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Editor's Corner

Dear Readers,

Recent months have witnessed an unprecedented intensification in property prices. A situation has arisen where owning a property is now beyond the reach of the middle- and lower middle-income strata of the households.

Demand for housing, a basic human need, has swelled over the years. This is attributable in the urban areas largely to the rural-urban migration and due to rising incomes. This has placed tremendous pressure on basic utilities and infrastructure. As planned development of affordable land has not been able to match the demand for housing, there is a growing shortage of affordable housing units. The phenomenon of auctioning residential land, and in the past even in the sites and services schemes meant for the poor, has resulted in the less well off being denied access to these pieces of property. Speculators have moved in and pushed up the prices beyond the reach of the common man. One, therefore, sees the growth in squatting on available open spaces and other government land, at the instance of a few professional land grabbers, resulting in the sprawl of the katchi abadis. Even this has to be paid for by the poor, not to the state, but to the land grabbers. This is indeed an unfortunate situation which requires much needed rectification and reform.

There is ample evidence to show that in all urban cities of Pakistan, growing urban population without any adequate provisioning of housing facilities has seen the birth of many slum areas, as squatter settlements or katchi abadis are found everywhere in Pakistan. The Governments in Pakistan themselves estimate that on the average in the Punjab, some 35% of the total urban population lives in katcha houses, and another 11.5% in semi-pucca houses. This implies that the population of katchi abadis is at the very least about 50 percent. In Karachi alone, it is estimated that more than half the population resides in katchi abadis. This has turned the metropolis into a large unplanned urban sprawl.

The price of property, across the spectrum of the urban areas in the country, ranging from the primate cities to the smallest urban settlements (no more than expanded villages) have risen for a variety of reasons. The large influx of home remittances following the 9/11catastrophe needed avenues of investment. The erratic behaviour of the stock market, the falling interest rates on savings instruments and the rising incidents of day-light dacoity left little or no choice, but to invest into property. This was a case of a large number chasing a small basket of available properties. Property owners soon realised that they were sitting on gold mines in a sellers' market. This caused the exponential increase in property prices, not just in land, but also in built-up houses.

The second reason was the low interest rates at which consumer finance was available to those with money. The banks were flush with surplus liquidity with no choice but to lend for consumption financing, such as for cars and other consumer durables. The highest rate of return was seen to be in land purchase. The price of land increased disproportionately more than the price of houses.

The third reason was the apparent security that this avenue of investment provided. All other forms of investment, barring only the purchase of precious metals and jewellery, attracted taxation on the capital

in the form of withholding taxes on incomes derived, and Zakat on the capital value of securities and deposits, and also exposed one to the need to declare the overall incomes and wealth. There was also the perception that investing in financial instruments would expose one to the tax authorities at some stage.

The fourth reason is its attractiveness as a hedge against inflation. Historically, land prices have tended to rise faster than inflation, thereby increasing wealth in real terms.

The phenomenon of rising land prices is not confined to the elite areas of the country's fabric of real estate, such as in the Defence Housing Authority schemes in all large towns, and the sites and services schemes of the Development Authorities and the Housing and Physical Planning or Housing and Urban Development Departments. The lands and properties situated in the DHA and defence forces housing schemes are the preferred option for most local and overseas Pakistanis for a variety of reasons. The least of these are the fast track transfer and titling system: with only a nominal transfer fee. Interestingly enough the real estate agents make more money than the state in any case. Their fee is 2% of the actual transaction price. The stamp duty is paid on declared value as is the mutation fee. The declared value is in most instances a small fraction of the transaction price. More interestingly, since the real estate agent receives his commission in cash even this is free from income tax.

In addition to better economic conditions, the diversification of banks' lending portfolios, whereby they have ventured into housing finance has resulted in increased construction activity, so enhance demand for land. People now prefer to get bank loans, purchase property, and pay monthly instalments to the bank rather than paying monthly rents. In this way they become owners of the property in due course of time.

The levying of additional development charges by the Defence Housing Authority in certain phases of Defence area, where the transaction were the highest will probably bring about some correction to the sky-rocketing prices of recent months. The State Bank of Pakistan has restricted banks/DFIs to not allowing Housing Finance for the specific purpose of purchasing land/plot; rather such financing would be extended for the genuine purchase of plot/land and subsequent construction schedule shown by the borrower. However, these are only a drop in the ocean of reforms that are required to end speculative investment into real estate.

One possible option is the re-introduction of capital gains tax and the need to produce evidence that the money invested into the property is legal – evidenced by an income tax clearance certificate. Also, on the supply side, the government should make more land available in all urban cities to reduce the price pressure on existing plots. Even though the latter may open a new channel of corruption, its benefits for the less well off in society would be that they could start to dream of becoming property owners owing to the reduction in the real estate prices these actions would cause.

Finally, to kick-start the construction industry which is so critical to economic growth, it is essential that land prices are at a level which would make housing affordable.

Ayesha Mahmood

Abstract of the Bulletin

Regional Trading Blocs

§ In recent years, there has been a growth in the number of regional trade agreements. They seek to reduce trade barriers between member countries, so stimulate regional trade.

§ There are different objectives for countries to form a regional arrangement.

§ When countries become members of a bloc, certain benefits accrue. These include among others, creation of larger markets which may assist in attracting foreign direct investment; increased competition amongst producers so allowing consumers to buy products from the cheapest source and promoting efficiency.

§ The formation of NAFTA has had a positive impact on Mexico. It helped the country come out of the crisis and record a growth in output, increase the trade with NAFTA partners, raise the share of exports/ imports to GDP, increase the diversification of exports and enhance inflow of foreign direct investment.

§ Pakistan – SAARC intra trade has been around 4%, while other regional blocs like the EU and NAFTA have larger intra bloc trade.

§ South Asian Free Trade Agreement is expected to strengthen intra-SAARC trade and economic cooperation.

§ Improved Pakistan-India relations could enhance trade in the SAARC region and result in economic and other benefits for the people of the region.

§ Research has been done to study regional trading arrangements in the WTO context. Often regional trade agreements support the WTO's multilateral trading system.

§ A World Bank study has shown how expanding opportunities for international trade can accelerate the progress towards poverty reduction.

Textiles & Clothing – Post Quota Regime

§ Global trade in textiles and clothing will face a big challenge from January 1, 2005, when export quotas will be eliminated.

§ End of the quota regime would increase competition among the major players in the international market.

§ A WTO study has shown that China and India will substantially increase their world market share in textiles and clothing.

§ Major investment has been made in Pakistan's textile industry, so to improve production quality and move towards more value added exports.

Pakistan and WTO

§ The WTO system has certain Agreements: Multilateral Agreement on Trade in Goods, General Agreement on Trade in Services and Agreement on Trade Related Aspects of Intellectual Property Rights.

§ Pakistan has taken a number of key initiatives in compliance with WTO Agreements.

§ Initiatives taken aim at strengthening technical institutions capabilities in standard setting, laws/amendments promulgated to provide intellectual property protection, reduction of tariff and non-tariff barriers, bringing improvement in productivity and quality standard of local industry etc.

Pakistan's External Sector

§ Pakistan's exports rose to over $12 billion in FY04, while imports climbed to $15.5 billion.

§ Textiles, rice and leather manufactures were the largest contributors towards enhanced export earnings.

§ The trade deficit has deteriorated in the first quarter of FY05.

Market Analysis

§ Despite some volatility, the market failed to break out of its narrow trading band during September and October. The KSE-100 Index lost a net 14.5 points over the two months to close at 5332. A weak September was followed by gains in October as a result of good corporate performance and high oil prices buoying up the large cap oil stocks.

Regional Trading Blocs

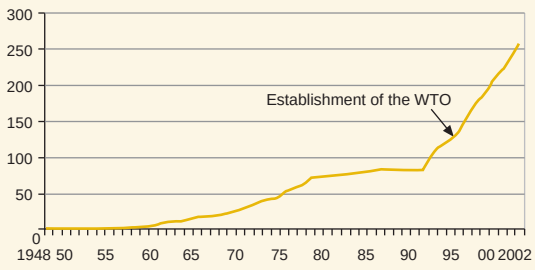
Growth of Regional Blocs

A major development in the trading realm has been the growth of regional trading blocs. Most countries –– industrial and developing are members of one of the many blocs, at times they belong to more than one. For example Mexico is a member of NAFTA, APEC Group of Three and LAIA, Pakistan is a member of SAARC and ECO, Bangladesh and India are members of SAARC and of Bangkok Agreement, Brunei, Indonesia, Malaysia are members of ASEAN and EAEC, Singapore and Thailand are members of ASEAN and EAEC.

Structure of RTAs

The structure of regional trading arrangement (RTA) varies greatly, but they have on thing in common – reducing barriers to trade between member countries. Recent years have seen a growth in their numbers; by May 2003, over 265 RTAs had been notified to the GATT/WTO, of which 138 were notified after January 1995 (the year WTO was created). Over 190 are currently in force; another 60 are believed to be operational although not yet notified (although some no longer exist or they remain insubstantial). Their numbers are expected to rise to nearly 300 by the end of 2005. The agreements include free trade agreements, customs union, preferential agreements and services agreements.[1]

Regional Trade Agreements in the World
1948-2002
Number of RTAs



Source: WTO Secretariat

Types of trade blocs

Regional groups or trade blocs try to lower trade barriers between them and stimulate regional trade. Literature on trading blocs mentions four different types of trade blocs:

§ *Free Trade Areas*
Countries belonging to the free trade area trade freely amongst them but have individual trade barriers with countries outside the free trade area. Examples include NAFTA, APEC and COMESA.

§ *Customs Union*
There is some degree of unification of custom or trade policies (definition given in footnote) e.g. the European Union.

§ *Common Market*
It is a customs union, which has in addition the free movement of factors of production such as labour and capital between the member countries without restriction e.g. MERCOSUR.

§ *Economic Union*
It is a common market, more deeply integrated. Members may adopt common economic policies.

Reasons for formation of RTA

Many reasons have been put forward why countries enter into a regional agreement. Security has played an important objective. The 1951 treaty establishing the European Coal and Steel Community out of which the EU grew was written after a long conflict between Germany and France and security was paramount. Security also played an important role in the creation of MERCOSUR in 1991. Members, Argentina and Brazil had emerged from a period of military governments, during which considerable tensions had characterized the bilateral relationships.

