accountability and efficiency enhancing.

d) Segregation of Production and Provision Functions

The separation of the service provision function from the production functions is also imperative to quality enhancement. This functional demarcation enables the creation of quasi-markets within the PSD space, whereby the central policy institutions are mandated with the production and design of the public services whereas the provisioning can be done through either the executive agencies or through an outsourcing to parastatal organizations. Evidence of this form of managerialism can be found in the case of the UK, which admittedly is not a good example in the developmental context but is considered here from the REE perspective, whereby the central agency responsible for health services NHS and its subservient District Health Authorities act as financiers and producers of the services that are delivered through autonomous hospitals act as providers (Lacey, 1997).

Of all the components of NPM, those consistent with the management decentralization hold the greatest promise given the underlying objective of a decentralized and democratic developmental state. However, for this managerial dimension to complement the overall governance decentralization,

democratization and developmental objectives, these must also be accompanied by more potent accountability systems. Drawing on the experience of developing economies where some form of PSR has been conducted on these lines and where accountability controls were weak and inadequate, managerialistic reforms may end up reinforcing arbitrary and corrupt behavior (Bank, World Development Report 1997: *The State in a Changing World*, 1997). This issue will be addressed in a much greater detail in the section on decentralization.

With this in the background, one ought to evaluate the policy-side experience in enhancing the state capacity on allocative and enforcement themes. The establishment or improvement in the enforcement and allocation capacities of the state requires, firstly, the state developing incentives for directing capital flows to priority industries. The experience of the developmental regimes in the East Asian countries substantiates this assertion, however holding that kind of coercive influence over the capital flow in contemporary times is not plausible, which is why the state needs to create incentives in the form of tax rebates on capital gains made in preferred sectors, higher interest rates amongst others. At the onset of the developmental policy regime in South Korea, for instance, most of the banks and Non-Banking Financial Institutions (NBFIs) were state owned which enabled the state to coordinate investment flows in consistency with its industrial and sectoral development priorities (Huang, 2008b; Joshi, 2012). This was in stark contradiction to the liberalized credit-based financial systems in the European economies and the US, and most of the East Asian developmental states (South Korea, Malaysia, Taiwan and China) used a subsidized credit regime in addition to other policy instruments such as concessionary tax incentives, export subsidies, and protectionist policies to reshape the incentive framework for the private economic agents operating in their economic space. Prior to the introduction of the neoliberal reforms and the SAPs, most of the developing economies of the world had instituted various growth enhancing policies which had a quite a few commonalities with the others. In terms of the policy orientations, the main commonalities found across most of the developing economies were that the developmental interventions by the state focused on enhanced growth allocation that was targeted at preferred growth sectors, and to foster expertise in these areas through incentivized directives.

Examining the policy regimes instituted by the East Asian developmental regimes, one can find evidence of the creation of '*nodal agencies*', that were mandated to gather sector specific research and information that was subsequently used for national development plans. The idea behind the establishment of these agencies is also complemented with insulating them of the influence of vested

interests and enabling a 'national character' and impersonal institutional status, a feature critical to the effective functioning of these agencies and the genuine developmental orientation of the bureaucracy (Bahl & Wallace ,2005). However, the efficacy of such institutions and their inputs in framing the national development strategies has been quite varied, with the exception of some East Asian States, in most of the developing countries that pursued a quasi-developmental agenda. This is attributable to various reasons of which inadequate political capacity, technical expertise, information asymmetries and rent seeking. For instance, in the case of India, the state's industrial subsidization strategy along with other protectionist policies during the 1970s to the early 1990s was widely hailed by the industrial constituencies but they vehemently opposed a strong Planning Commission that could monitor and enforce the directives. As a consequence, the state found it hard to meet the targets not only in the industrial development but also in the realm of the social policy imperatives. The inadequacy of political will, capacity and rent seeking was witnessed in Pakistan where the recurring phases of land reforms were promulgated by the central government and mandated to regional governments in the 1960s and 1970s, where the feudal interests dominated the legislatures and maximized their rent and endowment acquisition from the state's divestiture and distribution of land policy.

Finally, the enforcement as well as allocative capacities can be improved by instituting deliberative mechanisms in the political space e.g. giving space to the civil society organizations, citizen committees and locally embedded civic agencies, in the policy development processes. At the core of such deliberative mechanisms lies transparency and information disclosure, that can enable public accountability and reducing the costs of public resource allocation and policy enforcement. The oft-cited case of Participatory Budgeting in Porto Alegre, Brazil is one example of such deliberative mechanisms, which involved a range of CSOs, citizen committees and locally embedded civic actors to deliberate with the state officials (at the local level) on resource allocation. Not only has this policy experiment attracted a lot of policy and academic attention on democratic and deliberative grounds, but it has also been of positive effect to the responsiveness of public service design and delivery, and, effective and efficient public resource allocation.

Enhancing Domestic Resource Mobilization

The capacity of a state to mobilize resources is of critical importance to its success in establishing a developmental regime. Though an emerging field in both policy and academic discourse, resource mobilization, of which domestic resource mobilization is the key, not only enhances the state's ability to define its agendas due to greater sovereignty over policy development as well as its

ability to implement its vision. As necessary for any strategy with such a potential, resource mobilization tends to be the most political economic strategy given that a lot of contestation takes place over the type, amount and source of resource generation as well as the allocation of the resources across the state's jurisdiction, both social as well as economic (in sectoral terms). Therefore, the state's policy orientation alone is a necessary but an insufficient condition to realize the resource mobilization targets, and their equitable and effective allocation for socioeconomic development (Leftwich, 2001; Hinojosa, Bebbington, Barrientos, & Addison, 2008). This section shall outline how the resource mobilization capacity of the state can be enhanced and how the context specific issues determining the nature of the state-society relations affects the state's capacity of resource mobilization for its developmental objectives. When considering the resource mobilization, it must be noted that a country's resource mobilization can come in two distinct forms; international (fiscal resource flows from external bilateral or multilateral sources) and domestic (mainly through indigenous mobilization of fiscal resources through taxation, natural resource mobilization, and domestic savings). Given the overarching theme of this chapter, a greater focus shall be placed on the domestic resource mobilization since that is a key determinant of state resilience as well as the sustainability of a developmental policy (Bahl & Wallace, 2005; Latin American Program, 2012; Pierson, 2004; Robinson & White, 1998; Stein, Talvi, & Grisanti, 1998; Wylde, 2012).

In the analysis that follows, three main strategies of enhancing domestic resource mobilization have been considered:

- i. Mobilizing domestic savings
- ii. Fostering state-society relationship through Fiscal Reforms
- iii. Mobilizing Natural Resource Base

i. Mobilizing Savings

Going back to the basics of endogenous growth theory, an economy's long run growth rate depends on its domestic savings rate as the savings enable capital accumulation that can subsequently be devoted to investment into technological progress and innovation. While a detailed critical analysis of these growth theories, including the AK model, the Romer innovation theory, Lucas model (dealing more with the accumulation of human capital than physical capital formation), amongst others are beyond the current scope of discussion, the idea is to merely illustrate the theoretical significance of domestic savings as a key to economic growth. This research assumes the causal relationship of the savings to economic growth and long term development as positive and bi-directional in line with the

findings of Deaton (1999), and views the domestic savings mobilizations through the domestic resource mobilization lens exclusively. In order to cogently explain the savings in the backdrop of resource mobilization for developmental objectives, this section will deal with the experience and strategies employed by the developmental states in DRM and the success it enabled for their developmental goals.

If one views comparatively the resource mobilization trends exhibited by the developing countries from the mid-1980s till date, it can be spotted that in spite of commonalities in the regional fiscal efforts (often assumed as the main strategy for DRM, and expressed here in terms of Tax-GDP ratio), the savings rates varied greatly across the spectrum and so did their rates of economic growth. Table 3, presents an overview of the DRM and growth comparisons of the developing economies from a regional perspective. It can be seen that the trend rate of the fiscal effort has been fairly consistent across the developing countries in all these regions, but the main difference in the growth rates of all the other regions and the East Asian states (which were actively pursuing a developmental regime through the 1980s, 1990s and somewhat liberally during the 2000s) can be attributed to the high savings rate. The East Asia and Pacific region posted an average savings rate of almost double that of all other regions during the 1980s and 1990s, and while it continued to maintain a growth in an already high savings rate the South Asian average savings rate during the 2000s increased phenomenally. Although the South Asian economic regimes, primarily in Sri Lanka, India and Pakistan were more on the neo-liberal lines, the growth in savings can be attributed to the overall economic growth in the region, which is an illustration of a counter-argument on the direction of the savings-economic growth causality put forth by Aghion, Comin, Howitt, & Tecu(2009). Furthermore, it must be noted that the gross rate of savings in Sub-Saharan Africa in the period 1960-1980 increased from 18% in 1960 to 26% in 1980, before plummeting in the 1980s and 1990s due to the SAP regimes in their countries that not only resulted in a growth slowdown but also in the purchasing power and hence the income remaining post consumption for most of the constituents (Bank, World Development Report: Attacking Poverty, 2000).

Table 3: Regional Level DRM and Growth Performance of Developing Countries

| Regions | Per-capita GDP Growth | | Tax - GDP Percentage | | Gross Savings as GDP (%) | |
|-----------------------|-----------------------|-------------|----------------------|-------------|--------------------------|-------------|
| | 1985-2000 | 2000 - 2015 | 1985 - 2000 | 2000 - 2015 | 1980 - 2000 | 2000 - 2015 |
| Sub-Saharan Africa | 0.4 | 2.3 | 19 | 16.46 | 13.2 | 18.02 |
| South Asia | 3.3 | 5.4 | 12.5 | 9.58 | 15.1 | 34.8 |
| East Asia and Pacific | 6.1 | 8.7 | 15.3 | 11.2 | 31.2 | 48.15 |

| | | | | | | |
|---------------|-----|-----|------|------|------|-------|
| Latin America | 0.8 | 2.2 | 15.5 | 11.7 | 20.3 | 18.75 |
|---------------|-----|-----|------|------|------|-------|

Source: Own calculations based on World Development Indicators and IMF GFS

With this in the backdrop, it would be important to see how the East Asian states managed to bolster their domestic savings. The main strategy employed by the East Asian states was the incentivizing and coercively induction of a higher savings pool in through restricted credit, fiscal austerity, compulsory ex-ante contributions (pension funds or EOBIs), and encouraging savings through greater interest commitment by the state financial institutions. For instance, in South Korea a policy of multiple interest rates on government bonds held by the public was introduced that gave a higher yield to savers and lesser to those who had debt or credit obligations. The case of Taiwan is perhaps, an even more pertinent case, as it financed most of its industrialization related investments from the domestic savings pool rather than seeking external credit lines for investment (Huang, 2008a).

Most of the East Asian contexts during their developmental regimes had relatively or fully authoritarian political dispensations, thus not only were they able to be autonomous in policy formulation, insulate the policy formulation and implementation from the ‘special interest’ groups, but also in enforcing incentives or coercive mechanisms to achieve the designated targets. This could lead the debate into another associated realm – would the state ability to mobilize private domestic savings still be high in democratic contexts? The answer would be in a conditional affirmative, because contextual dynamics may play a far greater role than the regime nature. The key determinants of the success of savings mobilization in democratic contexts would include on the incumbent regime’s stability, broad support, economic situation (in a slow growing, highly inflationary context savings mobilization policies might create further adverse effects on the budget constraints), and the availability of adequate savings instruments in the domestic financial markets.

b) Building state-citizen relations through taxation

Regardless of the nature of the political regime, one of the key requisites of effective domestic resource mobilization is the ability of the state to foster effective state-citizen relations. While the socio-political dynamics of state-society relations have been discussed in the earlier section of state resilience, the economic (primarily fiscal) dynamics of state society relations depend on the fiscal regime including not only the taxation but also the assimilation and allocation of the revenue pool to socially beneficial projects. The notion of taxation as a determinant of the resilience of the state-society finds its roots in the fiscal sociology literature, and though an expansive overview of the literature and

the concepts lies beyond the current scope, this section will outline some of the key facets of this approach before engaging with the strategies that could yield such improvements.

The notion of 'fiscal sociology' pertains to the '..sociological aspects of taxation and public finances' (Campbell, 1993). Another key conceptualization of the notion was put forth by Schumpeter, [1991 (1918)], who considered it as a 'macro-historical paradigm that captured, embodied, and laid bare the dominant drivers of societal, political and economic change' (Moore, 2004). There is a considerable body of literature in the realm of fiscal sociology as well as public finance literature, where the role of taxation in state-building, socio-economic development and developmental capacity has been well-established (See for instance, Call & Wyeth (2008), Ghani (2005), Bahl & Wallace, (2005) and Latin American Program (2012)). The role of fiscal instruments, like taxation, and fiscal reforms is central to the enhancement of the state capacity as well as 'state-building for various reasons. Given the critical role of state capacity in the establishment of a developmental state, these become all the more important. Consolidating fiscal space has tax revenues as its most important component in order to ensure a sustainable access to resources imperative for allocations and investments in socio-economic development programs. Furthermore, taxation is also a key element of the state linkage with the citizenry not only because it provides the state with a 'mandate to deliver' public goods and be accountable to its constituents, but also acts as a platform upon which different interest groups contest for their interests. Also, the effectiveness of the state can also be gauged by the breadth of the fiscal base which illustrates the state's engagement with competing regional and sectoral interests, as the nature and extent of the state's response to these contestations indicates the extent of its authority and legitimacy (Bräutigam, Fjeldstad, Moore, & (eds.), 2008). Legitimacy, it must be noted, transcends the procedural dimension of electoral outcomes, as they go only so far as to enable the citizens to articulate their interests. The other half of the legitimacy equation is to meet the demands of the citizenry for which resource mobilization, allocation and effective provision of the public services are the main requisites.

Based on the above, it can be ascertained that the 'supply side' of state resilience (inextricably intertwined with the state-society relation or the social contract as discussed in Section 3.1) composes of the state's capacity to mobilize the resources to meet the citizen demands effectively. Resource mobilization, in this case, can be considered as revenue (tax) collection capacities and can serve as a potent indicator of where a certain polity can be positioned on the fragility and resilience spectrum (Di John (2010), Lieberman, (2002)). Therefore, the analysis from here on shall focus on the components of state revenue collection that improves the resilience of the state and its relations with its citizenry.

The primary component in this context is the state's monopoly over public revenue collection, and partly for the same reason as the state's exclusive monopoly over the violence. Inhibiting the capacity of non-state actors to extract rents from the citizenry that may in turn be used to challenge the writ of the state over territorial boundaries as well as inhibiting the state's capacity to deliver the mandated public services. Rent oriented exploitation of local populations, often through the threat of violence, has been witnessed in various contexts in the developing economies and sometimes in the recent history of the developed polities as well (e.g. the role of the Mafia in sections of Southern Italy). Given that such non-state actors and their rent exploitation in return of 'protection' commitments induce the same kind of compliance from the local groups of citizens as the state would mandate thereby shrinking the influence or a 'sense of obligation' to the state. Therefore, when communities, local groups of citizens or even enterprises are coerced into an exploitative compliance from organized political groups (that may be political, as in the case of Baloch insurgents in Pakistan, numerous cases of civil conflict in Africa and the Middle East) that challenge the writ of the state, there is a great potential for a conflict to arise. This conflict can, in addition to the sociopolitical distortions, can also inflict substantial damage to the state resilience.

The next important component of the fiscal regime and revenue allocation to foster resilience finds its roots in the levels of tax collection as well as the breadth of the tax net. Considering the revenue collection levels, it is a fairly intuitive notion that the greater the levels of the fiscal pool (not disavowing the constraints outlined by the Laffer curve), the greater would be the ability of the state to institute broad-based service delivery and social welfare programs would also have a bearing on state resilience. The other part of this equation is the breadth of the tax base, i.e. the sources of the state's tax revenue. This can also be considered in terms of the nature of the fiscal regime; progressive or regressive. This is an important aspect to consider when looking for the state's capacity expansion as well as the state-society resilience. The state can have its revenue from sources other than taxation too, e.g. in the case of the mineral resource rich countries most of the state revenue stems from the domestic extractive industries. The state finds itself unaccountable to the public because most of these revenues channel directly into the exchequer without the state having to go through the bargaining processes with the socio-economic groups. This will be dealt with in a greater detail in the subsequent sub-section. Indirect taxation policies, most notably VAT, as well as various trade taxes may be of limited prospects amid the pressures of globalization and liberalization (Fund, 2013).

Direct taxation, perhaps the most common source of state revenue in terms of personal income tax and corporate taxation, has a significant bearing on the extent of state resilience. This is

where the progressive or regressive nature of the tax regime plays an important role. In most of the developing contexts that are also characterized by what North (1990) considers as ‘elite capture’, the policy making institutions (executive and the legislature) are biased in their taxation policy to the elite sectoral interests. Evaluation of the quality of any fiscal system needs to take into account the efficiency and equity dimensions. While the former deals with the distortionary (both positive and negative) effects of fiscal directives on economic decisions, the latter is of a greater concern in the context of this discussion. The equity dimension of a fiscal system is further disaggregated into horizontal and vertical equity. Horizontal equity pertains to treating taxable sources possessing similar attributes equally i.e. any given level of income needs to be taxed at the same rate, regardless of whether the source of income was labor or capital. The vertical dimension of equity argues the converse i.e. disparate levels of income must be matched by disparate tax rates in accordance with the taxpayers ability to pay. Table 4 presents an overview of the tax instruments that the state has at its disposal and their implications on the efficiency and equity dimensions of the fiscal system.

Evidence of taxation as a tool to improve state-society relationship in line with the discussion above, can be found in the case of the Mauritian developmental regime. Based on the findings of Bräutigam et.al (2008), who present the case of the Mauritian government’s taxation on its sugar industry which is a key source of the country’s exports, it can be seen that it not only had significant improvements in the state-society relations but also enhanced the productive capacity of the sugar industry. Imposition of the tax on the sugar industry greatly increased the size of the revenue pool, as a result of which the government reduced personal income taxes and used these revenue flows for redistributive expenditures. Furthermore, a section of the fiscal flows from this tax were devoted to the R&D, infrastructural development and marketing purposes that enhanced the productivity of the sugar industry. Second, the revenue mobilized was absorbed in financing R&D, infrastructure development, and commercial capacity building that had positive contributions to the growth of the sugar sector. This fiscal tool also yielded huge solidarity gains in terms of the state’s ability to exercise its writ over its territorial expanse since the taxation affected the main source of employment in the rural areas. While such a tax imposition could be considered detrimental to the sectoral employment, it was not so in this case and the state ended up fostering a mutually beneficial rights and obligation arrangement with the farming community. Perhaps, the most notable point that distinguishes the Mauritian experience from other similar experiences, is that it was done in a democratic context that allowed for contestation, articulation and bargaining from all stakeholders.

c) Mobilizing Domestic Natural Resource Base

The extraction of natural resources such as mineral and hydrocarbon deposits has become a large (and for many still growing) part of developing countries' economies in Asia, Africa and Latin America. In terms of the resource mobilization capacity, states that have a natural resource base can also be considered to have a higher capacity for domestic resource mobilization and effective developmental capacity. A wide body of literature on the resource rich economies, developing and developed alike, extols the 'resource curse' which pertains to the correlation of natural resource abundance and a set of negative economic and socio-political consequences [Sachs & Warner (1997), Collier & Hoeffler (2005), Moore (2004), Robinson, Torvik, & Verdier (2002), Bellamy & Clark (2004)]. Nevertheless, there is also a significant evidence in the literature to the contrary as there are numerous resource rich states that did not exhibit these symptoms and thus opening the debate to what accounts for such variations. It is in this emerging avenue of research that this section operates as it examines the economic, social and political dynamics that underlie the 'natural resource led development paths' and the extent to which socio-economic developmental objectives are realized.

Most of the developing countries possessing an exploitable natural resource base, exhibit that the share of the natural resource rents constitute a major and growing section of the state's aggregate fiscal pool (IMF, 2013). These rents may come in the form of direct revenue flows to the exchequer in case of nationalized resource exploitation, or taxation or in terms of resource royalties. In either of these possible channels of resource rents flowing into the state's fiscal pool, there exists a great potential for the state to design and deliver social-welfare oriented public services in addition to the economic development prospects. Therefore, to realize these prospects and to build state developmental capacity using the mineral resource base, several requisites must be met.

One such requisite is the state's ability to avoid falling into what is known as the 'Dutch Disease' (DD). The possible ways of building state aversion to the DD include macroeconomic policy development that mitigates or at least counteracts the inflationary pressures that the huge foreign exchange inflows that the natural resource mobilization brings in, that not only affect the macroeconomic stability but also the competitiveness of the non-mineral production of the country (mainly manufacturing, and to some extent agricultural commodities). A review of the literature reveals that the mineral rich economies such as Norway, Chile, Botswana and Indonesia have emerged as successful examples of averting the Dutch Disease through a combination of various economic policy regimes. Most of the resource rents were channeled towards public debt settlements, foreign exchange accumulation, stabilization funds, social security funds, as well as

controls on the capital flows in the economy to ensure their absorption to productive sectors instead of speculative pursuits. And while the economic and developmental policy aspects of these countries can be considered similar in terms of the trajectories not the extent, their progress in the political liberalization or democratization has been disparate (Radice, 2008). In the case of Latin American economies like Bolivia, Venezuela and Chile, or the South East Asian economies like Malaysia and Indonesia, or the African economies like Zimbabwe and Uganda, ended up in entrenching the non-representative and non-responsive authoritarian regimes. All of these economies either had dictatorial regimes or factual (not substantial) democracies that revolved around single party rules that designed socio-economic policies only to benefit and legitimize their incumbencies.

Another facet of mobilizing domestic resource rents in particular, and DRM in general, is their utilization for social development policies, which is the crosscutting theme in this dissertation when considering the notion of development. An effective and targeted social development policy is not only imperative for broad-based development but depends critically on the amount of public resource allocation in the social policy which take the form of fiscal, policy prioritization and administrative effectiveness. However, the extent of public resource allocation (primarily fiscal) cannot be considered, apriori, as a proxy for actual incidence of expenditure and the extent to which they have actually yielded the desired objectives. It must be noted that while social policy remains a policy variable, the allocation and assimilation of the public resources is a function of the underlying economic and socio-economic landscape of the context in question.

2.4 DEMOCRATIC DEVELOPMENTALISM: SYNERGIZING DEMOCRACY AND DEVELOPMENT

At the core of the developmental state lies an establishment of “*..its principle of legitimacy its ability to promote sustained development and structural change in the productive system.*” (Castells, 1992). The resurgence of the developmental state idea in the development policy and academic debate, and in line with the emerging global dynamics, there is an emerging tendency towards giving developmentalism, democratic credentials as well. There are contrasting arguments, keeping the developmental state requisites in mind, on whether economic development fosters democratization and

democratic consolidation²⁹, or fostering state resilience and reconciling state autonomy through democratic participation enables the state to pursue a developmental policy orientation that yields socio-economic development. Based on this this, a more appropriate conceptualization of a democratic developmental state (hereon referred to as DDS), is that such a state:

“..not only has the institutional attributes of a classical developmental state, i.e. being autonomous and coherent, but also takes on board the attributes of procedural democracy”. Edigheji (2005)

This research considers this conceptualization to guide the subsequent analysis, while taking exception to the exclusively ‘procedural’ attributes and expanding the purview to include more substantive democracy attributes as well. The connection between the notions of democracy and developmental state is still a debated subject, especially when viewing the precedents established by the East Asian developmental states. Most of these East Asian states witnessed substantial economic gains under authoritarian regimes, with the exception of Japan where procedural electoral democracy was instituted in the aftermath of World War 2, but the authoritarian legacies remained for some time. The coercive and enforcement capabilities of the state have also been credited with the enhanced capacities of the East Asian countries [Evans (2012); Leenders (2007)], which then brings the compatibility of democratic norms with the developmental stance into question. Leenders (2007) argues that the case of the East Asian developmental model, in particular, illustrates the incompatibility of developmental policy framework pluralized politics where a multitude of groups have the ability to participate and articulate their interests in an unrestricted manner with the state.

Contrary to this viewpoint, it can be seen that the developmental policy orientations have also taken roots under democratic contexts. Agreeably, there are fairly intuitive reasons to accede to the former, given that formulating and instituting a growth and development strategy deems imperative a cohesive and disciplined state, a feature that can get undermined in a pluralistic democratic context given the heterogeneity of demands, articulation mechanisms and agents. However, if the whole debate on developmentalism has to be taken as a serious strategy for a more global application, it must be taken into account that while economic growth is an important goal in its own right, it may conflict with other development imperative such as income redistribution, social development, and extrapolating into the greater notion of state cohesion and resilience. Opening up the contestation and articulation spaces may influence the agenda and the effective implementation of state policies,

²⁹ See, for example, Lipset (1960) illustrated how economic development creates a large(r) middle class which fosters democratic consolidation

more often in a dilatory manner (Bräutigam, Fjeldstad, Moore, & (eds.), 2008). As a result of this, there are pressures upon the incumbent political forces to design their policies with a relatively more short-term results orientation that may also undermine the strategic objectives that a developmental stance is geared towards, in a bid to consolidate their support and legitimacy (especially applicable in the ‘electoral cycle’ scheme of things). However, if we look at the aggregate trends prior to the current phase of global democratic transitions it can be seen that the democratic regimes and autocratic regimes did not have a substantial ‘results-gap’ in the average growth rates of total incomes, even though few authoritarian regimes did register outlying high growth rates (Przeworski, Limongi, & Cheibub, 2000).

The analysis in this section shall first engage with the nexus of democracy and development, and the recurring causality debate. Subsequently, it will engage with the idea of Democratic Developmental States (and through analytical extrapolation, Democratic Developmentalism).

