BENEFITS AND IMPEDIMENTS TO TRADE COOPERATION BETWEEN PAKISTAN AND INDIA

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Abstract

Most-favored-nation (MFN) treatment is the first article of the General Agreement on Tariffs and Trade (GATT), which governs international trade in goods. As such, it is a general obligation for all the World Trade Organization (WTO) member countries. However, some exceptions are allowed by the agreement. For example, member countries can set up a free trade agreement that applies only to goods traded within the regional group. Or they can give developing countries special access to their markets (say through GSP scheme). Or a country can raise trade barriers (contingent protection) against products that are considered to be traded unfairly from specific countries. India and Pakistan have been denying the most favourite nation (MFN) status to each other purely on political basis, which is not an exception according to WTO rules. India took the initiative and granted MFN status to Pakistan in 1996, Pakistan is now considering reciprocating it. With the announcement, the business community and other stakeholders in the two countries are excited about the upcoming opportunities and challenges they might be facing in the future. They thus want to know as to how their businesses are going to shape up in the aftermath of granting of the MFN status. Business community and industrialists are curious and asking questions whether cooperative trade relations afterwards will face hurdles or not? They are interested to know how smooth will be the new trade relations. These are the precise questions that are addressed in this paper. After answering these questions, the paper puts forward strategic directions to guide policymakers to develop cooperative trade relations with India.

Introduction

With the announcement on the 2nd November 2011, that Pakistan will grant the most favored nation (MFN) status to India, business people and other stakeholders on both sides of the Pak-India border were excited about the expected change they are about to experience. This is particularly because they are privy to the perpetual stalemate in their relations for more than half a century. They are also thrilled because they want to know that in what way their lives are going to change due to this mega event. They are also curious and asking questions whether cooperative trade relations will face hurdles or not? How smooth will be the trade relations in the aftermath of granting of MFN status? Precisely, these are the concerns that are addressed by this paper.

A few words regarding the granting of the MFN status to India are in order. The MFN rule of the World Trade Organization (WTO) requires that at the port of entry, products made in trading partners' own countries are treated no less favorably than goods originating from any other country. In this very context, MFN treatment to a trading partner is a basic instrument of a freer trade policy. Pakistan is expected to re-grant the MFN status to India that it granted her between 1948 and 1965.[1] MFN means the two countries will not discriminate each other in the implementation of their trade policies. It will be the same policy instrument they are using for other WTO members.[2] It will not be more than this.[3] Of course, if the two countries take additional steps and go for a special and a separate trade agreement then that will have different implications from a purely MFN treatment.

Granting of MFN treatment will be a major Confidence Building Measure (CBM) and a right way forward that will definitely provide a strong foundation for any future trade cooperation either on bilateral or regional basis. MFN is a WTO obligation and should not be treated more than that. It should not be considered as trade cooperation, but a beginning towards cooperation. Without it, trade cooperation is indeed unthinkable. Thus, huge work in trade relations between the two countries awaiting in the time ahead.

This paper orbits around the context after the granting of MFN status to India by Pakistan. Given the focus of this paper, trade cooperation needs to be defined here. Trade cooperation between countries aims to facilitate each other for the promotion and sustainability of trade. Thus, trade cooperation is a strategy to promote trade expansion. Trade cooperation is primarily achieved through liberalizing trade and by creating harmony and coherence in trade policies. It is critical amidst sluggishness of our economies. Contrary to trade liberalization, protectionism intensifies recession and adversely affects growth. Accordingly, trade cooperation should be seen as vital for the development of two economies.

Rest of the paper is divided into seven sections. Section 2 assesses the existing structure of Pak-India trade. Section 3 examines the current trade regime in India. Potential tradable products are identified in section 4. Section 5 discusses the likely benefits of trade cooperation between India and Pakistan. Section 6 discusses the impediments to trade cooperation between India and Pakistan. Section 7 provides strategic directions to maximize benefits from trade cooperation while alleviating hurdles on its way. Finally, section 8 concludes the paper.

