

SUMMARY of the Article “Victims of our own narrative,” by Zafar Masud, Dawn [Published on January 6th, 2024]

Zafar Masud explores the dynamics of market narratives and the role of regulators in shaping economic outcomes, challenging the notion that the market inherently knows best. He contrasts the Chicago School’s belief in market efficiency with the perspective of behavioral economists, emphasizing that human behaviors influence and sometimes distort markets. The author cites instances such as the Asian currency crises and the 2008 banking crisis, highlighting the need for government intervention. In the context of Pakistan, the Heritage Foundation’s Economic Freedom Index places the country 152nd out of 180, indicating a heavily regulated economy. Masud stresses the importance of balancing economic freedom with effective regulation, advocating for regulators to prevent consumer exploitation, ensure perfect competition, and maintain a level playing field. He calls for a comprehensive effort to address conflicts, establish missing regulators, and enhance expertise, making them independent and centers of excellence. The article emphasizes the necessity of a dynamic regulatory environment aligned with Pakistan’s evolving business and social maturity, cautioning against premature reliance on markets without robust regulation.

Easy/Short SUMMARY:

Zafar Masud discusses market dynamics and the need for effective regulation, challenging the idea that markets always produce optimal outcomes. He emphasizes the importance of regulators in preventing exploitation, ensuring fair competition, and maintaining economic freedom. In the Pakistani context, he calls



for a balanced approach, addressing conflicts, establishing missing regulators, and enhancing expertise. The article underscores the significance of a dynamic regulatory environment aligned with the country's evolving business and social maturity.

SOLUTIONS of The Problem:

1. Enhancing Regulator Independence:

- Ensure regulators are independent, possessing the expertise to address conflicts and act as centers of excellence.

2. Establishing Missing Regulators:

- Identify sectors lacking regulators, and establish regulatory bodies to fill the gaps.

3. Building Regulatory Capacities:

- Invest in building capacities and expertise within existing regulatory bodies, ensuring they can effectively oversee various sectors.

4. Balancing Economic Freedom:

- Emphasize a balanced approach that combines economic freedom with effective regulation to prevent market failures.

5. Avoiding Discretionary Policy Responses:

- Encourage a balanced policy environment that appreciates ground realities, avoiding impulsive policy responses swinging from one extreme to another.

6. Inclusive Economic Institutions:

- Ensure regulators function as inclusive economic institutions, prioritizing the larger population's interests over extractive practices.

7. Assessing Regulatory Gaps:

- Regularly assess and address regulatory gaps, aligning regulations with next-generation laws to ensure relevance and effectiveness.

8. Creating a Balanced Policy Environment:

- Advocate for a policy environment that appreciates ground realities, attracting higher private-sector investment and supporting sustainable growth.

9. Dynamic Regulatory Environment:

- Emphasize the need for a dynamic regulatory environment, adapting to Pakistan's evolving business and social maturity.

10. Preventing Customer Exploitation:

- Enforce regulations that prevent customer exploitation, maintaining a fair and competitive market environment.

IMPORTANT Facts and Figures Given in the Article:

- *Pakistan's Economic Freedom Index Ranking:* 152nd out of 180 countries (Heritage Foundation).
- *Instances of Market Failures:* 1997 Asian currency crises, 2008 banking crisis in the US, and recent crises in Europe.
- *Regulatory Challenges in Pakistan:* Lack of independence and capacity, ranking 152nd in the Economic Freedom Index.
- *Author's Position:* Development and social-impact focused banker, public-sector specialist.

MCQs from the Article:

1. *What does Zafar Masud challenge in the article?*
 - A. The effectiveness of market narratives.
 - B. The notion that the market inherently knows best.



- C. The role of regulators in shaping economic outcomes.
D. The idea of government intervention in market crises.
2. *According to the Heritage Foundation's Economic Freedom Index, where does Pakistan rank?*
A. 50th
B. 100th
C. 152nd
D. 180th
3. *What historical events does the author cite to emphasize the need for government intervention in markets?*
A. 2010 European debt crisis
B. 1990s dot-com bubble
C. 1997 Asian currency crises, 2008 banking crisis in the US, recent crises in Europe
D. 1987 Black Monday
4. *What is the primary focus of Zafar Masud's advocacy regarding regulators?*
A. Complete deregulation of markets
B. *Balancing economic freedom with effective regulation*
C. Introducing more conflicts of interest
D. Allowing markets to operate freely without any regulation
5. *What does the author caution against in the article?*
A. Excessive government intervention
B. *Premature reliance on markets without robust regulation*
C. Independence of regulators
D. Ignoring conflicts of interest in regulatory bodies

VOCABULARY:

1. *Cogent* (adjective) (□□□□ □□□□): Clear, logical, and convincing.



2. *Imperfection* (noun) (نقص): A fault or defect in something.
3. *Orthodoxy* (noun) (تقليد): Authorized or generally accepted theory, doctrine, or practice.
4. *Behavioral Economists* (noun) (اقتصاديون سلوكيون): Economists who study the psychological and emotional factors influencing economic decisions.
5. *Speculative Asset Bubbles* (noun) (فقاعات الأصول المضاربة): Rapid increases in the prices of assets not justified by economic fundamentals.
6. *Intervene* (verb) (تدخل): Take action to improve a situation, especially in the economic or political context.
7. *Heritage Foundation's Economic Freedom Index* (noun) (مؤشر الحرية الاقتصادية لمنتدى الـهريـتاج): A measure of the economic freedom of countries, ranking them based on various indicators.
8. *Extractive* (adjective) (استخراجي): Relating to or involving the removal of natural resources from the earth.
9. *Impulsive* (adjective) (تلقائي): Acting or done without forethought.
10. *Holistic* (adjective) (شمولي): Characterized by the belief that the parts of something are interconnected and explicable only by reference to the whole.