Development and Democracy: Exploring the Nexus

While the relationship between democracy and development continues to be debated, especially in terms of the direction of causality, there are some assertions arguing that promoting democracy and development are mutually exclusive or a ‘cruel dilemma’ (Bhagwati, 1995 & 2002), and others consider them as complementary or reinforcing facets that operate in a symbiotic relationship. Democracy and development continue to be notions with constantly evolving connotations; does it simply occur as a result of economic growth of GDP, or are we to consider the broader notion of Human Development? The latter is of particular relevance to this research, given that Human Development goes beyond the narrow factor oriented economic approach and instead encompasses the broader notions of human prosperity. Admittedly, this remains a vague conceptualization so this research follows on Tsai (2006) operationalization of Human Development as ‘redistribution of collectively (in national terms) produced of goods, across income, education and healthcare avenues’. It must, nevertheless, be noted that while the scope of the two conceptualizations of development may vary, none enjoys an absolute stature as an understanding of development. For instance, high GDP growth does not result in broad-based development implications for the masses if the growth benefits are skewed in favor of a narrow segment of the populace. Similarly, human development initiatives remain a function of resources at the state’s disposal so in case of limited economic growth, the size of the redistributive pool shall also be limited.

The analysis in this section is guided by the assertion by Kohli (1986) that the way authority in a

polity is exercised defines the parameters that the incumbent regime can operate within with regard to economic policy development and implementation. The underlying idea is the primacy of political environment in defining the development trajectories whereby the nature of the political regime explains the different elements of the developmental trajectory; why the state seeks development, why it is limited/successful in realizing those objectives, and also what type of development policy is pursued. Intuitively, democracy remains an ideal political regime type for growth and development, yet there is also evidence to the contrary, especially in the East and South East Asian cases. This section analyses the democracy-development connection by examining the following:

- i) Why is democracy the ideal political environment requisite for development?
- ii) Why do some authoritarian or limited democratic contexts fare better at development?
- iii) Does the nature of regime really matter for Development?

a) Why is democracy the ideal political environment requisite for development?

Considering the divisiveness in the literature on the democracy-development nexus, the available literature is of limited effect in yielding consistent explanations on why democracy affects the development outcomes. While the scope of the debate is quite expansive, the analysis here shall be limited to the main arguments that are consistent with the scope of this research.

The oft-cited argument in favor of democracy, especially with the dominant development discourses on governance and institutional dimensions of development, is that democratic political contexts can ensure good governance which in turn promotes development (Leftwich, 2001). While both are non-equivalent concepts, the fact that both democracy and the good governance conceptualizations revere the notions of accountability, responsiveness, inclusion and transparency, lends the ‘mutually reinforcing’ argument some credence (Grindle, 2004, 2011). In a democratic context, the accountability pressures emanating from the electoral mechanisms is perhaps the biggest advantage that democratic dispensations have over its limited variants and even autocratic dispensations. The pressures of being removed from incumbency or not being re-elected in subsequent terms, theoretically fosters the responsiveness of governments to the constituents. Related to this is the institutionalization of electoral systems and political cycles, so a ‘change in the guard’ has very little distortionary effects on the economy owing to the institutionalized recurrence of political transition (Przeworski, Limongi, & Cheibub, 2000). This is a feature that autocratic regimes lack, and any attempt by the constituents to enforce a political transition comes at a greater

cost and distortion to the economic system. Distancing from purely theoretical discourse, it has to be noted that in reality while the democratic systems are more viable in avoiding prolonged periods of mis-governance, they can not guarantee avoiding sub-par development policies.

Another premise on the democratic promise for development is that democracies have a greater efficiency in resource allocation, given the informational advantages that come with the pressures to be responsive to the electorate constituents (Pzeworski, 2002). In this context, it is not only the responsiveness of the government to the needs of the constituents that is important, but also the ability and capacity of the governments to respond to them effectively as compared to other less 'deliberative' political systems, which establishes a strong linkage between democracy and its conduciveness for development. Furthermore, democratic political systems once functioning effectively are also conducive for broadbased and sustained process of inclusive redistribution of resources. Going beyond just the economic development parameters, effective and efficient redistributive mechanisms are also considered to have positive implications on the Human development, especially when the resource reallocation occurs in the social sectors such as health and education. However, the main issue regardless of the political system or the nature of the incumbent regime in this regard, is the ability or the willingness of the incumbents to 'credibly commit' to such redistributive norms. Whether or not they can, remains debated. Some of the arguments in the literature consider such a 'commitment' to be a rational course of action for the governments in developing economies as the economically poor segments and those with limited access to basic social needs, also happen to constitute a major segment of the populace. A commitment to and delivery of such redistributive benefits in such contexts, is thus politically expedient in addition to being positively developmental. However, the actual commitment of the governments to such avenues remains limited as per empirical evidence across both policy and academic research, primarily due to the absence of effective political pressures on the government, of which patronage and persistence of traditional power structures remains the most important reason (Pfiffner,2004).

An associated explanation of this has to do with the stage of democratization that the country is on. In the contexts characterized by ongoing democratic transitions, clientelism and traditional political networks continue to wield influence but the closer it gets to democratic consolidation, these inequalities are mitigated. This has been referred to as a possible 'Political Kuznets Curve' (Chong, 2001). The idea is that in the transitory phase or early democratization stages, the politics

undergoing the transition shall produce a surge in income inequality (and thus by extension social and political inequalities as well), before it smoothens out. Acemoglu & Robinson (2002) theorize the existence of a possible Kuznets curve as ‘capitalist industrialization tends to increase inequality, but this inequality contains the seeds of its own destruction, because it induces a change in the political regime toward a more redistributive system’.

Another main theoretical advocacy is that democratic political contexts also provide a stable environment for the economy. One part of this argument is related to the notion of institutionalized change discussed earlier in this section, but the main basis for this assertion lies in the argument that democratic contexts are better equipped to safeguard property rights and enforce contracts [Beetham (1997), Polterovich (2007)]. This research contends that the enforcement of property rights has less to do with ‘democracy’ per se, and more a function of the rule of law. Yet, it can be argued that this linkage is well founded as democratic regimes are oriented towards constitutional supremacy, of which enforcement and protection of property rights remains a subset (Olson, 1993). However, while the theoretical linkage is plausible, actual evidence illustrates that democracy can not necessarily be considered as an surety of rights enforcement (contractual and proprietary), especially in the contexts characterized by democratization because of the political elites’ self-concessionary and rent seeking behavior [Bermeo (2009), Przeworski, Limongi, & Cheibub (2000)]. In the contexts of consolidated democracies, however, due to the presence of strong accountability mechanisms such a surety has a higher probability.

Why do some authoritarian or limited democratic contexts fare better at development?

The interesting paradox in the debate on democracy and development’s linkage is evident in the case of the East and South East Asian states whereby limited democracy and a relatively autocratic developmental orientation led to these states registering phenomenal socio-economic development. Given that the complexity of the political systems in these regions, and recognizing the plurality of the developmental models, this section shall engage with some distinct characteristics that applied to most of the polities in the region instead of focusing on the economic policy milieu exclusively. While some of these concepts have been touched upon in the Section III, this section shall consider how likely each of these outcomes are as a product of the authoritarian process of governance as well as how the political environment was connected to the development outcomes across these contexts.

One main characteristic of the South East Asian and East Asian states has been the high level of

state capacity. The case of China, South Korea and Taiwan are particular examples in this regard as their economic growth and socio-economic development policies were framed against a backdrop of state-led protectionism and a market-oriented economic growth that was augmented by strong structural enforcement by the state. One of the key reforms in this regard was the Land Reform at the very outset of their developmental policy stance, which was aimed at creating a relatively equal structure of resource ownership in the society [Beetham (1997), Bhalla (1997)]. Drawing on Bhalla (1997), the case of South Korea in particular was the most significant illustration of this policy bearing fruit as economic growth (% growth in GDP per capita) was also accompanied by a corresponding improvement in the Human Development, including but not limited to Human Capital development as well. This in turn augmented the GDP growth in what is referred to as a 'virtuous cycle'. State capacity, as discussed in Section 3.1, also has its linkage with authoritarianism.

Another related attribute of the successful developmental states with limited democratic norms at best has been a higher degree of state autonomy. State Autonomy pertains to the degree to which the state has influence over indigenous policy design, implementation and continuity. In the contexts where the political space is less pluralized and is characterized by a single party and/or autocrat, the longevity of developmental policy framework has more chances of evading retraction or modifications from changes in incumbency. The case of Indonesia under President Suharto (1967-1998), South Korea under Park 1961-1979, Pakistan under Ayub Khan (1959-1969), are examples in support of this assertion as in each of these contexts significant GDP growth was witnessed as developmental plans were put into action with little opposition and over a longer term than in the democratic electoral cycles. An associated example, building on what was discussed in Section 3.3 (a) is that of Park regime in South Korea where the government implemented coercive savings policies that also included the suppression of consumption oriented investments (by firms and hence consumers). Such policies would have most likely failed in their implementation, had the nature of the regime been more democratic and thus the coercive abilities of more autocratic regimes provides a higher guarantee for effective implementation.

Drawing on the discussion in the preceding sub-section, political stability (disregarding the nature of the regime for now) is an important factor for development. Political stability is linked to both state capacity and state autonomy discussed above primarily in terms of how they accrue. The flipside of the autonomy and capacity enhancement is that most often this occurs in the absence of or the expense of an active civil society (as evident in the case of China). Looking at the case of the

East Asian economies (China, South Korea and Indonesia, in particular), the stability of the political system was achieved even under distinctly autocratic contexts, where the regime stability was a product of an inclusive economic progress. Basing on the lessons illustrated by the East Asian contexts, one can conclusively argue that where improvements in both economic growth as well as human development are registered in a process of transformative inclusive development, the incumbent governments regardless of their nature as well as the repressiveness have a higher probability of stability. However, this depends critically on another factor, which is the commitment of the governing elite to the developmental objectives. However, a higher degree of state stability and autonomy is counterproductive, if not characterized by a committed developmental elite whereby the orientation of the incumbent executive is in line with the developmental objectives, as compared to narrow self-interests.

Thus, why certain autocratic contexts are more successful than many democracies in the developing world is actually an observable function of high state capacity and autonomy in a stable political background, an overarching commitment to a developmental orientation by the incumbent political executives, all operating in tandem. This has been an attribute, primarily in the context of the Asian economic miracles where a simultaneous existence of each of these factors resulted not only in significant economic development (in GDP terms) but also sustained improvements in the Human Development realm. While it has to be acknowledged that this cannot be taken as a sure-fire way of ensuring socio-economic development, the evidence serves at best a normative direction whereby the role of state subject to the attributes discussed above, is highly providential in framing a trajectory for socio-economic development. The common pattern that emerges from the experiences of the successful autocratic dispensations is that social repression (not always vicious) enhanced state capacity and autonomy, triggering off a virtuous cycle whereby the legitimacy to govern was driven more by the observable gains in economic and human development realms than by the liberal political ideals and constitutional premises. The 'built –in stabilizers' in such systems exert significant pressure upon the incumbents to be more developmentally oriented for their own regime stability in particular and political stability in general.

c) Does the nature of regime really matter for development?

While the preceding two subsections engaged with the developmental outcomes of successful democratic and autocratic cases, this section shall build upon the arguments surmised earlier to examine *if* the reasons for the growth and development across the two ends of the regime spectrum

mutually exclusive? The main virtue of the authoritarian developmental contexts was the high level of state autonomy, whereas in the case of democratic contexts it is actually the converse – responsiveness and accountability to the citizens. While autonomy of the state entitles the incumbents a degree of independence to pursue rapid development with little articulation of contentions on the long term development strategies, the contrary case of democratic solidarity and consolidation exerts progressive pressures upon the incumbents through deliberative, responsive and accountable developmental policy frameworks. Furthermore, while the electoral pressures (as an accountability instrument) upon the incumbents to ensure wellbeing of citizens is hailed as a strength of democratic systems, the (relative) longevity of the autocratic regimes ensures unobstructed and consistent policy implementation is presented as a virtue of the autocratic systems. Going by these theorizations and arguments, the debate on what political system is most conducive to development remains inconclusive.

Democratic contexts generally are inhibitive in terms of any radical change, unlike the authoritarian regimes, as they need to arrive at least at a minimally necessary consensus amongst all representatives of the populace before any policy or framework can take root. This consensus, in line with the *real-politik*, can rarely be (if ever) unanimous but often involves significant bargaining with the political parties and agencies that are non-incumbent in the executive but are either on the opposition in the legislatures or represent large swathes of the population or even act as an influential articulation forum for the constituents (e.g. civil society organizations). The incumbent party emerging victorious from the electoral rounds cannot unilaterally promulgate and put into effect, policy frameworks of its own preference unless some consensus is reached with the other actors in the political and social space, failure to do wish exposes them to a dissatisfied electorates. This form of pressures are considered as the *Horizontal Accountability*, whereby the more the plurality in the political space, the higher the horizontal accountability.

While it makes the governing process more accountable and responsive to a broader set of citizen expectations, it can also lead way to *elite rent-seeking* behavior, especially in the contexts in a political transition, whereby the political elites with little vertical accountability to their electoral base negotiate rents horizontally to favor certain policies. Nevertheless, subject to strong and effective vertical downward accountability mechanisms, democratic regimes can be considered to be favorable to incremental development instead of radical development trajectories [Leftwich (2005), Polterovich (2007)]. While there is a high degree of intuitive credence that can be attributed to this assertion, this cannot be taken as a rule of the thumb as there is evidence that two mono-party

democratic contexts(having most of the liberal democracy features barring greater plurality), namely Botswana and Singapore have seen radical and positive developmental shifts. In both the countries, one major party has been at the helm of the affairs for most part of the country's existence; Botswana Democratic Party since 1966 and the People's Action Party in Singapore since 1959. This signifies that if there is a legitimate and committed political elite, with an almost unanimous support base, radical developmental reforms can still be instituted and taken to effect. Thus, only a particular form of liberal democracy can be conducive to radical development, which in turn is a function of the extent of socio-cultural and ethnic homogeneity of the populace as mono-party rules can be of little success in radical development trajectories in the contexts where multiple cleavages exist e.g. Ethiopia, India or Melanesian states.

The obvious connection to explore now is that what gains can be expected from the democratic '*incrementalism*' in developmental stance. As covered in 4.1 (a), incorporation of liberal democratic norms guarantees accountability, responsiveness, participation, amongst other facets of what is considered as 'good governance' although some of these facets of good governance can also be seen in limited democracies or autocracies, as the cases of Singapore, Malaysia, Botswana illustrate in Fig 1. Figure 1, illustrates this growth variance (a proxy for the broader developmental notion) across the regime types for 167 countries. Using the Polity IV dataset for the Democracy scores and log GDP/capita (1960-2012) for these countries, it can be seen that there is a greater smoothening out of growth variances as the state of democracy improves³⁰.

³⁰ The figure was taken from an NYU Development Research Institute discussion series. Democracy measure is derived from the Polity IV scores :(0-10 where 0 is total democracy and 10 is total democracy. Growth rates are a geometric mean (log values) for the period 1960-2012 of the GDP/capita growth per annum compiled from the World Development Indicator. However, an argument was also made in the same discussion on how basing it solely on the nature of regime downplays the role of other influential factors such as sectoral composition of growth, dependence on commodity exports, civil wars and other similar dimensions that could have a similar dispersion of development outcomes.

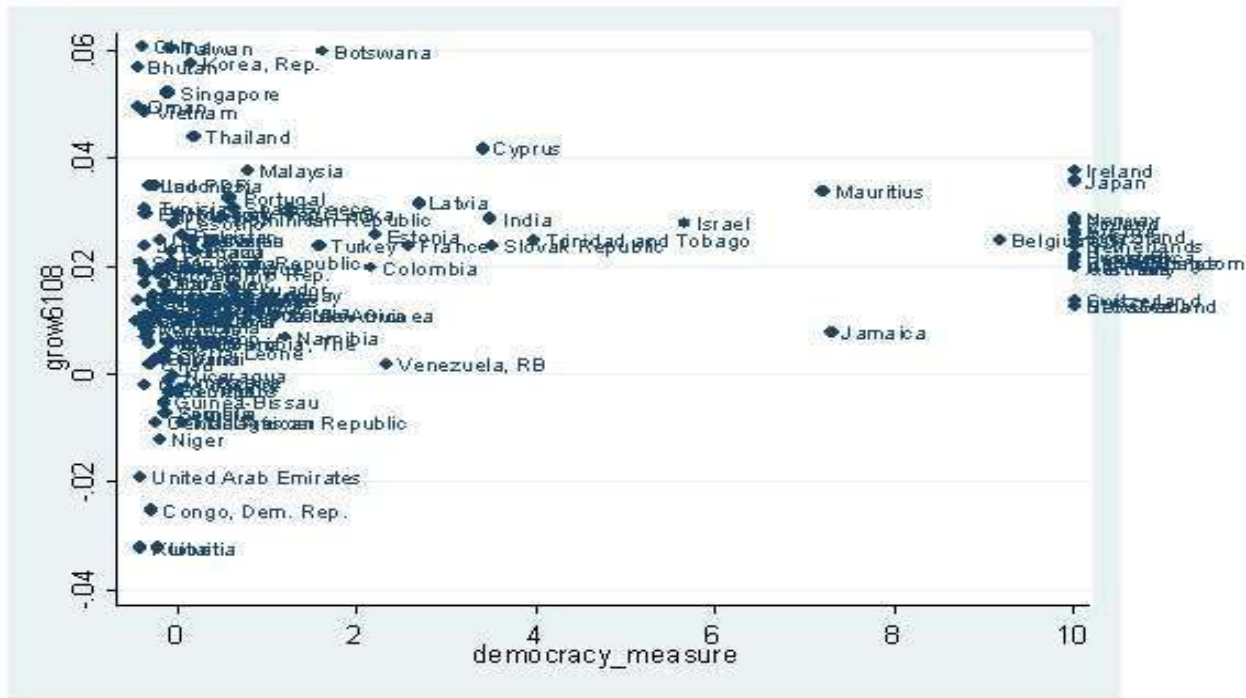


Figure 6: Growth variance according to Regime Types

Source: NYU Development Research Institute

As compared to the autocratic regimes, democratic regimes tend to be more conducive to the development of socio-political institutions as they derive their legitimacy through constitutional mechanisms, regime and political stability. Admittedly, making legitimacy a function of socio-economic development is not a viable concept as effective and inclusive developmental strategies may not be as palpable in one context as they could be in another, given that a host of socio-cultural factors and a historical institutional inertia is of a far greater effect in dictating the outcomes and the pace of the reform. Furthermore, institutionalized support to the regime in the form of constitutional cover enhances political stability as well as a certain degree of regime stability, indirectly facilitating steady and sustained development (Przeworski, Limongi, & Cheibub, 2000). Thus, the main difference between the type of regime and the extent of development is that while autocratic forms are more likely to obtain rapid and transformative developmental outcomes, they are also vulnerable to ‘policy disasters’ (Higgott & Nesadurai, 2002), democratic forms of governments can be built on incremental and stable grounds whereby the amplitude of growth might

be lesser but the stability and sustainability is much higher.

An associated feature that needs to be acknowledged is that the advantages of regime type are associated with the degree of their consolidation. Even in democratic contexts, in *real politik* scheme of thinking, the elite continues to be entitled to privileges compared to the rest of the society, a feature that takes far perverse forms in transitional democracies especially if characterized by endemic exclusionary structures, a characteristic of many developing countries of the world. The same strand of thought retains its credibility once considering the 'good governance' imperatives e.g. enforcing property rights and effective resource allocation [Tsai, (2006), Addison, (2002)]. Effective, efficient and responsive resource allocation may come as a consequence of the democratic consolidation. In the case of autocracies, the virtues related with autonomy, stability and transformative development remain a function of the degree of power consolidation, legitimacy, longevity and stability.

The temporal dimensions of the regimes in place are also of huge importance in terms of the stability of the political system, and through extrapolation, the developmental implications as well. This research diverges from most of the empirical examinations that consider development as a function of the immediate or short-term political background. Instead, it puts forth the argument of institutional inertia argument to state that whether a polity is autocratic or democratic at a given time has an influence on its developmental trajectory. The idea is that since the effects of consolidation or transition of political institutions begin to surface, not in the immediate but medium to long-term and the temporal effects are cumulative. Therefore, any analysis on the broader political stability or the developmental aspects of a certain regime/ political system must take into account the accumulated effect instead of the current nature.

While the debate on the relevance of the regime nature to the developmental trajectory continues, there are a few broader conclusions that can be drawn from the literature and the analysis in the earlier paragraphs. While democracy can be considered as more probable in fostering good governance, which in the absence of the requisite state autonomy and capacity may not yield high and sustained socio-economic development. The developmental implications of the regime type are more aptly functions of the degree of consolidation of each regime type. The advantages of consolidated democratic systems and consolidated autocratic systems (like those of the Confucian Authoritarian examples of East Asia) are easy to realize but in the transitional contexts there is a substantial ground that needs to be covered. The distinct advantages of either of the regime types

can be considered to merge somewhat in the contexts where democratic dispensations are characterized by limited plurality in the political space (e.g. democratic regimes in a mono-party context), but there are few observable examples of such a system with high developmental impact in the real world. Thus, the question should be directed not at which of the regime types is more conducive to highly transformative socio-economic development, but instead at what regime type offers greater sustainability to the process of socio-economic development. Looking at the cases where high economic development has been registered (East and South East Asian economies primarily) under authoritarian regimes, it must be enquired whether the policy frameworks and political organization behind such 'economic miracles' really desirable and worth replicating across the globe especially when they come without a credibly guaranteed corresponding social development (as argued, albeit apriori in the case of democracies)? The answer to that remains ambiguous at best and negative at least. Therefore, while the rapidly transformative attributes of autocracies, subject of course to state capacity, elite commitment and autonomy, are well-founded arguments, the gradual incrementalism that democratic dispensations entail is of a greater importance and value to the sustainable socio-economic development.

Democratic Developmentalism

Few states in the developing world have been able to sustain even the most basic elements of democracy, and of these only a few have been able to generate and sustain high per annum growth of their GNP per capita over the last thirty years, or to lift the bulk of their people out of poverty, hardship, and vulnerability: they include Botswana, Singapore, Malaysia, and Mauritius (UNRISD, 2008). These contexts present themselves as an example of developmental democracies as they are characterized by a developmental orientation as well as a democratic (at least procedurally) government. Building on the preceding section of regime nature and developmental impact, it can be observed that while there are good explanatory accounts of why some non-democratic or limited democratic contexts (in East and South East Asia primarily) have been able to manage rapid and sustained economic growth over time, there is very scant literature or account of why some of the democratic states have been able to do the same. This section examines what particular conditions enable a democratic state to generate the capabilities requisite for its transformation into a successful developmental state.

Intuitively, a democratic developmental state can be one that has a sustained medium to high economic growth rate (minimum 4% annual GDP per capita) over the medium to long term (5-10 years), while also being characterized by the democratic norms (Edigheji, 2005). Democratic norms,

for standardization purposes, are being considered in the minimal 'Schumpeterian' concept of democracy³¹: established national political system in which people, political organizations, and social groups have the liberty to pursue their interests in a peaceful, institutionalized process of competition, negotiation and cooperation. In real terms, this pertains to the free and fair electoral cycles, smooth transitions of incumbency, pluralized political space with low barriers of participation, and the protection of civil and political rights and liberties. The observable trends in the literature on the issue thus far has been that electoral democracy with competitive political parties is yet to play an important role in fostering democratic developmental states primarily owing to inadequate institutionalization and perverse clientilistic traditions (World , 2008). In addition, the process of democratic deliberation is crucial in creating a broader social consensus around the developmental plan. However, this requires the existence of a more substantive form of democracy than mere electoral democracy.

The experiences of successful developmental states thus far, illustrate that the ideological commitment of a 'developmentally oriented political elite' alone is not enough, but such a commitment must also be embedded in the broader societal aspirations. Intuitively speaking, a national development vision is particularly effective (as the case of Bolivia under Morales post 2006 illustrates) when there is a broad consensus around it, and vice versa (as observable in the case of Ethiopia after the Zanawi government incorporated a National Development Strategy). However, keeping the intuitive concepts aside, this section examines two propositions which, once considered in tandem, illustrate the main structural barrier that makes the establishment and sustenance of democratic developmental states an arduous affair. The first proposition borrows on Leftwich argument that a consolidated and stable democracy (in the minimalist representative form, as is the case with most of the developing economies) is a conservative system of power (Leftwich, 2005). The idea is that in such a form of democracy the processes of decision making as well as the policy outputs are 'conservative' as they are a function of inter-elite accommodation, concessionary consensus building, and the incrementalism (as discussed in the previous section), and are rarely rooted in popular participation. The second proposition is that developmentalism (as a more terminal policy framework than merely short term growth orientation) is radical and distortive in terms of changing the utilization and appropriation of resources directed at a structural

³¹ The Schumpeterian minimalist conceptualization of democracy is an 'institutional arrangement for arriving at political decisions in which individuals acquire the power to decide by means of a competitive struggle for the people's vote' (Schumpeter 1965: 269)

transformation of the polity. As a consequence of such a transformation, there is a corresponding transformation in the socio-political aspirations and interests that challenge the already existing ones. This is where the fundamental structural barrier to the establishment of a Democratic Developmental State comes in, that is that the imperatives developmental consolidation and democratic consolidation rarely, if ever, converge. It is important to mention that this assertion does not disavow the imperfections and distortive effects of democratic politics, but if the consensus-building and accommodation dynamics underlying the democratic processes are sidelined, the very edifice of the democratic system may be threatened (as has been witnessed frequently in the case of Pakistan where most of the military takeovers found their roots in the inadequacy of political bargaining).

Thus, for a democratic developmentalism to take root, a balance must be achieved between the rules and processes of stable democratic politics (accommodation, consensualism, incrementalism, negotiation, and other bargaining and contestation mechanisms) which lie in contrast to the developmental requisites of substantive changes to the economic and social structure of the context (and by extrapolation the interest structures existing within the polities). It is this structural barrier that must be mitigated by democratic regimes (at low and high levels of consolidation, alike) if they are to emerge as successful democratic developmental states.