Similar motives are found in the creation of ASEAN (to reduce tension between Indonesia and Malaysia), APEC, and the Central American Common Market (CACM). It is felt that regions that are economically highly integrated may tend to have less internal conflict. But experience has shown that this is not always true. Much depends upon the economic characteristics of the members of the region and upon the style and design of the integration arrangement.

[1]A free trade agreement liberalizes trade among its members, while each member has its own tariff policy towards the non-member countries. A customs union liberalizes the intra-bloc trade and establishes a common tariff policy towards the non-members. A preferential agreement is an agreement for a developed country (or a group of developed countries) provides unilateral tariff concessions to a developing country or group of developing countries to assist the later's economic development.

When countries band together in trade negotiations, there is evidence to suggest that it increases their bargaining power. The formation of the original European Economic Community in 1957 was the desire to increase bargaining power relative to the United States. The members of the EEC probably achieved twin objectives — they accelerated United States - Europe trade liberalisation in manufactures; Europe is a net exporter of manufactures to America and reciprocal liberalisation improved European access to American markets and they delayed trade liberalisation in agriculture. This raised the incomes of the European farmers.

Rise in bargaining power

Individual countries would have little regional power, but when they work together, they do raise the country's visibility. The Caribbean Community & Common Market (CARICOM), an alliance of small Caribbean island states is an example of regional solidarity, where they have succeeded in negotiating a whole range of preferential market access arrangements with Canada, the US and the EU.

Integration may help member governments meet their domestic issues. For instance NAFTA is not only about regional trade, but there is an implicit agreement between Mexico and the US that if the former maintains its policies it would have access to the US market and would have a more general claim on US assistance. One motivation for the US government was that it had a strong interest in encouraging Mexican economic growth in order to curtail Mexican emigration to the US.

There has been a change in the reasons behind the formation of trading blocs. The newer agreements are committed to increasing international trade, are more outward looking, compared to trading blocs set up earlier which were based on a model of import substitution and regional agreements with high tariffs to external trade. They have been created so that member countries benefit from the theory of comparative advantage, thereby specializing in the production of those goods that have a lower opportunity cost of production than other nations. As countries specialize in the production of goods, it becomes necessary to trade with countries that need these goods or that have resources that are not available to that nation.

New agree-ments for formation of blocs

While regional trade groups can provide members some political and economic benefits, they hardly offer an alternate to a country's engagement with the global economy. Except for a few like SAPTA, most of the blocs are small in size, and as such regional self sufficiency is not a reasonable option. While rich countries can rely on their local economies or of their neighbours to reap the benefits of a large market, they still seek to expand external trade to increase domestic prosperity.

Benefits of a bloc

When countries become members of a particular bloc, certain benefits accrue. These have generally been categorised into:

Competition scale effects: These refer to the benefits that arise from the possible increase in foreign direct investment. As markets integrate to create larger markets, trading blocs may assist in attracting foreign direct investment. For instance in the case of Mexico, foreign direct investment more than doubled the year after it joined NAFTA. Similarly, after the European Union was formed, the EU's share of worldwide inward foreign direct investment flows increased from 28% to 33% during the period from 1982 to 1993.

As trade blocs provide large markets, it also allows for economies of scale. By allowing for bulk production, economies of scale decrease the average cost of production by making it more efficient. Also trading blocs brings producers in member countries into closer contact, thereby increasing competition among them. This promotes efficiency and prevents monopolies from being formed.

Trade and location effects: As tariffs are eliminated, imports from other member countries will become cheaper, and demand patterns could change. This allows consumers to buy products from the cheapest source, thereby ensuring that production is allocated to those firms with a comparative advantage in production.

There is evidence to suggest that some trading blocs have helped in boosting member countries trade and financial flows. An IMF Working Paper 'How has NAFTA affected the Mexican Economy? Review and Evidence', has offered an assessment of the impact of NAFTA on growth and business cycle in Mexico.

NAFTA's impact on Mexico

NAFTA, an agreement between advanced countries and a developing economy has created the world's largest free trade area in terms of GDP and it is the second largest, in terms of total trade volume after the European Union. This agreement has helped generate significant benefits to the Mexican economy. It has had a favourable impact on exports and foreign direct investment flows.

Before the introduction of NAFTA in 1994, Mexico was facing serious macroeconomic imbalances – a widening current account deficit, problems in the financial sector, poor investor confidence, exchange rate and inflation uncertainty.

Trade with NAFTA increases

Several studies have shown that NAFTA helped Mexico come out of its crisis. Mexico received preferential treatment from the US as it maintained its reform program. The country showed positive results. Inflation declined and by 2003, Mexico enjoyed the lowest and most stable inflation rates. There was a strong growth in real output, significant opening of the economy in terms of rising shares of imports/exports to GDP. Most significant was the increase in trade with NAFTA partners. Mexico's exports to the US and Canada has more than doubled. It rose from 25% of its GDP in 1993 to 51% in 2000. Approximately 90% of total exports of Mexico went to the partner countries in 2002, while imports from the partner countries constituted more than 65% of total imports.

Exports diversify

The pace of export diversification increased after the inception of NAFTA, as Mexico started exporting more of manufactured goods. The average manufacturing share increased to more than 80% during the post-NAFTA period 1994-2002 from around 37% in the pre-NAFTA period (1980-1993). As a result, Mexico's export and import base has become one of the most diversified among emerging market economies. Mexico's exports to the US and Canada tripled in dollar terms between 1993 and 2002. Mexico's trade with NAFTA partners still accounted for around 40% of its GDP in 2002.

Intra-industry trade picks up

Intra-industry trade (defined as trade in similar but differentiated products) has picked up between Mexico and its NAFTA partners. OECD figures show that the share of intra-industry trade in Mexico's manufacturing sector rose from 62.5% in 1988-91 to 73.4% in the period 1996-2000. The trade bloc has also resulted in a substantial increase in the variety of products traded between Mexico and its partners.

FDI rises

Foreign direct investment flows between Mexico and its partners strengthened after NAFTA. The agreement had certain provisions, which improved the relative standing of investors from the partner countries in Mexico and also expanded the sectors in which they could operate. FDI flows to Mexico rose from $12 billion over 1991-93 to roughly $54 billion in the 2000-02 period, mainly on account of inflows from Mexico's NAFTA partners. Research has shown that Mexico's participation in NAFTA led to roughly 70% increase in FDI flows. Foreign multinationals increased their investment in Mexico in response to NAFTA as well as to the relaxation of various barriers on FDI flows since the mid 1980s.

Economic growth improves

The paper has further shown that regional trade agreements like NAFTA have a positive impact on economic growth in member countries. Mexico's growth performance has been better than it was before the agreement. GDP rose from an annual average of 2% in 1980-93 to an annual average of roughly 4% in 1996-2002. Mexico's performance has been better than several other emerging market economies, particularly after the 1995 crisis. Average growth rate of investment has been particularly impressive, as it rose almost eightfold during the period 1996-2002. Also to show an improvement has been the contribution of exports and investment to GDP.

There have been periods of crisis for member countries like the stock market crash in the US in 2000, the major financial crisis in the mid 1990s in Mexico, but with the implementation of sound domestic economic policies it ahs helped in boosting Mexican growth. NAFTA has been instrumental in improving macroeconomic as well as institutional policies in Mexico.

Pakistan, a member of two regional blocs

Pakistan is a member of two regional blocs — SAARC and the ECO. Since inception, SAARC intra-trade has remained low, so is the case with ECO. These two blocs have not been able to effectively promote intra-trade and investment in the region. While SAARC intra-trade has been around 3-4% only, other blocs like the EU and NAFTA have a 60% and 56% intra regional trade.

Selected Regional Trade Blocs

Merchandise Exports within Bloc

1970	1980	1990	1995	1997	1998	1999	2000	2001	2002	
High-income and low-and middle-income economies										
APEC*	57.8	57.9	68.3	71.8	71.6	69.7	71.8	73.1	72.6	73.3
European Union	59.5	60.8	65.9	62.4	55.4	56.8	62.9	61.6	60.8	60.6
NAFTA	36.0	33.6	41.4	46.2	49.1	51.7	54.6	55.7	55.5	56.7
Latin America and the Caribbean										
Andean Group	1.8	3.8	4.1	12.0	10.8	12.8	8.8	7.9	10.3	9.5
LAIA	9.9	13.7	10.8	17.1	17.0	16.7	12.7	12.8	12.8	11.1
MERCOSUR	9.4	11.6	8.9	20.3	24.8	25.0	20.6	20.8	17.2	11.6
Africa										
CEMAC	4.8	1.6	2.3	2.1	2.0	2.3	1.7	1.0	1.3	1.5
COMESA	8.7	6.0	6.3	7.0	7.1	7.7	7.4	5.7	7.0	6.4
ECCAS	9.6	1.4	1.4	1.5	1.5	1.8	1.3	1.1	1.3	1.3
ECOWAS	2.9	10.1	7.9	9.0	8.6	10.7	10.4	9.5	9.6	10.6
SADC	8.0	2.0	4.8	8.7	10.4	10.4	11.9	11.9	10.2	9.3
UEMOA	6.5	9.6	13.0	10.3	11.8	11.0	13.1	13.1	14.3	12.3
Middle East and Asia										
Arab Common Market	2.2	2.4	2.7	6.7	4.1	4.8	3.3	3.0	4.5	4.8
ASEAN	22.9	18.7	19.8	25.4	24.9	21.9	22.4	23.9	23.3	23.7
EAEC	28.9	35.6	39.7	47.9	47.8	42.0	43.8	46.6	46.6	48.2
ECO	1.5	73.2	3.2	7.9	7.5	6.8	5.8	5.6	5.5	5.9
SAARC	3.2	4.8	3.2	4.4	4.2	4.8	4.0	4.1	4.3	4.2
UMA	1.4	0.3	2.9	3.8	2.7	3.3	2.5	2.3	2.6	2.7

