

Trade on Human Terms¹

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Let me first warmly welcome Dr. Hafiz Pasha, UN's Assistant Secretary-General and Director for UNDP's Regional Bureau for Asia and the Pacific, and Mr. Haoling Xu, Country Director, UNDP Pakistan, and acknowledge UNDP's initiative of launching the Asia-Pacific Human Development Report. This report enhances the scope and depth of the debate on trade and offers valuable insights, messages and recommendations. Its main contribution is in providing a human context to trade liberalization. Unless addressed effectively, factors such as the lack of education, skills and work force productivity, along with poverty and income distribution implications arising from trade, can threaten trade competitiveness and prospects. Appropriate responses to these concerns will help, among others, to reinforce the achievement of the Millennium Development Goals.

In my brief presentation, I would like to comment on :

- (i) Changing trade dynamics and patterns which have regional and global dimensions;
- (ii) How Pakistan has positioned itself within the aggressive trade environment; and
- (iii) What is the future direction and policies being adopted by the Government to ensure export growth sustainability, and to withstand competition.

Changing Trade Dynamics and Patterns

Asia, as is well acknowledged by empirical evidence, has enjoyed an exceptional growth in trade in the 1990s. Consequently, Asia's share in world trade has doubled over the period 1990s-2003, and reached 30%. In some commodities this share has exceeded 50% of world trade and it is projected that this momentum will continue. What is amazing is that the phenomenal growth of the past decade has been largely private and market led though it has been accompanied by interesting regional alliances and investments.

Within Asia there are clear trends and changing dynamics which have both regional and global economic and social consequences :

- (a) Within Asia, 97% of trade comes from East Asia;
- (b) Emerging significance and size of China and India offers new opportunities and poses a threat to the regional comparators;
- (c) Changing trade dynamics with ASEAN are being well observed, its competitiveness is being hurt because of the regional complementarities and similarities within economies and a shift in investment from this region to China from Japan, Korea and other regions;
- (d) The equation between the least developed and less developed countries is changing; while the former is being offered some special privileges and concessions, the latter is facing complexities.

¹ Address at the launch of UNDP's Asia-Pacific Human Development Report 2006, "Trade on Human Terms", at a joint conference held by the State Bank and the UNDP at the Learning Resource Centre, SBP Karachi, on August 25, 2006

Trade Liberalization in Pakistan

Let me first get some facts out of the way. During the process of trade reforms in Pakistan, by FY01 the maximum tariff rate was reduced from 65% to 25%, tariff slabs were reduced from 42 to 4 in FY02,² and the average tariff on agriculture inputs was also reduced. Consequently Pakistan has become one of the least protected countries in South Asia. Trade openness as a percentage of GDP has also improved from 25.8% in 1999-00 to 34% in FY06.³

Impact of Trade Liberalization

So has Trade Liberalization led to any improvements in the economic and human development indicators ?

So far the post-liberalization period has witnessed an improved export performance which gathered pace particularly after 1999. Pakistan has registered an impressive performance as exports for FY06 stand at US\$ 16.5 billion, which is double the level of the US\$ 8.6 billion in FY00, with most of the growth occurring in the textile sector. There were concerns that the performance of Pakistan's textile and clothing (T&C) exports would suffer after the phasing out of the MFA regime, but these fears were largely unfounded as the T&C exports have actually shown an increase from January 2005.

There are two major ways through which increased trade openness has contributed to this impressive export performance. First, due to import liberalization, tariffs on raw materials and capital goods have come down at a higher rate, which has in turn increased the production efficiency of the exports. Secondly, increased competition has to some extent displaced the inefficient domestic production of import substitutes and consequently more investment has flown towards exports. This process was slow in the beginning but gained pace subsequently as capital investment increased manifold in the textile sector enabling textile exports to achieve extremely impressive growth rates in the post 1999 period. However, we are still in the process of achieving diversification in the export base and markets.

Regarding the impact of trade liberalization on growth, a simple time series analysis⁴ reveals that during the trade liberalization period, growth initially slowed down, before picking up again, and reaching a high of 8.6% in 2005. However, this kind of analysis can at most be indicative as a causal relationship cannot be estimated through this method. World Bank, in one of their recent studies, concludes that trade openness is one of the statistically significant variables which explain Pakistan's growth.

In line with the focus of the Human Development report, it would be pertinent to analyze the impact of trade liberation on human development in Pakistan. The overall incidence of poverty, measured in head count ratio, has come down in recent years. However, since there were many other factors at work in the process of economic growth, therefore one cannot easily attribute this reduction in poverty to trade liberalization alone.

The relationship between poverty and trade liberalization has been estimated in SPDC's Annual Review 2005-06⁵ according to which there is an inverse relationship between tariff

² Pakistan: Growth and Export Competitiveness, World Bank, 2006

³ Economic Survey of Pakistan, various editions

⁴ As undertaken in various studies

⁵ Trade Liberalization, Growth and Poverty, SPDC Annual Review 2005-06

reduction and poverty. However, their overall conclusion is that since trade liberalization leads to increased growth therefore positive aspects are captured therein.