The notions of the establishment and sustainability of DDS is inextricably linked to the notion of democratization. The processes of democratization are a heterogeneous affair across the contexts, and the available literature on the comparative experiences illustrates that the main impetus of democratization (in terms of the impulse as well as agents) have sometimes been predominantly internal (as in the case of Bolivia, Taiwan, South Korea, India, Philippines among others) and sometimes been external (as in the case of most developing countries in SSA, as a result of donor and bilateral agency(ies) advocacies) (UNRISD, 2008). The most commonly observable trend has been a varying mix of both internal and external articulation as observed in the Post-Communist CIS states or in South Asia (Pakistan, in particular). The internal pressures for democratization have sometimes been bottoms up (Bolivia, Venezuela, Philippines, as notable examples), but mostly it has been a result of elite negotiations and bargains devoid of any potent impulse or articulation from the broader citizenry. Regardless of where the impetus of the democratization reform came from, or the nature of the agents of reform, any transitory phase needs to be consolidated if it has to be sustained.

According to Przeworski et.al (2000), democratization is a *'process of institutionalizing uncertainty, of subjecting all interests to uncertainty'*, and while this is theoretically a good way to approach the notion of democratization, this research argues that democratic consolidation will be limited at best, unless the extent of uncertainty in the political system and the associated dynamics are systematically reduced. Prioritizing bargaining and inter-elite negotiations is essential for democratic consolidation, and where a functional consensus is actually achieved, the uncertainty underlying reform processes and the policy framework is reduced. While this remains a fairly intuitive concept, the complexity of *'real politik'* needs to be examined in terms of what particular conditions favor the process of democratic consolidation? A review of the available literature on the issue presents a variety of imperative political conditions (Ansell & Samuels, 2010; Eaton, 2008; White, 1998), however this research identifies three main imperatives as under:

- Legitimacy

While being a highly subjective concept to examine and quantify, the main idea behind legitimacy is the acceptance of the authority by the populace. Legitimacy, in turn, is rooted in three further realms; geographical (Constituents' acceptance of the state's territorial ambit), constitutional (constituents' acceptance of the formal rules of organization, distribution and exercise of political power) and political (constituents' acknowledgment that government incumbency is rooted in free and fair electoral rounds). In the absence of these forms of legitimacy, there is always a latent potential for state and political instability, including violent secessionist movement or civil conflicts that have been witnessed and continue to be witnessed in most parts of the developing world (Chechnya, Former Yugoslavia, Ethiopia and Eritrea, Pakistan and Bangladesh, amongst others.). Weak democratic systems have a higher degree of vulnerability to such fissures in the state and social stratification, which substantially inhibits the prospects of the establishment and/or sustenance of democratic developmentalism.

- Consensus and Constitutionalism

Democratic consolidation deems imperative an agreement upon the accepted 'rules of the political game' (North, 1990) by all the actors in the political space and the social groups, ideally incorporated into clear constitutional provisions. The organization, conduct and outcomes of electoral rounds need to be clearly demarcated and held subservient to the constitutional provisions. Furthermore, the organs of the state, most importantly the military be held subservient to the state executive with constitutional demarcation of its role and punitive deterrent provisions for its role in

the regime changes (at the behest of losers of the electoral rounds or as a function of its own whim to obtain incumbency), thereby mitigating any threats to the democratic institutional evolution.

- Policy restraint by winners

A key element of democratic consolidation is that the winners of the electoral rounds have to evade the tendency to exclusively pursue their own policy agenda at the expense of the unsuccessful political organization(s), agency(ies), social group(s), or sectorally rooted influences (military, private capital etc). There is a latent probability, as has been observed in the episodes of political instability and regime transitions in the developing world, that the social, economic and political stakeholders who yielded limited or no benefit from the electoral processes fear losing out on the interests they have in the system and may collude together to destabilize the established political order. The less there is to risk in the event of a loss, the lesser the probability of such agents to destabilize the established order. However, the onus of stability does not rest exclusively with those losing in the electoral rounds but also upon the victors, who must realize that their incumbency remains exposed to certain limits and the existence of plurality in the political space requires some power and authority to be shared across the political space. Thus, for democratic consolidation to occur, the incumbents must not monopolistically pursue contentious policy agendas without factoring in the risk exposure of the losing quarters.

While critical to the process of democratic consolidation, these three imperatives are arduous pursuits in their own right, especially in evolving political contexts as is the case with much of the developing countries, especially the two this research engages with. In the contexts characterized by endemic poverty and socio-economic inequalities, democratic consolidation can be a tall order to meet because of the underlying clientilistic political ethos coupled with the traditional forms of authority inhibiting any substantive impulses to participate in the political space (P. Bardhan, 2005; P. K. Bardhan & Mookherjee, 2006; García-Guadilla & Pérez, 2002).

2.5 DECENTRALIZATION AND DEMOCRATIC DEVELOPMENTALISM

Having examined the concepts, requisites of establishing a democratic developmental state and the imperatives of governance quality improvements, some of the recurrent imperatives across all these discussions have been accountability, responsiveness, participation, inclusion, and effective public service delivery. While the centrality of politics in development has been an oft-cited

concept, and the reinvigorated role of the state is not only unprecedented but complex. Thus, any discourse on building state capacity for broad-based and inclusive development as well as a socio-political inclusion is rooted primarily in the composition of the political agents in any given context, and the political agency does not pertain exclusively to central level of state but also local. This centrality of politics, with an increasing focus upon the local political space, has been argued vociferously in the literature with little account of how to establish growth and development oriented political structures and incentive-compatibility of broader political interests with the developmental agenda (Acemoglu & Robinson, 2012). Yet there is an increasing advocacy of the applicability of the economic theories of competition and incentive-compatibility that can be applied to understand the competitive dynamics of the political agents and the incentive structures once they are in incumbency.

This section, building upon the earlier discussion on decentralization in Chapter 1, presents an analysis of how successful economic development and democratization are more probable in the context of a decentralized democracy. The main intellectual impetus for decentralization extols its virtues for democratic, accountable and responsive governance, and its economic effects mainly on the lines of efficiency (in the delivery of core public services and goods. Given that the provision of public goods does not take place under competitive market conditions, and thus it is the state's responsibility to ensure responsiveness of the provision to the aggregated preferences of the constituents to the maximum extent possible. However, given the heterogeneity of individual preferences across the constituent base, the extent to which the state's tax and service provision mix reflects the aggregated preferences remains inadequate at best. Thus, in a context of decentralized governance, where the administrative and fiscal dimensions of public service delivery and resource mobilization is rooted in relatively more homogenous constituencies, the *'responsiveness deficit'* between the community preferences and the policy milieu is mitigated thereby enhancing allocative efficiency, and through analytical extrapolation, social welfare. While this is a strong advocacy of the pro-efficiency virtues of decentralized governance, the flip side of it has that it can reinforce or even exacerbate existing regional inequalities and service delivery inefficiencies. While decentralization in no way exclusively implies absolute autonomy, the role of the central government (especially in terms of central fiscal transfers) continues to be important for regional equalization.

Furthermore, considering the pro-centralization line of argument, local public service provision could also be more inefficient in terms of the cost of acquiring the information and the resource

mobilization; which can be far less costly endeavors under a centralized agency because of the 'economies of scale' effect (Triesman, 2000).

In theoretical terms, it is fairly intuitive and easy to argue that central government has its agents placed in each community to acquire aggregated information of community preferences and relay back to the centre at low cost. This data is then used by the centre, which produces all public goods and allocates the goods in the solicited amounts and qualities to the different localities. The main assumption in this model is that economies of scale exist (due to mass production and provision) and the costs of information gathering and back-forth delivery are lower than that of a decentralized setup. Assuming these hold, which in a static context may be a plausible stance but at best contentious in a more dynamic context, a case for centralized governance is quite convincing.

However, as this research has argued, the possibility of a centralized governance system being effectively representative and responsive of the constituents' preferences is inextricably linked to the structure of the governmental organizations and the underlying incentives as well as the incentives they produce. An associated argument can thus be that viewing the issue of governance structuring purely from the 'economic efficiency' lens is more probable to ignore the influential explanatory variables and thus any 'causal' conclusions emerging from a narrow analysis of the economic aspects engaging exclusively with the economic costs and benefits, would be more conflated.

Perhaps a more cogent case for decentralized governance can be built by engaging in a broader analysis of its governance virtues i.e. accountability, responsiveness, political participation, diversity in the policy mix and enabling a citizen stake in the polity. The responsiveness and accountability are perhaps the most influential arguments in the governance realm too, and can be considered as the political equivalent of economic efficiency. The proximity of the government to its constituents under a decentralized setup not only enables greater accountability (assuming minimal imperfections in the local electoral mechanisms) because of observation ease, but also fosters a greater responsiveness of the political incumbents to the needs of their constituents. Both these facets, reinforce the degree of congruence and consistency of the public policy design and delivery to the constituents' preferences. Intuitively and theoretically, this is a credible assertion however this continues to be an apriori strand of argumentation because there is also evidence in the literature about the susceptibility of local political space reinforcing elite capture or special interest-articulation (P. K. Bardhan & Mookherjee, 2006; Dauda, 2006; Guarneros-Meza & Geddes, 2010). Thus, the extent to which responsiveness and accountability can be maximized under decentralized

governance structures depends on the type of decentralization pursued, the sequencing of the reforms.

Getting back briefly to the possibility of decentralized governance becoming a tool for reinforcing centralized governance, there is limited evidence that it does (Akai, Hosoi, & Nishimura, 2009a; Andrews & Vries, 2007; Burki et al., 1999; García-Guadilla & Pérez, 2002). The decentralization of authority to local levels is argued to promote political participation as it enables a proximate political platform to the constituents while also fostering accountability which in addition to improving government responsiveness also promotes greater political stability due to bottom-up pressure. Thus, the probability of an effectively designed decentralization reform that yields local governance structures capable of effective gauging of constituent preferences as well as having strong incentives to attend to them, in a higher degree than in a centralized setup, is a strong enough impetus for the debate in the favor of decentralized governance even in a developmental backdrop.

Revisiting the prior discussion on the productive efficiency of centralized provision of public services vis-à-vis a decentralized local provision, the latter can have a greater *allocative* efficiency primarily because the incentives of the local government agents are more closely aligned to the interests of their constituency as compared to the former. However, this depends critically on the extent to which the local agents are *effectively* accountable to the constituents and the degree to which local participation is reflected in the electoral representation. This is a fairly intuitive considering that the central government agents have a broader constituency, interests and incentives to respond to, thus local government is by default more targeted and responsive to its core constituency.

This argument brings forth the critical role of institutions, incentives and accountability in the provision of 'local' public services, which in itself is a critical building block of a *political economy model*' (presented in the preceding chapter) of decentralization, local government and optimal local service provision (Faguet, 2002; Falleti & Lynch, 2009). While details of these models are beyond the current scope of discussion, they extol exclusively the degree of local governments' autonomy which is a function of local discretion over domestic resource pools, the nature of democracy at the local level (in terms of effective representation and accountability), the accuracy of information that the voters possess (for effective accountability through electoral rounds amongst others), and finally the existence of enforcement institutions or mechanisms (constitutional provisions, legal provisions) that regulate the activities of the local political agents to prevent the abuse of authority or misappropriation. These are of a good contribution in terms of putting forth a framework of

analyzing the political economy dimensions of decentralization and local governance.

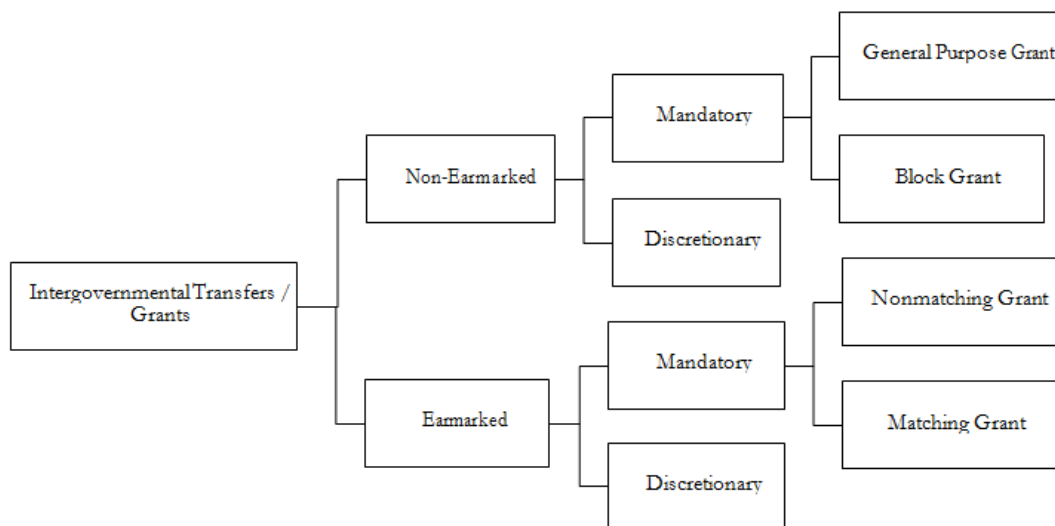
However, not only are all these facets variable cross-contextually speaking, but the ‘autonomy’ of the local governance structures may not necessarily be linked to all of these factors, e.g. local discretion of domestic resource pools may only be of importance in resource-rich contexts (Bolivia, Venezuela, Botswana, among others), but are linked also to the process of reform as a consequence of which such governance structures come into existence as illustrated earlier in Chapter 1. Governance reforms, in general and decentralization in particular, have significant implications for the public sector organization as well as its deliverables, and more so in the case of developing countries. The main reason for this complexity is because of the weak institutional frameworks, information mechanisms and capacity constraints. While the broader debate on decentralization is expansive given the current context, the analysis from hereon shall deal with the implications of the decentralization reforms in the context of establishing a democratic developmental policy framework. The analysis henceforth shall also serve as a prelude to the case analysis that follows in the two subsequent chapters. The primary focus in this section shall be on decentralization reforms’ impact on inter-regional equality and the broader notion of economic stability implicit in the analysis of which, are the notions of accountability, responsiveness and efficiency.

Implications for Equity

While there are numerous hypotheses and arguments in favor of this linkage, the degree and nature of the impact depends critically on the institutional framework and policy design processes including reform agents, interest articulation mechanisms and the sequential aspects of decentralization. In a context where the fiscal decentralization is the main reform agenda with the central government designs a fiscal distribution mechanism that does not redistribute resources to poorer regions of the polity, the reform is going to exacerbate existing inequalities instead of mitigating them. Contrarily, if the regions or the provinces do not redistribute their fiscal pools within their constituent jurisdictions, the extent and quality of ‘*localized*’ public service provision shall be suboptimal. Other equity promoting mechanisms include the fiscal transfer mechanisms, horizontal (across the same level) and vertical (downstream transfers from superior levels of government). Contingent upon the preferences of the political actors at the central and/or subnational governments, a framework for inter-governmental transfers (vertical or horizontal) with equalization components can be devised to ensure a comparable level of public service delivery (in quality and scale) throughout the polity. How such intergovernmental transfers/ grants are designed depends in turn on the existing state of inter-regional equality as well as a function of political

consociationalism and consensus (Akai, Hosoi, & Nishimura, 2009b; Garman, Haggard, & Willis, 2001; Rodden, 2001). Such transfers can assume various forms in their design as illustrated by Figure 3, and their design and monitoring further determines the extent to which decentralization fosters inter-regional equality of public service provision at various levels of state organization i.e. regional/provincial, towns and municipalities, and households.

Typology of Intergovernmental Transfers/ Grants (Horizontal & Vertical)



Source: Own compilation from OECD Fiscal Relations Database

The grants/ transfers can take two distinct forms; earmarked and non-earmarked. The former pertains to a grant or transfer that is disbursed conditionally for a specific purpose whereas the latter is an unconditional disbursement with no binding on the absorption of the fiscal resources by the subnational government. These grants, conditional or unconditional can further be categorized into discretionary or obligatory/ mandatory. The mandatory grants have legally mandated rules on the size and mechanisms of the disbursement and are usually a product of centrally sponsored revenue sharing agreements, both horizontally and vertically. Most of the grants and transfers made are of this nature. The discretionary grants on the contrary are not mandated by legal bindings or sponsored by the centre, but instead made on a ‘voluntary’/discretionary basis either vertically or horizontally, on an ad-hoc but not necessarily recurrent basis.

The earmarked mandatory grants can take the form of matching or nonmatching grants. Matching contributions augment subnational revenue contributions to the fiscal pools and are linked to the budgeted or actual expenditures for which the grants are earmarked. Any differences between the revenue contribution and its subsequent transfer back to the subnational level and the expenditure responsibilities of the subnational government will be bridged using these grants. Contrarily, all grants that are not disbursed in augmentation of subnational budget for the earmarked area are known as the non-matching grants. These forms of mandatory grants may also be a function of contingencies or even performance indicators.

Non-earmarked mandatory transfers can be in the form of general purpose or block grants. Such grants are aimed at increasing the subnational fiscal revenue pool without yielding any change to the relative prices of service provision. General purpose, as evident, has no binding upon the recipient to use it for a pre-specified absorption. A block grant on the contrary, is made with a specific purpose(s) but because of being non-earmarked the recipient has full discretion over the use of the grant within the thematic parameters of the grant (different from the earmarked grants in terms of the scope and the extent of discretion the grantor has on the utilization of the funds).

Using revenue sharing and fiscal transfer mechanisms sponsored by the centre for equalization purposes amongst the subnational governments, enables a redistributive regime that has significant implications not only for reducing inequalities but also fostering state cohesion. This is a crucial ingredient to the development and sustainability of a national developmental framework, where greater subnational stakeholding enhances the developmental capacity of the state. Fiscal equalization, when linked to strong accountability and performance indicators as the determinants of the disbursements enable not only policy consistency but also relative homogeneity in the quality of public service provision across the national space, with collaborative rather than competitive subnational policy framework. In the presence of significant regional inequalities, invoking competitive subnational economic policy framework shall exacerbate rather than mitigate the inequalities contrary to the Tiebout hypothesis. Once a certain degree of standardization in the fiscal capacities of each of the subnational constituencies is achieved, competitive economic policy frameworks in terms of tax- services mix can be pursued by the subnational governments and the ensuing competitiveness shall deliver the accountability, responsiveness, efficiency and innovation requisites that will reinforce the developmental trajectory by extending a bottom's up reinforcement instead of a top-down stipulation.

The degree to which decentralization has a potent bearing on the equity dimension across the

polity (transcending the relatively macro interregional equality by including also the socio-economic inequalities) is also a function of the degree of local accountability structures and the degree of political participation by the poor segments of the citizenry. If the local political space is inclusive such that poor people have limited constraints for active participation in the political space, there is an increased probability of responsiveness and accountability pressures upon the political leaders. Any democratic political system, at the local or national level is of limited substantive value in the absence of genuine political participation by all segments of the society. For example, India has a long-standing democratic tradition with a considerable degree of local governance apparatus as well yet the influential role of the caste system in social stature and political participation excludes a large segment of the population from an active stake in the political system or the governance process. Contrarily, in the contexts where there is strong local participation, e.g. Mexico, Cuba, Vietnam, there is evidence of targeted poverty expenditures due to greater articulation by the local governments [Tsai (2006)].

Implications for Economic Stability

Linked primarily to the fiscal decentralization reforms, there is now an emerging consensus on how to design decentralization reforms (fiscal primarily, but also administrative and political) owing to various instances of excessive ‘deficit-financing’ and ‘soft budget constraints’ of the sub national governments (Akai et al., 2009b; Rodden, 2001; Rodden & Wibbels, 2011). The evidence in both academic and policy debates on this issue boils down to one main factor; greater expenditure responsibilities decentralized to subnational levels than fiscal resources. Given that the control over the fiscal resources is an important tool for deriving influence, the centrally led decentralization reform processes across most developing countries has focused more on the expenditure and functional decentralization to the subnational governments without equipping with the fiscal base requisite to meet those obligations. As a consequence of this, the subnational governments have either had to obtain more grants or transfers from the centre or horizontally, or in some cases on the basis of sovereign guarantees from international sources as well. Contrarily, there is also evidence of a greater assignment of revenues than expenditure responsibilities which has instead resulted in suboptimal fiscal effort at the subnational level and inhibiting local domestic resource mobilization, both of which ultimately scale up in a national level fiscal crisis. This has been a recurrent feature in the case of Argentina, Brazil and Colombia (Latin American Program, 2012; Stein et al., 1998; Wylde, 2012).

Assuming effective subnational democracy in place, it can be considered that there will be heterogeneous preferences of the constituents across the different subnational groupings, and each subnational government may have a diverse set of preferences to match. Considering this against the DDS backdrop, if a subnational government has its agenda substantially different from the central government, there will be *coordination* problem between the two tiers. The soft budget constraints in the case of the subnational governments further complicates the scenario where provisions for central subsidization are in place. Where soft budget constraints are allowed to prevail with central transfer financing, the central government has a difficult task of coordinating the national fiscal and monetary policies (influenced by the borrowing by the subnational governments often under sovereign guarantees), thus exposing the national economy to instability.

The purely economic literature looks at this construct through the monetary and fiscal policy (appraised collectively through the use of the inflation variables) perspective [Triesman (2000), Asfaha(2007), Bräutigam, Fjeldstad, Moore eds(2008), IMF(2013), Stiglitz & Emran (2007)], a feature this research is constrained to contest on conceptual grounds. The conclusions generally are that decentralization (fiscal and administrative (functional)) can prove to have negative implications for inflation (due to higher public debts and money supply) and fiscal deficits (owing to deficit financing). However, if one considers that in assessing any possible impact of decentralization on macroeconomic stability, existing institutional and political arrangements of the context being appraised must be taken into account. These institutional and political factors can include the quality of the government, level of democracy, level of political stability or the level of corruption. Building upon the model produced by Zafarullah et.al.(2012), an estimation of these factors on macroeconomic variables reveals that decentralization, subject to the right kind of political and institutional adjustments can be conducive to macroeconomic stability (considered as inflation and fiscal deficit indicators)³². The estimation covers 62 countries for the period 1972-2001, with the observations structured as panel observations of 5 year averages, with the data pertaining to decentralization coming from the IMF GFS, and the institutional and political framework data coming from the Polity IV database. The results of the estimation illustrate that for fiscal decentralization to have a positive bearing on the extent of macroeconomic stability, a good political and institutional backdrop is imperative.

If the fiscal decentralization is effectively institutionalized i.e. clear revenue sharing mechanisms and expenditure responsibilities are stipulated then there would be lesser competition between the

³² See Macroeconomic instability and fiscal decentralization: an empirical analysis. Ahmad Zafarullah Abdul Jalil; Mukaramah Harun; Siti Hadijah Che Mat (2012).

subnational jurisdictions for fiscal resources hence reinforcing macroeconomic stability. Such an institutionalization finds its roots in a stable political setup whereby a consensus is established on the fiscal sharing and distribution models between the political entities of the national and subnational jurisdictions, the influential sponsoring role of the consensus building process being the responsibility of the centre. Thus by analytical extrapolation, where political systems are unstable and institutionalization poor as often the case with non-democratic or heavily contested political spaces in developing countries, without making a concerted effort to address these two issues, no benefit or stability on the macroeconomic front can be ensured.

Without engaging further on the debate, as it has been covered in the preceding chapter, the focus shall instead be placed on how to grapple with the pitfalls of the decentralization (fiscal mainly) for macroeconomic stability. Given the DDS backdrop and the preceding assertion that attention to the underlying political and institutional dynamics need to be made conducive shall be of a greater effect in realizing a more stable macroeconomic impact, the analysis from hereon shall engage with the elements in the reform process that must be taken into cognizance. These are listed and subsequently discussed as follows.

i) Enabling a Reform-conducive Framework

Building a conducive environment for the sustainability as well as the effectiveness of decentralization reforms finds its roots in the constitutional and legal mandates that stipulate the extent of subnational autonomy, rights, responsibilities and frame of action for the subnational governments. While this puts forth a foundation on which the decentralization reforms need to be anchored, this does not exclusively and independently guarantee the success of the reform process. There have been various instances recorded in the literature, both academic and policy, where distinct constitutional provisions and legal frameworks were defined yet the decentralization reforms were of limited effectiveness in realizing their core objectives. However, this section shall draw upon the examples of two developing countries (Ethiopia and Uganda) that have been often cited as good examples of establishing a sustainable enabling environment for decentralization in general, but more particularly the administrative and fiscal dimensions, given the ‘finance to follow function’ arguments of ensuring economic stability in decentralization reforms [UNRISD (2008)].

Central to all considerations of fostering a conducive environment for decentralization reforms, is the extent to which there is a strong domestic impulse to decentralize. The impulse or the rationale to decentralize is strongest in the contexts where ethnic or social cleavages exist, and the

diversity in the national context deems imperative a more diverse stakeholding in the governance infrastructure. In addition, the fiscal and administrative dimensions of decentralization in many developing economies are brought about amidst bureaucratized, relatively conflicting, and inadequately coordinated mechanisms whereby the centre also has a direct stake in the process of decentralization as it aims to retain as much influence as possible whilst also entailing ‘devolution’ of one sort or the other. The functional disengagement and ‘pass-on’ to the subservient subnational tiers when coupled with the inadequacy of subnational revenue, has been one of the main observable reasons for the adverse outcomes of decentralization. In a DDS framework, the central government needs to ensure that ‘finance must follow function’ maxim is held true. While the broader economic management as scale-dependent public services remain under the centre, the provision of ‘local’ public goods (such as municipal infrastructure, water and sanitation, primary health and education) must be augmented by an adequate fiscal base for optimal delivery.