Total Merchandise Exports by Bloc

	1970	1980	1990	1995	1997	1998	1999	2000	2001	2002
High-income and low-and middle-income economies										
APEC*	36.0	33.7	39.0	46.3	47.3	46.1	46.6	48.6	46.5	46.0
European Union	45.6	41.0	44.0	39.7	37.9	39.9	39.2	35.9	37.4	37.9
NAFTA	21.7	16.6	16.2	16.8	18.3	18.7	18.8	19.1	18.8	17.2
Latin America and the Caribbean										
Andean Group	1.9	1.7	0.9	0.8	0.9	0.8	0.8	1.0	0.9	0.8
LAIA	4.5	4.4	3.4	4.1	4.8	4.8	4.8	5.2	5.2	5.0
MERCOSUR	1.7	1.6	1.4	1.4	1.5	1.5	1.3	1.3	1.4	1.4
Africa										
CEMAC	0.2	0.3	0.2	0.1	0.1	0.1	0.1	0.2	0.2	0.1
COMESA	1.6	0.6	0.4	0.4	0.4	0.3	0.3	0.4	0.4	0.4
ECCAS	0.6	0.3	0.3	0.2	0.3	0.2	0.2	0.3	0.3	0.3
ECOWAS	1.1	0.4	0.6	0.4	0.5	0.4	0.4	0.5	0.5	0.4
SADC	2.2	1.6	1.0	0.8	0.8	0.7	0.6	0.6	0.7	0.7
UEMOA	0.3	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Middle East and Asia										
Arab Common Market	1.6	1.5	1.0	0.4	0.5	0.4	0.5	0.7	0.6	0.6
ASEAN	2.0	3.7	4.1	6.1	6.6	5.8	5.6	6.9	6.0	6.3
EAEC	11.3	15.1	20.9	26.1	25.4	24.2	24.7	26.1	24.4	25.2
ECO	1.5	1.2	1.1	1.2	1.2	1.1	1.2	1.3	1.3	1.3
SAARC	1.1	0.7	0.8	0.9	0.9	0.9	1.0	1.0	1.1	1.1
UMA	1.5	2.3	1.0	0.6	0.6	0.5	0.6	0.8	0.7	0.7

* *No preferential trade agreement.*

Source: World Development Indicators – 2004
The World Bank

Asia Pacific Economic Cooperation (APEC), North American Free Trade Area (NAFTA), Latin American Integration Association (LAIA), Southern Cone Common Market (MERCOSUR), Economic and Monetary Community of Central Africa (CEMAC), Common Market for Eastern and Southern Africa (COMESA), Economic Community of Central African States (ECCAS), Economic Community of West African States (ECOWAS), Southern African Development Community (SADC), West African Economic and Monetary Union (UEMOA), Association of South-East Asian Nations (ASEAN), East Asian Economic Caucus (EAEC), Economic Cooperation Organization (ECO), South Asian Association for Regional Cooperation (SAARC), Arab Maghreb Union (UMA).

- **Merchandise exports within bloc** are the sum of merchandise exports by members of a trade bloc to other members of the bloc.
- **Total merchandise exports by bloc** as a share of world exports are the ratio of the bloc's total merchandise exports (within the bloc and to the rest of the world) to total merchandise exports by all economies in the world.

Also SAARC trade with the industrialised world has been rising, especially with the European Union, America and Japan. Europe is South Asian countries most important trading partner and a major export market.

Direction of Trade of South Asian Countries

(%)

Countries	Industrialised Countries		USA		EU		Japan	
	1991	1999	1991	1999	1991	1999	1991	1999
Exports:								
Bangladesh	75.8	75.6	26.6	31.2	41.3	40.3	3.1	1.6
India	57.7	56.6	16.3	22.2	28.3	25.1	9.3	5.2
Maldives	63.0	76.5	22.2	17.0	37.0	36.6	3.7	1.3
Nepal	88.3	59.8	23.7	30.8	58.0	24.6	0.8	0.9
Pakistan	56.0	60.3	11.4	22.9	32.4	29.2	8.0	3.6
Sri Lanka	65.5	76.4	28.1	39.9	28.4	29.3	5.1	3.6
Imports:								
Bangladesh	36.5	27.5	5.1	5.3	14.3	10.1	9.0	6.7
India	52.1	45.8	9.7	9.0	29.9	26.6	7.0	5.9
Maldives	16.0	56.2	0.6	1.1	9.9	51.1	4.3	1.3
Nepal	44.0	10.6	1.4	1.6	12.2	5.1	21.6	1.9
Pakistan	58.4	40.0	11.2	6.4	27.0	17.3	14.8	7.7
Sri Lanka	36.9	36.6	5.7	2.8	15.7	21.9	11.7	7.2

Source: Globalization and Trade between Trading Blocs – A Study of SAARC and EU with Special reference to India

SAFTA to strengthen SAARC trade

Early this year, the SAARC countries signed the South Asian Free Trade Agreement (SAFTA), to strengthen intra SAARC economic cooperation and maximize the realization of the region's potential for trade and development for the benefit of their people. Among others, it seeks to reduce trade barriers w.e.f. January 1, 2006 when member countries would be reducing their import duties on all goods, with the objective to bring it down to zero. It would also identify non-tariff barriers and other restrictive barriers. South Asian region has the largest concentration of population and has a large potential market, which offers opportunities for growth. This has not been fully exploited to benefit the people of the region.

Thaw in the strained relations between India and Pakistan have brightened the possibility of increased regional trade. Earlier, despite many attempts to enhance regional trade, progress has not been effective because of political problems between the two large members of SAARC.

Pakistan's exports to India in the last four years has been less than one per cent of the total, resulting in a negative trade balance. The share of Pakistan's exports in India's total imports has been a negligible 0.124%. Similarly share of Pakistan's imports in India's total exports has been 0.33%.

In 2001-02, India exported only $186 million worth of goods to Pakistan, out of $44.45 billion of total exports. Pakistan's exports totaled $9.20 billion, but only $49.37 million went to India. The two countries have not always had such weak trade. Before partition and immediately after independence, India was Pakistan's most important trading partner. The strained relationship between the two countries has impacted economic integration in the South Asian region as a whole.

Pakistan does not extend normal GATT/WTO rights or the Most Favoured Nation (MFN) principle to India, but maintains a "positive list" of 600 goods that may be legally imported from India. India in principle granted MFN treatment to Pakistan in 1995-1996 and has no list of permitted or forbidden products, but the meager imports from Pakistan suggest that India has found ways of imposing a de facto ban on most imports from Pakistan. Informal trade between the two countries is much larger, estimated at $1 to 2 billion annually, involving such goods as chemicals, medicines, videotapes, cosmetics, and viscose fiber. These goods find their way either through third markets, such as Dubai and Singapore, or through smuggling.

Box Pakistan – India Who Stands to Gain

We would like to share with our readers the views of the Federation Pakistan Chambers of Commerce and Industry on the benefits of trade between the two major players of SAARC.

Energy Sector

The greatest economic benefit of trade relations between India and Pakistan would occur in the sphere of energy cooperation. India is one of the most rapidly growing energy markets in the world and will be able to absorb new sources of supply as they materialize in the region. Pakistan's potential role in fulfilling this need is not as a supplier but as a potential transit route for energy from Iran and Central Asia. This would require construction of one or more new pipelines, a major capital investment that makes sense only if the political stability and economic feasibility of the project can be counted on.

The economics looks very promising. A project proposal submitted by Iran this past January to both countries estimated that Pakistan would gain between $600 to $800 million per year in transit fees. It would also be able to use the pipeline to fulfil its own energy needs. India would benefit from diversified sources of pipeline gas and lower dependence on more expensive liquid natural gas (LNG). Even with LNG prices dropping, industry sources believe that there would be a significant cost advantage, especially to a pipeline from Iran.

The big drawback, which has thus far prevented any serious discussion of a pipeline project, is India's reluctance to make itself dependent on Pakistan for a strategically important commodity. If India and Pakistan were interested in moving ahead, however, it should be possible to structure an agreement so as to include a third party and make special provision for political risk. Energy cooperation between India and Pakistan would have a stabilizing effect on the region as a whole.

South Asian Association for Regional Cooperation, could provide a useful framework for discussions on non-energy trade. The SAARC member countries have already agreed to establish a South Asia Preferential Trade Agreement (SAPTA), with a view toward eventually moving toward a free trade agreement (SAFTA). The SAPTA agreement does not prescribe which goods are to be subject to tariff reductions for member countries; implementation has been through bilateral agreements. India has signed agreements with Bangladesh and Sri Lanka. These agreements initially covered primary goods that were not traded to any significant extent, but have gradually been expanded to include a more meaningful product list.

Economic Benefits

The economic benefits of goods traded are more diffuse than for energy. One estimate of the impact of complete free trade within the South Asian region puts the total at $14 billion. In the short term, a more realistic benchmark is the $1 to $2 billion that now moves through other channels. India-Pakistan trade will be doing well if it can exceed these levels.

Legalizing trade that now moves through third markets would cut transport costs and transit time for goods, resulting in lower prices for the consumers. Bringing smuggling into official channels would provide a much needed revenue stream to both governments. Because Pakistan would probably still import more than India, its government finances would benefit more from this change.

Expanded trade is likely to be in India's favor in dollar terms. Because the current level is so low, trade liberalization is unlikely to have much macroeconomic impact in either country. The impact on Pakistan is likely to be greater in relative terms, but the political sensitivity will also be higher.

Some of Pakistan's traditional exports of small manufacturers (such as sports goods and surgical instruments) may be well placed to take advantage of a new market opening up.

One potential area of mutual advantage is information technology. There is considerable interest in Pakistan in moving into IT. A fledgling Pakistani industry is unlikely to provide serious competition to the enormous Indian industry, but there could be some mutually beneficial business-to-business links that could be cultivated if the political context became more favorable to mutual trade. Since this industry does not depend on the movement of goods, it may have an easier time moving ahead than some other industries.

Beyond these trade-specific benefits, increased trade between the two countries could strengthen the outward orientation of both countries' market policies. Here too, Pakistan, with the smaller economy and more fragile external links, could especially stand to gain. Trade opening is one of the things that investors in both markets are looking for; again, Pakistan's more difficult economic circumstances mean that it would stand to gain the most. Arguably, however, the greatest dividend of India-Pakistan trade would lie in growing business on both sides of the border, thereby giving people a stake in the other country.