Structure of Current Pak-India Trade

Current official trade between India and Pakistan is less than $2.0 billion (Table 1). Trade balance has always remained in favor of India and is perpetually growing. Informal trade reportedly is in the range of$2-3 billion. At present, paradoxically, the total landed cost of imports (value of imports plus MFN tariff plus transportation cost) from, say, Dubai is lower than the landed cost (value of imports plus non-MFN tariff & NTBs plus transportation) on direct imports from India. This is simply the reason as to why Pakistani importers are using third countries to import Indian goods into Pakistan, or through border smuggling. Most of the available studies estimate 4-5 times total trade potential between the two countries.[4] Khan (2011) estimates trade potential of $42.0 billion if normal relations are assumed. In any case, these studies speak of large untapped trade potential of the two countries.

Table 1: Pak-India Trade (US Dollars in Million)

Year	Pakistan's Exports to India	Pakistan's Imports from India	Total Pak-India Trade	Trade Deficit with India
2004-05	288	547	835	259
2005-06	293	802	1095	509
2006-07	343	1235	1578	892
2007-08	255	1701	1956	1446
2008-09	320	1914	2234	1594
2009-10	260	1061	1321	801
2010-11	261 (1.07%)	1722 (4.31%)	1983	1461
2011-12	320 (1.44%)	1426 (3.36%)	1746	1106

Source: IMF (2010) and GOP (2012).
Figures in parenthesis are shares out of Pakistan's total exports and imports.

It may be noted that the complementarity index[5] shows that it is small (16% in 2003 and 19% in 2007, Table 2) and thus with status quo in our production and trade structure, the size of the index points out to low trade opportunities for Pakistan in the Indian market. Likewise, IIT with India is low (11% in 2003 and 20% in 2007). Such a trade structure and trends call for diversifying Pakistan's exports to India to reap the benefits of the bigger Indian market. Of course, this is not easy to accomplish. A lot would depend on how our policy assists domestic industries to restructure themselves, and introduce new products where industries can create competitiveness and India has a demand. It may also be noted from Table 2 that these indices of Pakistan for the rest of the world are somewhat higher than India. Therefore, complementarity of Pakistani trade with other countries is greater than India. This should also motivate policymakers to strive to create complementarities and intra-industry trade between two countries.

Table 2: Trade Complementarity and Intra-industry Trade Indices of Pakistan

Year	India		Rest of the World	
	Trade complementarity index (%)	Intra-industry trade index (%)	Trade complementarity index (%)	Intra-industry trade index (%)
2003	15.69	0.11	22.93	0.19
2004	16.33	0.26	23.86	0.20
2005	18.09	0.25	24.57	0.19
2006	17.46	0.15	23.95	0.22
2007	18.59	0.20	25.69	0.25

Source: Asia-Pacific Trade and Investment Agreements Database: www.unescap.org/tid/aptiad/index_cmpl_fm.aspx.

Overall export to import ratio of Pakistan for the period 2006-07 to 2010-11 is 54%, whereas, this ratio of Pakistan with India is only 19%. It implies that Pakistan's import dependency on India is much greater as compared with the rest of the world. This one-sided trade dependency needs to be corrected to allay the fears of the Pakistan industries.

Notwithstanding above, Table 3 shows the weak competitive strength of the Pakistani industries viz a viz Indian industries in both countries' markets as well as in the international markets.[6] It may be noted from the table that Pakistan's competitiveness increased till 2005 but afterwards it started declining. On the other hand, Indian competitiveness is continuously increasing and is very high as compared with Pakistan. Pakistan needs to introduce concrete policy measures on urgent basis to improve the competitive strength of its industries so that they are ready to face competition from Indian industries; something policymakers ignored so far.

Table 3: Indices of Competitiveness of Pakistan and India

Year	Pakistan		India	
	With respect to Indian market	With respect to the international market	With respect to Pakistani market	With respect to the international market
2003	0.18	0.18	2.79	0.76
2004	0.24	0.15	3.50	0.79
2005	0.31	0.16	3.14	0.91
2006	0.25	0.15	5.33	1.01
2007	0.19	0.14	6.31	1.08

Source: Asia-Pacific Trade and Investment Agreements Database: www.unescap.org/tid/aptiad/index_cmpl_fm.aspx.