Finally, a rapid instead of incremental process of reform exacerbates the governance complexities instead of ameliorating them. The institutional and policy frameworks to support the reform serve as a ‘structural’ and not substantive benchmark. An example of a strong enabling environment, which was also a product of an organic articulation rather than an externally driven impulse, is that of Bolivia. While it will be discussed in a greater detail in the subsequent chapter, the LPP (Law of Popular Participation) is a cogent example of establishing robust and sustainable institutions within which the reforms can be brought to form. Another aspect that must also be taken into account is the enforcement or actionability of the constitutionally mandated provisions. For instance, the South African constitution promulgated in 1996, established a strong functional role for the local governments that till now has been an issue of significant contention and even more recently so, as the South African political context deliberates on a developmental policy framework. The conclusion that can be drawn thus is that a strong enabling framework must precede and complement the decentralization reform process, with the caveat that it is a necessary but not a sufficient condition to ensure effective reforms.

ii) Balancing Subnational Functions and Revenues

While the inhibition of the central agencies to decentralize is frequently cited in the literature, the main explanation of this resistance is the central political actors’ desire to retain political influence and mileage that comes with the control over delivery of certain public functions. This has been the

main reason behind suboptimal choice of which functions to decentralize and at what pace. For instance, rapid decentralization of education and public infrastructure development functions to the local governments without ensuring an adequate capacity at the subnational level (either fiscally or administratively), can be used as a tool by the central agency to dilute political competition at the local level. Given that the local governments have greater accountability pressures, and their performance is given precedence over any consideration of their capacities to discharge the mandated functions, a decentralization-averse centre has an incentive to reinforce their shortcomings to regain political or administrative control of some public goods.

The second facet of the balance depends on the fiscal resources that need to be devolved to the subnational governments. A key observation in this regard has been that the central government led reform processes for fiscal decentralization generally assign the subnational revenue generation responsibilities to bases that are relatively immobile thus taking out any prospects of the spatial efficiency effects to be realized or be competitive with the central revenue bases (Moore, 2004). In this regard, four key issues stand out; a) gaps between the subnational revenues and expenditure responsibilities; b) non-efficient subnational revenue bases where the cost of revenue collection outshines the revenue collection; c) implementation deficiencies similar to the functional aspects discussed above; and d) individual local revenue bases have design deficiencies (in terms of static bases e.g. property taxes, complex subnational bureaucratic structures and inefficient collection mechanisms). The analysis that follows shall explore the issues related to transfers, indigenous local revenue mobilization design and implementation, in a broader sense as well as against the DDS policy framework.

In the context of local revenue generation, it is essential that the local governments need to focus on high yield and low cost local sources of revenue instead of spreading their tax base over many sources that are typically resorted to for local mobilization (Bahl & Linn, *Urban Public Finance in Developing Countries*, 2002). Examples of such high yield and relatively stable tax bases for local revenue could be the property taxes and user charges of local public infrastructure. Property taxation while being a viable source of finance has some typical constraints for effective exploitation especially in terms of its implementation. One of the reasons for such problems is the typical '*quid-pro-quo*' involved in matters of taxation; tax contribution is a function of the taxpayers' satisfaction with the provision of public services. Also, the imposition of the property tax, if it has to garner enough scale, would need to be broadbased which would include the middle and the lower middle income segments of the local space. Also associated to the valuation mechanisms are also

procedural complexities given that the tax base is stagnant over long periods, thus the constraints to their periodic revision and collection affect the ‘buoyancy of the tax source’.

The second potential source of stable local fiscal revenue can be the imposition of user-charges on locally owned infrastructure and also some royalty payments on locally generated resource rents, if applicable. However, there are also some institutional constraints in the imposition of such charges especially in the context of increases. These could come in the form of political sensitivities, difficulty in ascertaining the marginal cost effects, and also any potentially regressive effects on equity. In the contexts where royalties on locally based extractive industries are admissible, local governments need to establish a clear revenue/royalty entitlement formula with the central collection to ensure some guaranteed retention before the central transfers are instituted. However, this is an issue of concern as this might exacerbate regional inequalities especially where resource endowments are not evenly distributed across regions. In a DDS policy framework, where regional fiscal equalization and equity is an important requisite to an effective developmental policy design and implementation, this can be an issue of critical importance.

iii) Developing an effective intergovernmental transfer system

The establishment of intergovernmental transfer mechanisms is an important institutional arrangement in a decentralized polity in general and a DDS policy framework in particular. The main rationales for the establishment of such mechanisms are augmenting local/subnational resource pools to enable delivery of assigned functions, meet national redistributive objectives, and encouraging and supporting responsive local expenditures on certain public goods/services. However, there are several common issues and problems that surface across virtually all contexts involving the design of the transfer mechanisms. Unconditional or discretionary non-earmarked grants as discussed earlier, for example, are perhaps the best form of transfer to subnational governments in terms of redistribution. Conditional or earmarked grants, on the other hand are relatively a more viable way of encouraging subnational expenditures on earmarked public services. If designed appropriately, both conditional and unconditional transfers can be of good effect in yielding not only a scaled provision of the public services but also improve the quality and responsiveness of the subnational public service delivery.

Transfers to subnational governments while also forging inter-regional equity is a complex phenomenon primarily because of the associated technical and political considerations in defining a revenue sharing formula while also retaining appropriate incentives for subnational resource

mobilization. Equal resource allocations do not necessarily result in equal results, as the degree of inequalities within the beneficiary jurisdictions face may differ hence the impact of the transfers would also be varied. While there is also an increased advocacy for the ‘Finance to follow function’, a developmentally oriented central agency needs to determine the adequate balance between the functional and fiscal dimensions. Too much fiscal decentralization to subnational levels can have adverse economic implications (as discussed above), however all downside risks ought to be compared against the gains that a stable subnational revenue base offers. The modus operandi for the design and implementation of such transfer programs should thus be rooted in incrementalism; starting off from modest transfers with any subsequent scaling up contingent on the central evaluation of the subnational performance in resource absorption and service delivery outcomes.

iv) Developing subnational access to pluralized sources of capital

While the local governments in most developing countries continue to depend on central transfers with very little of their revenue pool being financed by local mobilization, there is also an emerging trend into expose the subnational governments to alternative finance and capital generation sources. Some decentralized governments (states, large municipalities, provinces) are granted direct access to commercial sources of finance (banks and bond markets) e.g. Brazil, Colombia, whereas in some developing contexts such as India the access is relatively limited. Moreover, in some developing countries such as Indonesia, Kenya, Pakistan, the subnational borrowing modalities can take the form of special government accounts or special purpose lending institutions for a clearly defined developmental or disbursal framework. This issue is on a slightly different tangent to the preceding discussions on revenue and functional intergovernmental transfers, where most of the local government finance requisites come under the transfer arrangements emerging under complex institutional and political arrangements that are at best, limited in allowing optimal discretion to subnational levels.

As a means of providing the subnational governments with a more diversified pool of options to solicit financial capital from the traditional sources (grants and subsidized loans and grants) to local and international private/multilateral avenues for loans or grant solicitation for self-financing earmarked projects. A spinoff advantage of linking them up to a diversified pool of options also fosters greater accountability and efficiency in the utilization and absorption of the funds secured as compared to the more relaxed variants of intergovernmental transfers. Such a linking cannot be

brought about without the central patronage, as the sovereign guarantee is normally not afforded to the subnational governance structures. Similar to the requisites of grants disbursement, the central government in the interest of diligence has to keep the domestic fiscal context in cognizance to ensure that subnational fiscal behaviour does not pose any detriment to the broader national economic stability. Only in the contexts where decentralized governance structures are well embedded and strong (for instance in Brazil, Argentina, Indonesia, South Africa), the development of direct subnational access to capital markets is more viable. However, the centre must maintain constant oversight and diligence over the subnational borrowing by establishing clear limits, standards and conditional guarantees of support in the event of bailout requests.

In the contexts where the institutionalization of the local governance structures in the domestic political space is weak, or where there is a functional-fiscal divide between, a special purpose earmarked institutional entity e.g. a municipal development bank may be a more viable approach than a direct access to the capital markets. Since these institutions are initially sponsored predominantly by the central governments either through indigenous domestic resource mobilization or through external flows from bi/multilateral sources. In such a context, the centre enjoys considerable discretion over the activities of the local governments though there must be countervailing checks to minimize any prospects of abuse of power. Under such an arrangement, with the centre having a greater discretion, there is also a greater prospect of linking the grants-loan mechanisms. In most of the developing countries, the loan and grant disbursements are done mutually exclusively, except in some instances where grants are used as incentive mechanisms to encourage prudent subnational absorption. Instituting an integrated grants-loans mechanism when devising subnational fiscal and functional empowerment has the potential of improving the effectiveness and efficiency of resource use.

DECENTRALIZATION AND DEVELOPMENTALISM IN BOLIVIA

3.1 CONTEXTUAL OVERVIEW

The preceding chapters have attempted to put forth the advocacies both for and against decentralization and its implications for democracy and development independently as well as collectively in the form of a democratic developmental state. If there is a single term to define decentralization reform experiences in both, form and impact, it would be heterogeneity; no single optimal process or sequence of reforms and thus a wide spread in the degree of effective decentralization as well. The growing awareness in the literature, both policy and academic, highlights the existing mismatch between the decentralization normative objectives and how it is implemented in practice thus skewing the results in the contrary direction; strained fiscal fronts, poor accountability outcomes, erratic trends in service delivery qualities. Central to any such reform process, as discussed earlier, are the political economy factors and how the interests and incentives of the stakeholders determine the form, sequence and outcomes of these reforms. This chapter attempts to provide an expository analysis of the decentralization reforms in Bolivia, by analyzing the actors, incentive structures, bargaining dynamics and the resulting outcomes for democracy and development in Bolivia. The Bolivian model of decentralization, as this chapter illustrates subnational domination in the design and implementation of the decentralization reform and exhibits strongly positive outcomes in terms of democracy, institutionalization, public service delivery responsiveness and efficiency while being less positive in core economic outcomes. The evaluation of the Bolivian case is largely from the perspective of second round of decentralization that were initiated in 2006, and the degrees to which it finds its roots in the 1994 LPP in terms of institutional and governance realms.

Classified amongst the poorest countries in the Latin American & Caribbean region, while also being one of the richest in terms of natural resource endowments (hydrocarbons) and soil conduciveness to productive agriculture, Bolivia is characterized by significant economic, ethnic, and social inequalities that have often been contentious³³. The indigenous

³³ A current example of this is the inter-regional conflict between the highlands (where the defacto capital, La Paz is situated) and the south eastern lowlands (*Media Luma*) which is a host to highly productive agriculture as well as substantial hydrocarbon resources.

population of Bolivia, also a demographic majority³⁴, has been one of the most consistently discriminated groups historically. Bolivia has the distinction of being the country that has witnessed the most number of *coup d'etats* in its post-independence political history than any other country in the world (Morales 1992). The 1952 Bolivian Revolution saw the Nationalist Revolutionary Movement's (Movimiento Nacionalista Revolucionario --MNR) accession to the government. Upon assuming the incumbency, the MNR set out to affirm its populist mandate by nationalizing large mining and export industries, redistribution of agricultural land, and the introduction of social transfer schemes. However, the radical reforms that the MNR under the leadership of Paz Estenssoro tried to introduce led to significant economic imbalances due to inflation and inadequate investment in productive economic sectors. The economic problems as well as the political instability led to the MNR government's deposition and a military government took over and in the later half of the 1960s and much of the 1970s, the focus shifted to the maintenance of internal order, and the introduction of a 'revolutionary nationalism' program.

The Banzer era (1971-78), a populist military regime supported by the MNR, witnessed substantial economic growth driven largely by the Bolivian commodity export demand. The governance coalition with the MNR was short lived and in 1974, following the demise of the coalition with the MNR, the labor movements intensified which led the Banzer regime to resort to repressive means of preserving their incumbency. Owing to growing external and internal pressures, the first round of negotiated transition to civilian government took place in 1982, with the UDP (Unidad Democratica y Popular) coalition gaining incumbency with Zuazo assuming Presidency. Following a phase of hyperinflation, consistently high fiscal and balance of payments deficits and an intense social backlash against the economic mayhem, new electoral rounds were called. These elections saw the resurgence of former General Banzer and the MNR leader Estenssoro, with the latter emerging as the victor for the fourth time owing to a coalition with the left-wing party MIR (Movimiento de la Izquierda Revolucionaria). Upon gaining incumbency, Estenssoro in a stark departure from his preceding tenures, instituted one of the most austere economic stabilization programs ever implemented in the LAC region (Sachs, 1987).

This new policy framework under Estenssoro, labelled as the NEP (Nueva Politica Economica), included divestiture of state interests from the non-performing public sector

³⁴ The demographic census in 2009 recognizes 36 groups of indigenous groups concentrated largely in Quecha (30% of the total population) and Aymara (approximately 25% of total population)

enterprises, privatization and deregulation to attract private and foreign capital investments, in addition to the inflation containing strategies. While the NEP was successful in grappling with the hyper-inflation, the austerity regime resulted in substantial suppression of the real wages which exacerbated the already high levels of poverty (Kohl, 2002). The era after 1985 is also known as one of *'pacted democracy'* in Bolivia, where Estenssoro and Banzer negotiated a political agreement for power-sharing in order to grapple the political fragmentation and push through the neoliberal reforms and austerity policies. This pacted democracy played a vital role in ensuring not only a policy consistency but also in the resolution of the political impasses in the 1989 and 1993 electoral rounds. The period from 1989-1993 saw a continuation of the liberalization and austerity framework while registering a modest economic recovery which was rooted partly in the resurgent prices of tin (the main export at the time) in the global market and the discovery of hydrocarbon reserves in Bolivia. The 1993 elections resulted in Estenssoro's MNR coming back into the power, this time under the leadership of Sanchez de Lozada, whose policy stance was a continuation of the preceding ones albeit more focused on creating viable environment for private capital engagement in the hydrocarbons sector³⁵.

While the *'pacted democracy'* did have positive implications for the Bolivian economic stabilization as well as enabling a degree of consolidation of civilian democracy, it also had an *exclusionary bias* as most of the demographically dominant indigenous groups felt excluded and marginalized in socioeconomic and political spheres, to a larger extent by the outcomes of the neoliberal reforms (Kruse, 1994). The 1990s saw the indigenous social movements increasingly challenging the agreements established by the political elites of the country. While the process merely surfaced during the early 1990s, it gained more momentum as the years went on and by 2000, the indigenous peoples movement got considerably well-organized and well-articulated that resulted in the ouster of President Lozada in 2003 and his successor President Mesa in 2005. The last few years of the 1990s saw the rise of Evo Morales, who was of an indigenous ethnic origin and also a union leader of the coca growers, as a leading representative of the diverse social movements against the political status-quo

Following the ouster of President Mesa in 2005, a fresh round of elections was conducted in which Evo Morales assumed the Presidency. Since he assumed office, Morales has

³⁵ Massive concessions were put forth to attract private capital in the form of 30-year operating contracts. Foreign capital inflows as a consequence doubled the capital of the state-owned energy companies and massive gas exploration. This surge in the investment and capital flows into the hydrocarbons sector resulted in as much as a fivefold increase in the annual resource royalties generated by the Bolivian state to about US\$ 500 million per annum in 2000 (IMF, 2001).

been instituting wider-ranged reforms in the political structure of Bolivia through constitutional reform as well as in the socio-economic realms. The constitutional reform project under Morales began in 2006, with an elected Constituent Assembly tasked with the formulation of a new constitution. Following various rounds of deliberations and revisions, the new constitution was formally instituted in 2009 after a public referendum whereby a 61% majority voted in its favor. The resultant transformation of the state structure and the socio-economic policy framework established a 'plurinational state'; an amalgamation of the institutional dynamics of liberal and representative democracy with the mechanisms of direct democracy and unmediated participation by civil society organizations (Albro, 2010). The fundamental departure that the 2009 Constitution took from the prior constitutional framework was the equal status of state law and indigenous systems of justice. The liberal state model is applied by the recognition of indigenous (socially embedded) forms of local governance, and the constituents' civil and political rights are augmented by a broadbased stipulation of socio-economic and collective rights of the indigenous populace. The economic agenda under the Morales government is also a pluralistic with private enterprise and state involvement in the economic space, albeit more skewed towards the latter, coupled with a communitarian and socially oriented economic organization. As a profound process of structural transformation, both in socio-economic and political terms, it enjoys broad support amongst the Bolivian populace (mainly the previously excluded groups) but continues to be heavily contested by the traditional elites and stakeholders in the dominant sectors of the economy. Given the fragmented and weak political opposition at the central level, much of this contestation emerges from the regional autonomy movements particularly in the southeastern lowlands (Media Luna as mentioned earlier) led by the elected governors and the 'civic committees'. While this shall be discussed in a greater detail in the sections following in this chapter, Bolivia presents perhaps the most appropriate model in terms analyzing the notions of decentralization, democratization and developmentalism individually as well as in tandem.

From a developmental standpoint, the Morales government has stipulated a national development strategy, under the title of *Plan Nacional de Desarrollo: Bolivia Digna, Soberana, Productiva y Democrática para Vivir Bien, Lineamientos Estratégicos* (National Development Plan: Dignified, Sovereign, Productive, and Democratic Bolivia to Live Well, Strategic Directions)³⁶,

³⁶ This chapter shall use National Development Plan (NDP) as a translated version of the *Plan Nacional de Desarrollo (PND)*, from hereon.

instituted in 2006 which remains enforced in phases lasting five years. Currently, the NDP is in the second phase of its implementation and as part of this plan, the Morales government maximized state's control on its extractives industry by stipulating new contracts for the international enterprises engaged in the hydrocarbons industry, while also increasing the influence of the state owned YPFB (Yacimientos Petroliferos Fiscales Bolivianos) as well as increasing the taxes on companies working in the extractives sector. The objective was to increase the size of the fiscal pool by directing most of the resource rents to the national exchequer and use them to deliver social services and benefits, as well as expanding the size of public investment. From a democratic point of view, the substantial subnational political empowerment emanating initially from the 1994 Law of Popular Participation (LPP – Ley de Participación Popular) and further consolidated in the post 2006 decentralization reforms, have enabled competitive politics at the local level with effectively responsive and accountable local governance structures.

The subsequent section shall put forth a transformation analysis of Bolivian state for the period 2006-2014, which would enable a composite view of the trends exhibited in terms of political transformation, economic transformation and the management of the transformation processes. The sections that follow shall contextualize these results and trends identified in the Bolivian decentralization reforms; reform dynamics, key actors, incentive structures, and sequential prioritization. While the focus of this research remains on the post 2006 decentralization reforms and their implications, it also considers in some detail the 1994 LPP as the current reforms are rooted institutionally and contextually in the structures established under the LPP. Given the underlying interests of the various national and subnational actors in the Bolivian socio-economic and political space, this chapter will draw on the political economy of decentralization literature to analyze the sequential developments and use some of the existing conclusions on the current scope of analysis as an explanatory methodological tool. Given the importance of political parties as actors in Bolivia, the partisan dynamics are central to understanding their incentive maximizing behavior. For instance, O'Neill (1998) presents the importance of the inter-temporal considerations of political parties; which are critical factors in understanding when and if decentralization reforms can truly be implemented. This argument is exhibited in the first round of reforms in 1994 by the MNR and continues to be of explanatory value in the ongoing reforms under MAS. Similarly, Haggard et.al. (1999) discuss how the

incentives of the incumbents in the executive and the legislature are shaped by the partisan interests.

Another strand of arguments is presented by Hellman (1998), although the analysis focused on the partiality of reform in a different context but it has value for the discussion on decentralization reforms as well. The analysis in this paper argues that the winners of the first round of reforms shall in their interest retention, pose obstacles for the subsequent rounds. This is of considerable explanatory value in the case of Bolivia, as the roles and responsibilities for the subnational governments in general continue to be largely disjointed. Such situations according to Herbst (2001), can result in accountability inadequacies and thus lead to self-reinforcing governance traps. As the fiscal aspects of decentralization continue to cloud the decentralization reforms across Latin America in general, but Bolivia in particular, Rodden et.al. (2003) and Webb (2004) argue that the enforcement of hard budget constraints on the subnational governments deems imperative a balance of ex-ante controls and ex-post consequences, and are critically dependent on the enforcement capacity of the centre. Equally important in the case of Bolivia is the strand of literature on rentier states and mineral rich contexts, whereby amongst others Ahmad et.al. (2011), Bahl et.al. (2004), and Morgandi (2008), present the intricacies of revenue sharing mechanisms across inter-governmental contexts and their effects on the equity and efficiency of the governments across these tiers.

3.2 LPP – THE FIRST PHASE OF DECENTRALIZATION IN BOLIVIA

The Ley de Participacion Popular (hereon referred to as LPP), came as a consequence of a long effort to decentralize government and expand its scale and penetration across the Bolivian polity, particularly in the marginalized rural communities that also constituted a demographic majority [CIPCA (1991), Molina Monasterios (1997)]. While the LPP was developed by a group of technocrats mandated by the then President Gonzales Sanchez de Lozada, and pushed through as a top down reform initiative, its implications were profound, it did not follow on the hypothesized centrally preferred sequence of AFP, but instead did a bit of all simultaneously. The LPP when first announced in January 1994 was received by widescale opposition but was nevertheless promulgated by the Congress as a Law in April 1994 and brought into effect from July. The magnitude of change in the balance of resource allocation and political power that came about as a consequence of the LPP was enormous as shall be seen subsequently. The four main facets of the LPP were:

- 1) The share of national fiscal revenue pool transferred from the central to municipal governments was established at 20%. Prior to this promulgation, the fiscal apportionments were made on an ad-hoc basis that was heavily influenced by political dynamics. However, under this law this 20% was to be further distributed on a strict per capita basis
- 2) All public services in the realm of basic healthcare, primary education, roads, irrigation, culture and sports infrastructure, were functionally accorded to the municipalities with the administration, maintenance, investment and equipment requisites being a local responsibilities.
- 3) Establishment of Oversight Committees (Comites de Vigilancia) to oversee the absorption of the fiscal resources devolved under the LPP, and to propose new projects. These groups were comprised of members from local communities and/or grass-roots organizations who could have the fiscal flows to the municipality blocked if they considered a misappropriation in their allocation at the local level.
- 4) 198 new municipalities were created, and existing ones expanded to include suburbs and surrounding rural areas.

The envisaged outcomes of the LPP were that effective participation would be manifested at the municipal level in terms of the mandatory planning documents including the annual plans, and the municipal development plans. The local community level capacity building under the LPP envisaged a collaboration with the CSOs and NGOs based within the local space.

Impact of the LPP

This reform did usher a new era for the local governance of a vast majority of the Bolivian towns and cities, whereby for the first time each town/city had its own local government accountable to its constituents instead of the central state's prior status of an 'absentee landlord'. Furthermore, in the antecedent times, all allocations for urban development were accorded to municipal capitals or indirectly through the regional development corporations organized at the departmental level. As a result, about 86% of the total national fiscal devolution was captured by three cities with only 14% available for the rest of the country (See Table4). The promulgation of this law was heavily criticized in terms of being a central dictation and the transfer of responsibilities (both revenue and expenditure) were considered as

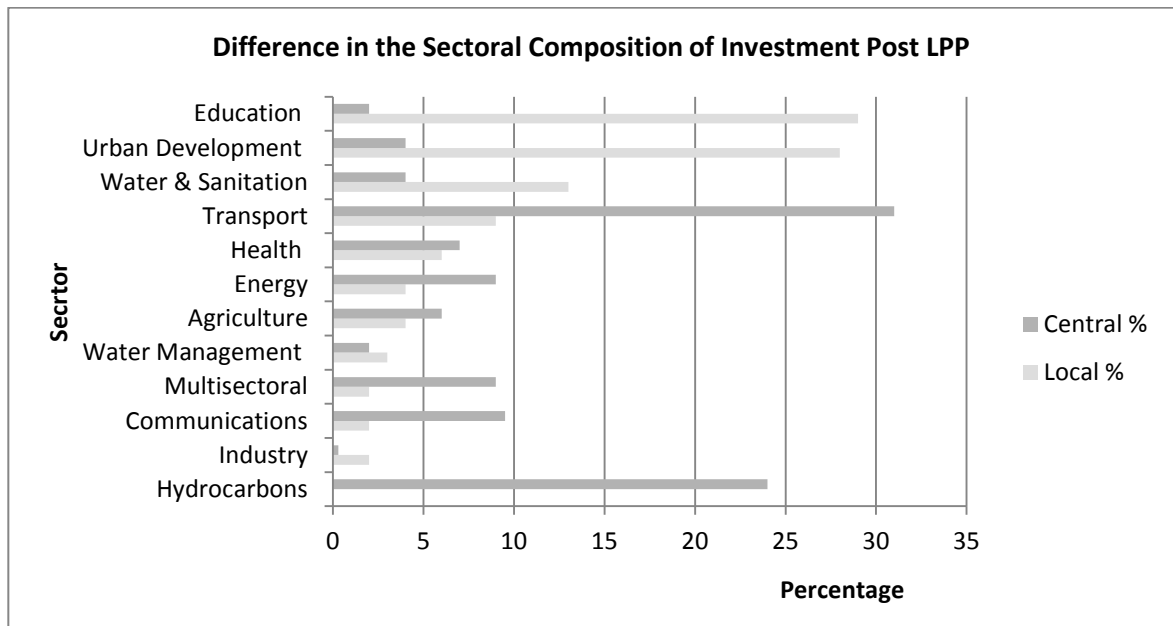
an abdication of its duties by the central state. (Ayala, Bostos, Viana, Molina, Mayorga, & Exeni, 2011).

Table 4: Intergovernmental Finance Distribution Pre- and Post LPP 1994

| City Year | Central to Subnational Revenue Sharing (Bs'000s) | | | Total Central Transfers Absorbed (%) | |
|-------------------------|--|---------|----------|--------------------------------------|------|
| | 1993 | 1995 | % Change | 1993 | 1995 |
| La Paz | 114,292 | 61,976 | -46% | 51% | 10% |
| Cochabamba | 25,856 | 38,442 | 49% | 12% | 6% |
| Santa Cruz | 51,278 | 63,076 | 23% | 23% | 10% |
| <i>Total (3 cities)</i> | 191,426 | 163,494 | -15% | 86% | 27% |
| Rest of Bolivia | 32,099 | 444,786 | 1286% | 14% | 73% |
| Total | 223,525 | 608,280 | 172% | | |

Source: Faguet (2002)

While the above illustrates the distribution of fiscal resources in the preceding and subsequent period of the LPP, it would perhaps be more important to illustrate how the sectoral composition of the public investment by the central and subnational levels. The figures below show the differences in the sectoral investments by the subnational and the central governments in 1993-1994 and 1995-1996. The central investments illustrate the pre-LPP time and the subnational/local investments illustrate the investments in the aftermath of the LPP. The difference in the magnitude of investment across all these functionally devolved structures is significant. Prior to the LPP, the central government's investment were the highest in the transport, hydrocarbons, energy and multi-sectoral realms. The aggregate investment across these 4 sectors amounted to 73% of the total public investment in the period immediately preceding 1994. However, after the functional and fiscal decentralization under the LPP in 1994, the local governments' investment preferences are exhibited in their sectoral investment proportions. The highest investment was in education, followed by urban development, and water and sanitation with the aggregate investment across these three sectors tallying to 79% of the total subnational investments. This further illustrates the difference in the priorities between the central and subnational governments in Bolivia.