Looking Ahead: Getting Past the Political Barriers:

It is easy to list the benefits of expanded India-Pakistan economic relations, but much more difficult to develop a road map for getting there. Ultimately, trade is unlikely to be the lead issue in this complex relationship. Both sides are accustomed to their current economic isolation from one another. Once the two countries' leaders decide to start a political dialogue, expanding trade could become a useful adjunct to the political process, instead of being hamstrung by it. There is great need to open up Lahore –Wagha and Khokhrapar land routes to boost bilateral trade.

Regionalism and WTO

Most WTO members belong to a regional trade agreement. The main exceptions (by July 2003) are Macau China, Mongolia and Chinese Taipei. The number of RTAs has spread rapidly in the 1990s, stretched across countries at different levels of economic development. A major feature of modern RTAs is their extensive product coverage than in earlier agreements. Also many go beyond the traditional tariff-cutting exercises. They may now cover services, investment, intellectual property, technical barriers to trade, dispute settlement and so on.

Research has been done to study regional trading arrangements in the WTO context. WTO Regional Trade Agreements: Rules state, "When a WTO member enters into a regional integration arrangement, it departs from the guiding principles of non-discrimination defined in Article 1 of GATT, Article II of GATS and elsewhere". The WTO members are however, permitted to enter into such arrangements under specific conditions which are spelled out in three sets of rules: -

- § Paragraphs 4 to 10 of Article XXIV of GATT (as clarified in the Understanding on the Interpretation of Article XXIV of the GATT 1994) provide for t he formation and operation of customs unions and free-trade areas covering trade in goods;
- § The so-called Enabling Clause (i.e., the 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries) refers to preferential trade arrangements in trade in goods between developing country Members; and
- § Article V of GATS governs the conclusion of RTAs in the area of trade in services, for both developed and developing countries.

The WTO in a note, Understanding the WTO Regionalism: friends or rivals has briefly discussed the issue. Often regional trade arrangements support the WTO's multilateral trading system. Regional agreements have allowed groups of countries to negotiate rules and commitments that go beyond what was possible at the time multilaterally. In turn, some of these rules have paved the way for agreement in the WTO.

Services, intellectual property, environmental standards were some of the issues raised in regional negotiations and later developed into agreements or topics of discussion in the WTO.

Regional trading arrangements

The WTO agreements recognize that regional arrangements and closer economic integration can benefit countries. It also recognizes that under some circumstances regional trading arrangements could hurt the trade interest of other countries. Normally, setting up a customs union or free trade area would violate the WTO's principle of equal treatment for all trading partners (most-favoured-nation). But GATT's Article 24 allows regional trading arrangements to be set up as a special exception, provided certain strict criteria are met.

In particular, the arrangements should help trade flow more freely among the countries in the group without barriers being raised on trade with the outside world. In other words, regional integration should complement the multilateral trading system and not threaten it.

Similarly, Article 5 of the GATS provides for economic integration agreements in services. Other provisions in the WTO agreements allow developing countries to enter into regional or global agreements that include the reduction or elimination of tariffs and non-tariff barriers on trade among themselves.

A paper, "Regional Trade Agreements and the WTO" by Jo-Ann Crawford and Sam Laird has discussed this issue. They have come to the conclusion that the background of unilateral reforms and increased membership of the strengthened multilateral system should mean that the recent strong trend towards regionalism is somewhat less dangerous to third countries and to the multilateral system than earlier experiences. This conclusion is reinforced by the nature of the new agreements, which have wider coverage of products and instruments than earlier agreements, enhancing the degree of integration.

Literature on the issue has shown that there is no simple answer to whether regionalism encourages or discourages the evolution towards globally freer trade. Similarly, there is no unanimous view on whether the emerging mega-blocs of RTAs will facilitate or frustrate the making of multilateral agreements. It has been shown that the emerging mega-blocs ignore, for the most part, the least-developed countries, particularly those in sub-sahara Africa and South Asia.

The paper has tried to find an answer as to whether RTAs harm third countries and weaken the MFN principle. As RTAs are discriminatory,

it is not surprising that trade within such blocs is generally growing faster than trade from non-member. On the other hand, trade with non-members is growing at about the same rate as world trade in general, and in some of the smaller, more dynamic RTAs, trade with non-members is growing faster than world trade. It is argued in the literature that more comprehensive coverage inclines countries to take a more positive view of general liberalisation.

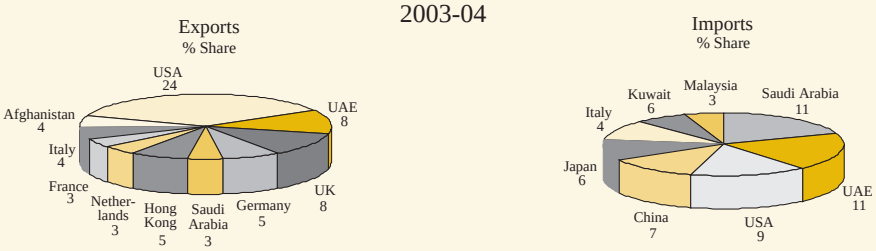
There can be little doubt that the main economic advantages to participants in regional trade agreements would be even greater if the liberalisation were carried out on a wider multilateral scale. RTAs are a second best solution.

Trade can reduce poverty

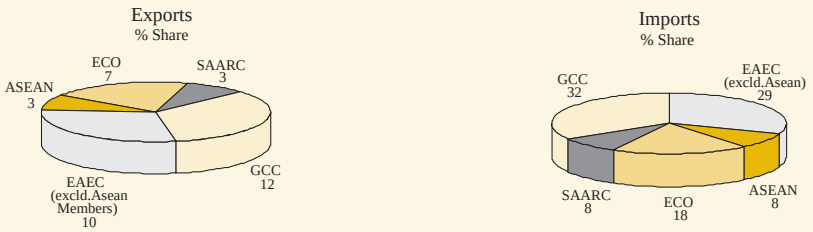
A World Bank publication 'Global Monitoring Report 2004', has in one of its chapters discussed, how expanding opportunities for international trade can spur growth and accelerate progress towards poverty reduction and the other Millennium Development Goals. Goal 8 — Develop a Global Partnership for Development, would require among others, non-discriminatory trading and financial system, tariff and quota free access for exports of the least developed countries. This would require increased efforts by the developed countries to open up market access for goods and services produced in developing countries. This is particularly the case in agriculture, textiles and clothing, and labour intensive services — sectors where developing countries typically have a comparative advantage.

The majority of the world's poor live in countries such as China, India, Pakistan and Indonesia that are not likely to be part of regional trade agreements with the major developed countries. Also, RTAs are unlikely to achieve significant progress in areas such as agriculture that matters most to the poor. It is important that RTAs minimize discrimination against non-members and not divert attention away from the multilateral WTO process.

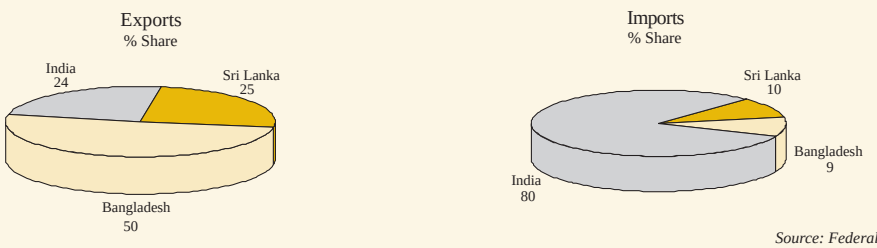
Pakistan
Major Trade Markets
2003-04



Pak Trade with
Major Trading Blocs in Asia & Middle East



Pak Trade with SAARC



Source: Federal Bureau of Statistics

Textiles & Clothing – Post Quota Regime

Countries around the world are preparing for the changes that will come in January 2005 with the implementation of the various agreements of the World Trade Organization. There are many aspects to this but we shall be restricting our paper to the impact of dismantling of quotas on the textile and clothing sector in various countries.

Agreement on Textiles & Clothing

The $350 billion global trade in textiles and clothing faces a big challenge from January 1, when export quotas will be lifted and the textile and clothing sector will become subject to the general rules of the General Agreement on Tariffs and Trade. For nearly two decades (1974-95) they were governed by the MultiFibre Agreement (MFA), followed by the Agreement on Textiles & Clothing (ATC), which came into force with the establishment of the WTO in 1995. It was considered as a transitory phase between the MFA and the full integration of textiles and clothing into the multilateral trading system. It was agreed to take place in four steps over a 10-year period.

After the WTO was formed in 1995, the developed countries led by the US, and the EU demanded increased protection of their intellectual property rights and a deregulation in the trade of services with the developing world. In order to accept this, developing countries insisted that the MFA system of quotas be dismantled and they be given the ability to freely export their textile and apparel products to the US, Europe and Canada. An agreement emerged in 1995 – Agreement of Textiles & Clothing.

Quotas to be dismantled

End of the quota regime would allow free competition in the international trade of garments and clothing. Some developing countries would gain, mainly those who have the export potential but are restricted because of quota restrictions, while others, to whom quotas provided protection against their low competitive ability would face tough competition and may not be able to take advantage of the new trade regime. Quotas had guaranteed market access to many developing nations and secured employment for their people. This would no longer exist.

China's share to rise

Notable Asian textile producers like China, Vietnam, India, Bangladesh, Sri Lanka, Pakistan, Thailand, Malaysia and Indonesia would be competing with each other for a higher share in textile and clothing exports. A paper titled, "The Global Textile and Clothing Industry post the Agreement on Textiles and Clothing" WTO, shows that China was the world's largest exporter both of textiles and clothing in 1995 as well as in 2002. Its world market share increased from 22.5% to 30% over this period in the clothing sector and from 16% to 22% in the textile sector.

US market

Of the total imports of textiles to the US, during 1995-2002, China's market share has been fairly stable, while Mexico's market share has shown a sharp increase, probably reflecting the impact of NAFTA. Pakistan's share has risen, while higher income Asian suppliers such as Chinese Taipei and Hong Kong have seen falls.

Of the total clothing imported in the US, China has a 16% share, Mexico has raised its market share sharply (from 7% in 1995 to 12% in 2002), while shares of Bangladesh, Indonesia and India have remained stable. Sri Lanka has entered the market and there has been a notable growth in its share.

