7 CONCLUSION

Pakistan has recorded persistent trade imbalance with India during the last ten years. The growth in bilateral trade between Pakistan and India over the years has been dismal and quite volatile. Low volumes of trade and low trade integration between the two countries have their roots in their respective trade systems, as both India's and Pakistan's trade regulations are relatively restrictive. Despite recent reforms to open up trade, India's average tariffs remain relatively high at 22.2 percent in 2003 compared to 14.9 percent in Pakistan and a developing country median of 11.2 percent. India has the largest number of tariff peaks in South Asian Region, which are concentrated in the agricultural, automobile, and textiles and garments sectors. In addition, India's most complicated and pervasive non-tariff barriers as well as export subsidies and domestic protection have made difficult for Pakistani products to enter into Indian market.

There is substantial scope for improving trade between the two countries. The potential of trade estimated by various reports ranges between $0.75 billion to $6.5 billion. The trade compositions of India and Pakistan reveal that there are 1181 items worth $3.9 billion which are common between Pakistan's exports and India's imports during FY04. Potential of exports is estimated at $2.5 billion for 692 items under which Pakistan's export unit values are less than that of Indian imports. Similarly, against 2646 common items of Pakistan's imports worth over $7 billion in FY04, India had exports worth over $15 billion. Potential of imports is estimated at $2.7 billion under 48.7 percent of these items, for which the unit values of Pakistan's imports are more than the unit values of India's exports**.** Even after excluding the items which are currently permissible for imports from India; about 45 percent of the items remain in the common list which could be imported from India at a lesser cost than the current cost of import from the rest of the world. It is estimated that allowing import of such items from India (i.e. expanding the current list of positive items) the average saving for Pakistan could range between $400 million to $900 million.

In terms of Revealed Comparative Advantage (RCA), although Pakistan ranked above India in both textiles and clothing sectors, this advantage should be interpreted cautiously. The higher magnitude of RCA Index in case of Pakistan shows the country's vulnerability of export earnings to the sector specific events. Pakistan's economy is far less diversified as compared to the Indian economy and depends heavily on the textile industry. Textile sector still represents 46 percent of total manufacturing and provides 65.6 percent of Pakistan's export receipts. Unless efforts are made to improve this situation, granting unrestricted access to Indian textiles in Pakistani domestic market may have serious repercussions for the whole economy.

The comparison of textiles exports of both Pakistan and India identifies 176 common items which have comparable unit values. Out of these 176 items, India has a price advantage, i.e. lower realized export unit value in 48 textile products while Pakistan has price advantage in 128 textile products. Since other factors like quality, production and design of products, etc. are also important, it is hard to conclude on the basis of just export unit value that granting of MFN status will result in a uni-directional flow of textile products, i.e. Indian products flooding the domestic market of textile products.

In the iron and steel sector, the average import unit value of Indian iron ore during FY04 was slightly higher than the average import unit value of total iron ore imports primarily due to the considerably cheaper imports from Iran. It is, therefore, unlikely that the imports from India would be able to maintain its dominating supplier status. Under the iron and steel products, about 47 items are identified that are cheaper to import from India on the basis of lower unit value of Indian exports compared to the import unit value of Pakistan's imports from the rest of the world. Besides, the quantum of items being already imported can also be enhanced.

During FY03 and FY04, Pakistan imported 4.3 percent and 6.8 percent of its total import of chemical and pharmaceutical products respectively from India. Out of total imports of $2.9 billion (1105 items) in FY04, India supplied 353 items worth $196.8 million. Out of total imported chemicals and pharmaceutical products from India, 166 items had a lower unit value of imports compared to the unit value of the same items imported from elsewhere. These items have the potential for enhancing imports from India.