Future Direction of Trade Liberalization in Pakistan

The Human Development report has discussed some of the possible concerns which a developing country may have to address while liberalizing its trade regime. It has given specific recommendations as well as an eight point agenda. I will discuss the areas which are relevant to Pakistan in the context of the recommendations given in the report.

a) The pace and nature of the reforms

A developing country has to adopt a measured approach aimed at lowering the tariff and non- tariff measures in a phased manner. Pakistan has adopted an escalating tariff structure with higher tariffs on consumer goods, and comparatively lower tariffs on intermediate and capital goods. This approach has allowed Pakistan to make a smooth transition in becoming a more open economy without incurring high social costs.

b) To support trade promotion the Government is now focusing on the development of supportive Infrastructure

In the Federal Budget FY07, out of the PSDP of Rs.270 billion, Rs.119.5 billion has been allocated for the development of physical infrastructure and roughly the same amount, i.e. Rs. 119 billion, for social development. The share of development expenditure in the total budgetary outlay has increased sharply to 33.1% as against 25.5% in FY06. In a focused infrastructure improvement program, National Trade Corridor Plan (NTCP), all the major sub components of physical infrastructure such as ports, roads, railways, aviation etc are targeted for further development and improvement. Moreover, it also aims to reduce procedural bottlenecks and tariff costs to bring them in line with regional averages.

Likewise for trade promotion, over the years Government has been taking steps such as organizing international trade fairs, seminars etc to increase the marketability of Pakistani products. The Ministry of Commerce has also announced a number of steps in the Trade Policy for FY07 which aims at increasing exports. These include :

- Establishment of the Trade Development Authority of Pakistan (TDAP)
- Establishment of a specialized SME Export House as a corporate entity with public private partnership, run by professional management.
- Simplification of temporary export procedures
- Steps to improve the skill level in the textile sector
- Amendments in the Long Term Financing for Export Oriented Projects (LTF-EOP) with the help of SBP.
- Zero rating of Tariffs on sectors with export potential, and other import liberalization measures.

c) Agriculture

Agriculture is especially vulnerable to trade liberalization as the local farmers are poor and the terms of trade in this sector are heavily skewed towards developed countries. In Pakistan, although we have liberalized the agriculture sector and have reduced subsidies on inputs, but at the same time we have also increased the support prices and the availability of agriculture credit. So we have been careful and have followed a balanced approach but since agriculture employs a substantial portion of our

population, I feel that going forward, we have to be very vigilant and proactive in this sector.

d) Increase in competitiveness

We need to get beyond the emphasis on cheap labor as the only way to increase competitiveness. Too much focus on this aspect is in fact detrimental to the welfare of the workforce as it will promote subsistence wages and hamper the ultimate objective of improving the standard of living of the population. The most important aspect to focus on is the productivity and skill level of the work force. The traditional structure of our domestic economy has lacked a focus on competitiveness, enhanced quality, or increased productivity of the industries. With rapidly disappearing protections, only a trained, efficient, productive and innovative workforce can meet the challenges of globalization.

In recognition of the importance of this factor, the Government of Pakistan has allocated an amount of Rs. 28.2 billion on technical education and Rs.5.6 billion on skill development under the MTDF. Several other steps have also been taken in the Trade Policy 2006-07.

Long term improvement in the quality of workforce can only be brought about by improving the education system in the country which presently is one of the most underdeveloped systems in the world. In this regard, the Government has decided to give a higher priority to education as social development allocation has also been increased. It is planned to raise the total public allocation for education to 3.6% of GDP by 2010, and private sector expenditure is expected to add another 1.5 percent.⁶ However, a lot more needs to be done in order to achieve the desired results.

e) Multilateral and regional Cooperation

The current failure of Doha Rounds is undoubtedly a great setback as successful negotiations would have given the opportunity to developing countries to have greater access to the international markets. The collapse of talks has necessitated that developing countries consider other options and one such feasible option is to have a regional focus. In this regard, Pakistan is a member of SAFTA⁷ which is a regional agreement among the seven South Asia countries that form the South Asian Association for Regional Cooperation (SAARC): Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. SAFTA came into effect on 1 January 2006, with the aim of reducing tariffs for intra-regional trade among the seven SAARC members. Pakistan and India are to complete implementation by 2012, Sri Lanka by 2013 and Bangladesh, Bhutan, Maldives and Nepal by 2015. It replaces the earlier South Asia Preferential Trade Agreement (SAPTA) and may eventually lead to a full-fledged South Asia Economic Union. So going forward, Pakistan is by and large on the right track.

⁶ Medium Term Development Framework 2005-2010, Planning Commission of Pakistan

⁷ South Asia Free Trade Agreement

Future Direction and Policies

Going forward, the Government has taken several initiatives. Due to fierce competition, unit prices in the textile sector are declining. Secondly in the European market, we are disadvantaged due to the imposition of anti-dumping duty on bed-linen. The Government however has made intensive efforts to neutralize our handicaps, as a result of which the European Commission has reviewed the anti-dumping duties on bed linen and reduced it from 13.1% to 5.8%. Furthermore Pakistan was also made a beneficiary of the new EU GSP scheme, under which our textile products imported into the EU will be allowed a 20% concession on the MFN Tariff, whereas for non-textile items the EU import tariff will be reduced by 3.5%.

Additionally, Pakistan is seeking from the US increased market access in textiles, of around US \$2 billion per year. If this initiative materializes, 400,000 new job opportunities would be available in the country, with a direct impact on poverty. Issues concerning the Bilateral Investment Treaty (BIT), Reconstruction Opportunity Zones (ROZs) and Trade and Investment Framework Agreement (TIFA) are currently also under discussion.

In conclusion, I would like to say that although the way forward for Pakistan and for that matter, the Asian region as a whole, is an increased volume of trade, but there is greater need for the terms of trade to incorporate human development concerns.