EU market

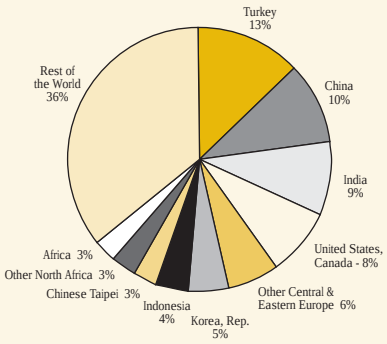
Looking at the EU market, imports of textiles grew by about 3% between 1995-2002. There has been a substantial shift from intra EU trade to imports from lower cost external suppliers. Turkey's market share has risen following the EU-Turkey customs union. Switzerland is no longer in the list of 10 largest exporters, while Bangladesh has now been added to the list and gained a significant market share.

The WTO study has shown how the market shares will change in both, the EU and the US after quota elimination. China and India are expected to account for the major share of world trade in textiles and clothing, while smaller exporters like Bangladesh and Sir Lanka will also increase their market shares, as their exports of textiles increases. Countries losing market shares are African countries that have had preferential access to the market before the phasing out of

Market Shares before and after Quota Elimination - Textiles

EU

Before



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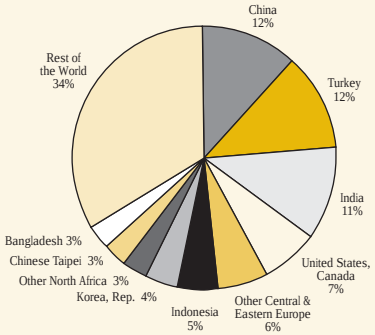

USA

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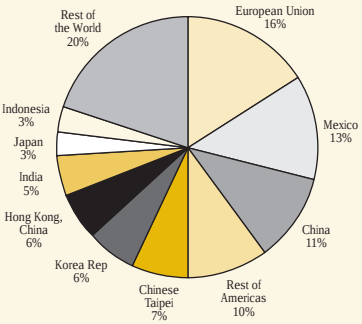

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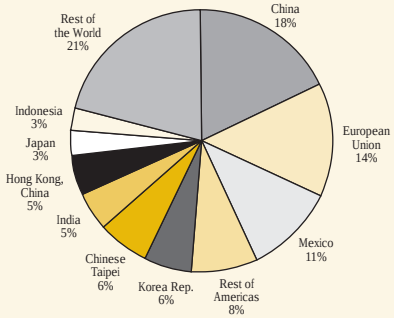

Market Shares before and after Quota Elimination - Clothing

EU

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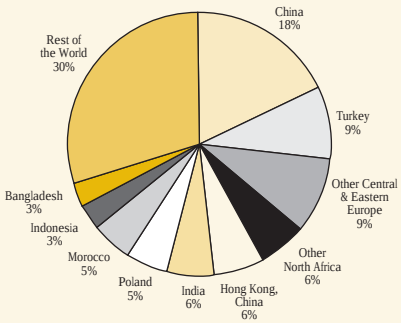

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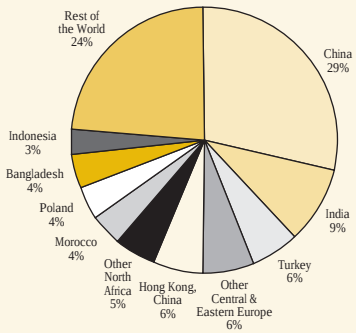

USA

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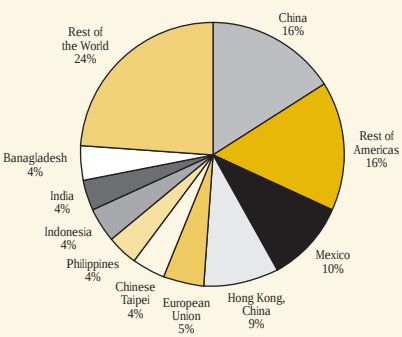

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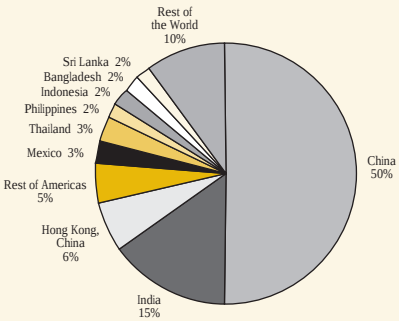

Source: The Global Textile & Clothing Industry post the Agreement on Textiles and Clothing World Trade Organisation

quotas and Latin American countries. Turkey and Eastern Europe are also in danger of losing market shares in the clothing sector in EU compared to 2002.

China / India to dominate the market

China and India are expected to dominate the production of textiles and apparel. China will increase its share of clothing imports into the US from 16% to 50%, while India's share will rise from 4% to 15%. In Europe both these countries are forecast to control 38% of the clothing market after the quotas end. While these two countries are expected to dominate the textile and apparel industries, other countries are also working towards the new era and are likely to remain important exporters to the US and EU.

As the decades old system of export quotas is scrapped, the ensuing competition should slash prices for consumers, but for those countries that have used the guaranteed access that quotas provided to build garment industries there could be problems.

Textiles provide jobs

In southeast Asia, garments are the country's biggest earner. The IMF forecasts that the abolition of quotas could reduce its economic growth to below 2% from above 5% in recent years. In Bangladesh 3500 garment factories employ 1.8 million workers, more than 80% of them women, while in Cambodia the garment sector employs 300,000 workers, mostly young women. India, which employs 35 million textile workers, expects to gain from the end of quotas, while China will grab half of all US clothing imports. Pakistan is expected to gain, given its cotton production and quality of its garments.

Textile industry of Pakistan remains the largest contributor to the GDP, exports and employment. Major investment of over $3 billion has taken place in expanding existing capacities, in higher value added exports and towards product diversification. A programme called Textile Vision – 2005 was launched to attract more investment in the sector and diversify its products. This investment activity has resulted in a growth of exports to over $12 billion in the last fiscal year.

Pakistan's textile industry focuses on BMR

The industry is adopting new technology, and has invested over $3 billion in BMR for improving production quality and moving towards more value addition. It imported $585 million worth of machinery in FY04 and $532 million in FY03. The Budget 2004-05 has reduced customs duty on all types of plants, machinery and equipment not locally manufactured to 5%. In addition there will be no sales tax and withholding tax. This should help the balancing, modernization and replacement programme of the textile industry. The industry is also installing shuttle less and air jet looms and increasing its spinning capacity. It is focusing on cleaner cotton programme, for even though it is amongst the major cotton growing countries, it has not been able to produce cotton, which can be graded in the A-index. The ginning sector continues to be weak. Further the industry is making efforts for greater market access, so to improve its trade volumes. If regional trade picks up, there is market of nearly three billion people and the textile industry could be benefit.

Pakistan's textile and clothing sector accounts for 64% of the country's total export earnings. Once quota restrictions are lifted market access/share would depend on the level of capacity expansion achieved, up-gradation of technology and the economies of scale created to became more cost competitive. Pakistan will have to move up the value chain and shift its focus towards value added products and build capacities capable of timely delivery of significant volumes at competitive prices. Quality and environmental standards will have to be looked into, if the domestic textile industry is to adjust with the requirement and new demand in the post quota era.

Pakistan and WTO

Engr. M. A. Jabbar*

The WTO system as it has emerged from the Uruguay Round consists of certain substantive Agreements: Multilateral Agreement on Trade in Goods including the General Agreement on Tariffs and Trade and its associate Agreements, General Agreement on Trade in Services (GATS); and Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS).

Agriculture

It is expected that under UR agreement, market forces would result in domestic prices rising to world prices, which would stimulate domestic production. Tariffs in developed countries were reduced by 36% on fruits and vegetables, and 48% for such non-traditional products as flowers, providing Pakistan improved export opportunities.

The results on rice and wheat could have mixed effects. The agreement to reduce subsidies on rice and wheat maintained by developed countries could result in increased market access. The reduction on subsidies and resulting price increase would mean that total expenses of Pakistan for wheat imports, in wheat deficit years, will rise.

WTO Agreements on TBT and SPS

To meet the requirements of WTO Agreements on Technical Barriers of Trade (TBT) and Sanitary and Phytosanitary Standards (SPS), Pakistan has taken a number of key initiatives aimed at strengthening technical institutions capabilities in standard setting, compliance.

In Pakistan, ISO 9000 amd ISO 14000 certification is rising and reportedly now well over 3,000 companies are ISO-9000 certified. As for ISO 14,000 certifications, out of a total of 103 countries, Pakistan ranks 56th with only ten ISO 14001 certified firms (out of 35,523 firms in the world) while India is 19th. All these companies are certified by foreign based bodies. Against this backdrop, Pakistan National Accreditation Council (PNAC) was set up in 1998 in Ministry of Science & Technology and in 1999, under ADB-assisted Trade Export Promotion & Industry Program (TEPI) Project, it launched the accrediation services for ISO 9000/ISO 14000 certification bodies and laboratories.

According to Pakistan Country Report on Trade and Sustainable Development prepared by Sustainable Development Policy Institute (SDPI), in October 2002, the TBT and SPS agreements present both an opportunity and a constraint. The two agreements seek to increase market access for the exports of its member countries. However, the prerequisite is that they abide by the strict rules the WTO has formulated for the development of mandatory technical regulations, voluntary standards and conformity assessment procedures. This is where developing countries like Pakistan come up short.

They do not possess the institutional and technical capacity to develop, advocate and formalize such standards in WTO fora, nor the conformity assessment and accreditation bodies to certify that domestic industries are complying with international standards. While the WTO, in principle, offers technical assistance to developing countries to develop these capabilities, the concern expressed by various stakeholders suggest that Pakistan has not tapped into these opportunities.

Textiles and Clothing (ATC)

One of the principal objectives of Pakistan during the UR was not only to achieve elimination of Multifibre Arrangement (MFA) but also the full integration of the textiles and clothing into the GATT in order to secure greater access to international markets.

A number of studies have evaluated the welfare effects for developing countries of MFA elimination. According to a study which examines the impact of removal of non-tariff barriers, tariff reductions and elimination of MFA, South Asia's output of textiles could increase by 12% and exports by 26%. In clothings, output could increase by 91% and export by 254%. The gains are large because these countries are considered amongst the lowest cost producers most severely constrained by the MFA.