The potential advantages for Pakistan appear to be generally large, reaching from lower prices, higher choice for consumers, and increased efficiency and market access for producers to higher revenue for the government. Moreover, trade liberalization with India can foster economic growth and broaden the process of regional integration as well. Complete elimination of tariffs under SAFTA may increase the intra-regional trade by 1.6 times the existing level. At the aggregate level, Pakistan and India could increase their bilateral trade by 79 percent, by entering a PTA. This needs to be viewed against the cost of non-cooperation, which was estimated by an earlier RIS study to be about $ 511 million for Pakistan, and a peace dividend of $2.6 billion in another study.

Pakistan's ability to benefit fully from bilateral trade opportunities will depend on successfully seeking greater access to the Indian market. Currently India's trade regime offers limited access to some important segments of its domestic economy, especially in agriculture, manufactured goods and consumer goods. To ensure that Pakistan's producers in the northern part of the country are not exposed to a sudden increase in competition on account of lower transport costs, most of the import trade should be initially conducted through sea-lanes. Once the interest of domestic producers has been protected, the land route can be opened to most commodities. Restricting the land route for trade in early stages will also limit smuggling while proper customs facilities are developed at border points. In case of those imports for which India is the principle supplier, protection can be ensured to domestic producers with tariffs on MFN basis.

Granting MFN status to India is an economic issue with international repercussions. Being a signatory of WTO, Pakistan is required to open its markets for India without any discrimination. In case, Pakistan grants MFN status to India, it will have to dispense with the present importable list and ease other non-tariff barriers on items to be importable from India. At present, high tariffs and non-tariff barriers in India are one of the major obstacles to grant the MFN status to India and liberalize trade between the two countries. Pakistan can only benefit from granting MFN status to India if the latter ensures a level playing field by removing some non-tariff barriers and reduces tariff on items of interest to Pakistan**.** In order to resolve this issue and tap the potential to push the process of bilateral economic co-operation ahead for the benefit of both sides, the India-Pakistan Joint Study Group (JSG) on Trade and Economic Cooperation has been constituted.

Pakistan and India have already signed SAFTA agreement. Sri Lanka, Bhutan and Nepal have already signed bilateral free trade agreements with India. Now both the countries should prepare themselves in terms of quality and effective marketing to face the global challenges in the face of the WTO whereby there will be no barriers in global trade.

Access to Indian markets can be negotiated in a bilateral framework. Keeping in view the balance of payments concerns, Pakistan should initiate negotiations, to seek phasing out of restrictions on its exports to India. There are recent precedents of bilateral negotiations between major trading partners in response to growing trade imbalances arising due to trade restrictions, e.g. US-Japan trade negotiations.

Pakistan can also adopt a stepwise approach: initially expanding the list of importable goods to include industrial raw materials (dyes, chemicals, paper, plastic, iron ores, etc.) from India which are already being imported from other countries for Pakistani industry and more cheaply available in India. Such imports will be cheaper and save precious foreign exchange by saving the transport cost also. The list can be gradually extended in response as India offers more access to Pakistan's exports. Meanwhile, Pakistan can expand the list of permissible imports to include all those items for which Indian tariffs and quantitative restrictions equivalents are equal or to lower than tariffs in Pakistan.

One of the major factors of Pakistan's lower exports to India is that the Pakistani goods are deficient in competitiveness. In a world of cut-throat competition, a country needs to offer high quality and cheaper products to increase its share in the export market. For increasing its exports to Indian market, local industries must be strengthened through government patronage; technical support and information back-up to improve their viability to match in quality and price with the Indian products.

The infrastructure and other facilities available in Pakistan's Export Processing Zones (EPZs) provide enormous potential for Indian investors which could be utilized to establish joint ventures between the two countries. Moreover, the establishment of

Special Economic Zones at Gawader and other cities (like China and India) offering exemptions from various taxes, import and labor laws besides providing manufacturing facilities and raw materials at international competitive price may also be a good option to attract foreign direct investment. Potential sectors for joint ventures include: agricultural products, food processing, auto spare parts, minerals, chemicals, pharmaceuticals, leather, textiles, tires, information technology, telecommunication, power and natural gas pipelines projects etc. There is a need to set up an institutional mechanism in both countries to guarantee each other's investment.