Current Trade Regime in India

Broadly speaking, the Indian trade regime relies on tariffs, para-tariffs and non-tariff measures (NTMs) to restrict imports to its territories. Its overall applied tariff rate is 12 percent. In addition to MFN tariffs, India also uses different para-tariffs[7] including entry tax to a state, octroi, sales tax at the import stage, different surcharges, taxes on foreign-exchange transactions, service fees affecting importers, etc. (Table 4).In particular, why para-tariffs are not a preferred trade policy instrument? It is because para-tariffs in India are normally subject to arbitrary implementation and are non-transparent. They are often driven by specific interest-groups to protect their industries or use the revenue earned from it to finance their activities.

Textiles and agricultural commodities are sensitive areas of trade for Pakistan and are major areas of concern. These are the areas where Pakistani exporters face major hurdles in India. It may be noted from Table 4 that, whereas for textiles average MFN tariff rate is 9.6 percent, however, when other import related taxes (such as para-tariffs) are added to it then overall tariff rate becomes 23.5 percent. Likewise, in the case of agricultural commodities the average MFN tariff rate is 33.4 percent, but when other import-related taxes are added then the traders have to face the total import tax burden of 41.8 percent.

The concept of tariff equivalent incorporates the impact of all NTMs in addition to regular (nominal) tariffs and para-tariffs, and is often many times that of the nominal tariffs. It makes the Indian nominal tariffs are redundant, i.e., meaningless. High NTMs virtually prohibit our exports to India. Thus, India has a 'disguised tariff structure' which shows that its nominal tariff rates are lower, however, all trade hurdles are embodied in NTMs and para-tariffs.

Table4: India's Trade Regime: 2011

MFN Applied Tariff Rate (Overall Average = 12%) Para-tariffs: entry tax, octroi, sales tax, additional surcharges, etc.		**Non-tariff Measures (NTMs)**	**Export-related Incentives**
Manufacturing Average	**Agricultural Average**		
Overall manufacturing: 8.9%. **Textile:** 9.6% (when other import related taxes are added then 23.5%). **Clothing:** 10% (when other import related taxes are added then 22%)	33.4% (when other import related taxes are added then 41.8%)	NTBs (QRs, bans), bureaucratic and administrative mishandling (red tapism) , security clearance, licenses, conformity assessment, accreditation, labelling and marking rules, SPS certificates, country of origin certificate, end-use certificates, state trading, education cess (3%), support price, anti-dumping	Duty remission and exemption schemes, tax holidays in EPZs and export oriented units, central government subsidies for agriculture, state subsidies for electricity, and water, input price controls, concessionary export finance, marketing assistance,

		measures, pre-shipment inspection for imports, visa restrictions and surveillance of visitors to India, banking limitations and restrictive trade routes.	insurance.

Source: WTO (2012).

Potential Tradable Products

The list of products reported in Table 4 is based on the Revealed Comparative Advantage (RCA) technique pioneered by Balassa (1965, 1977 and 1986).[8] Based on this analysis, four different likely effects are discussed in Table 5.

It may be noted that 'industries that are likely to experience losses' with trade opening with India are those where only India, and not Pakistan, exports according to its comparative advantage in the international market or those products where India export without having comparative advantage but it has relatively less disadvantage as compared with Pakistan. These industries include: tea, animal feeds, jute textiles, organic-inorganic compounds, soaps, insecticides, perfumery, rubber tyres & tubes, glassware, cycle, household equipments, miscellaneous machinery, automobile and parts, lighting fixtures & fittings, furniture, footwear, printed matter (Table 5).

Pakistani industries that are likely to face 'weak threat' from Indian imports are those where both India and Pakistan export in international market according to their comparative advantage, yet India has an edge over Pakistani industries. These industries include: spices, starch, manufacture of leather, floor coverings, and wood manufacture (Table 5).

Pakistani industries which can gain after the granting of MFN status to India are those that have an edge over India in terms of comparative advantage or have lower disadvantage over India. These industries include: fish, rice, dry fruits, sugar, cotton, wool, cement, leather, yarn, cotton fabrics, clothing, cutlery, surgical instruments (Table 5).

Industrial users in Pakistan can gain by importing raw materials/inputs/machinery from India where Pakistan is a net importer of these. These raw materials/inputs/machinery include: iron ore, aluminium ore, copper ore, pig iron, metal products, fuel wood, printing book binding machinery (Table 5).