Our exports would, in 2005 face severe competition from other major suppliers like China, Hong Kong, Thailand, Bangladesh

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etc. Potential growth of Pakistan's exports will depend on the ability of producers to improve the quality of their exports, bring improvements in productivity and restructuring of the domestic industry. However, the pressure is mounting on textile industry from foreign buyers for compliance with social, labour, health, hygienic and environment standards. This needs to be addressed on top priority basis.

Tariff and Non-Tariff Barriers

Pakistan is committed to bind about 33% of its tariff lines. Approximately 81% of Pakistan's agricultural import tariffs (HS Chapter 1-24) are bound, most at ceiling rate of 100%. Tariffs on tea, wheat, maize and sugar are bound at ceiling rate of 150%. For industrial products (HS Chapter 25-97) Pakistan bound 25% of its tariff, most at ceiling rates of 40% or 50%. For these products, tariff reductions were to take place in five equal instalments beginning in July 1995. For a number of products like leather items, travel goods, wood products, some textiles and certain equipment, tariffs will be bound at ceiling rates of 22% to 30%. Tariff reduction on textiles and clothing are scheduled in 10 equal instalments.

As for non-tariff barriers (NTBs), Pakistan is committed to abolish import licensing for most goods, permitting foreign companies to export goods. The government has also promised to convert remaining NTBs into tariffs, reduce maximum and raise minimum tariffs, incorporate various ad hoc import taxes into customs duties, and reduce numerous duty exemptions and concessions.

General Agree-ment on Trade in Services

Pakistan participated in the GATS negotiations, but did not undertake extensive commitments. However, Pakistan signed the second protocol to the GATS which pertains to financial services, which apply to insurance, banking and other financial services. Pakistan also provided offers in the negotiations on Basic Telecommunication which were completed on February 15, 1997.

Pakistan's schedule of specific-commitments consists of both horizontal and sector-specific commitments. The sector-specific commitments cover 47 activities within the business, communications, construction/engineering, health, financial and tourism/travel services.

Pakistan also submitted two Lists of MFN Exemptions, one relating to telecommunications on April 11, 1997, and the second relating to banking and other financial services on February 26, 1998. Under Article II of the GATS, Pakistan maintains MFN exemptions for four financial services/activities with a view to presenting reciprocal requirements, Islamic financing transactions, and joint ventures among ECO countries. Pakistan also maintains exemptions in two identical communication services in favour of countries/operators signatories of bilateral agreements on rates with the PTCL.

It may be mentioned that the maintenance of Article II exemption is not unusual: it is understood that 79 member countries maintained 390 MFN exemptions. However, such exemptions should not exceed a period of ten years (beginning from 1995). In any event, they shall be subject to negotiation in subsequent trade liberalization.

Trade Related Intellectu al Property Rights

As a member of the WTO, Pakistan is committed to fulfilling TRIPs obligations. Copyrights piracy is considered very high, affecting imported computer software, film videos and textile designs. Pakistan like other developing countries was given deadline of 1-1-2000 (i.e. five year period) to bring into conformity with WTO commitment its copyright laws etc. Pakistan is not yet fully ready to implement its commitment.

In Pakistan, five laws/amendments have been promulgated, to provide intellectual property protection under TRIPS standards.

1. Patents Ordinance, 2002
2. Trademarks Ordinance, 2001
3. Copyrights Amendments Ordinance, 2000
4. Industrial Designs Ordinance, 2000
5. Registration of Layout designs of integrated Circuits Ordinance, 2000

In developed economies, intellectual property laws are regulated under a single umbrella organization to reduce the regulatory impediments that discourage entrepreneurs from compliance with regulations. In Pakistan, all three areas (copyrights, trademarks, patents) are managed separately by different federal ministries, i.e. Ministry of Education (copyrights), Ministry of Commerce (Trade Marks) and Ministry of Industries & Production (Patents).

To improve the administrative and enforcement scenario, the government of Pakistan has approved establishment of an umbrella organization called 'Pakistan International Intellectual Property Rights Organization' and, as per Trade Policy 2003-04, "necessary legislation will come soon so that PIPRO can start functioning". This organization is intended to fill the much-needed gaps in the areas of IPR policy articulation, legal and enforcement issues, research and development, up-gradation of outdated systems and procedures, coordination, human resources development, etc.

Trade Related Investment Measures

Under the TRIMs Agreement, WTO members agreed not to apply any TRIM inconsistent with GATT Article III (National Treatment) and Article XI (quantitative restrictions) subject to the exceptions permitted under GATT 1994.

Pakistan is committed to phase out the "deletion programmes." Pakistan has deletion programme for automobiles, electronics, electrical products and engineering items, which were to be phased out within five years of the entry into force of agreement. However, transition period could be extended, on the request of individual developing/LDC countries if there are difficulties in eliminating TRIMs. In July 2001, Pakistan alongwith six other developing countries received extension of the transition period through the end of 2001 and in November 2001 further extensions were granted for period upto end-2003. Thus, instead of the extension of seven years demanded by Pakistan, WTO Council of Trade and Goods (CTG) has granted only a two year extension up to December 2003 for the implementation of the deletion program. Reportedly consideration of one further request for extension of the transition period is pending.

Anti-Dumping

There is prima facie evidence that cases of imposition of Anti Dumping Duties (ADDs) against different sub-sectors of the textile industry have been registered in order to protect jobs of textile Industries of developed countries. This is seriously impacting on Pakistan's economy. Even in cases where investigations do not lead to eventual imposition of definitive ADDs, trade is disrupted in the interim period and valuable customers are lost. Given the backdrop of increasing anti-dumping measures against our exports, we need to implement anti dumping measures to protect domestic industry against the onslaught of unfair competition. In this context, following ordinances have been promulgated in Pakistan:

- Anti dumping law 2000
- Countervailing Duties Ordinance 2001
- Safeguard ordinance 2002

National Tariff Commission (NTC) with the assistance of Central Board of Revenue has been assigned the task to implement these ordinances in Pakistan. Since the promulgation of Anti-dumping law, NTC has levied 27.33% anti-dumping duty for a period of 5 years on Tinplates of thickness of less than 70.5 mm and width of 600 mm or more imported from South Africa. It has also imposed provisional anti-dumping duty at the rate of 96.50% on Roquette Freres of France and 91.12% on P.T. Sornini Corporation of Indonesia, for allegedly dumping Sorbiol 70% Solution, a Sweetener of pharmaceuticals, etc.

Dispute Settlement Body

The developing countries including Pakistan are facing problems of hiring law firms to advise and represent them in WTO related cases. Exorbitant fees of these law firms ranging from $ 200 to $ 600 an hour, restrict the developing countries from seeking relief. This underscores the need to train local lawyers with WTO expertise.

Customs Valuation

After availing the grace period of 5 years, the Finance Act 1999-2000 amended the Section 25 of the Customs Act 1969 to accommodate the necessary changes for adoption of GATT code of valuation based on transaction value.

There is, however, a general complaint that rules and regulations are not being observed by customs officials with respect to custom valuation. Instead of observing the transactional value system, they apply various procedures including the fixation of ITP on the basis of weak evidences, loading of the declared value with or without any evidence or any other method devised by the assessing officer on case-to-case basis.

Pakistan's External Sector

Non-traditional exports picking up

Pakistan's exports continue to be concentrated in cotton, leather, rice, synthetic textiles, and sports goods accounting for 82.6% of total exports (2002-03), with textiles alone contributing 64%. However, non-traditional exports like onyx, handicrafts, precious stones, jewellery, furniture, fruits/ vegetables are gradually picking up. Similarly while it trades with a large number of countries, the US, Germany, Japan, UK, Hong Kong, Saudi Arabia and Dubai are the major trading partners.

Composition of exports

A positive development has been the change in the composition of exports. While the share of manufactured goods has risen, the share of primary and semi-manufactured exports has significantly fallen over the years. Today manufactured goods account for 78% of total exports, against 57% in 1990-91, with semi-manufactures making up 12% and primary commodities 10%, which is half of their shares recorded a decade earlier.

Unit value of exports rises

In 2003-04, exports were over $12 billion, a 10% increase over a year earlier. Of the overall growth in exports, textiles remained the largest contributor followed by rice, and leather manufactures. Per Unit earnings from these commodities were higher, and though for some items, quantum exported rose, the rise is attributable to price effect. Quantities and Unit Values of major exports for the last five years is given in the Annexure.

Imports grow

In FY04, imports grew by nearly 27% to $15.5 billion against $12.2 billion a year earlier, primarily because of larger imports of machinery and chemicals indicating the increase of economic activity in the country. Capital goods imports constitute 26% of the total, while petroleum makes up for 20%. In the machinery group, imports recorded a 39% growth in FY04 against FY03. Within this group, all sub-groups with the exception of agricultural machinery witnessed growth. Notable increase was recorded by aircraft, ships & boats, road motor vehicles and textile machinery.

Automobiles is one of the fastest growing manufacturing sub-sector and with increasing demand, the domestic manufacturers are increasing their capacity utilisation, and a number of new assemblers have started commercial production. Import of textile machinery has also gone up with lower import duties on import of machinery not manufactured locally and with an increase in the pace of technological up-gradation by the industry.

Trade deficit widens

The trade deficit deteriorated in the first quarter of FY05 to $839 million, compared with $145 million in the comparable period of FY04. The larger deficit was due to a 38% higher import bill, primarily as a result of increased import of petroleum and machinery which make up for 43% of the total imports. Machinery import was dominated by road motor vehicles, textile machinery and others. In the primary commodities category, palm oil imports rose by 16.6% to $178 million, followed by import of tea which rose by 43% to $58 million. Wheat of a sum of Rs.14 million was imported against a negligible amount in the comparable period a year earlier.

Petroleum import bill rose to $944 million in 2004-05 (July-Sept) a 38% increase over $685 million in the comparable period last year. Imports of agricultural and chemicals also rose by 40% to $908 million. Unit prices of the mentioned categories had risen in the period under review.

Unit Price - Imports

($/MT)

Items	July-September 2004-05	July-September 2003-04	% Change
Tea	1676	1560	13.3
Palm oil	486	449	8.2
Wheat	254	-	-
Petroleum	262	210	24.8

Exports growing at 17% lagged behind the growth in imports. Textile manufactures accounted for 64% of the earnings, followed by other manufactures (17%) while the rest was shared among the other exports. In the textile group, knitwear showed a substantial jump of

57% to $575 million, cotton cloth 16% to $436 million and cotton yarn 12.2% to $250 million. Exports of bedwear, tents, canvas and art silk and synthetic textiles declined in this group.