Source: Faguet 2002

While the above was intended to give a macro-level picture of the subnational discretionary expansion, the focus shall now shift upon the impact of the LPP in specific realms³⁷. In particular, the impact shall be evaluated in terms of: a) Government Efficiency and Developmental Planning, b) Political Accountability.

a) Government Efficiency and Developmental Planning

While the advocacies in support of administrative decentralization in particular, and decentralization in general, extol its reductionary effects on the size and costs of governance in addition to the efficiency gains in the social spending (Randinelli, McCullough, & Johnson, 1989), the Bolivian experience presents a stark contrast. Following the LPP, the overall size of the government expanded as the local bureaucracies had to be staffed and led to a creation of 30,000 new jobs in the subnational governments across Bolivia (Booth, Suzanne Clisby, & Widmark, 1996). The growth of the bureaucratic structures has two major implications for the subnational tiers of government;

³⁷ This discussion here builds on the unstructured discussions/ interviews I had with representatives of municipal governments and central government representatives as part of another project on the Politics of Domestic Resource Mobilization, and some literature obtained in the process.

- i) The availability of fiscal revenues for local absorption becomes a function of standardization and well-established rules, and
- ii) The subnational governments need to develop their own revenue sources to sustain the structures rather than relying exclusively on central transfers.

Especially concerning with the latter, such expansion in the role of the municipal governments led to the diversification of their own revenue base which resulted in additional taxes and thus faced resistance in the local constituent base. Furthermore, increasing the central revenue sharing with the subnational governments along with additional functional devolution resulted in an adverse outcome for most of the municipalities that did not have the adequate administrative capacity to deliver the assigned functions that were previously under the departmental or the national mandate.

The increase in revenue sharing by the central government failed to address the already divergent capacities in the subnational space, as some of the more urban municipalities who had a greater revenue generation capacity compared to their rural peers were more effective in pluralizing their revenue pools through local sources. For instance, in La Paz, less than 20% of the municipal revenues came from the central transfers whereas in most of the rural municipalities 100% came from the central transfers (Faguet 2002). While this remains consistent with the stylized differences between the urban and rural areas (Lipton, 1980), this remained an issue of concern and to a certain degree, continues to be in the ongoing phase as well. The rural municipalities are also the main source of labor and food production, and the transfers did not do much justice to them.

While the explicit focus of the LPP was to meet decentralization and not the developmental objectives, there were conceptions amongst its proponents that the transfer of resources to the local and municipal levels would have developmental implications as well. Despite the numerous projects that were initiated to integrate the economic and municipal development, they remained largely limited in effect.

b) Political Accountability

In the aftermath of the LPP promulgation, the clientilistic politics and financial misdemeanor still persisted in both, the public and private sector. In 1997, a report concluded that if corruption could be curtailed the GDP could grow by 60% (Economists, 1997). In the

aftermath of its promulgation, the advocacies against the LPP asserted that this would “decentralize corruption” and local capture by the established political and economic elites. This CDC report further reported the commonly accepted figures for the kickbacks ranging from 10-25% in the procurement of services at the municipal level. Furthermore, in 2003, the accounts of 25 municipalities were frozen by the national treasury on account of inadequate fiscal reporting whereas another 185 municipalities had not filed one or more financial reports (IMF, 2004). The failure of the LPP, however, was only to extent of not ameliorating corruption instead of causing it. However, there were still positive trends emerging in terms of local mobilization against corruption as a subset of the overall social mobilization by the indigenous groups.

The LPP was also somewhat successful in changing the course of the resistance to the broader national neoliberal reforms by enabling progressive resource allocations enough to dilute their rigor (Kohl, 2002). Up until 1985, where all opposition to the neoliberal reform led programs took national and class-based forms e.g. the Bolivian Workers’ Confederation (Bolivia Confederación de Trabajadores) would issue protest calls that would result in national shutdowns. With greater focus being placed on the local politics and governance under the LPP, the opposition oriented its focus on the grassroots territorial organizations and municipal contestation for resource allocations instead of being engaged on the national issues. However, it must be noted that while such locally based social movements and opposition movements have had some notable successes e.g. Cochabamaba Water Wars, such successes could not always be scaled up to national level gains (Finnegan, 2002). The indigenous movements that have since the early 1990s been quite an impetus behind all spinoff movements did not, for the most part, register the same gains in the local realm in terms of dislodging or pressurizing local elites, as they did on the national front.

In conclusion, the LPP was a significant departure from the closed access political and socio-economic state model that had existed in Bolivia, yet it had major shortcomings in its implementation due to limited enfranchisement of the general populace in its design. Allegorically similar to how introduction of formal democratic institutions does not guarantee the substantive aspects of democracy; the LPP was also constrained in delivering broad-based and substantive results. The main positive legacy of the LPP was been that it, for the first time, enabled participation by the previously excluded groups of the populace, in bringing the process

of resource allocation and its subsequent absorption within the scope of influence of the public, and perhaps, most importantly in shaping the expectations of the government that a majority of the Bolivians established in its aftermath. The LPP and the associated decentralization reforms led to an increased recognition and importance of the subnational domains as alternative platforms to the traditional political actors.

3.3 THE SECOND PHASE OF DECENTRALIZATION IN BOLIVIA

The second phase of decentralization began in 2006 as the MAS government assumed incumbency, with a stronger emphasis on the deepening the regional autonomy primarily in terms of enabling fiscal capacities of the subnational structures keeping in view their increased political articulation.

The current round of decentralization was at its outset, characterized with two significant developments: election of Department Governors (Prefectos), and the expansion in the fiscal transfers by employing 2/3rd of the additional fiscal revenue generated under the Hydrocarbon Law (referred to as HL from hereon). The election of the Prefectos at the outset was a significant event as the elected Prefectos derived their mandate from the department constituents rather than the head of the state or the central government. In terms of the expansion in the divisible fiscal pool, this was a significant event as a substantial additional contribution, to the tune of US \$ 240 million in 2006 (IMF Article IV, 2006) was not matched by any expansion in the functional obligations of the prefectures/ departmental governments. Enacting these two at the very outset of the tenure as well as constitution-making process served the purpose of credible signaling of the MAS government's commitment to regional autonomy and participatory governance. However, the main pitfall of this was that the bargaining capacity of the centre was significantly reduced.

Following on the legacy of the LPP, it is evident that the normative goals behind the decentralization reforms will be of limited effect if they are not being enacted in a basic framework of fiscal transparency and responsibility; one that overcomes horizontal imbalances while also ensuring that the 'finance must follow function'. In general, the second phase of decentralization builds on the preceding LPP in terms of deepening political decentralization but most importantly bridge up the fiscal capacities of the subnational governments to deliver

well on their functional responsibilities and complement the national developmental policy framework.

Intergovernmental Arrangements in ‘Plurinational’ Bolivia

The organization of the state under the new constitution promulgated in 2009 retains the unitary nature of the state that is further divided into 9 departments that comprise of a total of 330 municipalities³⁸. As covered earlier, the Departmental governments fall under the supervision of the Governors (prefecto) who gain incumbency through a popular election with a subsequent endorsement of the centre. This constitutionally defined ‘hybrid’ nature of the Prefectos, manifests a vertical duality of representation and accountability to the departmental constituents as well as the central government. Each department also has its own Departmental Council that is popularly elected, mandated primarily with defining a departmental policy framework that incorporates the aggregate preferences and requisites of the constituent municipalities, but most importantly approving the departmental budgets. However, departmental budgets are not clearly delineated³⁹. A majority of the departmental budgets are absorbed in secondary infrastructure, electricity supply, irrigation, and other physical works. The departments have no authorization to raise their own tax revenues, even though they can raise it through service or usage fees, and most of their revenue basically comes through the central transfers. At the lowest level are the municipalities that are headed by popularly elected mayors and have municipal councils in place. Their scope of activity pertains to the provision of urban services with an envisaged role of complete discretion over the health and education sectors within their respective jurisdictions, although this has been limited to ‘management’ till now because of capacity constraints.

The municipalities are authorized to diversify their fiscal pool by raising indigenous revenues through local sources e.g. property or automobile taxes. In addition, the new Constitution also recognizes two additional autonomous entities; indigenous autonomies and regions. The former comprises of municipalities based on ethnic considerations and traditional rights, while the latter (Regions) are established on demand of adjacent municipalities. Both these entities are funded through the central allocations to the departments. There is also a

³⁸ The terms “department” and “departmental government” are used interchangeably, except as otherwise noted. The term “subnational governments” refers to both departments and municipalities.

³⁹ Department governments participate in the elaboration and partly also in the execution of a number of ministerial budgets of the central government.

provincial level which operates between the departments and municipalities, and it serves as a platform for the political representation of the prefect; however it has no expenditure responsibilities or revenue privileges.

With the political legal structures addressed, it would be more advantageous given the focus of this chapter to look at the fiscal indicators of the subnational governments to gauge the extent of change in the subnational fiscal behaviors after the expansion in the divisible pool. The table below presents these trends in terms of three indicators that measure the extent of expenditure decentralization, revenue decentralization, and finally the extent of transfer dependence. In the light of the new constitutional framework and the expanded fiscal transfers to the subnational levels, the subnational expenditures constitute a progressively higher proportion of the total public expenditures while also becoming more dependent on central transfers (particularly in the case of municipalities. However, if viewed in the regional perspective the role of Bolivian subnational governments in terms of scale and functional responsibilities may not be as significant as Brazil or Argentina (both federal countries), but in terms of depth of the decentralization reforms (political, fiscal and administrative forms of decentralization in reinforcing simultaneous existence) it fares much better.

Table 5 : Fiscal Decentralization Indicators 2006 -2010 (in %age)

| <i>Departments/ Prefecturas</i> | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|------|------|------|------|------|
| Expenditure Decentralization Ratios | 16.4 | 15.7 | 11.0 | 15.7 | 11 |
| Tax Decentralization Ratios | 0.3 | 0.2 | 0.2 | 0.1 | 0.1 |
| Transfers Dependency Ratios | 96 | 96.3 | 93.7 | 92.9 | 92.1 |
| Excl. Wages and Salaries for Health and Education | 90 | 93 | 89.4 | 88.4 | 5.4 |
| <i>Municipalities</i> | | | | | |
| Expenditure Decentralization Ratios | 17.1 | 14.9 | 19.6 | 20.6 | 20.3 |
| Tax Decentralization Ratios | 5.5 | 3.9 | 3.3 | 3.4 | 3.1 |
| Transfers Dependency Ratios | 65.9 | 68.7 | 77.3 | 74.1 | 75.5 |
| <i>Subnational Governments</i> | | | | | |
| Expenditure Decentralization Ratios | 24.4 | 24.9 | 36.1 | 36.3 | 31.3 |
| Tax Decentralization Ratios | 5.8 | 4.1 | 3.5 | 3.5 | 3.3 |
| Transfers Dependency Ratios | 82.6 | 85.5 | 86.8 | 84.7 | 83.8 |
| Excl. Wages and Salaries for Health and Education | 74 | 79.7 | 82.7 | 80.4 | 79 |

Notes: Expenditure Decentralization= Expenditure of Gov. Level/ Total Public Expenditure | Tax Decentralization = Tax of Gov Level/ Total Government Tax Revenue| Transfer Dependence = Transfer Receipts/ Total Fiscal Pool of the Specific Gov

Source: IMF Government Finance Statistics/ Art IV upto 2010, National Accounts (Various)

3.4 MAIN ACTORS AND INCENTIVE STRUCTURES IN PHASE 2 OF DECENTRALIZATION

Given the rise of the MAS party from subnational political space to the central level, the main political mandate of the new Morales regime was to initiate a process of substantive political change that at its outset focused on forging a new constitution and state structure. An important point to note here is that the preference and order of decentralization reforms pursued by the MAS government were reflective of the Subnational Dominance Path as elucidated in the Sequential Theory, primarily because all these preferences were developed and amply articulated by MAS at the subnational level before they assumed the national stage.

Political decentralization was the top of the agenda of the Bolivian decentralization following 2006, with even greater pressure coming from the subnational level for greater autonomy⁴⁰. Furthermore, with the elections of the Prefectos of the nine departments at the outset of the reform process incorporated a new set of bargaining agents contesting for greater shares of the national divisible pool. While structurally they remain under the President, the fact that they have been elected through popular direct election entitles them to a much higher leverage once articulating their claims and credibly bargaining with the centre. The interesting case of this round of decentralization has been that right after the elections of 2006, the promulgation of the Hydrocarbon Law, a previously united subnational front saw the bigger Departments developing their individual preferences and motivations to participate in the decentralization game, thus defining new norms of the political context in which the bargaining over the resource pool takes place.

The driving forces behind Bolivia's ongoing decentralization effort are not its needs for service delivery improvements, reduction of regional inequalities or greater fiscal responsibility, despite their importance. They are instead competing pressures for control and distribution of revenues originating from the country's natural resources, particularly revenues from hydrocarbons and land usage. The overall agenda of regional autonomy is mainly a result of the articulations of the Media Luna departments, comprising of Santa Cruz, Tarija, Beni and Pando. As mentioned earlier, the wealth of these regions in terms of agriculture and hydrocarbon

⁴⁰ Along with issues of land distribution, indigenous rights, distribution and use of hydrocarbons revenue, the issue of greater regional autonomy was the key element of this new social contract in Bolivia.

endowments is significantly higher than the other regions of Bolivia, which has been at the heart of their objective of greater local retention of the revenues coming from these sectors. In terms of GDP/capita, Santa Cruz is the wealthiest jurisdiction and hence assumes the dominant role in the ML. In addition to the economic attributes of the ML regions, there is also a strong regional identity especially in Santa Cruz, which transcends all notions of political or other group based allegiances. The main demand of the Santa Cruz region, for instance, has been the withholding of 2/3rd of the locally generated tax and customs revenue, with only 1/3rd transferred to the central divisible pool. This continues to be a highly contested subject between the centre and Santa Cruz in particular (as well as ML regions in general), since it is difficult to distinguish between the local and central taxes generated in a certain territory as the central taxation does not involve only the territorial collection but also the taxation generated from the economic activity of households and enterprises located in that territory.

To interpret the incentives and of all the relevant political actors in the current decentralization game, the game framework outlined in Chapter 1 can be used.

All regions yield a total product, a proportion of which is taxed by the Central Government who exercises full discretion over its use for redistribution or retention. In the status quo the tax rate is $0 < T < 1$. The total income generated for this tax rate is Y . The total tax revenue that the CG receives equals TY , while the disposable income of the regions collectively is $Y(1 - T)$. In each period, the CG has two strategies. It either maintains the status quo, which means that the tax rate does not change or it can retaliate by increasing the tax rate to T^{np} so that $T^{np} > T$. For the tax rate T^{np} , the income generated is Y^{np} and the disposable surplus/income of the regions is $Y^{np}(1 - T^{np})$.

From the perspective of the regions, they have two strategies. They can either concede to the tax rate proposed by the CG or they can retaliate and demand for T^p such that

$$0 < T^p < T < T^{np} < 1.$$

The total income generated for this tax rate is Y^p . At all times, the cost of retaliation of the regions is μ , where $0 < \mu < 1$, whereas the cost of increasing T for the CG is r where $0 < r < 1$. Every region has its own share of contribution to the total disposable income individually given by $\phi(Y - YT)$ where $0 < \phi < 1$. In the previous setup, it was assumed that at $t=0$, all regions operate collectively and no contestation over individual shares exists. However, if there is a disparate contribution of the regions to the collective output yield Y , then

there are different constraints that face individual regions in their bargaining processes with the CG. The higher the \emptyset , the greater would be the bargaining power with the CG as the potential increase in surplus due to favorable bargaining results would still be higher than the cost of retaliation μ .

The main preference of the central government here is assumed to be redistributive and would be to retain a section of the receipts from taxes for central expenditures and policies, and transfer the remainder back to the Departments and the Municipalities. Looking at the trends of Departmental Contribution in the National GDP, it can be seen that the 4 ML Departments contribute 80% of the total GDP.

Table 6: Departmental Share of Bolivia National GDP

| Department | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | Mean 2005-14 |
|------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|--------------|
| Chuquisaca | 4.4 | 4.58 | 4.44 | 4.63 | 4.49 | 4.47 | 4.35 | 4.52 | 4.84 | 4.97 | 4.57 |
| La Paz | 24.51 | 24.06 | 24.57 | 24.52 | 25.16 | 25.13 | 25.31 | 25.2 | 24.96 | 25.2 | 24.86 |
| Cochabamba | 16.85 | 16.06 | 15.89 | 15.3 | 15.24 | 14.91 | 14.25 | 14.21 | 14.12 | 14.2 | 15.10 |
| Oruro | 4.92 | 4.85 | 4.97 | 5.5 | 5.61 | 5.89 | 5.97 | 5.07 | 4.89 | 4.77 | 5.24 |
| Potosí | 4.54 | 5.5 | 5.41 | 6.4 | 6.85 | 7.16 | 7.44 | 5.86 | 5.48 | 5.43 | 6.01 |
| Tarija | 11.24 | 11.79 | 12.76 | 12.26 | 11.61 | 11.32 | 12.07 | 13.52 | 14.29 | 13.69 | 12.46 |
| Santa Cruz | 29.54 | 29.09 | 28.22 | 27.67 | 27.2 | 27.28 | 27.05 | 28.22 | 28.11 | 28.48 | 28.09 |
| Beni | 3.05 | 3.21 | 2.77 | 2.77 | 2.95 | 2.9 | 2.64 | 2.51 | 2.43 | 2.41 | 2.76 |
| Pando | 0.94 | 0.86 | 0.97 | 0.95 | 0.89 | 0.94 | 0.93 | 0.9 | 0.87 | 0.86 | 0.91 |

Source: Compiled from INE 2016

Going back to the game setup, the four ML regions could pursue their interest maximization by forming a sub-coalition to expropriate the other members of the initial coalition, since they have a greater aggregate power than the remaining members.

$$\emptyset_{ML\ Subcoalition}(Y - YT) > \emptyset_{Remainder}(Y - YT)$$

The Central Government Preference would be to aim for regional fiscal equalization, and to ensure that an adequate level of public services is extended to all population. The ML regions, as per the game framework outlined in Chapter 1, retaliate from the established fiscal status quo, demanding a greater retention of the locally generated revenue. Regardless of the political motivations and the ‘hard to satiate’ demands of these regions, the guiding premise remains that the administrative centre in La Paz has limited responsiveness to the local needs of

Santa Cruz coupled with the perceptions of the central government and politics being too distant, inefficient and corrupt, and the redistributive fiscal regime of the centre shall come at the expense of the local development plans.

The other departments in the ML, including Beni and Pando, have limited representation in the national political space hence their scope of influence is constrained vis-à-vis Santa Cruz in the preference articulation to the centre. Their stance on the autonomy demands shall be consistent to that of Santa Cruz as long as they register improvements in their fiscal and political positions, but their scope of influence on Santa Cruz itself remains limited. The slightly less politically influential, but significantly influential in terms of the fiscal contributions in the ML region, is Tarija which has a substantial hydrocarbon endowment base and thus has a direct stake in the higher subnational retention of the rents.

Apart from the ML, the main four highland departments of La Paz, Oruro, Potosi and Chuquisaca are against the demands of greater autonomy put forth by the Media Luna departments. These regions, in addition to having a majority of the indigenous peoples, also happen to be the main support base for the incumbent political party, MAS. The anti-exploitation political rhetoric of the MAS was influential in its assumption of executive incumbency with a view to maximize the power of a central state. While there continues to be a strong impulse in the debate on regional autonomies and further decentralization, the MAS strategy to constitutionally cover the creation of 'regions' has been considered as its attempt to dilute the departmental powers and strength through a 'divide and rule' strategy (Eaton, 2009). The MAS orientation for greater equality and socio-economic inclusion also faces inhibitive pressures from the enhanced regional autonomy, as it seeks to gain a greater central share of the hydrocarbon revenues from Tarija for redistributive transfers, while also instituting a land reform in the Santa Cruz department.

In terms of the political capacity and the 'collective action' ability across the Bolivian national space, the MAS is perhaps the strongest political force in the Bolivian political space by virtue of its strong and stable electoral support base as well as its coalitions with various indigenous social movements that span all departments. It is also important to note that in terms of putting forth a united front against the interest articulation of the ML departments, the highland departments have limitations especially in terms of resisting co-optation attempts by the ML or to reject credible incentive commitments by the ML. Amongst the highland departments, Oruro and Potosi have less unambiguous stance on their support or opposition of

the regional autonomy demands. This is partly also because of the probability of losing out if the outcome of the decentralization process is redistributive fiscal regime from the centre as per the constitutionally defined requisites of revenue distribution scales. Perhaps the most important departmental player in this context is the department of Cochabamba, which is in geographically between the highlands and the ML. While its stance has moved from a prior opposing one to one that concedes to the demands of regional autonomy, its influence and political stature is not significant enough to act as a mediator in this contestation.

The aforementioned highlights the divergent interests of the nine new bargaining entities given their distinct objective functions, and the fact that they do not have the unilateral position of proposing and would generally operate on a response function to what the central initiative stipulates. The only instance of the departmental unison in interest articulation was in 2005 at the time when the HL was being deliberated as it was in the collective interest of all subnational entities. While this division does exist at the inter- departmental level, these are not manifested in the municipal levels. The incumbent executive in particular, with the political backing of MAS and its allies, considers the municipalities as an avenue to coopt in their interests. Decentralizing fiscal resources directly to the municipalities could potentially undermine the departmental contestation for autonomy, following on with the political tactics detailed in Dickovick (2006). The reason is that the municipalities consider the departmental autonomy as an infringement on their scope of authority as they have existed (the degree of effectiveness not withholding) even prior to the LPP. While the municipalities never had as much autonomy and discretion prior and after the LPP and thus the attribution of ‘agency’ status is not appropriate, they are in possession of the ‘first mover’ advantage in the realm of subnational governance in Bolivia. The only avenue where the interests of the municipalities and the departmental governments coincide is the automatic revenue sharing mechanisms stipulated in the new constitution, whereby any change in the national or departmental taxation would have a direct effect on their revenue flows.

3.5 CONSOLIDATING DECENTRALIZATION AND DEVELOPMENTALISM IN BOLIVIA

With the political decentralization already completed in structural terms in 1994, and further consolidated in terms of substantive aspects in the period following 2006 with the HL and the departmental elections, as well as constitutionally guaranteed status of municipalities and departments coming under the 2009 Constitution, the current decentralization agenda is

dominated by the fiscal dimensions. In line with what this research set out to illustrate, the Bolivian decentralization reform saw its basic impulse in 1994 as well as post 2006 in subnational domination in framing the narrative and the sequential aspects of the reform evolution endorse the PFA sequence argument as well.

The functional or administrative decentralization accompanied every round of decentralization reform in Bolivia, the first round was dominated by political decentralization (in a structural sense) with an unprecedented administrative decentralization to the subnational governments. Despite being a centrally stipulated reform, the LPP did articulate the centre's preferential sequencing in administrative/functional decentralization but the main trigger for the LPP remained the increased interest articulation of the populace at the grassroots, hence the political decentralization became the primary output of the LPP. The second round, in effect from 2006 onwards has focused on expanding and consolidating the subnational political space while moving on to forge a new fiscal pact with the subnational governments to ensure their capacity to deliver on the functions previously assigned. The impulse for enhancing the political consolidation in the MAS government can be linked to the subnational roots of the MAS, as it gained much of its political stature in the subnational political space before emerging on the national horizons.

This section shall engage with this centrality of fiscal reforms to consolidate decentralization as well as the inclusive development goals of the MAS government, and analyze the dominant articulations and contestations within the purview of fiscal decentralization reform. Implicit, yet central to this analysis is the use of these intergovernmental fiscal arrangements to enact a stable and sustainable socio-political order that positively reinforces the developmental framework as well. This section shall first analyze the National Development Plan with the aim of contextualizing the developmental policy framework in effect, and subsequently analyze the main issues in the current decentralization phase to build a cohesive state structure that delivers on the visions of the NDP.

i. The Bolivian National Development Plan (2007)

The PND Plan Nacional de Desarrollo: Bolivia Digna, Soberana, Productiva y Democrática para Vivir Bien, Lineamientos Estratégicos (National Development Plan: Dignified, Sovereign, Productive, and Democratic Bolivia to Live Well, Strategic

Directions) introduced in 2006 and formally instituted under a Presidential decree in 2007, details the political and economic agenda of the incumbent Morales government. This plan was initially promulgated for the period 2006-2011 as a medium term plan, subject to revisions every five years, conditional upon the retention of political consensus and incumbency⁴¹. As a stipulation of the strategic vision for Bolivia, the main objective of this plan and those stemming from it, remains transcending the entrenched political economic model based on primary exports and socio-political exclusion of a majority of the populace. The main focus areas of the NDP span across four main realms; Dignity, Sovereignty, Productivity, and Democracy.

ii. The Fiscal and Institutional Imperatives for Consolidated Decentralization

As mentioned earlier, the sustainability and the degree of developmental success under the NDP and the new constitutional framework is critically dependent on how the intergovernmental institutions and resource distribution mechanisms are established. Especially in the aftermath of the new constitutional framework that stipulates a greater subnational political and administrative role, the importance of the fiscal decentralization is extremely high. Thus, for any mutually reinforcing ‘decentralization-developmentalism’ connection to take roots in Bolivia, an institutional and fiscal agreement between the centre and the subnational governments is imperative in terms of how revenues from strategic sectors and central transfers need to be framed, roles and responsibilities for each level of government, local taxation, and the institution of non-inhibitive ‘hard budget constraints’ on subnational governments for overall fiscal responsibility and macroeconomic stability.

iii. The Primacy of Resource Rents

As mentioned in the preceding sections, the agreements that culminated into the promulgation of the National Hydrocarbons Law in 2006 represented a preamble to the ‘new social contract’ primarily in terms of broader sharing of the national resource pool in a broad-based and inclusive manner. The subsequent nationalization of the hydrocarbon industry, as well as the production tax imposed in the HL, constitutes the largest sectoral contribution to the national fiscal pool especially upto 2014 with high commodity prices (IMF, 2008). The HL finds its roots in the articulation of virtually all socio-political groups in the Bolivian polity,

⁴¹ <http://www.planificacion.gob.bo/pdes/>

including the marginalized indigenous majority as well as the resource rich regions in the Media Luna. In comparison to other aspects of the decentralization reforms in Bolivia, this law created opportunities for bargaining in a new resource pie at no detriment to the existing resource pools of the actors in the political and socio-economic space, and all stakeholders gained from it (including the central government).