A caveat may be pointed out here. The list of industries given in Table 5 is an indicative and not a precise list. This is because while preparing it only 3-digit level products were considered. To be precise one needs to conduct an analysis at 6- or 8-digit level. This was beyond the scope of this study.

Table 5: Likely Effects of Trade Opening with India on Pakistan Industries

Effect	Major Industry
Industries that can suffer	Tea, animal feeds, jute textiles, organic-inorganic compounds, soaps, insecticides, perfumery, rubber tyres& tubes, glassware, cycle, household equipments, miscellaneous machinery, automobile and parts, lighting fixtures & fittings, furniture, footwear, printed matter.
Industries with weak threat	Spices, starch, manufacture of leather, floor coverings, wood manufacture.
Industries that can gain	Fish, rice, dry fruits, sugar, cotton, wool, cement, leather, yarn, cotton fabrics, clothing, cutlery, surgical

	instruments.
Products where user can gain where domestic production is either zero or negligible	Iron ore, aluminium ore, copper ore, pig iron, metal products, fuel wood, printing &bookbinding machinery.

Source: Based on the Author's analysis.

Likely Benefits of Trade Cooperation

In the context of trade cooperation with India in the aftermath of MFN, following are the benefits and hurdles that are likely to be faced by the Pakistan industries:

- **Trade cooperation a CBM**: Trade cooperation in itself is the most important CBM in the economic and political relations of the two countries. Future relations between two countries will depend on how cooperative are trade relations.
- **Simplification of trade measures**: With one set of MFN tariffs for all countries, it would simplify the rules and makes them more transparent. This will also lessen the problem of establishing and implementing the rules of origin (RoO). It will thus restrict trading partners to take undue advantage from liberalized trading environment.
- **Specialization in production and exports**: Trade cooperation would allow specialization in production and exports this and will thus enhance competitiveness.
- **Economies of scale and scope**: Trade expansion through cooperation means greater opportunities to benefit from economies-of-scale and -scope. This would also allow establishing agglomeration (cluster of industries) and drawing benefits from it.
- **Greater research and development**: Larger firms benefiting from economies-of-scale and scope will have greater opportunities for research and development (R&D). Consequently, the quality and range of products can be improved with trade expansion through trade cooperation.

- **Growth and employment**: Trade cooperation will provide opportunity for sales in bigger Indian markets – more sales means higher economic growth and productive jobs creation.
- **Availability of cheaper and quality goods**: With trade expansion through cooperation, consumer's access to better quality and cheaper goods along with bigger variety of goods.
- **Enhanced trade business**: If no trade corridor is given to India to reach Afghanistan and Central Asian Republics' (CARs) markets then all trade carried out with India directly by Pakistani traders will create employment and business will flourish in Pakistan. If Indians are given a direct access then India may not only dump its goods in Afghanistan that may renter into Pakistan through illegal trade channels. Not only this, Indian traders will also bring back cheaper raw materials to feed their efficient value added industries to produce goods for export to Pakistan, thus depriving Pakistani value added industries who may not withstand to Indian competition.
- **Availability of cheaper raw materials**: Pakistani industry that uses higher import content and are inherently uncompetitive will benefit from cheaper imports of Indian parts and raw materials. Such industries can make long term trade contract for their benefit.
- **Revenue generation**: Mixed results are expected for revenue generation. Tax revenue may increase to the extent of creation of imports and that some smuggling will be diverted to legal trade channels. Conversely, tax revenue may fall because now Pakistan will have to use MFN tariffs rather than non-MFN tariffs.
- **Improved competitiveness**: With trade cooperation, protection may erode in the short- to medium-run for our industries. However, in the long-run with proper adjustment and restructuring of industries they will be able to compete with the Indian imports.

- **FDI inflows**: Regional and international investment to Pakistan may increase; as MFN status and future bilateral trade cooperation may encourage long term collaboration with Indian and other foreign firms.
- **Balance of payments improvement**: With the removal or easing of Pakistan-centric NTMs through trade cooperation agreement, Pakistan may be able to reduce its trade deficit with India.
- **Surge in IIT**: Intra-industry trade is expected to increase and will provide sustainability in trade relations. Because it will create dependency as compared with inter-industry trade.
- **Enhanced role of MNCs**: Many products of India-based multinationals are cheaper in India than in Pakistan; multinationals may further lower their prices if trade opening with Pakistan increases their scale of production. Whereas this will benefit consumers, it will erode protection to Pakistani industries. Some Pakistan based MNCs think that they can penetrate into Northern Indian markets from Pakistan if they are allowed to do so. This will in turn benefit Pakistan in terms of growth, employment, export earnings and tax revenues.