In the primary commodities category export of rice, fish and fish preparations, fruits, spices and wheat declined by 2.8%, 31%, 20%, 36% and 100% respectively. Among the other manufactures, exports of football rose significantly and non-traditional items like engineering goods rose by 42%, gems 200%, molasses 110%. Certain sub-categories like leather manufactures, footwear, and surgical goods showed decline in export earnings.

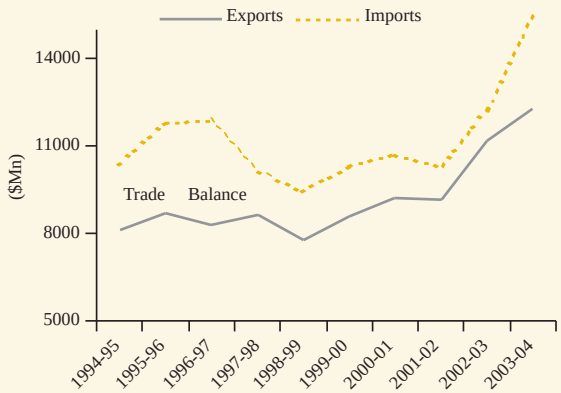
During the quarter July-September 2004-05, higher unit prices were realized through the export of some of the major items, as shown below: -

Unit Price – Exports

Items	Unit	July-September 2004-05	July-September 2003-04
Cotton yarn	$/MT	2341.3	1912.4
Cotton cloth	$/Sq. Mtr.	0.7135	0.7114
Knitwear	$/Doz.	22.1	22.4
Bedwear	$/MT	5414	5714
Towels	$/MT	3759	3974
Readymade garments	$/Doz.	36.0	36.4
Carpets & rugs	$/Sq. Mtr.	60.6	58.9

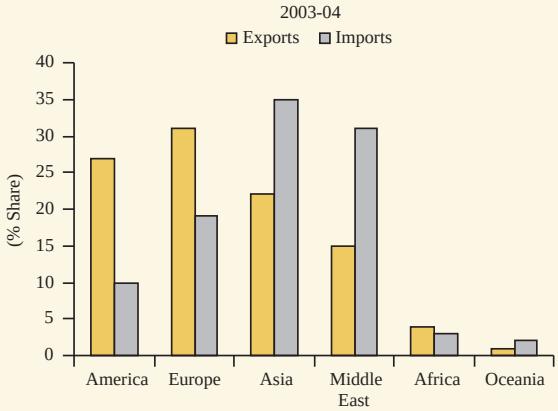
Pakistan Global Trade

Trade Balance



Trade By Regions

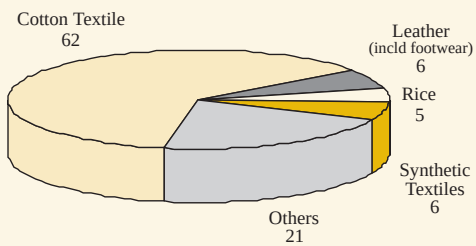
2003-04



Commodity Trade 2003-04

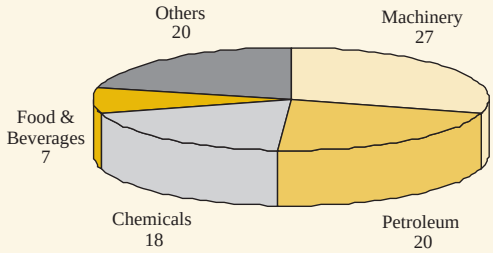
Exports

% Share



Imports

% Share



Annexure

Unit Value & Quantities - Major Exports

($ Mn)

Items	Unit	1999-00			2000-01			2001-02			2002-03			2003-04			% Change in 5-Years 2003-04 over 1999-00		
		Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value
Rice	000 MT	1916.1	539.67	281.65	2372.1	512.61	216.10	1684	448.23	266.12	1820	555.46	305.20	1794	627.21	349.62	-6.37	16.22	24.13
Raw Cotton	000 MT	83.0	72.55	874.58	134.9	139.12	1030.96	35	24.73	706.57	55.1	49.02	889.66	37.3	47.75	1280.16	-55.06	-34.18	46.37
Fish & Fish Preparations	000 MT	89.8	138.89	1545.68	82.2	137.74	1675.63	85	125.64	1486.86	93.2	134.50	1443.13	104.9	156.25	1489.51	16.82	12.50	-3.63
Leather	000 Sq. mts	12898.0	175.16	13.58	17254.0	227.68	13.20	17290	239.93	13.88	15349	234.7	15.30	15524	242.9	15.65	20.36	38.67	15.22
Cotton Yarn	000 MT	513.0	1071.60	2089.04	547.2	1073.20	1961.17	540	929.69	1721.65	519.3	928.36	1787.71	509.1	1141.22	2241.64	-0.76	6.50	7.30
Cotton Fabrics	Mn.Sq.mts.	1574.7	1096.20	0.6961	1685.0	1017.70	0.6040	1909	1130.83	0.5923	2036	1345.65	0.6609	2379	1711.79	0.7195	51.08	56.16	3.36
Synthetic Textiles	Mn.Sq.mts	641.0	457.65	0.7140	840.0	536.52	0.6387	655	410.03	0.6261	788	574.31	0.7288	653	467.7	0.7162	1.87	2.20	0.32
Knitwear	000 Doz	39313	886.68	22.55	38838	898.95	23.15	36556	845.94	23.14	52133	1146.67	22.00	66894	1471.43	22.00	70.16	65.95	-2.45
Bedwear	000 MT	132.6	709.92	5354.40	147.9	734.92	4968.00	181	918.56	5074.92	242	1329.06	5491.98	247	1388.35	5620.85	86.27	95.56	4.98
Towels	000 MT	51.2	195.63	3818.52	67.1	241.02	3590.10	79	267.71	3401.65	101	374.84	3711.29	104	411.96	3961.15	103.13	110.58	3.74
Readymade Garments	000 Doz	30420	771.73	25.37	3607	825.63	22.89	41415	874.95	21.13	36457	1092.61	29.97	27871	1003.5	36.01	-8.38	30.03	41.92
Other Textile Madeups	-	-	307.56	-	-	328.26	-	-	350.9	-	-	359.77	-	-	420.19	-	-	36.62	-
Carpets & Carpetting	000 Sq.mts.	5156.0	264.28	51.26	6026.0	276.25	45.84	5085	249.57	49.08	4259	220.90	51.87	3982	220.27	55.32	-22.77	-16.65	7.91
Leather Manufactures	-	-	338.66	-	-	405.25	-	-	383.19	-	-	386.55	-	-	403.11	-	-	19.03	-
Footwear	000 Pairs	7509	37.20	4.95	7574	40.90	5.40	9210	54.43	5.91	13300	85.89	6.46	12239	87.61	7.16	62.99	135.51	44.49
Sports Goods	-	-	279.15	-	-	268.00	-	-	304.48	-	-	335.17	-	-	309.54	-	-	10.89	-
Surgical & Medicinal Instruments	-	-	120.13	-	-	116.82	-	-	145.05	-	-	149.96	-	-	124.03	-	-	3.25	-

Unit Value & Quantities - Major Imports

($ Mn)

Items	Unit	1999-00			2000-01			2001-02			2002-03			2003-04			% Change in 5-Years 2003-04 over 1999-00		
		Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value	Quantity	Value	Unit Value
Wheat	000 MT	2005.8	283.5	141.34	80	15.4	192.50	267.2	50.02	187.20	147.9	28.72	194.19	108.0	23.61	218.61	-94.6	-91.67	54.67
Tea	000 MT	108.64	210.44	1937.04	111.9	206.4	1844.50	99.4	156.56	1575.05	108.1	172.74	1597.96	118.4	196393	1663.26	9.0	-6.42	-14.13
Soyabean Oil	000 MT	202.4	8.4	436.76	128.4	44.1	343.46	34.3	12.67	369.39	82.7	47.49	574.24	80.6	82.66	1025.56	-60.2	-6.49	134.81
Palm Oil	000 MT	848.5	325.1	383.15	1015.1	283.5	279.28	1162.5	380.33	327.17	1210.9	539.31	445.38	1272.4	608.22	478.01	50.0	87.09	24.76
Sugar	000 MT	66.6	14.8	222.22	930.1	251.9	270.83	85.7	23.45	273.63	8.3	2.62	315.66	11.0	3.19	290.00	-83.5	-78.45	30.50
Pulses	000 MT	293	89.6	305.80	364.8	113	309.76	460.3	135.94	295.33	394.4	115.64	293.20	255.4	73.65	288.7	-12.8	-17.80	-5.70
Fertilizer	000 MT	1120.9	197.6	176.29	954	170.5	178.72	1219.3	176.23	144.53	1295.2	239.77	185.12	1321.4	281.27	212.86	17.9	42.34	20.74
Plastic Material	000 MT	391.7	332.9	849.89	408.2	354.3	867.99	457.9	352.71	770.28	513.2	421.10	820.54	583.4	526.40	902.30	48.9	58.13	6.17
Medicinal Products	000 MT	11.7	59.4	22170.94	10.4	238.7	22951.92	9.7	228.13	23518.56	8.7	221.80	25494.25	9.6	268.20	27937.50	-17.9	3.39	26.01
Petroleum&Products	000 MT	16263	2804.4	172.44	16983.5	3360.9	197.89	16368.9	2807.01	171.48	15241.6	3066.44	201.19	13289.8	3159.24	237.72	-18.3	12.65	37.86
Synthetic Text.&Clothing	000 MT	166.3	152.5	917.02	174.8	161.8	925.63	213.8	187.49	876.94	246.4	221.65	899.55	249.2	255.03	1023.39	49.8	67.23	11.60
Iron & Steel and Scrap	000 MT	1051.4	328.4	312.35	1191.9	320.9	269.23	1540.5	386.68	251.01	1443.6	450.20	311.86	1739.6	582.13	334.63	65.5	77.26	7.14
Paper & Manufactures	000 MT	175	117.5	671.43	160.5	125.3	780.69	197.1	136.82	694.17	217.1	131.67	606.49	255.0	159.11	623.96	45.7	35.41	-7.07
Power Generating Machine	-	-	141.7	-	-	197.9	-	-	203.80	-	-	268.53	-	-	265.46	-	-	87.34	-
Textile Machinery	-	-	211.0	-	-	370.2	-	-	406.91	-	-	531.94	-	-	585.66	-	-	177.56	-
Construction Machinery	-	-	88.4	-	-	82.5	-	-	118.58	-	-	101.23	-	-	101.11	-	-	14.38	-
Road Motor Vehicles	-	-	345.5	-	-	320.9	-	-	329.92	-	-	501.18	-	-	632.45	-	-	83.05	-
Electrical machinery	-	-	155.0	-	-	131.6	-	-	128.05	-	-	216.68	-	-	246.76	-	-	59.20	-
Rubber Crude	000 MT	55.6	37.0	655.47	58.7	39.2	667.80	65.4	41.12	628.75	63.8	49.11	769.75	78.0	68.17	873.97	40.3	84.24	31.33
Rubber Tyres & Tubes	000 Nos.	2825	69.4	24.57	2789	62.5	22.41	3156.7	66.56	21.09	3809.9	78.26	20.54	3853.6	87.03	22.58	36.4	25.40	-8.07