Being a product of a predominantly subnational articulation process, this law also came about as a victory for the regional interests which provided a further impetus for the 'regional autonomy' movement in the subsequent years which still continues. The complex bargaining and contestation around the revenue sharing of the hydrocarbon rents has been discussed in some detail in the preceding section but one main impetus to the increased subnational contestation of the resource rents was the central government led reduction in the divisible surplus by 30% in order to create the fiscal space for instituting the *Renta Dignidad* project (INE, 2010). This was the first change made to the HL by the centre which significantly reduced the fiscal base of the subnational governments (primarily the departments), however there were other modifications of the same effect to the HL in the years following 2006 (IMF, 2008 & 2012). The shares of fiscal distribution have changed over the course of the law's implementation and with the NDP in the background, and since 2008 onwards the share of municipalities in the hydrocarbon transfers has been higher than that of the departments, even after taking the additional 30% by the centre into account. This preferential status of the municipalities over the departments has been explained in Section IV, as they present a more potent prospect of political support for the MAS to switch the bargaining more in the favor of the central government.

While the incidence of such political expediencies does fall in the realm of rationality in terms of the interest articulation and bargaining strategies of the actors, the incentives of each participating actor in the process are also shaped by the nature of the resource itself. The revenues coming from hydrocarbon sources have a certain degree of uncertainty given their linkage to global commodity markets and the vulnerability to price fluctuations amid changing international macroeconomic dynamics. As a result of this volatility and the discretionary adjustments by the central government, in 2008, the central transfers to departments amounted to US\$ 78 million against the budgeted US\$ 263 million and for the municipalities US\$ 267

million against a budgeted US\$ 160 million⁴². Given such circumstance, it is probable that such changes shall lead to a more short-term bargaining horizon by the relevant actors and inhibit any credible medium-long term inter-temporal transfer commitments.

The previous bargaining was targeted at getting increased shares from an increasing resource pool, and thus it is probable that any future impulses for austerity budgeting in the wake of declining hydrocarbon revenues will have political implications for the centre vis-à-vis the subnational governments. This equation is further complicated by the fact that preferential allocations to the municipalities by the centre have already created consistent interests with the centre and any recessionary changes shall have a depletive effect on the municipal level political consolidation of the centre. Given this context, since 2010 new avenues for negotiation have been brought to the fore that aim at a percentage based transfer in addition to the budgeted amounts annually. While this is still an ongoing process to the extent that this research has discovered, the objective is to ensure that the new formula would be equity-enhancing and compensate for any subnational expenditure gaps after they have been rationalized according to the context, and awarded on per capita basis similar to the transfer formulas existing for centre-municipal transfers.

For the new formula to be more conducive to the departments, the centre has offered some concessions in terms of the departmental expenditure discretions. In 2006, in the aftermath of the HL promulgation, the departments only had expenditure discretion over 8% of the received transfers, and the gradual reduction in the earmarked transfers from the centre have led to the departmental expenditure discretions to around 19% of the total transfer receipts by 2010. A simultaneous concern for the centre is the articulation of the resource rich departments to retain a greater share of the revenues produced in their jurisdiction, which is a politically and economically warranted claim, but acceding to these articulations may have implications for the inter-regional equity especially the downside risks for the non-resource rich departments. The concessions offered by the centre in this regard have been significantly mismatched on grounds of equity. As of 2010, the transfers from the hydrocarbon resource pool allocated on the basis of per capita have been US\$ 45 per capita to Potosi department (with a poverty rate of 79.7%), as compared to the Pando department's receipt of US\$ 466 per

⁴² Comparing the initial allocation for 2008 based on Decree no 28421 (1.848 million Bolivianos) with the 2008 allocation (554 million Bolivianos) underlying the Decree no. 29322 as well as taking into account the reduction for Renta Dignidad. Data: FIAM (2008)

capita despite having a lower (yet sizeable) poverty rate of 72.4%. Table 7 below illustrates the departmental revenues as of 2010:

| Table 7: Departmental Revenue in US\$/capita (2010) | | | | | |
|--|---------------------|------------------------------|------------------|------------------------|--------------|
| <i>Department</i> | <i>Poverty Rate</i> | <i>Hydrocarbon Transfers</i> | <i>Royalties</i> | <i>Revenue Sharing</i> | <i>Total</i> |
| Potosi | 79.7% | 45 | 64.9 | 56.6 | 66.5 |
| Beni | 76.0% | 81.6 | 38.8 | 55.8 | 176.2 |
| Pando | 72.4% | 466 | 113.4 | 78.3 | 57.6 |
| Chuquisaca | 70.1% | 61.9 | 27.7 | 53.6 | 43.2 |
| Oruro | 67.8% | 79.1 | 30.2 | 57.9 | 67.1 |
| La Paz | 66.2% | 23.4 | 2.5 | 50.8 | 6.7 |
| Cochabamba | 55.0% | 27.8 | 19.2 | 49.1 | 6.1 |
| Tarija | 50.8% | 95.2 | 366.4 | 51.6 | 13.3 |
| Santa Cruz | 38.0% | 23.1 | 17.6 | 46.2 | 6.8 |

Source: IMF Government Finance Statistics 2011 | Poverty rates based on 2004 estimation of Bolivian Ministry of Statistics | Transfers also include municipalities as exclusive departmental allocations could not be found.

Another feature on the ongoing bargaining has been to redefine the divisible pool by considering the aggregate fiscal receipts of the central government and then allocate them to the subnational governments. The positive aspects of such a redefinition would be that the departmental contestations based exclusively on hydrocarbons would be mitigated as well as increasing the probability of departmental acceptance of the transfers, given that they would now be smoother as compared to an exclusive reliance on the volatile hydrocarbon revenues. Nevertheless, it still remains a function to the departmental ability and willingness to consider the consequences of such an adjustment on a relatively longer time horizon, but if this model of transfers is accepted than not only does it enable them to develop inter-temporal policy outlooks and also credibly commit to them because of reduced uncertainty arising out of consensual agreement.

iv. Defining Roles and Functional Obligations

In addition to the contestations on the magnitude of fiscal shares from the hydrocarbon pool, the initial articulation for autonomy put forth by the Santa Cruz department argued for complete functional decentralization of all public service responsibilities (barring those with proven scale effects of central provision e.g. national defence). While this was an ambitious claim to make in the first place, the idea behind it was that with greater functional responsibilities the departmental bargaining power over fiscal resources shall be higher given the ‘finance to follow function’ maxim of optimal fiscal decentralization. This claim was considerably rescinded but there is still a persistence in the departmental demands for greater functional responsibilities than currently assigned. Its implications for the consolidation of the decentralization and developmental framework are not those of conflict (as in the case of hydrocarbon transfers), but the effects are instead on the vertical division of authority across the governmental levels.

In the current framework, the expenditure responsibilities are disjoint and fragmented across the various governmental levels. While such forms of functional decentralization allow for greater responsiveness and autonomy of the different governmental levels, it significantly weakens the accountability requisites which has adverse governance outcomes. This obscurity of roles and responsibilities is further complicated by the hybrid nature of the departments themselves (as elaborated earlier in Section IV) – they are accountable to the elected Prefecto but also depend on the central government ministries as they prescribe the operational and strategic modalities.

Taking note of this, in 2008, a regulation was issued in conjunction with the HL, the enforcement of which has been inadequate, that earmarked the absorption of resources for sector-specific investments, and also redefine the responsibilities of each level of the government mandated with their delivery(UNRISD, 2013). The 2009 Constitution further increased the obscurity surrounding the distinct role and responsibilities of the governments by defining four forms of responsibilities; a) concurrent, b) shared, c) delegated, and d) exclusive. Which sectoral responsibility needs to be categorized as what according to these forms has led to a ‘passing the buck’ behavior amongst the governmental tiers. The new constitution’s provisions allowing the establishment of ‘regions’ and ‘autonomies’ further complicates the responsibility debate as new jurisdictions have been added without explicit specifications of

their mandates. It must be noted that the allocation of responsibilities is not purely a 'legal' concern but instead is an issue of negotiation of control over the inputs required for service delivery, and since the discretion over the production factors is not always negotiable, there is a tendency to 'coordinate' the service delivery rather than engaging in the delineation (Bolton & Farrell, 1991).

The resolution of this assignment problem is well-suited for central government's action which can adopt a 'result-based' management approach as seen in the case of Brazil and Argentina (Ahmad, Brosio, & Shah, 2011). In the context of Bolivia, this result orientation can be linked to the central developmental framework's social inclusion objectives, whereby a central concession to the departmental demands of functional expansion is publicly and institutionally established, thus marking departmental exclusivity in the responsibility of providing that particular service. Such an arrangement not only grants the departments the expanded discretion over the assigned functions, but also leads to a dual accountability; to the centre and to its local constituents. The evaluation of the service delivery quality can be tracked using service quality indicators, administered either as social audits or specialized audits by the centrally deputed agency. A probable consequence of such an arrangement could be asymmetry, as the central government will have to negotiate the functional expansions with each department but the positive consequence would be a greater clarity in the precise responsibilities.

Such a strategy needs to be incremental in its institution and could thus increase the probability of moving away from the 'coordinated' delivery mechanisms to clearly divided responsibilities. Furthermore, the political pressures due to the bi-directional vertical accountability of the departments could also enable shifting the costs of production factors as well as service provision exclusively to the level of government assigned with it. However, transfer of cost responsibility must be made in the context of hard budget constraints upon the subnational governments to retain pressures for greater efficiency while also mitigating the chances of the costs being shifted back to the central government. Albeit a slightly longer term strategy, the imposition of the budget constraints must be accompanied by pluralized revenue mix at the subnational level as well, which is discussed in the following part.

v. **Diversifying Subnational Revenue Mix**

Amongst the articulations by the ML regions for greater autonomy, there have been claims under the broader notion of autonomy for either withholding locally collected national taxes or the regional discretion over their administration. The objective, with the arduous nature of actually implementing this claim in practice, remained diversifying the local fiscal pool and reducing dependence on central transfers - a critical concern across all decentralized systems. If conceded to, such an arrangement where a richer subnational government retains a larger share of the locally generated fiscal revenue, would have inhibitive effects on the redistributive capacity of the central government thereby exacerbating the inter-regional inequalities as well. However, it also needs to be mentioned that this claim by ML (with Santa Cruz as the main protagonist) made an allowance for inter-departmental redistribution, whereby from the 2/3rd of the locally generated central tax retained by the department, 10% would be set aside for inter-regional redistribution. Another form of inequality can also come as a consequence of this claim being accepted, and that has to do with the inability or capacity constraints of other departments to establish 'buoyant' tax bases within their jurisdiction. A related aspect is also the departmental willingness to bear the 'political cost' of taxation, and a natural equilibrium exists with the central government bearing this cost (Sobel & S., 1998 Vol. 96, No. 1/2).

In addition to the complexities outlined above, there are also some technical dimensions that make this process particularly tough in the Bolivian context. Despite the fact that the fiscal position of Bolivia since 2006 has been remarkably solid (see Fig. 2), the macroeconomic environment remains vulnerable to external shocks because of significant dependence on hydrocarbons, which makes it especially hard to identify which tax sources can be decentralized to regional governments without exacerbating the central government's (and thus national) fiscal vulnerability. This is of an even greater concern in the Bolivian context, where the tax regime has a narrow base of potentially buoyant tax avenues like individual taxation. Given the populist roots of the incumbent government coupled with substantial fiscal base provided by the hydrocarbon revenues, there has been little impulse to broaden the tax base or alter the tax rates which in the case of personal income taxes have remained at 13% for the period 2007-2014 (IMF, 2014). Any change in the taxation revenues would also have a direct bearing on the municipalities as their revenue pools are predominantly linked to the central transfers. As mentioned earlier, the revenue sharing mechanisms emanating from the HL as well as the 2009

constitution, retain and reinforce the municipal privileges from the earlier LPP. Another layer of complexity was added to the equation with the subsequent entry of the departments in the state organizational structure with no distinctly mandated tax bases, the municipalities were granted new tax bases that would have been more suitable if administered by the departments because of the scale effect, e.g. automobile taxes, property taxes or infrastructure usage fees.

Given the divergent incentives in the subnational political space of Bolivia, the only prospect of subnational taxation would be tax-sharing whereby the departments can exploit the tax bases in conjunction with the national government or the municipalities e.g. municipalities collect the recurrent property ownership taxes but any taxation on the sale or change of property ownership goes to the departmental pool. The possible downsides of such an arrangement is that the municipalities and the departments may end up over-consuming the common resource pool or in a bid to expand their respective or collective share, impose tax rates higher than the efficient level (in the light of the Laffer Curve effects mentioned in Chapter 2), or even more so, leave everything unchanged and expect the gaps to be subsidized by the centre which in turn would have to raise additional taxation and thus bear its political cost. Given this milieu of contrasting incentives and the possible permutations of subnational fiscal diversification options discussed here, this research is constrained in providing or suggesting an optimal way forward. Nevertheless, the issue remains central to the consolidation of decentralization in Bolivia as a whole as well as an inclusive developmental policy framework.

vi. Establishing an Institutional Framework for Fiscal Prudence

In the broader debate on decentralization, one issue that recurrently appears a potential risk of decentralization is fiscal imprudence by the subnational governments which complicates the overall macroeconomic stability of the country. Bolstering fiscal responsibility is an issue of high importance for Bolivia, especially as it confronts a downward trend in commodity prices, that were the main source of state revenue and the finance devolution to the subservient tiers. In the case of Bolivia, despite its recent resilience on the macroeconomic front, growing articulations for greater regional autonomy from the departments as well as a broader developmental framework that aims for a broad-based socio-economic transformation, have exposed the country not only to the substantive nature of the task at hand but also the scale of resources required to make it happen. While most of the

dynamics and options available for consolidating the political and administrative decentralization through fiscal decentralization whilst reinforcing the central developmental outlook have been discussed in the preceding sections the focus here shall be upon the institutional mechanisms in place to avoid subnational fiscal imprudence.

Under the new constitution, with the state organization spelled out, corresponding institutional arrangements have also been established to govern subnational fiscal affairs including their solicitations. The main features are as follows:

- Long Term Debts can be acquired by the subnational governments through the national treasury system, Sistema de Tesoreria del Estado. External debt finance has a sovereign guarantee provided by the central government. However, a congressional/legislative assent is a pre-requisite before an external debt can be acquired by the central or the subnational government.
- Short-term domestic debt can be raised laterally across the municipalities/prefectos so long as it is sanctioned by the National Ministry of Finance.
- Debt regulation for all subnational governments (municipal and departmental) for all sources of debt is the 20/200 rule, i.e. the maximum limit of debt servicing is 20% of their current revenue, with the total debt stock value not exceeding 200% of the current revenue.
- Municipalities and Departments can access funds through the Fondo Nacional de Desarrollo Regional (FNDR)/ National Fund for Regional Development, for investment purposes only and not to meet current expenditure gaps.

Given this institutional and legal stipulations, an element of concern in the current articulation of regional autonomy is that the rationalization of subnational limits to acquiring debt financing has not featured in the narrative. The reason why this is an issue of concern is the probability of the departments reneging on their debt commitments if they are granted autonomy, leaving the central government to deliver on the debt settlements. Up until 2010, most departmental governments have exhibited the appropriation of a high share of their revenue pools to debt-servicing and in some cases the debt stock is considerably high. Table 5 presents a composite view of the debt portfolio holdings by the departmental governments exclusively:

Table 8: Departmental Debt Portfolio Estimates (2010-11)

| Department | (US\$ millions) | 2010 | 2010 | Debt Ratio | Debt Ratio |
|------------|-----------------|-------|--------|---------------|---------------|
| La Paz | 31.34 | 13.14 | 58.09 | 42% | 185% |
| Oruro | 19.3 | 6.5 | 29.43 | 34% | 152% |
| Potosi | 18.86 | 5.03 | 54.73 | 27% | 290% |
| Cochabamba | 43.45 | 5.12 | 63 | 12% | 145% |
| Chuquisaca | 20.66 | 4.21 | 43.83 | 20% | 212% |
| Tarija | 107.94 | 7.63 | 86.25 | 7% | 80% |
| Santa Cruz | 69.4 | 12.6 | 103.62 | 18% | 149% |
| Beni | 30.38 | 7.12 | 53.12 | 23% | 175% |
| Pando | 21.93 | 3.54 | 14.11 | 16% | 64% |

Source: IMF Government Finance Statistics 2011

From Table 5, it can be seen that the debt-stock and the debt-servicing ratios are mostly on the higher side, with Potosi and Chuquisaca being the clear outliers in terms of debts-to-stock/revenue ratio. In terms of debt servicing/revenue ratios, La Paz (paradoxically also the administrative capital), Oruro, Potosi and Beni are in contravention of the established rule. While this partly signals the inadequacy of credible enforcement by the central government, an explanation for such high ratios can also be the presence of long term debts acquired prior to the rule imposition. In this case, this presents another legal challenge as the status of the prefectures had been ambiguous once they were established in 2005/6; as their legal status was that of deconcentrated central government institutions. This implies that their debt obligations automatically fall into the central government's realm of responsibility, despite the fact that the management and absorption of the debt was under a high degree of departmental discretion.

The way forward in this case, in addition to a credible enforcement of the established rules by the central government e.g. linking subsequent transfers to the department's ability to manage its debt portfolio within the prescribed limits, could be a gradual phase-out of the debt obligations through the unspent transfer balances held by the departments. Given the short term horizons against the backdrop of volatile resource flows (as explained earlier), the phase outs should not be done on multi-year basis, but instead a short term cutoff needs to be

stipulated by the centre within which the surplus balances from HL transfers as well as other revenue transfer contributions be devoted to debt servicing.

3.6 CONCLUSION

The decentralization reforms in Bolivia in their second phase have assumed the form of a bargaining game, the complexity of which was significantly bolstered by the new bargaining entries at the departmental level. In the current round of decentralization reforms, a polarity of interests has been observed between the ML regions and the highlands. While none of these groups have the capacity or the consensus to operate and bargain in unison with the central government, their disaggregated and divergent interests lead to a complex political context against which the overall decentralization needs to be consolidated in a manner that reinforces the developmental policy framework put into effect by MAS government. At an aggregate level, the Bolivian polity has registered notable improvements across democratic, economic and management realms. It is by no means an adverse scenario to have a high degree of subnational interest articulation and bargaining, and it is actually a merit of the decentralization reform experience of Bolivia that the reform took a subnational domination route where the responsiveness of public governance and service delivery has undoubtedly improved. Yet, the manner in which all competing contestations and subnational bargaining is managed shall not only dictate the efficacy of the reform process but also the extent to which Bolivia as a polity can break away from its historical roots of socio-economic underdevelopment.

In terms of reform consolidation, the interest articulation and bargaining strategies of the central government under Morales are also noteworthy. With its posturing depicting the departmental autonomy as a centripetal force to its objectives (mainly in the ML), the central government has instituted cooptation mechanisms for the municipal level governments to dilute the rigor of the departmental interests. The consequence of this can be that this bargaining may eliminate some inefficiency, both allocative and productive; it might end up reinforcing some of the same. The actors in the subnational and the national political space are playing 'nested games' (Tsebelis, 1990) in terms of resource pool division, diversification of local fiscal pool through taxation and indigenous revenue mobilization, expenditure and functional assignments, and the subnational debts. The probable culmination of which shall be an intergovernmental framework with efficiency constraints. This remains the main challenge

before the objectives of reform consolidation as well as socio-economic transformation that Bolivia envisages under the ongoing NDP.

The case of Bolivia also presents a good exhibit of the partial decentralization debate; whereby the early winners of decentralization are the most likely sources of resistance for any subsequent attempts. Since it is an ongoing process, the prediction of outcomes would be inaccurate at best. This research sought to illustrate the sequential dimensions emerging under a subnational domination path, and in the course of examining the Bolivian case it also put forth a contribution to the existing literature on decentralization in terms of the institutional dilemmas that could emerge as a consequence of the reform consolidation.

CHAPTER 4

FEDERALISM & DECENTRALIZATION IN PAKISTAN: IMPLICATIONS FOR DEMOCRACY AND DEVELOPMENT

4.1 CONTEXTUAL OVERVIEW

The virtues of federalism and subnational empowerment have surfaced recurrently in political as well as economic theories from the times of Madison & Hamilton to Musgrave (1961) to Oates (2006) and Weingast (2009). The common denominator remains that in ethnically and socially heterogeneous contexts, state policy is most conducive to the preferences of its constituents when a multi-tiered governance structure exists, with each level having a distinct mandate. Higher levels of government (at the central level) are more suited for the provision of nationwide public goods (such as defence) to retain the benefits of homogeneity in standards, non-excludability and scale effects, while the lower levels of the government (regional/provincial or local/municipal) are better suited in the provision of locally responsive public goods (waste management, local infrastructure, water and sanitation, amongst others). Distinct mandates, clearly defined functions, and adherence to the stipulated parameters by each tier of the government also enable a greater degree of targeted accountability by the citizen. As compared to a high concentration of power in a potentially exploitative centre, federalism enables diluted power among multiple tiers of government, which may also be mutually competitive horizontally and dependent vertically. From a purely political standpoint, such a dilution in the concentration of power illustrates a path to peace, order and stability especially in contexts marred by deep socio-political cleavages. From a purely economic point of view, the decentralized federal systems enable a higher responsiveness of the government to constituents rooted in greater preference revelation and access to information, as well as the benefits arising as a consequence of intergovernmental competition.

Federalism transcends mere administrative rearrangements, and involves substantive political rearrangement that results in limiting central autonomy in policy design, implementation and enforcement. Building upon the Hamiltonian paradox, while limited central autonomy augurs well for subnational empowerment and federalism, it also results in limiting the strategic control of the centre. This could be a detrimental feature, as decentralized entities may face higher costs of coordination as well as provision owing to scale constraints.

Furthermore, when the reform is not responsively structured and the relevant interests in the decentralized scheme are averse to renegotiation on a circumstantial basis, decentralization under federalism may instead result in hampering efficiency, accountability and exacerbating instability of the federation itself. This may be a consequence of greater incentives by individual subnational governance structures to expand their expenditures beyond their contribution and externalize the costs to the others or the superior governmental level(s), resulting in an overgrazing of the common fiscal resources which could have significant macroeconomic implications.

With this in context, this case study examines the experience of federalism in Pakistan, which has been characterized by ‘potholes, detours and prospects’ alike (Shah, 2010). The Hamiltonian paradox discussed earlier has also been a recurrent observation in Pakistan, given a consistent divergence of the de-facto and de-jure in governance – run predominantly as a unitary state despite being formally a federal state. The 18th Constitutional Amendment in 2009/10 has been a key development in substantive decentralization and federalism in Pakistan, diluting the influence of a traditionally powerful centre in the favor of the provincial or subnational governments.

Considering the second main trajectory of the sequential theory of decentralization – national dominance path, the case of Pakistan holds great resonance. There have been multiple substantive attempts at decentralization in Pakistan since its independence in 1947, primarily through the different administrative structures of the government; national to provincial, national to local, and provincial to local. While all these three manifestations differ with each other, the main similarity between each of them remained in the underlying motivation. The first three attempts at governance reform through decentralization had been made by a non-representative, autocratic, unelected centre whereas the current reform process (instituted in 2009/10 and still in a consolidation phase) is the first one to be instituted under elected governments. The paradox, as stated earlier, surrounding the decentralization in Pakistan is that the three military regimes directly in government for 34 years, have actively pursued decentralization and devolution of power, whereas all elected governments have deliberately subdued subnational politics and governance. This paradoxical situation between authoritarian and democratic politics in Pakistan, presents an interesting avenue for research not only in terms of decentralization and local governance but also in terms of the bargaining

strategies employed by the ruling elite⁴³, and more broadly on the strength of the federation itself. The decentralization reforms whenever pursued have always followed a national dominance path, where the protagonists of the reform have used it as a tool for further centralization of powers in the non-representative centre (Cheema, Khwaja and Qadir, 2005).

4.2 EVOLUTION OF THE STATE STRUCTURE IN PAKISTAN

The state of Pakistan was envisaged as a federal state at the time of its inception. This was partly attributable to the fact that prior to independence, the founding party continued to articulate demands for increased provincial autonomy under the British rule. In addition, the modalities employed under the Partition Plan (1946) required that the Muslim majority provinces and the Muslim members of provincial legislatures were to choose whether to remain within the Indian federation after decolonization or come together to form a federation of Pakistan. The need for federal system was also an imperative, given that the nation was essentially created on an ideological basis and not ethnic, linguistic or social basis. While being a strong point of articulation, it was important for the state to focus on addressing the heterogeneity of ethnicities, customs, language and social norms, to assure the stability of the newly created polity. Following its independence, the Government of India Act 1935 was adopted as the interim constitutional order with minor changes, while a Constituent Assembly was tasked with creating a new constitution. It must be noted that the Government of India Act 1935, as a colonial instrument, created a federal system but the distribution of authority and powers was skewed towards the centre which was held by the British. The Republic of India was also established at the same time as Pakistan in 1947, but its constitutional experience was on a different trajectory right at the outset – instead of provisionally invoking the Government of India Act 1935, the Indian Independence Act 1947 was instituted as a provisional constitution that took all conducive provisions from the various Indian Councils Acts (1858, 1861, 1892, 1909) and the Government of India Acts 1919 & 1935 (Waseem, 2006).