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Victims of our own narrative
Zafar Masud

“Market knows everything best” is considered the most cogent of arguments by free-market supporters. This may be true in some instances but in most cases it’s unfounded, given the inherent imperfection of markets. While Chicago School orthodoxy says markets produce the best outcomes for society, behavioural economists insist that it’s humans who make markets. This means that humans can strive to improve their functioning.

Shiller, a Yale-based behavioural economist, argues that markets are shaped by ‘animal spirits’; individual actors have irrational tendencies, which can be amplified by the collective mood of the market. This sometimes results in irrational and suboptimal outcomes, such as speculative asset bubbles. Dr Bogan, a Cornell economist, aptly encapsulates it: “Markets are not perfectly efficient because it’s a collection of people, and they have flaws, biases, imperfections. And so markets aren’t perfectly efficient either”.

Even in a ‘relatively’ perfect environment, markets tend to be imperfect. The 1997 Asian currency crises, the 2008 banking crisis in the US, and most recently in Europe, are typical cases in point where governments had to intervene to save falling ‘free-market players’ in the ‘larger public interest’.

The fact is that it’s the interest of people which is at the heart of any policymaking. While markets should be free to operate with minimal regulations, regulators must have enough in their arsenals to ensure that there’s no exploitation of consumers, and there should be perfect competition and a level playing field.

In Pakistan’s case, markets and economic freedom are challenged and at the same time regulators’ independence and capacity are hampered. In the Heritage Foundation’s Economic Freedom Index, Pakistan ranks 152nd out of 180 countries. This indicates a heavily regulated economy. The worst situation is

where there's no regulator or government agency — significantly lacking expertise (like E&P, agriculture, etc) and at times having a conflict of interest of sorts (like CAA, FBR, etc) — to act as regulators. A serious effort is warranted to alleviate these conflicts; establishing regulators where they're missing, and building requisite capacities and expertise where they exist, making them independent and centres of excellence.

Markets must be allowed to make money but without customer exploitation.

Our business and social maturity lifecycle is also in its infancy and warrants a dynamic regulatory environment while keeping markets functioning with adequate economic freedom. This makes the role of regulators even more central and inevitable. It's not only the re-constitution of the economy, it's the reprioritisation of the entire society and its actions to create an efficient market. As society becomes more responsible, the need for regulation will certainly subside. However, leaving things entirely to the markets prematurely, without a robust regulatory environment could result in irreparable loss to a country that has over 40 per cent of the population below the poverty line and is confronted with abject illiteracy. We must take stock of our realities on the ground, and then devise the required role of regulators, who would ensure avoiding distortions through interventions necessary to keep order in the market.

Ha-Joon Chang in *Edible Economics* states: "We fundamentally go wrong when we start stating economics as a science. The critical thing to keep in mind here is that economics is not a science; there are no perfect provable answers. There is no single economic solution or model that works in all situations — choosing the right economic answer depends on the circumstances of the economy and the conditions it faces. Economics is a study of human activity with all the emotion, ethical stands and imagination that everything human involves".

Our policymaking pendulum, in Pakistan, swings from one extreme to the other, with policies implemented in patches, lacking cohesion, which end up doing more harm than helping the functioning of markets. For example, the ambition of following the free market monetary system whilst pursuing pro-elite, rent-seeking policies on the fiscal side, results in market failures, leaving the tools available to control inflation and unemployment less effective or even redundant at times. Therefore, 'holistic and balanced' are the functional words for all our policy actions — from macroeconomic policy to regulating markets.



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Modesty is the key and balance is a necessity. Human nature is a reality; people, nations, and markets are unique, and their maturity life cycles are distinct. The right mix of free markets and regulation is needed based on the specific environment. The line must be drawn by the government to ensure that regulations and timely actions shall only come into force to protect the interest of consumers; otherwise, let the markets operate freely. As Stefan Dercon alludes in his fascinating book *Gambling on Development*: “Success does not depend simply on whether the development process is state-led or market-led. Relevant factors are the quality of public administration systems, and how well policies and investment projects are implemented. Countries need to find a balance which is appropriate to their context”.

Markets must be allowed to make money but without customer exploitation and creating undue advantage of market failures and that’s where the role of regulators comes in handy to protect the ‘interest of the larger population’. It’s all about creating a prosperous, equitable, and stable society. Regulators shall be ‘inclusive economic institutions’ and not ‘extractive’, in the words of Acemoglu and Robinson. While law by its very nature is definitive, regulations give regulators a wide landscape now known as “regulatory discretion”, and there’s always a risk that the regulators are quick to frame new regulations and resultantly over-regulate. It is also vital that the regulators assess, contextualise and address regulatory gaps in the light of next-generation laws and regulations.

In Pakistan, while we surely need strong regulators to tackle market failures and protect consumer interest, a balanced policy environment is imperative, which appreciates ground realities, instead of discretionary and impulsive policy responses that swing from one extreme to the other. This equilibrium certainly ensures attracting higher private-sector investment and supports stronger, sustainable growth and job creation.

The writer is a development and social-impact focused banker and a public-sector specialist.

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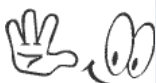
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