Source: Federal Bureau of Statistics

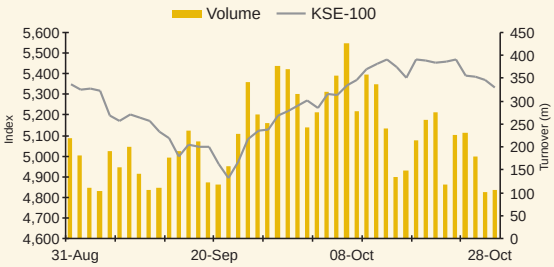
Market Analysis

Market Review

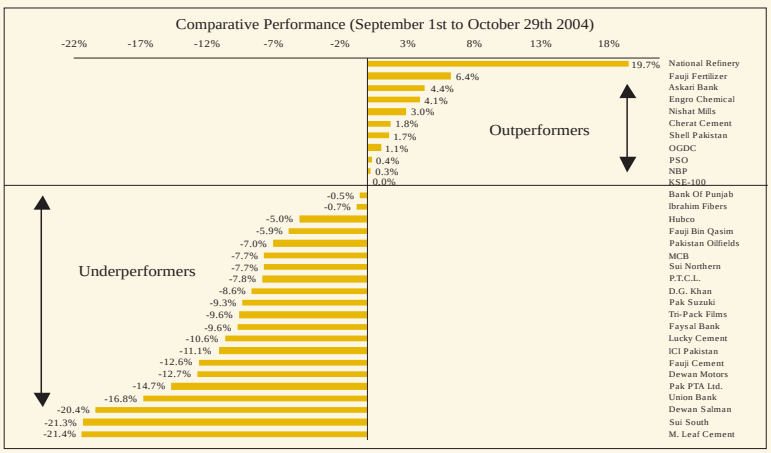
Over the months of September and October 2004, the KSE-100 Index dipped to a low of 4891 points and rose to a high of 5470 points, but in the end failed to break out of the narrow band within which it had been trading since April this year. The index fell 14.5 points net over the two months to close October at 5332. September was the real bearish month, in which the Index lost 128.8 points and average daily trading volumes dropped to 198 million shares per day. October was more positive. Despite losses in the final week of October, the index managed to close up 114 points during that month and average trading volume rose to 245 million shares per day.

September was bearish in part because the SECP announced early in the month that the process of phasing out the badla/COT market would begin from October 8th, 2004. The Index fell 123 points on the day following the announcement. There was further weakness later in the month when it

KSE-100 Index (Sep - Oct 2004)



became clear that efforts to remove the CVT imposed in the 2004-05 budget would not bear fruit. Technical problems at Hubco's plant leading to the closure of some of its units did not help. The negative sentiment continued until the final week of September, when after reaching the level of 4890 - the lowest Index level since early March - institutional support came in to reverse the momentum. PTCL's announcement of a much higher than expected Rs5 per share dividend gave a significant boost to the market in the final week of September too, and this continued driving the Index upward into October.



High oil prices boon for market

The single most positive event for the Index in October was the surge in oil prices. Oil prices had been rising since May, but in October, with world oil prices breaking US$55 per barrel (NY Light Crude) at one point, the large cap oil stocks which dominate the KSE-100 Index (PSO, OGDCL, NRL) began to perform.

Paradoxically, while the high oil prices are bad for the economy- increasing the trade deficit, adding to the weakness of the rupee, and raising fuel costs for industries- for the local equity markets the impact is positive because of the predominance of large cap oil sector companies whose bottom-lines benefit when oil prices rise. Hence the surge in international oil prices were viewed with mixed emotions by the market, but the net impact was positive for the Index.

Strong corporate earnings

Corporate earning have generally been very good. During the Sep-Oct period, there were both annual/ semi-annual earnings announced for the period ending Jun'04, and quarterly earnings announced for the period ending Sep'04. As mentioned, PTCL's full year earnings and dividend were exceptionally high and helped to turn sentiment around in the end of September. Towards the end of October, better than expected earnings by the fertilizer sector, as well as very good earnings by the oil sectors (OMCs and E&P companies), and banks added to the upward momentum. The best performing stocks over the two month period include FFC, Engro, Shell, OGDCL, NRL, Askari Bank and NBP. It is no coincidence that all of these also reported extremely good earnings in October.

Some economic factors are causing concern

Inflation in the September-October period remained above 9% as measured by the CPI and this is not a healthy sign. While most of the inflation was non-structural and could not be countered by raising interest rate (food and beverage group inflation of 13.13% during the month of October accounting for 40.34% of total CPI inflation), an increasing amount is due to house rent (10.17% increase in house rents in October, contributing 23.4% of the increase in CPI inflation), and this is structural.

Equally worrying has been the fact that the rupee has devalued 4.4% versus the dollar between the start of September when it was Rs58.74/ US$ and the end of October when it reached Rs61.34/ US$. The SBP may try to defend against a further drop in the rupee, but the underlying problem is that Pakistan's current account balance has slipped into a deficit from a surplus last year because of the jump in the trade deficit (US$839m trade deficit in 1Q05 alone). It is likely that unless oil prices drop and the size of the trade deficit reduces, the rupee will remain under pressure over the next few months.

The SBP has already stated that it will gradually increase interest rates, and this was exemplified by the 6-month T-bill auctions in which the weighted average yield increased from 2.6% to 3.0% in the September auction and then again to 3.19% in the October auction.

All of the above economic trends are a cause for worry, and have contributed towards the lackluster market performance over the last 6 months.

Recommendation

The best strategy in the current market environment is to focus on long-term investments in companies, which have shown the best earnings performance. The top sectors in this regards are banks, fertilizer, and energy (oil).

(Contributed by Taurus Securities Ltd, a subsidiary of National Bank of Pakistan)

Key Economic Indicators

Economy Size & Growth			2000-01	2001-02	2002-03	2003-04
GNP - Market Prices		Rs. bn	4108.2	4425.4	4973.1	5576.3
GDP - Market Prices		Rs. bn	4162.6	4401.7	4821.3	5458.1
Per Capita Income	Market Prices	Rs.	29269	30910	34074	37495
	Market Prices	US$	501	503	582	652
Growth						
GDP		%	1.8	3.1	5.1	6.4
Agriculture		%	(-)2.2	0.1	4.1	2.6
Manufacturing		%	9.3	4.5	6.9	13.4
Wholesale & Retail trade		%	4.5	2.8	5.9	8.0
Rate of Inflation		%				
Consumer Price Index**			3.6	3.5	3.1	4.2†
Wholesale Price Index			6.2	2.1	5.6	7.5†
Balance of Payment		$mn				
Exports (f.o.b.)			8933	9140	10889	9175‡
Imports (f.o.b.)			10202	9434	11333	9932‡
Trade Balance			(-)1269	(-)294	(-)444	(-)757‡
Services Account (Net)			(-)3142	(-)2617	(-)2128	(-)2260‡
Private Transfers (Net)			3898	4249	5737	4386‡
Current Account Balance			(-)513	1338	3165	1369‡
Fiscal Balance		% of GDP				
Total Revenue (Net)			13.3	14.2	15.0	14.3
Total Expenditure			17.2	18.8	18.6	17.5
Overall Defict			4.3	4.3	3.7	3.3
Domestic & Foreign Debt						
Domestic Debt		Rs. bn	1799.2	1757.6	1879.2	2028.4
As % GDP			43.2	39.9	39.0	37.2†
Total External Debt & Liabilities		$bn	37.139	36.532	35.474	35.846†
as % GDP			52.1	51.0	43.0	37.8†
as% of Foreign Exchange Earnings			259.8	237.0	181.1	168.7
Investment & Savings		% of GDP				
Gross Investment			17.2	16.8	16.7	18.1
Gross Fixed Investment			15.8	15.5	14.8	16.4
National Savings			16.5	18.6	20.6	19.8
Domestic Savings			17.8	18.1	17.4	17.6
Foreign Investment		$mn	182	475.0	820.1	629.0
Portfolio			(-)140	(-)10	22.1	(-)131.3
Direct			322	485	798.0	760.4
Monetary Aggregates		%				
M_1			3.0	15.2	26.2	17.5
M_2			9.0	15.4	18.0	12.3
Literacy Rate		%	49.0	50.5	51.6	54.0
Foreign Exchange Reserves^		$mn	3220	6432	10719	12511†
Exchange Rate++		Rs./$	58.4378	61.4258	58.4995	57.5378
Stock Market Growth Rate		%				
SBP General Index of Share Prices**			(-)7.9	10.1	91.9	61.9†
Aggregate Market Capitalisation			(-)13.4	20.0	83.1	96.7†

Source: Economic Survey 2003-04

* Constant Factor Cost of 1999-2000 ** Base 2000-01
† July-May ‡ July-March
^ Excludes FE 13/CRR and includes Indian pending transfers, new FCA and Trade Nostro.
++ Average during the year.
M_1 Outstanding stock of currency in circulation+demand deposits of schedule banks+other deposits with SBP.
M_2 M_1 +outstanding stock of time deposits+outstanding stock of FRCDs.