While the first constitution for India was promulgated in 1950, Pakistan saw its first constitution coming out in 1956. A main reason for this was the political instability post 1952 which saw four governments changing in a 4 year period hampering the consistency required for the constitutional process to get truly off the ground. The first Constitution was

⁴³ More details can be found in Aslam, G (2010)

promulgated in 1956, which explicitly declared Pakistan as a federal state, however the centripetal impulses of power distribution persisted (Shah, 2011). Owing to the political crises that ensued in its aftermath, this constitution was abrogated in 1958 and a martial law was imposed. This marked the beginning of the political instability that has marred the establishment of a stable political culture in Pakistan, as military governments have since ruled the country for an aggregate period of more than three decades.

The first military takeover of the government occurred in 1958 with the imposition of martial law by General Ayub Khan. Under his regime, the promulgation of the second constitution took place in 1962 which was prepared by a non-representative bureaucratic body. In the aftermath of its promulgation, a legislative assembly was established and presidential elections were held in which General Ayub Khan retained his position. Following his resignation in 1969 and an intermittent transition under another military dictator, a democratically elected government took office under Zulfikar Ali Bhutto as the Prime Minister in 1971. This period of democratic rule lasted until 1977 when it was overthrown by another military chief Gen. Zia-ul-Haq, however the most important event in this democratic phase was the promulgation and ratification of a new constitution by a representative government in 1973. The Zia regime lasted from 1977 until 1988, whereby political parties were barred from actively participating in the political space until 1986 and a legislative assembly based on non-partisan elections assumed office in 1985. Democratic rule returned to the fore after 1988 until 1999, during which time the PPP and the Pakistan Muslim League (PML) alternated in incumbency for short periods. None of these two parties were able to complete their terms in both rounds of their incumbency. A military coup in October 1999 dislodged the government of PML and the government was headed by the then military chief, General Pervez Musharraf as the Chief Executive. Upon assuming the government, the Musharraf regime held the 1973 constitution in abeyance, and in its stead, introduced the Provisional Constitutional Order as the governing framework of the state.

Holding the constitution in abeyance was not directed at the abrogation of the constitution, and hence the military regime had to receive a nod of 'legitimacy' from the Supreme Court. The Supreme Court declared the coup d'état as legitimate and necessary and gave General Musharraf a period of three years to transfer the government back under democratic civilian rule. In 2002, in line with the Supreme Court's ruling, Musharraf conducted a referendum for Presidency in which he was the sole contender which enabled him to earn an additional 5 years constitutionally mandated term as President. Soon after his

referendum, President Musharraf called for general elections to elect the national and provincial legislatures, in October 2002. Prior to the elections, the Musharraf regime also instituted a Legal Framework Order (LFO, 2001) as an addendum to the PCO that ensured that the power would lie with the Presidency, regardless of the outcome of the elections for the provincial and national legislatures. The LFO also expanded the adult suffrage by lowering the voting age to 18 years as compared to a prior 22 years, which was subsequently also ratified after the 1973 constitution was put into effect in the aftermath of the elections. In 2008, as a result of fresh elections at the national and provincial levels, the government was assumed again by the civilian democratic parties, with the PPP emerging as the victor and Musharraf still retained the presidency until August 2008, when he resigned owing to the threats of impeachment. The PPP government that assumed office in 2008 was the first ever civilian government to complete its constitutionally mandated tenure of 5 years in 2013 in the country's 66 year history.

The administrative structure of Pakistan is composed of four provinces, two autonomous and disputed territories, one federal capital territory, and a group of Federally Administered Tribal Areas (FATA). Details of these are as follows:

Table : Administrative Structure of Pakistan

| Administrative Unit | Status | Population | % of Total Population |
|----------------------------|------------------------|-------------------|------------------------------|
| Azad Jammu & Kashmir | Autonomous/Disputed | 2,972,501 | 2% |
| Balochistan | Federating Unit | 13,162,222 | 7% |
| FATA | Federally Administered | 3,930,419 | 2% |
| Gilgit Baltistan | Autonomous | 1,441,523 | 1% |
| Islamabad | Capital Territory | 1,151,868 | 1% |
| Khyber Pakhtunkhwa | Federating Unit | 26,896,829 | 14% |
| Punjab | Federating Unit | 91,379,615 | 47% |
| Sindh | Federating Unit | 55,245,497 | 28% |

Source: Compiled using data from Federal Bureau of Statistics, Pakistan

4.3 PARADOX OF SUBNATIONAL DEMOCRACY IN PAKISTAN

While the evolution of federalism from the constitutional/legal point of view has been briefly reviewed, it is also important to observe any structural reforms in governance that enhanced subnational influence/participation. Interestingly, the political history of Pakistan

shows a “paradoxically countercyclical pattern for subnational (especially, local) democracy” (Cheema, Khan, & Myerson, 2013). Thrice in the history of Pakistan, electoral democracy has been introduced at the local (Municipal) levels (1962, 1985, and 2001), which have either been rolled back or “replaced with unelected administrators” (Cheema, Khan, & Myerson, 2013) once the civilian governments return. The most recent establishment of democratic local governments under the LGO 2001 during the Musharraf regime were, and predictably so, rolled back by the revived civilian democratic government at the central and provincial levels. At the time of its promulgation, the local governments established under the LGO were granted a seven year protection to let the system gain some root, at the culmination of which the provincial governments were to decide upon their future (UNDP, 2010). As a result, a complete civilian tenure in government (2008-2013) elapsed without the establishment of local democratic governments, and was instead characterized by a re-bureaucratization at the local levels.

With this in context, we need to examine why decentralized political governance at the local levels has been a cause championed by the military regimes and less so by the civilian governments in Pakistan. A popular assertion, which this research also concedes to in the context of Pakistan, is that the elected local governments are established to dilute the political strength of the established political parties and to lend greater legitimacy and a consolidated alternative political base to the incumbent military regime (Cheema et al. 2006). Elected local governments could offer a non-representative central government a vital political connection to the constituencies throughout the nation, whereby the local incumbents have a direct articulation channel with the centre which in its own interests of consolidation has an incentive to be of a greater responsiveness [Cheema et. al. (2006), Myerson (2009)]. An illustration of this can be found in the 2001 reforms, where the non-representative centre confronted a strong entrenchment of party politics in the broader political space, especially at the central and provincial levels. The incentives of the centre were thus truly reflected in the award of progressively greater authority to local governments vis-à-vis the provincial governments.

The devolution of authority under the LGO took the form of greater devolution from the provinces to the local governments, with the central scope of authority very negligibly changed. Across all of the local governance reforms thus far in the history of Pakistan, a common feature has been the non-partisanship of the local elections. This remained the case with the 2001 LGO as well, and though the partisan interests exhibit a considerable degree of

resilience in their presence (even though covert), the degree of leverage they had over the centre or the local governments themselves is considerably reduced as compared to partisan local governments. The rules against the partisan local elections are also an influential bargaining and incentive-maximization strategy for the non-representative centre, as it can go for a selective enforcement of the rules. This feature of the local governance structures established under the military regimes offers some explanation of the civilian democratic governments' aversion to allow the local governance structures to exist. Rather intuitive, the mainstream political parties in Pakistan (PML and PPP) saw the local governments established under the LGO 2001 as representative of the 'dictatorial' interests and according to their perceptions, the local governments represented a class of defecting politicians that were detrimental to their political interests.

In democratizing contexts (apt in the case of Pakistan, but also selectively applicable in other contexts) the rational incentives of the established political interests incumbent at the provincial and central level of governments may be skewed against the establishment of democratic local governments, as they are seen as a competition for power and patronage (Cheema, 2006). Illustrative of this assertion, is the conduct of the elected representatives of the political parties at the central and provincial legislatures in Pakistan, who have committed to the reform local democratic governments and even passed legislations in this regard but the implementation continues to be deferred on different pretexts.

Some political parties, like the MQM (Muttahida Quomi Movement / National Allied Movement) who have a regionally and ethnically concentrated political base in the urban regions of the Sindh province (of vital economic significance to Pakistan), to persist with their demands for local governments as it would enable a stronger bargaining position for them to seek 'political rents' in the form of ministerial incumbencies at the central level. The temporal pattern of MQM's articulation substantiates the assertion of 'political rent-seeking behavior' as it always brings up the Local Government debate (often through street agitations and even violent actions) whenever politically expedient or whenever their narrow political interests were being challenged by the Provincial Government led by the PPP (with a predominantly rural political base, but with desires of gaining greater political and fiscal influence in the urban areas).

Given these factors, the aversion of the civilian dispensations to elected local governments to the establishment of elected local governments can be understood in addition to why it assumes more of a 'bargaining power' tool rather than its more substantive

implications of democratization, accountability and responsiveness. Much of this resistance to electoral democracy at the local levels also finds its roots in the ‘limited access’/elitist structure and organization of the established political parties in the Pakistani political space (Hussain & Hussain, 2009).

The political parties in Pakistan are, in their organization and functioning, “highly centralized and their national and provincial leadership exercises substantial control on all legislative nominations and strategic decision-making” (Cheema, Khan, & Myerson, 2013). Built mainly on the basis of elite coalitions and patron-client dynamics, the organizational structure of these political parties does not extend down to the grass-roots level, and where it does the structures act as reinforcements or executors of the agendas of the higher levels of the party. A cross-country Democratic Accountability Survey conducted under the auspices of Duke University posits that the Pakistani political parties are characterized by “high levels of organizational centralization and average levels of organizational extensiveness” (Kitschelt and Palmer, 2010; Cheema, Khan, & Myerson, 2013). The survey observations further reaffirmed the similarity of these dimensions across the 5 main political parties in the country (PPP, PML-N, JUI, JI, MQM). The barriers to entry in the federal and provincial political space, are also reinforced because of the absence of local democratic politics which is both a result of and support to, the high dynastic dominance in the political parties in particular and political space in general.

The introduction of local democratic politics and local governance based on genuine participation and democratic norms would not only help in the broader notion of democratic consolidation but also reduce the barriers of entry in the political space at the national and provincial levels. This consolidation could also deter any attempts at a non-democratic assumption of incumbency, as historically the political vacuum at the local level has been the main source for the political legitimacy of the military regimes.

4.4 LOCAL GOVERNANCE ORDINANCE 2001⁴⁴

Hailed as one of the most comprehensive local governance reforms and attempts at decentralization of governance, it is important to analyze why it failed to gain roots despite its acknowledged merits such as liberalizing political space and service delivery improvements (World Bank, 2006; Aslam, 2011). The local governance reform was initiated in August 2001

⁴⁴ This section is based on a series of discussions and interviews. Details in the Annexures.

under the Local Government Ordinance (2001), which legally had the stature of a Presidential directive under the Provisional Constitutional Order (PCO), but not safeguarded in the national constitution of 1973 that was at that time being held in abeyance. This was a fundamental weakness of the reform process right at its outset. The reforms envisaged under the LGO were more comprehensive and ambitious, however, they faced stiff opposition from the major political parties and the civil society organizations on account of the perceived detriment to federalism arising as a consequence of reduced provincial autonomy. This was also made a basis for rolling back the LGO in 2008 once the civilian democratically elected government gained incumbency, with the formally provided justification that it undermined the mandate and capacity of the provincial governments to implement its policies (UNDP, 2010).

As a federation divided into four provinces (Punjab, Sindh, Baluchistan, and Khyber Pakhtunkhwa), a Federally Administered Tribal Area (on the Afghan Border) and a capital territory (Islamabad), the establishment of the local governments was the creation of a third layer of the governance structure. This third layer was further disaggregated into three levels; districts, tehsil (municipality), and the lowest tier was Union Council. The Union Council consists of proximate villages or towns (in urban contexts) in the Tehsil. Each administrative tier at the local level had its own council and was headed by a mayor (Nazim, in local terms) and a deputy mayor (Naib-nazim). All three levels were to be governed by officials coming through a process of elections. In terms of administration, as many as 10 formerly provincial departments were transferred functionally to the district and municipality level. The new arrangement had the district mayor (Nazim) assume the status of the 'executive head of the district', with a District Coordination Officer (a member of the bureaucracy) appointed by the provincial government reporting to it (Bureau, 2001). Owing to the reporting structure, the district mayor was also made responsible for the performance management and stipulating the job modalities. Furthermore, the LGO also enabled the local councils to over-rule executive decisions, and empowered them to make independent decisions on all matters, with the exception of budget approvals. In the case of budget approvals, the local/district executive held considerable power over the local council - whereby it could establish standing committees to have an oversight over the activities of the local executive (Aslam, 2011). The local council also had the discretion to establish standing committees for monitoring of the executive's activities. The monitoring committee had an authority to suggest remedial courses

of action to the local government, including the local executive (District Mayor) (Aslam, 2011).

The functional assignment to the local government (administrative decentralization), was perhaps the main feature of the local governance systems emerging under the LGO with those existing prior to them⁴⁵. As compared to the preceding institutional framework in the subnational space, the provincial government performed a majority of the state functions, but under the LGO the elected local government and the provincial government were integrated at the district and municipality level, and the provincial administration or bureaucratic accountability division was abolished, with the locally serving bureaucracy accountable to the elected local government. While the scope of the functional responsibilities of the local governments greatly increased post the LGO Devolution, along with the discretion over the allocation of expenditures and establishment of priorities, the degree of financial decentralization was largely limited. This was because districts governments were not given any revenue generation privileges and had to depend on provincial (and by extrapolation, central transfers) through the provincial finance commission mechanism. Furthermore, most of the devolution of power under the LGO was from the provincial to the district level amidst no transfer of powers (administrative, fiscal or political) from the central government to the subnational governments (districts and provinces included).

Prior to the Local Governance Ordinance, there was no significant inter-governmental linkage (i.e. between the Central/Provincial Governments and Local Governments), the inter-governmental conflict possibilities were minimal. However, in the aftermath of the LGO, the elected local governments had an expanded set of functional responsibilities that were previously provincial responsibilities, as well as a greater degree of control over the provincial bureaucracy (Cheema, Khwaja, & Qadir, 2006). Since this devolution was instituted in the absence of any elected provincial governments as well as the non-partisan basis of local elections, no integrative efforts either structurally or mediatory were made to enhance provincial-local coordination, which had operational implications for both. In addition, the indirect election of the District Nazim created distortions in the incentive structures, especially since the district mayor under the LGO was most powerful actor in the local government system as the head of the executive as well as the legislative branch of the local government.

⁴⁵ The local governments established during the 1980s under the Zia regime were mostly suspended during the 1990s so in fact prior to the current devolution there were no elected representatives at the local level and their powers were exercised by provincial bureaucrats as local government administrators (Cheema, Khwaja, & Qadir, 2006).

Local governments in Pakistan enjoyed under the LGO enjoyed considerable discretion in the regulation of local matters, expenditure allocation for local goods, and procurement processes (Niaz (2010)). However, most of this authority was concentrated in the hands of the Nazim (Mayor). In the case of budget approval, for example, the Nazim had the authority to propose the budget liable for consideration by the Local Council. This provision significantly restricted the discretion of the local council in relation to the non-elected bureaucracy and, especially, the Nazim. The incentive compatibility mechanism implicit in this arrangement was that the re-election of the mayor would be contingent upon the satisfaction of the union councils: a factor that would allow the Union Councilors to exert a greater influence over the mayor. However, in a political landscape that is dominated by individuals who control the entry into political competition and the intermediation between the state and the citizen as mentioned in the prior section, indirect election of the head of the local government unit opens up the possibility of capture of these offices by the local elite (Hussain & Hussain, 2009).

Given the dearth of local revenue sources, most of the local fiscal pool was financed through the fiscal transfers from the provincial and central governments under the Provincial Finance Commission as discussed earlier. While the horizontal distribution of these funds across local governments was formula-based (primarily based on population), the vertical distribution that determines the retained and allocable amounts was largely at the discretion of the province. The local governments also had the platforms of central transfers delivered in ear-marked forms. A pitfall of such an arrangement is that the discretionary transfers provide “an incentive to the local government to respond to the preferences of the center in order to get access to funds, rather than to their constituency” (Yelmaz, 2010). As a result, the central governments/ political actors have a greater scope for patronage and clientilistic conduct by linking transfers to political considerations. This ends up reinforcing and perpetuating existing, sub-optimal power structures and strengthens the patronage relationships, and can become an effective channel of rent distribution.

Finally, the main structural flaw with the decentralization under the LGO was that it was developed and instituted in a context when the Constitutional framework was held in abeyance. Despite the new governance structure instituted under the LGO (2001) and its subsequent ratification by the 17th Constitutional Amendment in 2003, Pakistan continued to constitutionally be a “two-level federal state i.e. the local governments are not recognized as an established third tier of government by the 1973 Constitution” (Shah,2012). While the 17th

Amendment was initially aimed at constitutionally ratifying and sustaining the establishment of a third tier of the state at the local levels, it ended up allowing their establishment for a 7 year period. During this 7 year period, the provincial governments could make any changes to the legislations regarding Local Governments with the approval of the President (Bureau, 2001; Shah, 2012). The implicit feature of this was that at the end of the 7 year period, the provincial governments were to decide whether or not the local governance structures were to be retained, and if so, what revisions to the legislation were to be introduced. This was, in fact, the main provision employed by the subsequent civilian government to roll-back the Local Governance frameworks under the 18th Amendment.

4.4 DECENTRALIZATION AGAINST THE BACKDROP OF 18TH AMENDMENT

Two most comprehensive decentralization reform processes in the history of Pakistan, according to this research, have been the reforms of 2001 and the 18th Constitutional Amendment in 2009 that is hailed as the first major step towards making the state federal in function and not just the form, with a systematic national dominance sequence of decentralization reforms. The decentralization reforms undertaken in 2001 under the title of Local Governance Ordinance and the Devolution of Power Plan, were the first comprehensive decentralization reforms as they involved changes in the “administrative level of decision-making, the accountability of the decision-making authority (political or bureaucratic), and the nature and amounts of the available fiscal pool” (Cheema, Khawaja and Qadir, 2005). The LGO 2001 was a radical one, under an autocratic regime and instituted under the Provisional Constitution Order, and thus without a formal constitutional cover. It also involved a great deal of decentralization of provincial powers to local levels, without any decentralization of the central powers to the subnational tiers (provinces and the local tiers). As a consequence, the sustainability of these reforms was low despite yielding delivering service delivery improvements and empowerment to local governments⁴⁶.

In 2008, this arrangement was rolled back following a democratic transition as the Pakistan People’s Party assumed the government. While very important constitutional changes were passed in 2009 and 2010 in support of federalism, major reforms were also instituted in the areas of finances and administrative/ functional responsibilities of the subnational governments (i.e. provincial governments of the federating units). However, the political

⁴⁶ Aslam, G. and Yilmaz, S. (2011), Impact of decentralization reforms in Pakistan on service delivery—an empirical study. *Public Administration and Development* 31: 159–171. doi:10.1002/pad.591

decentralization in terms of reinvigorating and reinstating a sustainable grassroots governance infrastructure remained ignored. In the aftermath of these reforms, the governments of the federating units/ provinces have infact became more powerful in terms of their administrative discretion and fiscal resources. Given the disparities (territorial size, demographics, and fiscal and administrative capacities) of the provinces, a process of contestation and bargaining is also underway for a revival of further decentralization reforms that empower the third tier of the state - municipalities.

Owing to the inadequate responsiveness of public policy to the citizen demands in the aftermath of the constitutional reforms and regional empowerment, the 2013 elections (historical elections as it was the first time a transition between two elected governments took place following a completion of mandated tenure) saw the reinvigoration of the local governance as one of the popular electoral slogans (See Table 11)⁴⁷. Table x provides an overview of the major parties⁴⁸ positions at the time of the general election.

Table 9 : Major Political Parties in Pakistan

| Rank | Party | Popular Votes General Elections 2013 |
|------|---------------------------------|--------------------------------------|
| 1 | Pakistan Muslim League (PML-N) | 14,844,104 |
| 2 | Pakistan Tehreek-e-Insaaf (PTI) | 7,679,954 |
| 3 | Pakistan Peoples Party (PPP) | 6,977,218 |
| 4 | Mutahidda Qaumi Movement (MQM) | 2,456,153 |
| 5 | Jamiat Ulama-e-Islam | 1,461,371 |

Source: Own compilation based on ECP data (2013)

The electoral results of the 2013 General Election saw PML-N gaining a clear majority in the Centre. However, the regional/ provincial results had three different parties gaining clear majority in three out of the four federating units whereas a coalition government led by the PML-N was formed in the fourth.

⁴⁷ A comparative analysis of the election manifestoes of the major political parties in the 2013 General Elections, was conducted by Pakistan Institute for Legislative Development And Transparency (PLDAT) across issues pertaining to economy, society, political issues and foreign policy. http://www.pildat.org/publications/publication/elections/Election2013_ManifestoesComparison.pdf

⁴⁸ The status of the parties is based upon the votes they obtained during the 2013 General Election. See Table XX

Table 10: Parties forming Provincial Governments

| Province | Party in Government |
|--------------------|----------------------------|
| Balochistan | Coalition led by PML-N |
| Khyber Pakhtunkhwa | PTI |
| Punjab | PML-N |
| Sindh | PPP |

While being a historic election as it saw a democratically elected government transfer the power to another democratically elected government, the 2013 election results were also important as they resulted in three national level parties campaigning for the centre emerging as clear victors in three of the four federating units. The PPP and PML-N have been in Governments at the central and regional levels multiple times in the past, their dynastic orientation, allegations of graft and misappropriations⁴⁹, and limitations in delivering on their mandates led to the rise of the PTI, a relatively new party gaining new grounds across the national electoral space, predominantly in the urban centres. The electoral campaign thus was a contest between well-established parties with a prior record of incumbency, and a new party promising accountability and change, and with each of these three main parties forming governments in three major large provinces ushered in a form of plurality never witnessed before, while also having implications for the decentralization and developmental prospects of Pakistan.

The implications for decentralization have been significant because while all the main parties campaigned with the establishment of local governance structures as a key element of their manifesto, upon gaining incumbency the enthusiasm for enacting the promised reform was much less. As detailed in the findings of Kitschelt and Palmer (2010), the party structure for PPP, PML-N as the two main parties was highly centralized and largely patriarchal therefore there was a resistance to establishing a local governance system to ensure that their political base remains consolidated. PTI, while being relatively less centralized in terms of party organization, had similar concerns of losing the gains made at the provincial level and central levels by having the opposing parties dilute their support in their new constituencies. In accordance with the 18th Amendment, all provincial assemblies nevertheless passed the

⁴⁹ Hussain & Hussain (2009)

Local Government Acts in 2013, with the exception of Balochistan which had passed it in 2010 (UNDP, 2011).

Table 11 : Party Position on Decentralization and Local Governments 2013 General Elections

| Party | Proposed Programme in Election Manifesto | Scope |
|---|--|--------------|
| ANP ** | <ul style="list-style-type: none"> i. Local Government election to be held ii. Women representation to be ensured in the LG iii. Centre to retain control of defence, foreign affairs, currency, communications and such other subjects that the federating units agree to in the Council of Common Interests iv. Implementation of the 18th Constitutional amendment to be ensured particularly with regards to oil, gas, water and power, energy, health and education | Basic |
| JUI (F) *** | No specific reference is made to the subject in the manifesto | None |
| MQM ** | <ul style="list-style-type: none"> i. Devolved local government system will provide ways for urban-rural integration ii. The LG system will help to further devolve power, authority and resources from District Level to Town level and further down to UC and ward levels iii. Election for the LG to be held within 3 months of general election | Extensive |
| PML (N)*** | <ul style="list-style-type: none"> i. Local Government election to be held within six months of the general election ii. Under Article 140 A of the constitution, every effort will be made to secure a certain degree of uniformity in the LG system within and among the provinces iii. New laws providing for the new LG system in replacement of the LGO 2001 system are to be adopted by consensus for optimum devolution iv. Women will be given representation in the LG system | Detailed |
| PPP*** | <ul style="list-style-type: none"> i. Each province shall by law establish a LG system and devolve political, administrative and financial responsibility and authority to the elected representatives of the LG. Article 140 A of the constitution to be upheld ii. The election commission of Pakistan will oversee the LG elections | Detailed |
| PTI*** | <ul style="list-style-type: none"> i. An effective, efficient and representative LG system will be established ii. Authorities, responsibilities and resources will be devolved iii. Peoples participation in the local government will be ensured iv. A bottoms-up system will be introduced v. Each village will be governed by a Village Council vi. All governance functions in the cities and towns will go to the municipality and the city government will raise independent revenue for city development | Extensive |
| ** Predominantly Regional Party *** Predominantly National Party | | |
| Source: Own Compilation based on PILDAT Survey (2013) | | |

Employing the game-theoretical model presented in Chapter 1, albeit with a slight revision, the interests and preferences of the three main parties in the subnational space in developing and instituting Local Governance Systems can be better analyzed. Given that all three of these parties have a national scope and aspirations focused on governing in the centre, competitive behavior and the ‘progressive ambition’ would incentivize strategies to dilute the support base of the each other with all means at disposal. However, in this case, the party already in power at the centre (PML-N) has a greater ability to further its own agenda.

An analytical proxy of a ‘dictator’ shall be applied to the dominant party i.e. PML-N at $t=0$. The objective is to frame the analysis operating on Schelling’s idea of free activity in a strategic interaction context; the dynamics of “bargaining, of arriving at understandings and misunderstandings, for accommodation and co-operation and for conjectures about each other’s decision processes, value systems and information” (Schelling, 1961). Following on Aslam (2010), the analytical focus is on how the surplus is divided, what strategies are employed to secure preferred outcomes and greater shares of the surplus, critical factors behind their bargaining power and the exogenous factors that have a bearing on the outcome.