Likely Impediments to Trade Cooperation

Following are the impediments that preclude trade cooperation between Pakistan and India:

- **Non-granting of MFN status by Pakistan**: So far non-granting of the MFN status to India by Pakistan is one of the major hurdles in trade cooperation between two countries.
- **High tariffs and para-tariffs as well as NTMs**: A pertinent question is, will conferring MFN status to India eliminate the so-called Pakistan-centric NTBs? Probably not! It needs to be understood that NTBs on face of them may not be Pakistan-centric. But, the way NTBs are mis-handled by the Indian officials make them extremely harsh against Pakistani exports. It may

be underlined that high trade restrictions results into high incidence of smuggling and trade misinvoicing that in turn circumvent the very objective of our trade policy.

- **Subsidization**: India provides subsidies to its local industries and agricultural commodities of interest to Pakistan (see, Table 4).
- **Customs Procedures**: Cumbersome customs procedures and non-transparent regulations. Pakistan and India signed Customs Cooperation Agreement (information, data, and harmonization) in November 2011. Let us see how it is implemented.
- **TBTs**: India's TBTs are very stringent, they discriminate against our exports. Different agencies and states follow different standards. It often becomes difficult for our exporters to meet these standards as our national standards are not recognized by India. Pakistan and India signed Limited Mutual Recognition Agreement (standards) in November 2011.
- **Lax enforcement of IPRs**: Insufficient protection of industrial property rights (patents, trademarks, etc.). And different standards of enforcements create hurdles for our exports to India.
- **Fierce Competition**: Fierce competition from established players in the Indian market denies entry for new potential entrants from Pakistan.
- **Lack of Exportable Surplus**: Lack of exportable surplus of desired specification and absence of required structural changes denies the available export opportunities in India.
- **Lack of Competitiveness***:* Lack of competitiveness and competitive nature of export products in two countries.
- **Lack of Standardization**: Lack of standardization, differences in specification and poor quality of products.
- **Lack of Information**: Lack of information in terms of export potential, import needs, domestic economic policies and infrastructural facilities.

- **Inadequate Transportation**: Inadequate transportation, logistics and communication infrastructure: only one active border post.
- **IS Policies**: Import substitution policies of the past era still remain prevalent in both countries that do not encourage them to take decisive measures for trade opening.
- **Smuggling and Trade Misinvoicing**: Illegal trade flows (smuggling and trade misinvoicing) are prevalent across the border. Cost of smuggling is much lower as compared to MFN tariffs and tariff equivalent.
- **Lack of Banking Facilities**: Lack of banking facilities in each other's country. A move is recently made.
- **Non-Existence of Dispute Settlement System**: Non-existence of dispute settlement institution or body where traders can settle trade disputes. In this regard, a "Redressal of Grievances Agreement" (commercial disputes resolution mechanism) was signed in November 2011.

Strategic Directions

Current magnitude of trade deficit with India warrants that Pakistan should explore all possible avenues to expand its exports to India. One such possibility that is in Pakistan's interest and is likely to be beneficial for us is to negotiate a Trade Cooperation Agreement with India in the aftermath of the MFN treatment. This is also because after the MFN treatment the size of trade deficit is likely to go up further. The exact extent of trade cooperation will depend on the nature of complementarities and competitiveness of our tradable goods. Pakistani policymakers face an uphill task from challenges that demand a balance between protectionism and export growth. This can be achieved by having an equitable trade cooperation agreement that will ensure fair, sustainable and mutually beneficial trade relations.

Given the impediments and challenges to Pakistani trade, how the policymakers go about from here to further develop

Pak-India trade relations. I put forward the following strategic directions (SDs).

- **SD 1**: Enter into a Trade Cooperation Agreement with India. Minimum level of trade cooperation is granting of MFN. Without it there is no justification for trade cooperation. Of course, in the near future full-fledge cooperative trade relations might not be possible. In the absence of normal political relations, if we become extremely dependent on India, any event like the 'Mumbai' can jeopardize all the success achieved by the two countries and India can adopt the beggar-thy-neighbor policy as it did back in 1948. A Comprehensive Trade Partnership Agreement may be considered once Trade Cooperation Agreement delivers positive results. But at this moment it is out of sight.
- **SD 2**: Preparing domestic industry for post-MFN stage.MFN will effectively liberalize our trade regime and our industries will face a very different and unprecedented environment to which they are not accustomed. Therefore, we need to devise very special measures to cope with the upcoming situation.
- **SD 3**: Leveraging and expanding the existing industrial strength. This can be achieved by enhancing competitiveness of export firms by introducing better technology and diversification in production.
- **SD 4**: Creating complementary specialization and IIT. Trade can both be competitive or complementary in nature. Those who take the myopic view emphasize more of competitive nature of trade and hence would like the use of safeguard measures to protect local industry. But in the long run for sustainability and growth of trade Pakistan needs to also promote trade complementarities and encourage IIT.
- **SD 5**: Encouraging re-export activities after MFN. Re-export is likely to be major activities in the future. Therefore, Pakistan needs to develop special trade policies for trans shipment to CARs, Afghanistan and China exclusively through its traders and not directly by the Indians.

- **SD 6**: Improving customs, transportation and logistics infrastructures. To materialize trade expansion both countries would need to cooperatively work on the improvement of physical and institutional infrastructure. With the present infrastructure arrangements, it would be very difficult to accomplish the trade potential.
- **SD 7**: Improving trade facilitation measures. It includes faster border crossing of cargo, streamlining of documentation requirements, coordination of border agencies, opening up of new border crossings and strengthening of the existing ones, strengthening of customs clearance procedures to facilitate movement of bulk and low volume cargo, improvement of electronic data interchange, telecommunications, and easing of visa restrictions. What is essentially needed is to improve the trade facilitation system to make whole of our supply and value chains competitive and dynamic.
- **SD 8**: Asking India to remove Pakistan-centric NTMs. Stringent Indian NTMs often act as a de facto barrier to trade. Therefore, in future trade negotiations with India, Pakistan should push forward for the elimination of Pakistan-centric NTMs (especially, the use of their handling procedures for Pakistani exports). Concomitantly, Pakistan needs to put its own house in order. In this context, traders and businesses should proactively engage with the government and support governmental efforts. A participatory approach is the need of the hour to identify most problematic trade barriers and to find and implement suitable solutions.
- **SD 9**: Rationalizing and simplifying TBTs and SPS measures. These are the major hurdles in trade of two countries. Streamline standards, quality controls, technical regulations, material testing, etc. Harmonize legal regulations for IPR. Remove procedural difficulties to open up commercial bank branches in two countries. Banking services are essential for letter of credit (LC) opening and cross border transfer of funds. Sanitary and phytosanitary as well as laboratory

inspections of one country should be accepted in the other country.

- **SD 10**: Improving Pakistan's trade regime. Use 'escape clause' to allow protection to declining industries. This WTO clause provides a basis to safeguard domestic industries. The rationale for safeguard protection is to give an industry sufficient time to adjust or restructure to vigorous import competition. Safeguard provisions include anti-dumping duty, countervailing duty, infant industry protection measures, emergency protection, balance of payments measures, and national security. Since safeguard provisions are holes in the multilateral trading system, as they can seriously undermine trade liberalizing dynamics; therefore, safeguard measures need to be imposed on a non-discriminatory basis.
- **SD 11**: Assigning the role of market intelligence collection to commercial attaché in India. Indian ambassador is proactively engaged in such activities in Pakistan; likewise Pakistani diplomats should be vigilant in India. Market intelligence collected by Pakistani diplomats should cover Indian Central and State policies regarding tariffs, para-tariffs and NTBs besides others, and information about competitors from other countries in Indian markets.
- **SD 12**: Introducing pragmatic and realistic measures. We should not be defensive in our policies. Because defensive policies are doom to be a failure. Get benefits from upcoming opportunities, where possible exploit them. This is the way international trade works. In our policies, it appears that we only care about industries. We should equally care about traders, businesses, transport companies, and other support companies because they also create national income and generate employment. As there are always certain losers and gainers. It is the job of the government to develop schemes of compensation to losers by taxing a bit to gainers, this is necessary for the required restructuring.
- **SD 13**: Penetrating Indian Markets. In all those items where Pakistan exports in international market on the basis of comparative advantage while India does not,

Pakistan should penetrate in Indian markets by utilizing its underutilized capacity or by enhancing the existing capacity. In this regard, improvement in productivity of industries should also bring forward larger exportable surpluses.