The revisions include some additional strategies available to the players as compared to the original framework developed by Aslam (2010);

a) Maintain status-quo / ‘Play by the rules’:

The regional governments continue delivering on the assigned mandate without getting confrontational based on progressive ambitions and aspirations of gaining influence at the centre at $t+1$. Delivering on the mandate may deliver enough political capital in the form of good performance and service delivery record in the subsequent general elections.

b) Changing the opponents payoffs

This could take one or more of the following forms:

- Each player uses available resources for preferential allocations to regional constituencies where it has a majority.
- Each player diverts resources to opposition’s constituency to gain greater political capital and win it in the next electoral round

c) ‘Brinkmanship’/ Coercion strategies

This could take one or more of the following forms:

- Central government can withhold or scale down discretionary transfers

- Non-cooperation in mitigating horizontal imbalances
- Provincial Governments have the authority to dismiss LG officials, elected and appointed.

If Strategy A is chosen and all players maintain the status-quo and let their performance and service delivery determines their fate in the subsequent electoral round, there is a greater incentive for each player to deliver on its commitments to its constituents. However, under this strategy there is an opportunity cost of forgone political capital in the event of the inadequacy of the opposing player in delivering on its commitments.

If strategy B is preferred, and a player chooses to use all its available resources for preferential allocations to constituencies where it has a majority in a bid to further consolidate its support base, the down-side risk would be increased disparity within the region thus further alienating a potential support base.

Contrarily, under the same strategy if the player chooses to devote a greater share of available resources to the constituencies where it doesn't have a majority or an adequate support base with the aim of winning their loyalties, then there is a downside risk of losing out support from those constituencies where it has a strong support base as fewer resources would be available than expected.

If Strategy C is preferred then any political capital gained would necessarily come at the expense of developmental progress within the region and also have potential negative spill-over effects beyond the region; for instance, the strength of the federation.

The choice of either of the confrontational strategies (B or C) shall be constrained by the same inequality as in the original framework, i.e. costs and tradeoffs associated with the predated on the opposition's support base are less than the gains that can be credibly expected at $t+1$.

With this framework in context, it is easier to evaluate the decentralization and local governance frameworks developed by each of the provinces in the aftermath of the general elections in 2013. While the Local Governance Acts were promulgated by the provinces in 2013, their enforcement and implementation through formal local bodies' election did not take place until 2016. The striking feature of the results of these elections, and a confirmation of the Bardhan & Mookherjee (2000) hypothesis of local spaces being more prone to retrenchment of established interests at higher levels of government, has been that the local

elections have been won predominantly by candidates of the same party that is governing at the provincial level. For instance, in the province of Punjab, where the PML-N is in power at the provincial level, the local elections have seen the party's candidates win 25 out of the 33 districts in the province⁵⁰.

All four federating provinces had their Local Government Acts promulgated by 2013, and some of them were contested in the courts by the opposition parties (UNDP, 2015), which lead to the delay in the establishment of the LG structures. A review of all four of the Local Governance Acts also illustrates an example of brinkmanship of provincial governments, whereby all four provincial governments have retained the authority to suspend or dismiss heads of an elected local government⁵¹. Another common feature across all four LGAs has been the limited devolution of functions or finances to the local governments. Provincial Finance Commissions are established under the LGAs which will make transfers to the local governments in the province. In addition, the local governments have very limited powers to raise their own taxation/ revenue and their fiscal auditing is conducted by the provincial governments.

4.6 DEMOCRATIC & DEVELOPMENTAL IMPLICATIONS OF THE 18TH AMENDMENT

With the civil-military oscillations in the control of the state, there has been a renewed engagement in the national political narrative in the aftermath of the 2008 elections with Constitutionalism. Agreed upon by all political parties, the new narrative extols the execution of all functions of the state, transitions and distributions of the powers, government transitions and inter-governmental dynamics to be governed and conducted under the stipulated constitutional framework as promulgated in 1973. Where inadequate, revisions to the constitutions can be made following a 2/3rd majority support across all provincial and national legislative bodies (Constitution of the Islamic Republic of Pakistan). Decentralization, in the backdrop of this narrative, has assumed administrative and fiscal forms predominantly with the political decentralization only occurring at the centre-provincial level. Nevertheless, as

⁵⁰ <http://dunyanews.tv/en/Pakistan/366635-PMLN-sweeps-Punjab-in-local-body-polls>

⁵¹KPK: <http://lgkp.gov.pk/wp-content/uploads/2014/03/GOKP-2013-Khyber-Pakhtunkhwa-Local-Government-Act-2013-Print-Version.pdf>

Punjab:

https://www.af.org.pk/Acts_Fed_Provincial/Punjab%20Acts_since_2002/Punjab%202015/The%20Punjab%20Local%20Government%20Act%202013.pdf

Balochistan: <http://www.pabalochistan.gov.pk/uploads/acts/Local%20Govt.%20Act.htm>

Sindh: http://sindhlaws.gov.pk/setup/Publications_SindhCode/PUB-15-000059.pdf

a reform in progress and amid increasing articulations of democratic local governance returning into the national political narrative post 2013 general elections, there exists a possibility of democracy substantively and sustainably re-appearing in the local arenas.

The first constitution of Pakistan promulgated in 1956, envisaged Pakistan as a “decentralized federation with significant fiscal and administrative responsibilities being assumed by the lower levels of government” (Shah, 2012). The central government, on the contrary, was given a greater discretion over developing its revenue base requisite for direct federal expenditures and transfers to ensure standardization of public service delivery and redistribution to ensure inter-regional equity. The current constitutional framework when first instituted in 1973, enhanced the centralization tendencies in public spending responsibilities, and also stipulated service delivery responsibilities across the two tiers of the government under Federal Legislative List and the Concurrent Legislative List (Joint responsibility of centre and province). Table 1 provides an overview of the fiscal and functional responsibilities of the federal and subnational governments as stipulated in the 1973 Constitution prior to the 18th Amendment. The objective behind the establishment of these lists was to delineate responsibilities as well as enable an interim period whereby with the central equalization efforts, the provincial governments build their fiscal and administrative capacities to assume these responsibilities fully (Shah, 2006).

Nevertheless, the centre continued to encroach on the responsibilities and privileges of the provinces, the provinces in turn on the local governments, and hence the division of responsibilities and the fiscal endowments requisite to deliver on those responsibilities emerged as a main issue of contention in Pakistan, owing to which an institutional mechanism of National Finance Commission was rolled into action.

The first deliberated and consensually agreed National Finance Commission (NFC) Award in 1991 geared towards granting an “unconditional access” to a greater pool of the federal divisible pool (Pasha and Shah, 1996; Shah, 2012). Important facet of this award was the initiation of the process of expenditure realignment aimed at granting provinces a greater discretion over the ‘concurrent’ responsibilities, but this occurred without any discretion over additional or new revenue stream. This resulted in further increasing the reliance of the provinces on the central transfers. As per this 1991 award, which continued to be the revenue distribution formula till 2001, the federal transfers to the provinces financed a greater portion of the provincial operating expenditures and in the case of Balochistan the transfer financing amounted to 99% of the provincial expenditure (Shah, 2007). This process was reversed under

the LGO and the PCO discussed earlier, where the centre's pursuit of diluting established political support devolved both resource endowments as well as functional responsibilities from the provincial to the local governments. While the reforms under the LGO did result in service delivery improvements at the local levels, they were considered incomplete in the sense that they did not rationalize the federal and provincial powers, and in effect led the centre to encroach on both federal and provincial responsibilities (and hence resources) as stipulated in the 1973 constitutional framework.

With the transition back to civilian democratic government in 2008, the consensual narrative across the political space was to 'uphold democratic norms' by re-strengthening the provinces and rolling back the governance reforms under the LGO. The outcome of this consensual commitment to also led to the 7th National Finance Commission Award in 2009 (still in effect as of 2017), whereby the smaller provinces were given a greater share to the resource pools in a bid to build inter-provincial harmony and also meet the equalization requisites. Under the 7th NFC, an enhanced allocation was given to the smaller provinces. Indicators such as population density, poverty levels, and domestic fiscal effort were incorporated as determinants of the fiscal revenue sharing formula.

Table 12: Functional Distribution across Government Tiers

| Legislative Responsibility | Services | Actual Allocation of Functions |
|--|--|---|
| Federal Government¹ | Defense, External Affairs, Posts and Telegraphs, Telephones, Radio and T.V., Currency, Foreign Exchange, Foreign Aid, Institutes for Research, Nuclear Energy, Ports and Aerodromes, Shipping, Air Service, Stock Exchange, National Highway, Geological Surveys, Meteorological Surveys, Censuses, Railways, Mineral Oil & Natural Gas Industries | Federal Government |
| Federal/ Provincial Governments² | Population Planning, Curriculum Development, Syllabus Planning, Centers of Excellence, Tourism, Social Welfare, Vocational/Technical Training, Employment Exchange | Federal/Provincial Governments |
| Provincial Government | Historical Sites and Monuments, Law and Order, Justice, Tertiary Health Care and Hospitals, Highways, Urban Transport, Secondary and Higher Education, Agricultural Extension, Fertilizer and seed distribution, Irrigation, Land Reclamation | Provincial Governments |
| Local Governments³ | Primary Education, Curative Health, Preventive Health, Water Supply Drainage and Sewage, Farm-to-Market Roads, Land Development, Rural Developments, Link Roads, Intra-Urban Roads, Street Lighting, Garbage Collection, Fire Fighting, Parks and Playgrounds | Primarily Provincial with Minor Local Government Involvement Local Governments |

1. According to Federal Legislative List

2. According to Concurrent Legislative List

3. According Provincial Legislation

Source: Shah(2009) Constitution of the Islamic Republic of Pakistan 1973 (Sch. Including 17th Amendment)

Table 13: Finance Decentralization under the 7th NFC Award

| | |
|---|--|
| Total Divisible Pool | 56%-57.5% of the following sources of federal revenues: Personal and corporate income taxes, wealth tax, sales tax, excise duties on tea, tobacco, sugar, and other excises. Amount FY 2010-11: PKR 865.8 billion (US\$ 9.62 billion) |
| Formula for provincial allocation | Population – 62% weight Poverty – 10.3% weight Provincial tax effort – 5% Inverse of Provincial Population density – 2.7%weight |
| Provincial shares In Population Punjab: 57.4% Sindh: 23.7% KPK: 13.8% Baluchistan: 5.1% | Provincial shares in NFC Allocation Punjab: 51.7% Sindh: 24.6 KPK: 14.6% Baluchistan: 9.1% |

Source: Institute of Public Policy (IPP), 2011, Shah (2011)

In terms of its institutional dimensions, the 18th Amendment has substantially reformed the institutions established as intergovernmental coordination mechanisms i.e. the Council of Common Interests (CCI) and the National Economic Council (NEC). The CCI is a coordination and deliberative body headed by the Prime Minister (or a designate), the Chief Ministers of all provinces and federal government representatives. While its prior jurisdiction was nominal in terms of providing solicited provincial input in federal matters, the 18th Amendment enhanced its potency by making it responsible for all matters related to the federation⁵². The NEC, also a constitutionally mandated body for oversight over national economic policies, previously composed of the Prime Minister, and Presidentially nominated members (with the constraint holding that at least one representative of each province must be nominated). In the aftermath of the 18th Amendment, the composition was altered to enable a greater influence of the provincial governments such that two provincial members in addition to the provincial Chief Minister and four federal government representatives nominated by the Prime Minister would now compose the NEC.

This has enabled a greater deliberative scope for the provincial interest articulation in the national policy making, to avert any scope for centralized high-handed policy stipulations. Furthermore, this Constitutional amendment also enabled substantive changes in the division and devolution of powers between the federal and provincial levels of the government whereby the previously entrenched ‘Concurrent List’ was disposed off altogether, and a functional reassignment to the Federal Government was done contingent upon the directions of the CCI, with all other functions devolved to the provinces. Notwithstanding the functional reassignments and devolution, there has been very limited reassignment of taxation responsibilities to the provincial governments. The taxation powers remain predominantly with the central government, which were further reaffirmed by the provincial governments owing to the scale advantage argument (Yelmaz,2010).

In terms of the provincial exposure to capital mobilization avenues, the 18th Amendment also enables the subnational governments to access domestic and international

⁵² The composition remained the same as before (Prime Minister, all Chief Ministers and three nominated Federal Government Representatives), but the scope of responsibility was expanded to include .."decision making, monitoring, supervision, and control responsibilities over the Federal Legislative List Part II, which includes the following: railways; minerals, oil, and natural gas; hazardous materials; industrial policy; electricity; major ports; federal regulatory authorities; national planning and economic coordination; supervision and management of public debt; censuses; provincial police powers beyond provincial boundaries; legal matters; regulation of the legal, medical, and other professions; standards in education and research; interprovincial coordination; and conflict resolution" (IPP, 2011).

sources for credit and finance, albeit within the parameters defined by the NEC. These limits continue to be revised circumstantially and are not mandated at fixed rates in a legal framework as observed in the ‘80-20 rule’ as practiced in Bolivia. In addition to enhanced avenues of credit finance, under this amendment the provincial governments were also equipped with a relatively more dynamic and buoyant tax base in the form of sales tax on services. In 2013, the fiscal proceeds from this tax base alone generated around 0.5% of the GDP in fiscal revenues (IPP, 2013 and Government of Pakistan, 2013).

Table 14: Functional Responsibilities under the 18th Amendment

| Federation/CCI (Joint Federal-Provincial) Tasks—Federal Legislative List Part II | |
|--|---|
| Electricity | Provincial police operations beyond provincial boundaries |
| Minerals, oil and natural gas | Industrial policy |
| Railways | National Planning and National Economic Coordination |
| Major Ports | Coordination of Scientific and Technological Research |
| Census | All regulatory authorities under a federal law |
| Public Debt | Standards in higher education and Research, scientific and technical institutions |
| Federal corporate entities including Water and Power Development Authority and Pakistan Industrial Development Corporation | Interprovincial matters and coordination |
| Legal, medical and other professions | |
| Federal Functions—Federal Legislative List Part I | |
| Defense | International and inter-provincial trade |
| External Affairs and international treaties | Nuclear Energy |
| Immigration and citizenship | Airports, aircraft, air navigation, air and sea travel and shipment, lighthouses |
| Post and Telecommunications | Patents, trademarks, copyrights |
| Central banking, Currency, Foreign Exchange, | Stock exchanges and futures markets |
| Corporate regulation including banking and insurance | National highways and strategic roads |
| Fishing beyond territorial waters | Federal geological surveys and meteorological organizations |
| Standards of weights and measures | Local government in cantonment areas |
| Provincial Responsibilities | |
| All residual functions | |
| Local Government Responsibilities: By provincial government determination | |

The current system also established 2015 as a milestone for a transforming the governance structures such that the power concentration at the central level is replaced by concentration at the subnational level. Under this milestone, all major economic and social

functions shall be performed and designed by the provinces. This is exhibited in the shifting trends in the financial and functional pools of the provincial governments as illustrated in Tables 15.

Table 15: Summary of Fiscal Decentralization under the 18th Amendment

| Fiscal Year | Indicator | Federal Share | Provincial Share |
|--------------------|--|----------------------|-------------------------|
| FY 2009-10 | Revenue collection | 94% | 6% |
| | Revenues retained | 65% | 35% |
| | Expenditure share | 66% | 34% |
| | Residual Fiscal Gap after transfers | -1% | +1% |
| FY 2011-12 | Revenue Collection | 90% | 10% |
| | Revenues retained | 61% | 39% |
| | Expenditure share | 64% | 36% |
| | Residual Vertical Fiscal Gap after transfers | -3% | +3% |
| FY 2014-15 | Revenue collection | 85% | 15% |
| | Revenues retained | 45% | 55% |
| | Expenditure share | 45% | 55% |
| | Residual Vertical Fiscal Gap after transfers | 0% | 0% |

Note: Any allowances for local expenditures come from the provincial pool

Source: Economic Survey of Pakistan (2011), Shah (2011/2012) IMF Government Finance Statistics Module

Amongst this functional devolution, there has also been a dispensing away of viable central roles like fostering a mutually beneficial economic union, protecting minorities and disadvantaged groups, disaster response and risk mitigation, and framing an overall strategic developmental orientation. Particularly, in the context of political and economic cohesion, it is imperative that natural resource endowments are viewed as national subjects instead of being made into provincial realms such that the rents from these resources can be invested at a higher scale of effect and equity at the central level. The current framework makes it into a provincial subject, which has potential for divisive pressures between the provinces and hence expose the federation to risk. This argument finds its roots in the inter-provincial conflict over Hydel resource distribution and the Kalabagh Dam construction, as well as the distribution of gas and extractive revenues across the provinces. Especially considering the latter, the divisiveness is particularly pronounced in Baluchistan which is host to a substantial mineral and extractives base yet deriving the least benefit.

A decentralized system works best if there are potent platforms for interest articulation by the citizenry (through effective political decentralization), and a finance-functional harmony. Particularly important is to ensure that expenditure decentralization must also be accompanied by the taxation/revenue generation decentralization such that reliance on higher level transfers is reduced and also create greater incentives for fiscal transparency and accountability.

Furthermore, the current constitutional framework post the 18th Amendment does not revisit the mechanisms in place for central fiscal transfers to provincial governments under the NFC award. These NFC awards are guided, as mentioned earlier, by the objectives of fiscal equalization horizontally and vertical gap reduction. However, with the functional devolution of the social service provision and infrastructural development to the provincial levels, the role of the federal government in finance provision and establishment of minimum standards is important.

4.7 CONCLUSION

The LGO and the 18th Constitutional Amendment have both been substantive attempts at subnational empowerment; with the former less than the latter by virtue of the absence of the constitutional cover and its autocratic sponsors. Despite having its merits, LGO has little formal relevance in the current scheme of decentralization and federalism discourse in Pakistan. The 18th Amendment thus emerges as the most recent and comparably expansive decentralization reform that has fostered an environment conducive for federalism. Perhaps the greatest merit of this round of reform has been the underlying political consensus and its constitutional embeddedness. Whether or not the current decentralization from the centre to the provincial levels also leads to provincial to local decentralization in the subsequent rounds remains to be seen, but in terms of fostering a greater national cohesion and deepening democracy it does exhibit potential. In addition, a clearer delineation of the functionalities has reduced the scope for arbitrary unwarranted federal intervention in provincial subjects, thus reducing the centre-provincial frictions.

The institutional reinvigoration of the CCI, for example, is another important outcome of this amendment, as it creates inter-governmental deliberative platforms that can be used for grievance redressal. Furthermore, it also fosters subnational interest articulation that was previously inhibited by federal unilateralism. The key shift in the current constitutional framework puts the provinces at the core of both policy formulation and its implementation, which not only makes the governance structure more proximate to the citizenry but also clarifies which levels must be held accountable for any suboptimalities in service delivery. The greater proximity of the government to the citizenry enabled by the 18th Amendment may also lead to a relatively higher level of citizen participation in the public policy frameworks while also creating greater pressures for accountability and responsiveness by the governments

to the citizens which would be further enhanced if local levels also came to the fore. The amendment's predominant engagement with the devolution of functionalities and linking the fiscal endowments at the expense of any rationalization of the mandates of central and provincial functions and discussion on local governance structures or division of the provinces into smaller administrative units.

To an extent, the 18th Amendment may have unintentionally compounded these threats by reasserting an obsolete model of two-tier federal governance. Instead of a disparately powerful centre, under the 18th Amendment it is a disparately powerful province. The extent to which the increased authorities at the provincial levels have led to a corresponding improvement in the public service delivery or even grappling with the challenges to the state in terms of rule and order, is suboptimal. On the whole, federalism in Pakistan may have taken the most substantive of its leaps with the 18th Amendment; there are some downside risks that can prove highly detrimental if not dealt with caution. The overall focus of all political actors, the central and provincial governments has to foster greater inter-regional harmony to ensure state stability and cohesion. However, with the enhanced provincial autonomy and opposing political parties holding office in three of the four main regions, there exist divisive risks too. The 18th Amendment stands well on the grounds of democratic consolidation but it cannot be considered a panacea for the governance constraints of Pakistan as it is at best an incomplete process – completion of which would deem imperative more fundamental reforms that ensure greater public responsiveness but also a stable political and economic union due to greater efficiencies and accountability mechanisms.

CHAPTER 5

CONCLUSIONS AND FURTHER OUTLOOK

The global development narrative is increasingly, and rather appropriately, considering the primacy of governance and institutions as a key determinant of the success of policy frameworks. There are a variety of policy frameworks and technical solutions that have come to the fore as panaceas for the inadequacies of development policy frameworks which have delivered on the expected goals in some contexts while failing in others. Thus, the focus has to be realigned to why they work where they do, and what are the underlying drivers and determinants of effective policies. Decentralization of governance has followed a similar path – emerging as a potent tool for enacting state and governance reforms, yet has been marred by experiences that remain mixed at best. The extent to which decentralization is conducive to enhancing development and democratic transition/ consolidation is still a subject of debate. This research contends that the impulse to decentralize finds its roots in many different combinations of incentives and power structures – from an autocratic central government pre-empting the demand of its constituents and enabling their participation in the governance process as in the case of Bolivia under the Ley de Participación Popular, or an autocratic government at the centre using decentralization reforms as a tool for dislodging existing opposing political organizations by developing a new support base at the subnational level as in the case of Pakistan.

This research has endeavored to examine the role of decentralization in conjunction with democracy and development. In doing so, it has focused primarily on the incentives of the stakeholders sponsoring and introducing the decentralization reforms, the order and sequencing of the reform and most importantly the underlying bargaining between the stakeholders during the reform design and implementation. Building upon the sequential theories of decentralization and the two distinct reform trajectories postulated by Faletti (2009)– a bottoms up subnational dominance path, and a top down national dominance path. Given the contrasting objectives of national and subnational actors when decentralizing, the preferences of the centre are to devolve administrative and functional responsibilities to the lower levels of the state before relinquishing any financial or political control. The subnational preference remains greater political autonomy followed by financial resources and then deciding which functions and administrative responsibilities can be

undertaken.

A gap that this research has attempted to fill, however imperfectly, is that it explored the possible nexus between a decentralization reforms and the establishment of a democratic developmental state. Based on a synthesis of various conceptualizations of the Developmental State this research identifies it as a state that is committed to a national development agenda that has at its core capacity and outreach, and geared towards an inclusive growth trajectory that targets poverty alleviation and, effective and efficient public service delivery. The main scope of decentralization reforms in the establishment of a developmental state is in terms of pluralizing political space at the local levels, enabling a more deliberative policy arena, while also fostering greater responsiveness of public service delivery and enhanced accountability of the government due to its proximity to the citizenry.

Given the history of developmental states, such as the East Asian states, the notion of a democratic developmental state may seem like an oxymoron and a loose conceptual stitch. This is largely attributable to the perceived incompatibility of the key features of the individual constructs of democracy and Developmentalism; e.g. autonomy of policy making is critical to developmental policy and accountability is a critical requirement of democratic norms, but under a DDS making the policy framework accountable may compromise the autonomy of developing one. However, when considering developmentalism, the concept does not pertain to an absolute form of state but instead implies a process of progression and development with a social dimension instead of narrow economic dimensions, generating historical paradigms and configurations. It can thus, be considered as a process of deep social transformation, rationally operated against a politically committed state, to bridge the economic and social progress gaps.

In validation of the Bresser-Pereira (2016) argument, this research developmentalism is more suited for contexts characterized by structural and distributive imbalances whereby its transformative conduct needs to be systematic, socially oriented and politically sustained change. Furthermore, developmental state is not a monolith of sorts. According to Joshi (2012) three types of developmental states exist; Human resource Developmental State, Resource Developmental State, and the Human Developmental State. The case of Bolivia fits in the category of a Resource Developmental State where it is using its natural resource rents for socio-economic uplift. However, an attempt has been made by this research to suggest that the Developmentalism can be complemented by decentralization reforms, primarily in terms of pluralizing policy arenas and providing an articulation platform to

diverse groups while retaining consistency with the National Development Plans.

This research has also attempted to contextualize the decentralization, democracy and development nexus in the context of two Lower Middle Income Countries sharing a political history in terms of the autocratic regimes and political exclusion for the masses. Both countries have different state structure, with Bolivia being a Unitary State and Pakistan being a Federation. This on one hand enables the broader study of decentralization and its implications for democracy and development across two systems of government and state-structure, but at the same time enables the analysis of an interesting paradox. The structure of the state in Pakistan has been Federal in its form, but unitary in function up until the constitutional reform of 2009/10 following which it has been making leaps towards being federal in function as well. The structure of the Bolivian state has been unitary both in form and in function, and continues to be so after the promulgation of the new constitution in 2009. However, with the departments getting more autonomy vis-à-vis the centre, and a greater space for preference articulation in the decision-making space in the now Plurinational State of Bolivia, it is often considered as emerging federation. Finally in the context of the case studies, the two countries chosen for the case study are also indicate the subnational dominance path (Bolivia) and a national dominance path (Pakistan).

Limitations and Avenues for further research

Due to a paucity of resources and time, this research remained predominantly secondary with the exception of unstructured interviews and discussions with Country Experts and officials involved in the decentralization reforms from both countries during my research mobility and my subsequent pursuits. Primary research and focused group discussions in the field (especially in Bolivia) could have added a greater value to this research.

In terms of the outlook, this focus area of this research is still an avenue with very limited research, particularly in the area of Democratic Developmentalism and Decentralization. There are multiple states including but not limited to, Botswana, Ethiopia, Colombia are currently engaged with democratic developmentalism/ neo-developmentalism which will be an interesting avenue for me to explore as I go on. Furthermore, this theme is an emerging research area particularly in the backdrop of Domestic Resource Mobilization and Financing for Development in the developing countries. I would endeavor to acquire more insights both theoretically and empirically in this realm.

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