- **SD 14**: Obtaining Cheap Indian Raw Materials. Irrespective of the fact whether India has a comparative advantage or not in producing raw materials, if it can deliver raw materials to Pakistan at cheaper rates than the rest of the world, it should obtain these raw materials from India to feed its value added industries.

Concluding Remarks

One thing is very clear that life after MFN will not be the same and easy as protection to domestic industries will be eroded. Trade will introduce competition that Pakistani import-competing industries will face from Indian products in Pakistan, and Pakistani export firms will face from third countries' exporters as well as from Indian industries inside Indian markets. Incidentally, Pakistani industries are already facing *de facto* competition from Indian smuggling and trade misinvoicing as well as from international competitors in our export markets. This is an encouraging sign. Profit after the grant of MFN status will not be so easy for our firms with inertia of past policies. With granting of MFN status it is expected that immediately all the Indian goods coming from third world countries will become India's direct trade; however, a part of border smuggling will continue, as the cost of smuggling in general is much lower than the MFN tariff equivalent. All in all, there will be an import surge from India that will definitely pressurize our balance of payments and industries. To cope with the situation adoption of above strategic directions will reform and prepare Pakistani industries to effectively face the upcoming competition from the Indian trade.

A Trade Cooperation Agreement in the future would further facilitate trade. This may be implemented at the beginning without any institutional mechanisms in place. It should be treated different from a Comprehensive Trade Partnership Agreement where an institutional framework is drawn out to improve economic and technical cooperation. For instance, by having a Joint Council whose role would be to periodically define guidelines for economic cooperation.

We conclude on a cautious note. That is, Pakistan needs to be vigilant! Unless India becomes a trustworthy trading partner and neighbor, our too much dependency for trade on India may be injurious for our industries and the economy. We witnessed back in 1948 that to impose its policy of devaluation on Pakistan, India refused to import anything from Pakistan. Thus, we should carefully manage our bilateral trade relations with India and watchfully and skill fully move forward in developing cooperative trade relations.

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Notes

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[1] Both India and Pakistan granted the MFN status to each other after ratifying the GATT in July 1948. This relationship between the two countries continued till 1965. Trading halted between the two countries after the war of 1965. Trading relations, however, resumed after the *Shimla* agreement, with four items on the 'positive list'. India granted MFN status to Pakistan in 1996, at which time Pakistan did not reciprocate.

[2]Pakistan is also granting MFN treatment to non-WTO countries.

[3]Because the initial contracting parties to the General Agreement to Tariffs and Trade (GATT) were quite small, 23 in numbers, the benchmark for MFN is the best treatment offered to any country.

[4]See, Batra (2004), CII (2005), Kemal, *et al.* (2002), Mahmood (1996), Mukherjee (2005) and Nabi and Nasim (2001).

[5]This index measures the degree to which the export pattern of one country matches the import pattern of another. A high degree of complementary index is assumed to indicate more favorable prospects for a successful

trade arrangement. Value of zero indicating no overlap and 100 indicating a perfect match in import-export pattern.

[6]Competitiveness is defined as the capacity of an industry to increase its share in international markets at the expense of its trading rivals. It is thus an index of market power. See, www.unescap.org/tid/aptiad/index_cmpl_fm.aspx.

[7] Para-tariff is a charge on an imported good instead of, or in addition to, a tariff. It is also called a "secondary tariff." In practice, para-tariff has the same effect as of a tariff.

[8]The RCA index suggests that it may not be necessary to include all factors affecting a country's comparative advantage in the analysis. Instead, the index proposes that comparative advantage is "revealed" by observed patterns, and in line with the theory of international trade, one needs pre-trade relative prices that are not observable. Thus, inferring comparative advantage from observed data is named as "revealed comparative advantage (RCA)" (see,Mahmood and Al-Haji, 2009).